

CITY OF FREEPORT
FREEPORT, TEXAS

ANNUAL FINANCIAL REPORT

FOR THE YEAR ENDED
SEPTEMBER 30, 2013

KENNEMER, MASTERS & LUNSFORD, LLC
CERTIFIED PUBLIC ACCOUNTANTS
8 WEST WAY COURT
LAKE JACKSON, TEXAS 77566

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CITY OF FREEPORT

Freeport, Texas

*Annual Financial Report
For the Year Ended September 30, 2013*

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FINANCIAL SECTION

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Kennemer, Masters & Lunsford

CERTIFIED PUBLIC ACCOUNTANTS

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Independent Auditor's Report

To the Honorable Mayor, Members
of City Council, and City Manager
City of Freeport
Freeport, Texas

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Freeport, Texas (the "City") as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Freeport, as of September 30, 2013, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 2 to the financial statements, in 2013, the City adopted new accounting guidance, GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, and recorded a prior period adjustment. Our opinion was not modified with respect to these matters.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 11 through 24, and the budgetary comparison information, the Texas Municipal Retirement System, and the Texas Statewide Emergency Services Personnel Retirement Fund Schedules on pages 84 through 87, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The introductory section, and other statements and schedules, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements.

The other statements and schedules and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the other statements and schedules and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the basic financial statements as a whole.

Honorable Mayor, Members
of City Council, and City Manager
City of Freeport
Page 3

The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 23, 2014, 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering City's internal control over financial reporting and compliance.

Kennemer, Masters & Hunzford, LLC

Certified Public Accountants
Lake Jackson, Texas
June 23, 2014

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CITY OF FREEPORT, TEXAS

Management's Discussion and Analysis For the Year Ended September 30, 2013

As management of the City of Freeport (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, 2013. We encourage readers to consider the information presented here in conjunction with the City's financial statements, which follow this section.

Financial Highlights

- In May 2010, the City of Freeport (the "City") took over the operations of the Freeport Economic Development Corporation's (the "Corporation") marina. This involved collection of dock fees and payment of operating expenditures, which included operating leases. The City established a separate fund (Special Revenue) to account for these operations, and contracted a manager for the marina operations.
- During the prior year, the City and the Corporation froze the payments of principal and interest and the accrual of interest until such time as the Marina is complete and an agreement of the amount and timing of debt payments can be reevaluated.
- The assets and deferred outflows of resources of the City of Freeport exceeded its liabilities and deferred inflows of resources at the close of the most recent fiscal year by \$ 29,239,677 (net position). Of this amount, \$ 3,770,141 (unrestricted net position) may be used to meet the government's ongoing obligations to citizens and creditors in accordance with the City's fund designation.
- The City's net position of \$ 29,239,677 increased by \$ 1,088,659 from the prior year.
- As of the close of the current fiscal year, the City of Freeport's governmental funds reported combined ending fund balances of \$ 11,247,046. 38.94% of this total amount, \$ 4,379,904 (unassigned fund balance) is available for use within the City's fund designation.
- At the end of the current fiscal year, total fund balance for the general fund was \$ 11,537,857 and the unassigned fund balance was \$ 4,808,735. These amounts were 112.55% and 46.91% of the total general fund expenditures.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the City of Freeport's basic financial statements. The City's basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide financial statements. The *government-wide financial statements* are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

CITY OF FREEPORT, TEXAS

*Management's Discussion and Analysis
For the Year Ended September 30, 2013*

The *statement of net position* presents information on all of the City's assets and deferred outflows of resources, and liabilities and deferred inflows of resources, with the difference between the two reported as *net position*. Over time, increases or decreases in net position 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 position changed during the fiscal year. All changes in net position are reported when the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in the future fiscal periods (e.g., uncollected taxes and earned but unused compensated absences).

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The *governmental activities* of the City include general government and administration, public safety, public works, and cultural and recreation. The *business-type activities* of the City include the operations of water and sewer, golf course, and ambulance.

The government-wide financial statements can be found on pages 26 through 29 of this report.

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

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

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

CITY OF FREEPORT, TEXAS

Management's Discussion and Analysis For the Year Ended September 30, 2013

The City maintains nine individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General Fund and the Marina Operations (special revenue fund), which are considered to be the major funds. Data from the other seven funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of combining statements on pages 90 through 93 of this report.

- **Proprietary Funds.** The City maintains three individual *proprietary funds*-Enterprise Funds. Information is presented separately in the proprietary fund's statement of net position, statement of revenues, expenses and changes in net position, and statement of cash flows on pages 36 through 41 of the report for the Water and Sewer Enterprise Fund, Golf Course Enterprise Fund, and Ambulance Enterprise Fund; which are considered to be major funds. Enterprise funds are used to report the same functions presented as business-type activities in government-wide financial statements. The City uses enterprise funds to account for its water and sewer, golf course, and ambulance operations. Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail.

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 43 through 81 of this report.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information that further explains and supports the information in the financial statements. Required supplementary information can be found on pages 84 through 87 of this report. The combining statements referred to earlier in connection with non-major governmental funds are presented following the required supplementary information on pensions. Combining and individual statements and schedules can be found on pages 90 through 108 of this report. The Schedule of Expenditures of Federal Awards is found on page 121.

Government-wide Financial Analysis

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. In the case of the City of Freeport, assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources by \$ 29,239,677 as of September 30, 2013.

A large portion of the City's net position, in the amount of \$ 17,250,932 (59.00%) reflects its investments in capital assets (e.g., land, buildings, improvements, equipment, machinery, construction in progress), less any debt used to acquire those assets that is still outstanding. The City uses capital assets to provide service to citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

CITY OF FREEPORT, TEXAS

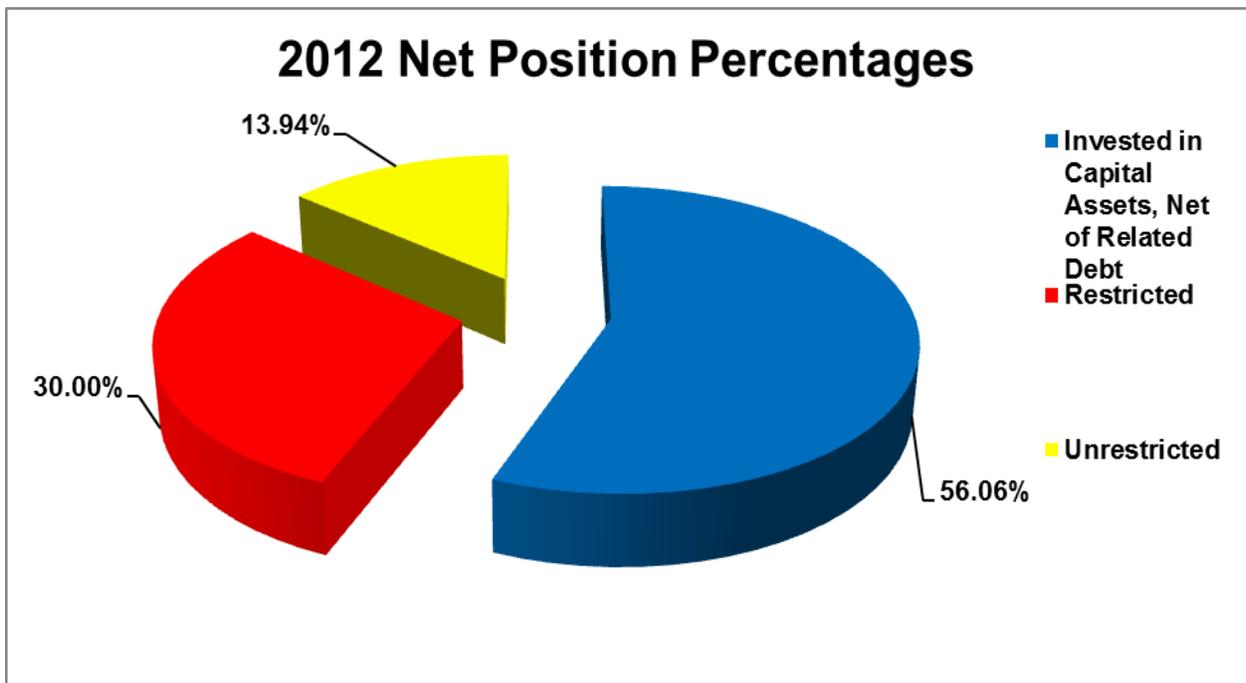
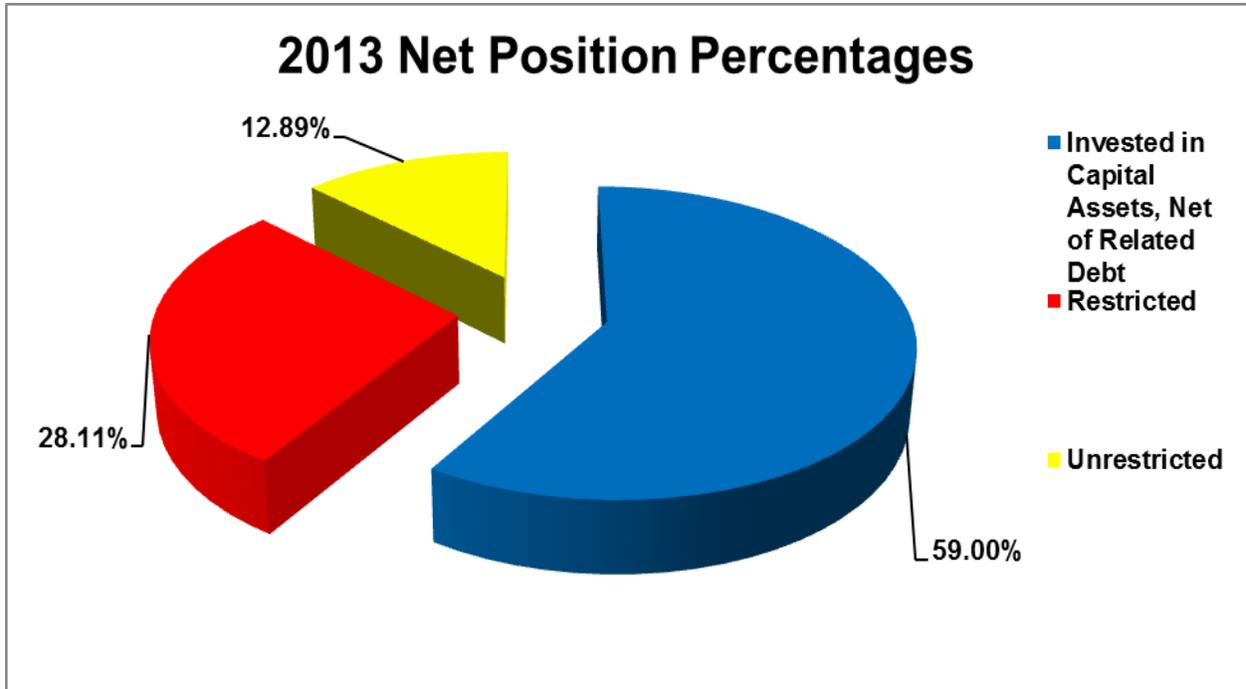
Management's Discussion and Analysis
For the Year Ended September 30, 2013

An additional portion of the City's net position of \$ 8,218,604 (28.11%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net position of \$ 3,770,141 (12.89%) may be used to meet the government's ongoing obligations to citizens and creditors.

As of September 30, 2013, the City is able to report positive balances in all categories of net position for the government as a whole. The business-type activities report a negative amount in unrestricted net position.

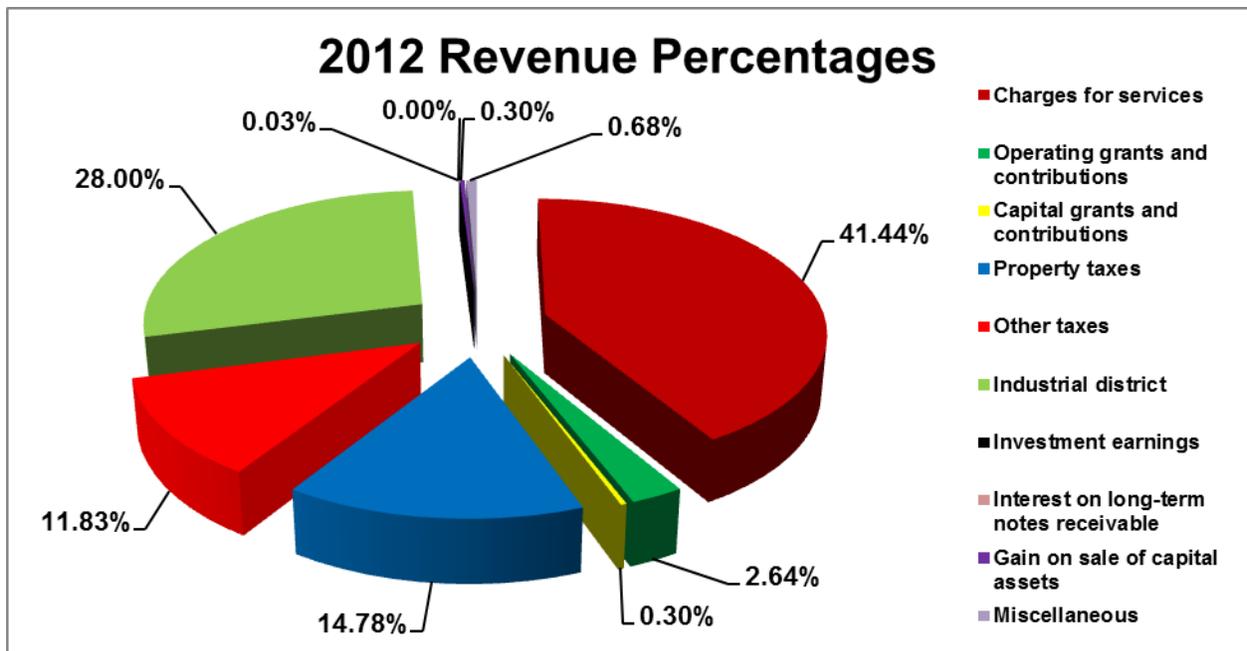
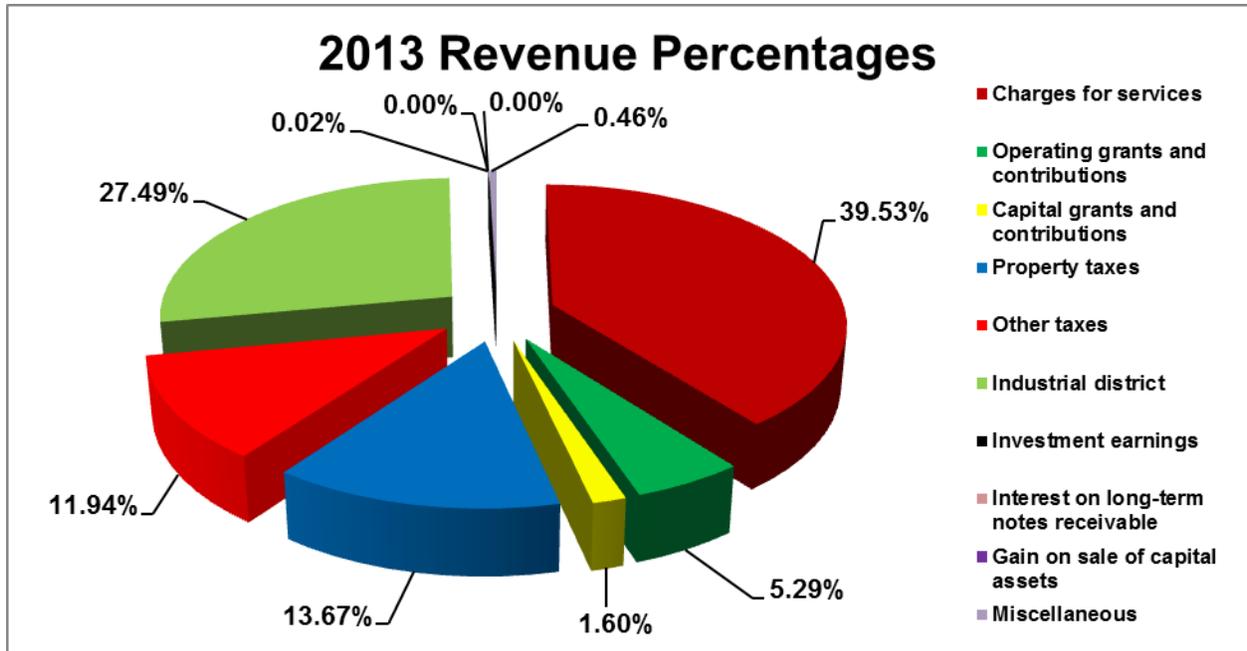
CITY OF FREEPORT'S NET POSITION

	Governmental Activities		Business-type Activities		Totals	
	September 30,		September 30		September 30,	
	2013	Restated 2012	2013	Restated 2012	2013	Restated 2012
Current and other assets	\$ 5,909,321	\$ 5,783,242	\$ 432,373	\$ 507,854	\$ 6,341,694	\$ 6,291,096
Long-term receivables	8,083,539	8,083,539			8,083,539	8,083,539
Capital assets	<u>15,715,181</u>	<u>15,005,598</u>	<u>7,554,896</u>	<u>7,237,972</u>	<u>23,270,077</u>	<u>22,243,570</u>
Total assets	<u>29,708,041</u>	<u>28,872,379</u>	<u>7,987,269</u>	<u>7,745,826</u>	<u>37,695,310</u>	<u>36,618,205</u>
Current and other liabilities	789,973	746,195	764,918	469,620	1,554,891	1,215,815
Long-term liabilities	<u>6,135,012</u>	<u>6,419,263</u>	<u>765,730</u>	<u>832,109</u>	<u>6,900,742</u>	<u>7,251,372</u>
Total liabilities	<u>6,924,985</u>	<u>7,165,458</u>	<u>1,530,648</u>	<u>1,301,729</u>	<u>8,455,633</u>	<u>8,467,187</u>
Net Position:						
Invest in capital assets, net of related debt	10,377,214	9,391,372	6,873,718	6,532,014	17,250,932	15,923,386
Restricted	8,202,427	8,416,304	16,177		8,218,604	8,416,304
Unrestricted	<u>4,203,415</u>	<u>3,899,245</u>	<u>(433,274)</u>	<u>(87,917)</u>	<u>3,770,141</u>	<u>3,811,328</u>
Total net position	<u>\$ 22,783,056</u>	<u>\$ 21,706,921</u>	<u>\$ 6,456,621</u>	<u>\$ 6,444,097</u>	<u>\$ 29,239,677</u>	<u>\$ 28,151,018</u>

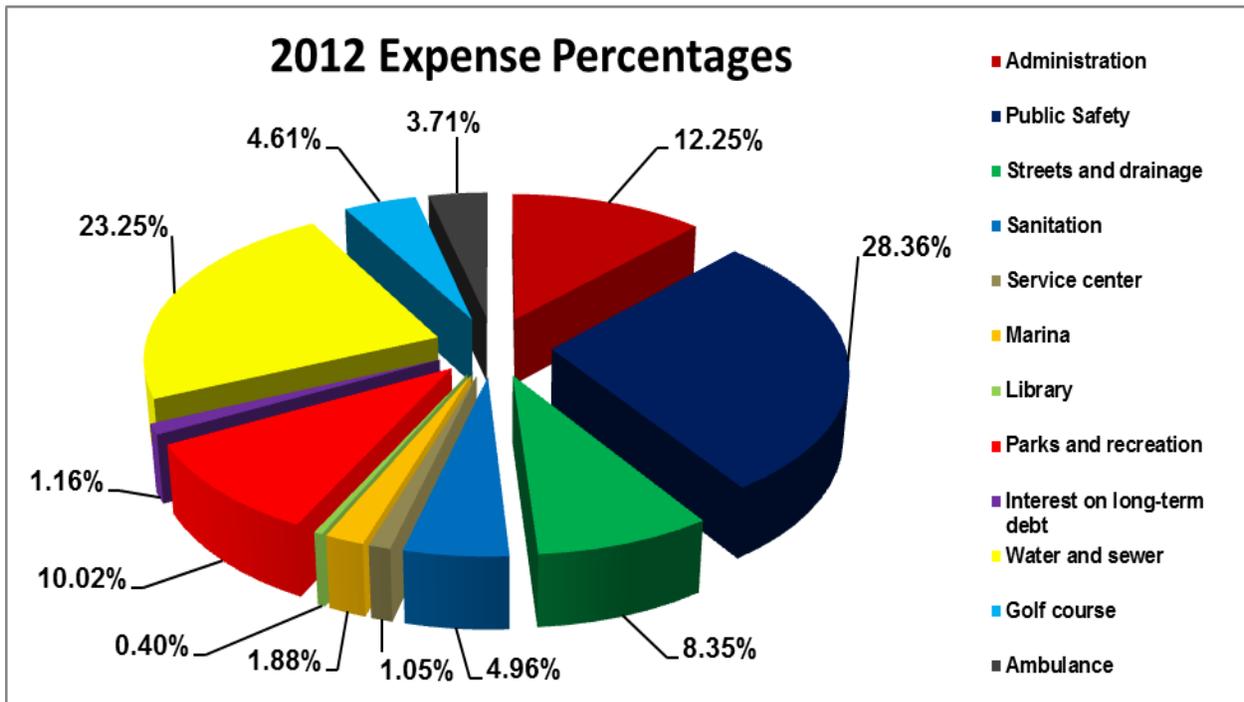
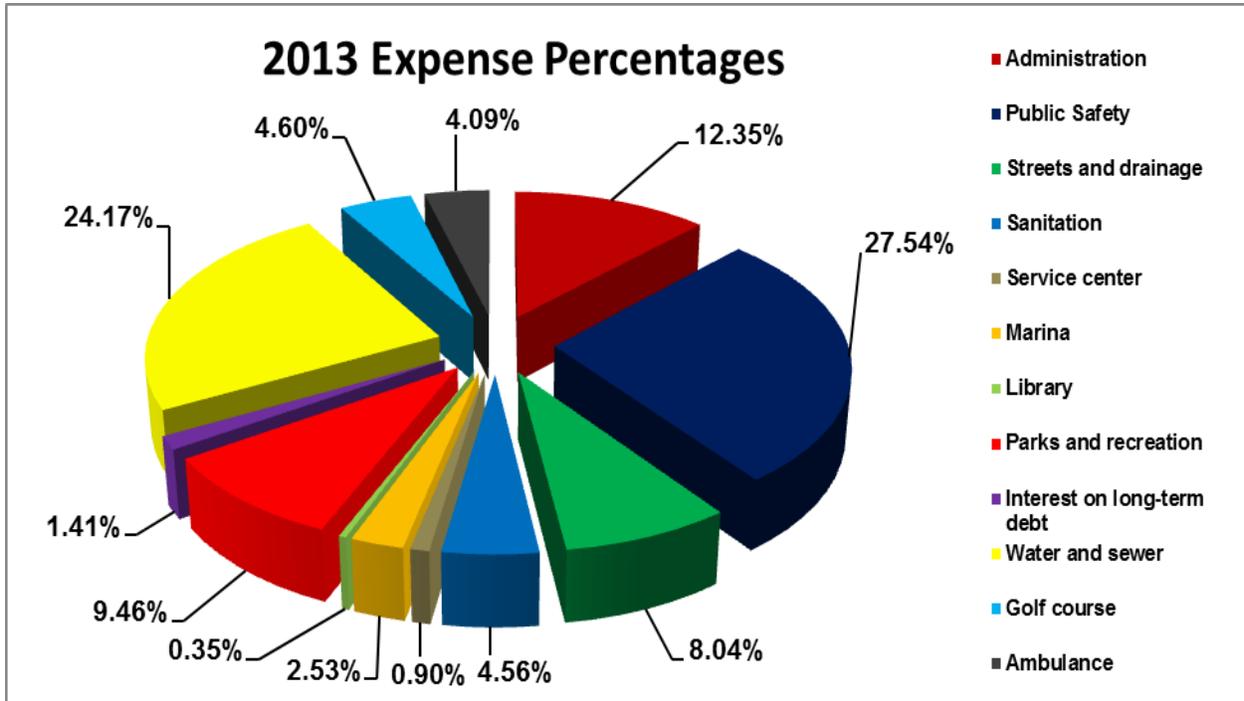


CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2013

Analysis of the City's Operations. The following graphs provide a summary of the City's operations for the years ended September 30, 2013. Governmental activities increased the City of Freeport's net position by \$ 1,076,135 and the business-type activities increased the City's net position by \$ 12,524.



CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2013



CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2013

CITY OF FREEPORT'S CHANGES IN NET POSITION

	Governmental Activities		Business-type Activities		Totals	
	September 30,		September 30,		September 30,	
	2013	Restated 2012	2013	Restated 2012	2013	Restated 2012
Revenues:						
Program Revenues:						
Charges for services	\$ 2,405,898	\$ 2,054,223	\$ 4,617,204	\$ 4,973,425	\$ 7,023,102	\$ 7,027,648
Operating grants and contributions	853,399	448,987	86,910		940,309	448,987
Capital grants and contributions			285,053	50,045	285,053	50,045
General Revenues:						
Property taxes	2,428,164	2,505,767			2,428,164	2,505,767
Other taxes	2,120,609	2,005,458			2,120,609	2,005,458
Industrial district	4,884,316	4,748,786			4,884,316	4,748,786
Investment earnings	3,972	5,038	79	51	4,051	5,089
Gain on disposition of capital assets		50,399				50,399
Miscellaneous	82,447	115,746			82,447	115,746
Total revenues	<u>12,778,805</u>	<u>11,934,404</u>	<u>4,989,246</u>	<u>5,023,521</u>	<u>17,768,051</u>	<u>16,957,925</u>
Expenses:						
Administration	2,059,996	2,065,722			2,059,996	2,065,722
Public safety	4,492,872	4,782,099			4,592,872	4,782,099
Streets and drainage	1,341,802	1,407,419			1,341,802	1,407,419
Sanitation	760,582	835,764			760,582	835,764
Service center	150,225	177,731			150,225	177,731
Marina	422,178	316,233			422,178	316,233
Library	57,964	67,066			57,964	67,066
Parks and recreation	1,578,706	1,690,335			1,578,706	1,690,385
Interest on long-term debt	234,956	196,014			234,956	196,014
Water and sewer			4,030,789	3,921,527	4,030,789	3,921,527
Golf course			767,541	777,904	767,541	777,904
Ambulance			681,781	625,071	681,781	625,071
Total expenses	<u>11,199,281</u>	<u>11,538,433</u>	<u>5,480,111</u>	<u>5,324,502</u>	<u>16,679,392</u>	<u>16,862,935</u>
Increase in net position before contributions and transfers	1,579,524	395,971	(490,865)	(300,981)	1,088,659	94,990
Transfers	(503,389)	(259,862)	503,389	259,862	-0-	-0-
Increase in net position	1,076,135	136,109	12,524	(41,119)	1,088,659	94,990
Net position – beginning (restated)	<u>21,706,921</u>	<u>21,570,812</u>	<u>6,444,097</u>	<u>6,485,216</u>	<u>28,151,018</u>	<u>28,056,028</u>
Net position – ending	<u>\$ 22,783,056</u>	<u>\$ 21,706,921</u>	<u>\$ 6,456,621</u>	<u>\$ 6,444,097</u>	<u>\$ 29,239,677</u>	<u>\$ 28,151,018</u>

CITY OF FREEPORT, TEXAS

*Management's Discussion and Analysis
For the Year Ended September 30, 2013*

Financial Analysis of the City's Funds

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

Governmental funds. The focus of the City of Freeport'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 of Freeport's governmental funds reported combined ending fund balances of \$ 11,247,046. 38.94% of this total amount (\$ 4,379,904) constitutes unassigned fund balance. The remainder of the fund balance is either non-spendable or restricted to indicate that it is not available for new spending 1) non-spendable for long-term receivables \$ 6,639,208, 2) restricted for tourism \$ 25,504, 3) restricted for debt service \$ 51,870, 4) restricted for capital projects \$ 54,029, 5) restricted for municipal court security \$ 21,260, 6) restricted for municipal court technology \$ 2,342, 7) assigned for beach maintenance \$ 6,617; 8) assigned for narcotics operations \$ 63,517, 9) and assigned to main street \$ 2,795.

The General Fund balance increased by \$ 463,388, the Marina Operations (special revenue fund) decreased by \$ (153,384), and the other governmental funds decreased \$ 238,636.

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

Net position at September 30, 2013 amounted to \$ 6,456,621. Total net position increased by \$ 12,524 (or 0.19%).

General Fund Budgetary Highlights. Differences between the original budget and the final amended budget resulted in a \$ 570,868 increase in estimated revenues and a \$ 841,412 increase in appropriations which involved a number of budget items. The more significant items are summarized below.

- \$ 107,675 increase in budget funding for the Central Lift Station.
- \$ 35,000 increase for Police Department federal narcotics expense to spend Federal Seized Funds received in the prior year.
- \$ 107,024 increase in EMS (Ambulance) capital outlay to purchase a new ambulance.

The City's overall budgeted revenue increased 7.36% or \$ 1,292,831; primarily due to an increase in grant revenues.

Capital Assets

The City of Freeport's investment in capital assets for its governmental and business-type activities as of September 30, 2013, amounts to \$ 23,270,077 (net of accumulated depreciation). This investment in capital assets includes land, improvements, buildings, utility plant, furniture, equipment and vehicles, and construction in progress.

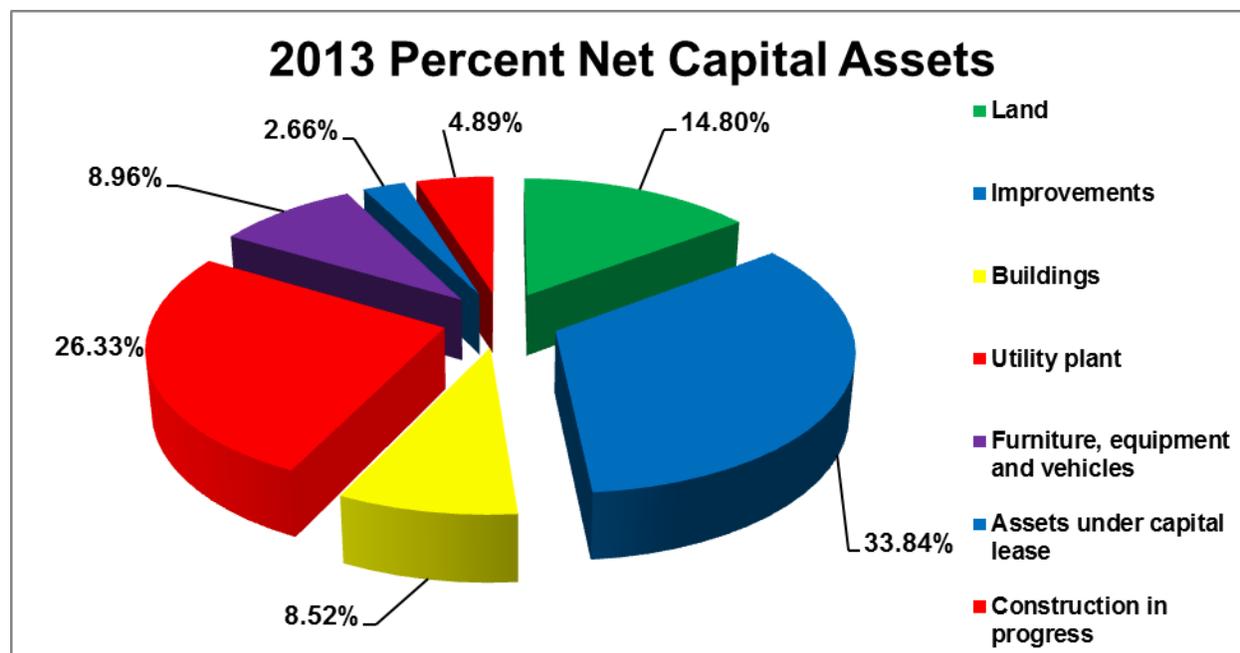
CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2013

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

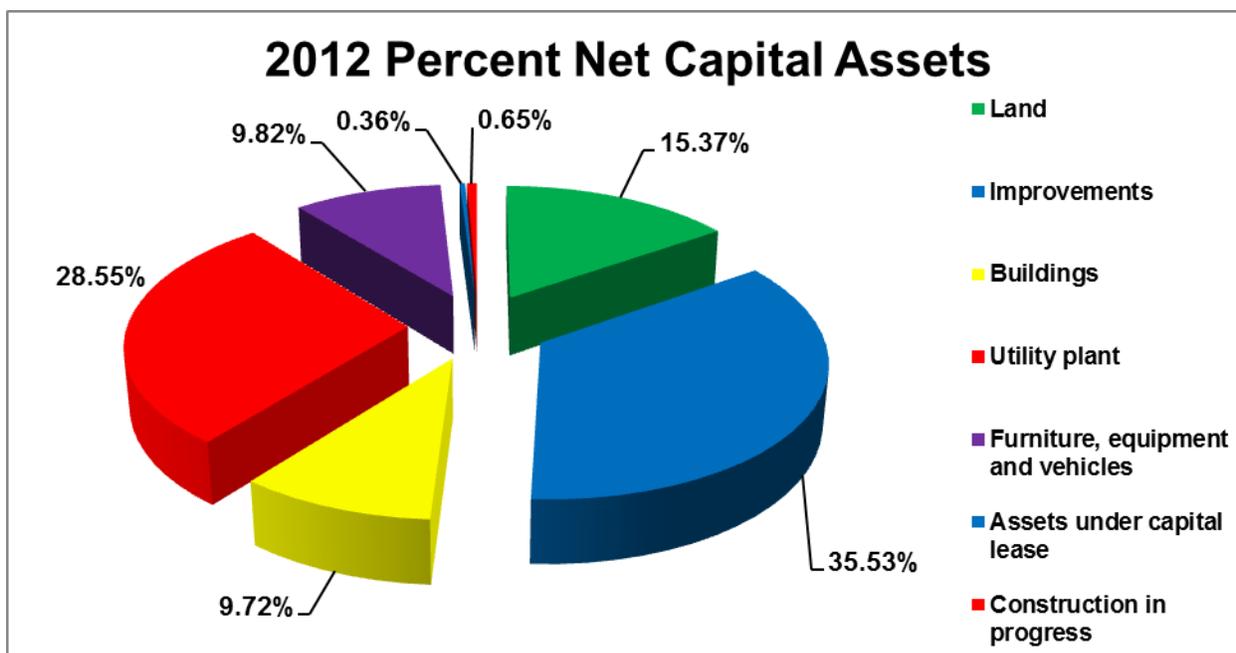
- CDBG Project – Central Lift Station
- New ambulance
- 2008 Port Security Grant for the Police Department
- 4 – new Chevy Tahoe's for the Police Department

Capital Assets
Net of Accumulated Depreciation

	Governmental Activities		Business-type Activities		Totals	
	September 30,		September 30,		September 30,	
	2013	Restated 2012	2013	2012	2013	Restated 2012
Land	\$ 3,048,548	\$ 3,024,568	\$ 395,630	\$ 395,630	\$ 3,444,178	\$ 3,420,198
Improvements	7,770,513	7,769,993	104,210	132,442	7,874,723	7,902,435
Buildings	1,876,839	2,048,324	105,389	113,702	1,982,228	2,162,026
Utility plant			6,127,209	6,350,052	6,127,209	6,350,052
Furniture, equipment and vehicles	1,802,443	2,018,377	283,429	165,772	2,085,872	2,184,149
Assets under capital lease	365,190		253,976	80,374	619,166	80,374
Construction in progress	851,648	144,336	285,053		1,136,701	144,336
Total	\$ 15,715,181	\$ 15,005,598	\$ 7,554,896	\$ 7,237,972	\$ 23,270,077	\$ 22,243,570



CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2013



Additional information on the City of Freeport's capital assets can be found in Note 6 on pages 61 through 64 of this report.

Notes Receivable

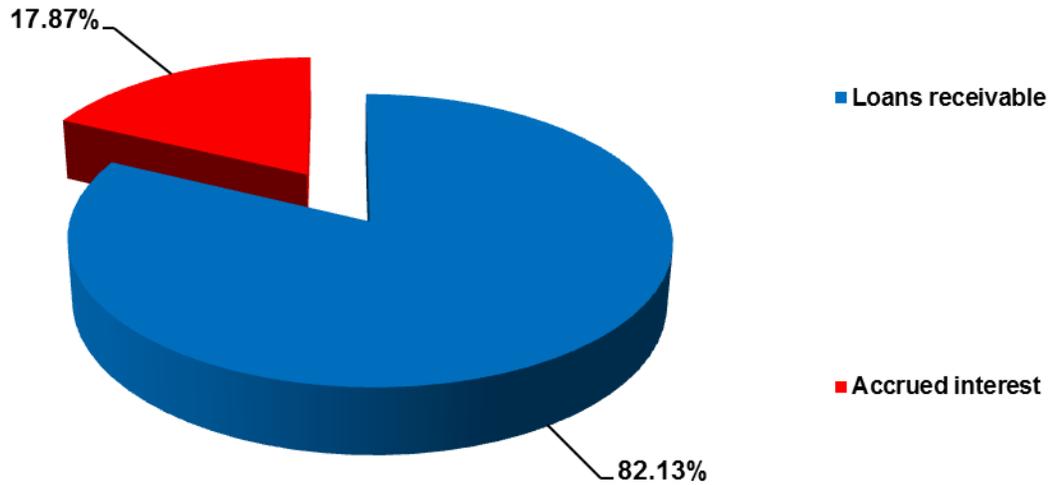
At the end of the current fiscal year, the City of Freeport had a total note receivable of \$ 6,639,208. Of this amount, \$ 6,000,000 represents a loan made during the year ended September 30, 2007 to the Freeport Economic Development Corporation. The remaining \$ 639,208 is a consolidated loan with the Freeport Economic Development Corporation from prior years.

Long-Term Receivables Outstanding

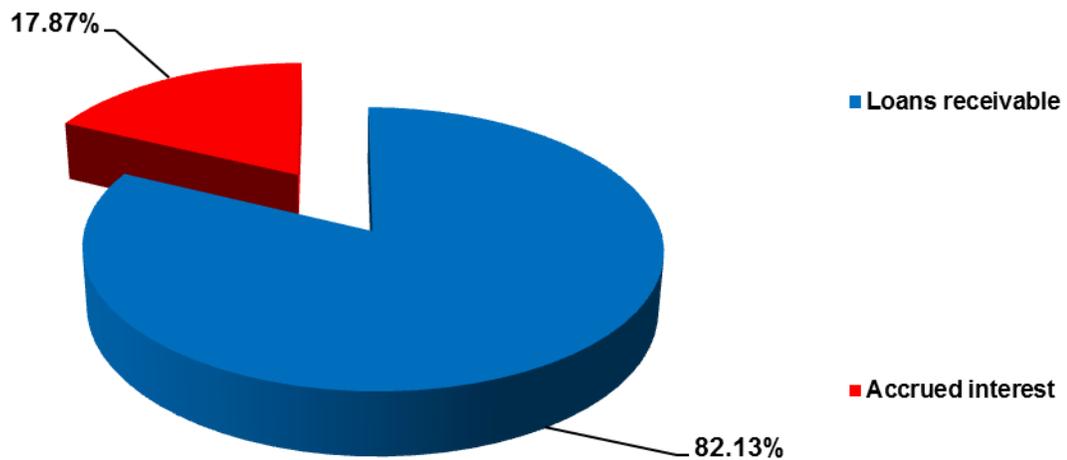
	Governmental Activities		Business-type Activities		Totals	
	September 30,		September 30,		September 30,	
	2013	2012	2013	2012	2013	2012
Loans receivable	\$ 6,639,208	\$ 6,639,208	\$	\$	\$ 6,639,208	\$ 6,639,208
Components of Long-Term Loans Receivable:						
Accrued interest receivable	<u>1,444,331</u>	<u>1,444,331</u>			<u>1,444,331</u>	<u>1,444,331</u>
Total	<u>\$ 8,083,539</u>	<u>\$ 8,083,539</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ 8,083,539</u>	<u>\$ 8,083,539</u>

Additional information on the City of Freeport's long-term notes receivable can be found in Note 16 on pages 78 through 79 of this report.

2013 Percent Long-Term Receivables



2012 Percent Long-Term Receivables



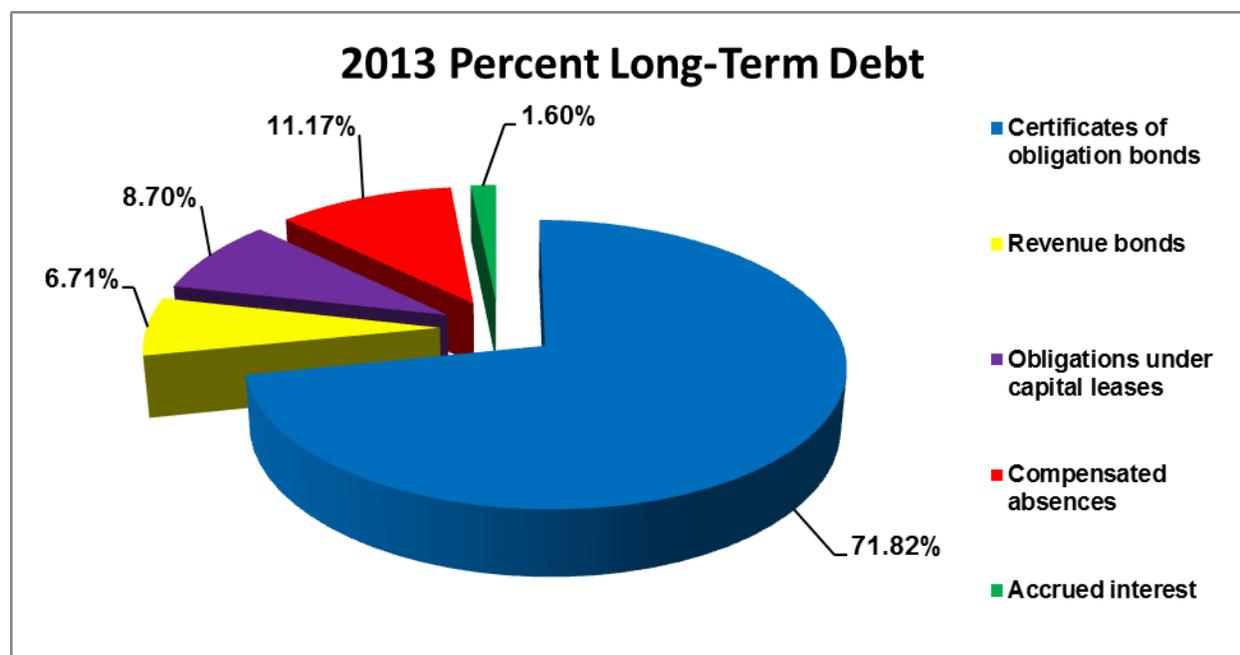
CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2013

Debt Administration

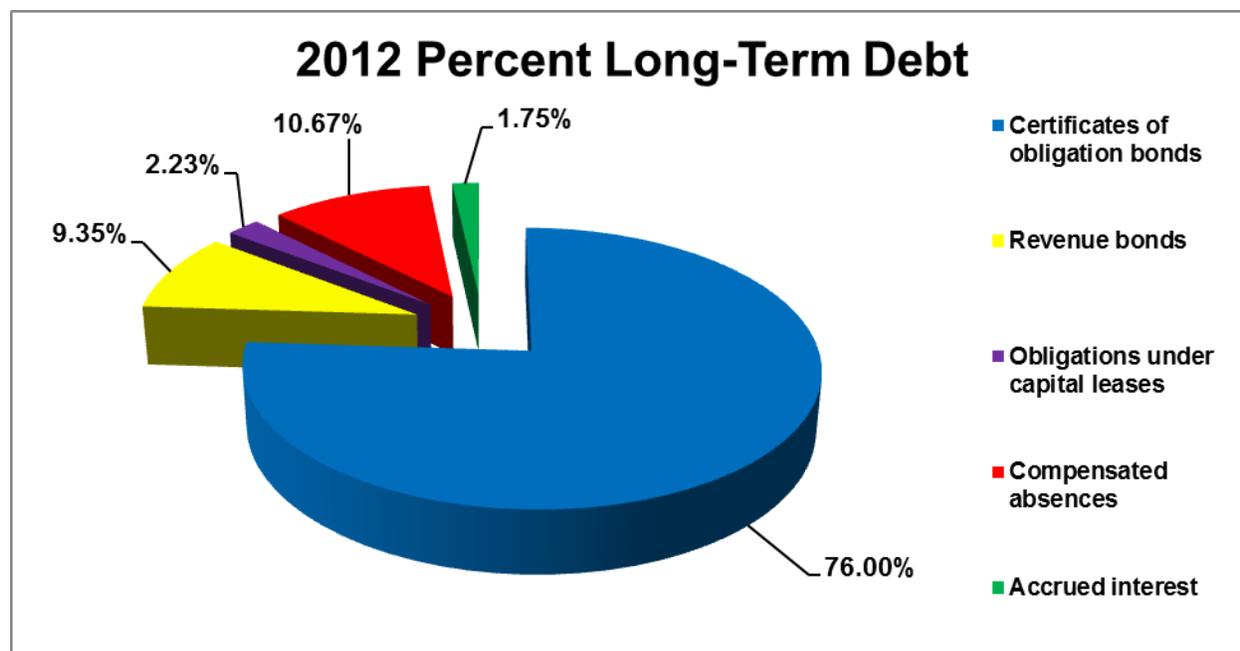
At the end of the current fiscal year, the City of Freeport had a total bonded debt and certificates of obligation payable of \$ 5,419,000. Of this amount, \$ 4,956,000 is comprised of bonded debt backed by the full faith and credit of the City. These bonds will be retired with revenues from property and sales taxes. The remaining \$ 463,000 represents bonds secured solely by water and sewer revenues.

Long-Term Debt Outstanding

	Governmental Activities		Business-type Activities		Totals	
	September 30,		September 30,		September 30,	
	2013	2012	2013	2012	2013	2012
Certificates of obligation bonds	\$ 4,956,000	\$ 5,511,000	\$	\$	\$ 4,956,000	\$ 5,511,000
Revenue bonds			463,000	678,000	463,000	678,000
Obligation under capital leases	381,967	103,226	218,178	58,334	600,145	161,560
Compensated absences	697,876	694,603	73,324	79,333	771,200	773,936
Components of Long-Term Debt:						
Accrued interest	99,169	110,434	11,228	16,442	110,397	126,876
Total	\$ 6,135,012	\$ 6,419,263	\$ 765,730	\$ 832,109	\$ 6,900,742	\$ 7,251,372



CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2013



Additional information on the City of Freeport's long-term debt can be found in Note 14 on pages 71 through 74 of this report.

Economic Factors and Next Year's Budgets and Rates

Certified assessed valuations decreased 4.11% over the preceding year. The property tax rate decreased to 0.0675586, with .166882 as Interest & Sinking component and 0.508704 as the Maintenance & Operations component. From the Interest & Sinking component 0.04854 was used to pay the Certificates of Obligations, Series 2003 issued on October 23, 2003 and 0.05146 was used to pay the Certificates of Obligations, Series 2008 issued on March 3, 2008.

The price of water from the Brazosport Water Authority increased from \$ 1.85 to \$ 1.92 per thousand gallons and will become effective October 1, 2013.

Request for Information

This financial report is designed to provide a general overview of 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 Office of Finance, 200 West Second Street, Freeport, Texas, 77541, or call (979) 233-3526.

BASIC FINANCIAL STATEMENTS

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF NET POSITION

September 30, 2013

	Primary Government			Freeport Economic Development Corporation
	Governmental Activities	Business- Type Activities	Total	
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES				
Assets:				
Cash and cash equivalents	\$ 4,074,708	\$ 5,963	\$ 4,080,671	\$ 387,261
Receivables (Net of Allowance for Uncollectible):				
Taxes	309,579		309,579	
Accounts	353,085	989,595	1,342,680	
Other	46,324		46,324	
Due from other governments	324,447		324,447	132,675
Interfund balances	801,178	(801,178)	-0-	
Inventory		10,249	10,249	
Restricted Assets:				
Temporarily Restricted:				
Cash and cash equivalents		227,744	227,744	
Noncurrent Notes Receivable:				
Due in more than one year	8,083,539		8,083,539	
Capital Assets (Net of Accumulated Depreciation):				
Land	3,048,548	395,630	3,444,178	474,700
Improvements	7,770,513	104,210	7,874,723	1,181,862
Buildings	1,876,839	105,389	1,982,228	3,556,062
Utility plant		6,127,209	6,127,209	
Other				1,179,372
Furniture, equipment and vehicles	1,802,443	283,429	2,085,872	38,173
Assets under capital lease	365,190	253,976	619,166	
Construction in progress	851,648	285,053	1,136,701	
Total assets	<u>29,708,041</u>	<u>7,987,269</u>	<u>37,695,310</u>	<u>6,950,105</u>
Deferred Outflows of Resources:				
Total deferred outflows of resources			-0-	
Total assets and deferred outflows of resources	<u>\$ 29,708,041</u>	<u>\$ 7,987,269</u>	<u>\$ 37,695,310</u>	<u>\$ 6,950,105</u>

(continued)

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF NET POSITION - Continued

September 30, 2013

	Primary Government			
	Governmental Activities	Business- Type Activities	Total	Freeport Economic Development Corporation
LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION				
Liabilities:				
Accounts payable	\$ 652,813	\$ 547,788	\$ 1,200,601	\$ 10,945
Accrued wages and benefits	97,093	16,591	113,684	
Liabilities payable from restricted assets		200,339	200,339	
Unearned revenue	40,067	200	40,267	
Noncurrent Liabilities:				
Due within one year	1,220,911	385,567	1,606,478	65,320
Due in more than one year	<u>4,914,101</u>	<u>380,163</u>	<u>5,294,264</u>	<u>9,471,129</u>
Total liabilities	<u>6,924,985</u>	<u>1,530,648</u>	<u>8,455,633</u>	<u>9,547,394</u>
Deferred Inflows of Resources:				
Total deferred inflows of resources			<u>-0-</u>	
Net Position:				
Invested in capital assets, net of related debt	10,377,214	6,873,718	17,250,932	(3,106,280)
Restricted For:				
Notes receivable	8,083,539		8,083,539	
Tourism	25,504		25,504	
Debt service	15,753	16,177	31,930	
Capital projects	54,029		54,029	
Municipal court security	21,260		21,260	
Municipal court technology	2,342		2,342	
Unrestricted	<u>4,203,415</u>	<u>(433,274)</u>	<u>3,770,141</u>	<u>508,991</u>
Total net position	<u>22,783,056</u>	<u>6,456,621</u>	<u>29,239,677</u>	<u>(2,597,289)</u>
Total liabilities, deferred inflows of resources and net position	<u>\$ 29,708,041</u>	<u>\$ 7,987,269</u>	<u>\$ 37,695,310</u>	<u>\$ 6,950,105</u>

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

CITY OF FREEPORT
Freeport, Texas
STATEMENT OF ACTIVITIES

September 30, 2013

Functions/Programs	Expenses	Program Revenues		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary Government:				
Governmental Activities:				
Administration	\$ 2,059,996	\$ 7,792	\$ 27,543	\$
Public safety	4,592,872	420,019	577,986	
Streets and drainage	1,341,802	439,903		
Sanitation	760,582	828,569		
Service center	150,225			
Marina	422,178	318,270		
Library	57,964			
Parks and recreation	1,578,706	391,345	42,678	
Interest on long-term debt	234,956		205,192	
Total governmental activities	11,199,281	2,405,898	853,399	-0-
Business-type Activities:				
Water and sewer	4,030,789	3,550,402		285,053
Golf course	767,541	524,578		
Ambulance	681,781	542,224	86,910	
Total business-type activities	5,480,111	4,617,204	86,910	285,053
Component Unit - Freeport Economic Development Corporation:				
Economic Development:				
Marina	273,713			
Beautifications projects	58,363	1,100		
City of Freeport debt services Series 2003A	205,192			
Interest on long-term debt	90,420			
Total component unit	627,688	1,100	-0-	-0-
Total	\$ 17,307,080	\$ 7,024,202	\$ 940,309	\$ 285,053
General Revenue:				
Taxes:				
Property taxes				
Other taxes				
Industrial district				
Investment earnings				
Miscellaneous				
Transfers				
Total general revenues and transfers				
Change in net position				
Net position – beginning (restated)				
Net position – ending				

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

Net (Expense) Revenue and Changes in Net Position			Freeport Economic Development Corporation
Governmental Activities	Business- Type Activities	Total	
\$(2,024,661)	\$	\$(2,024,661)	\$
(3,594,867)		(3,594,867)	
(901,899)		(901,899)	
67,987		67,987	
(150,225)		(150,225)	
(103,908)		(103,908)	
(57,964)		(57,964)	
(1,144,683)		(1,144,683)	
(29,764)		(29,764)	
(7,939,984)	-0-	(7,939,984)	-0-
	(195,334)	(195,334)	
	(242,963)	(242,963)	
	(52,647)	(52,647)	
-0-	(490,944)	(490,944)	-0-
		-0-	(273,713)
		-0-	(57,263)
		-0-	(205,192)
		-0-	(90,420)
-0-	-0-	-0-	(626,588)
(7,939,984)	(490,944)	(8,430,928)	(626,588)
2,428,164		2,428,164	
2,120,609		2,120,609	719,028
4,884,316		4,884,316	
3,972	79	4,051	306
82,447		82,447	
(503,389)	503,389	-0-	
9,016,119	503,468	9,519,587	719,334
1,076,135	12,524	1,088,659	92,746
21,706,921	6,444,097	28,151,018	(2,690,035)
\$ 22,783,056	\$ 6,456,621	\$ 29,239,677	\$(2,597,289)

CITY OF FREEPORT

Freeport, Texas

**BALANCE SHEET
GOVERNMENTAL FUNDS**

September 30, 2013

	<u>General Fund</u>	<u>Marina Operations Fund</u>	<u>Non-Major Governmental Funds</u>	<u>Total Governmental Funds</u>
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES				
<u>Assets</u>				
Cash and temporary investments	\$ 3,980,392	\$	\$ 94,316	\$ 4,074,708
Receivables (Net of Allowance for Uncollectible):				
Property taxes	242,198		67,381	309,579
Sales tax	265,352			265,352
Accounts	128,425		4,205	132,630
Other receivables	46,324			46,324
Due from other governments	35,402		23,693	59,095
Due from other funds	1,111,614		64,035	1,175,649
Noncurrent Receivables:				
Notes receivable	<u>6,639,208</u>			<u>6,639,208</u>
 Total assets	<u>12,448,915</u>	<u>-0-</u>	<u>253,630</u>	<u>12,702,545</u>
 Deferred Outflows of Resources:				
Deferred outflows of resources				<u>-0-</u>
 Total deferred outflows of resources	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>
 Total assets and deferred outflows of resources	<u>\$ 12,448,915</u>	<u>\$ -0-</u>	<u>\$ 253,630</u>	<u>\$ 12,702,545</u>

CITY OF FREEPORT

Freeport, Texas

**BALANCE SHEET
GOVERNMENTAL FUNDS - Continued**

September 30, 2013

	General Fund	Marina Operations Fund	Non-Major Governmental Funds	Total Governmental Funds
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
LIABILITIES, DEFERRED INFLOWS OF RESOURCES				
<u>Liabilities and Fund Balances</u>				
Liabilities:				
Accounts payable	\$ 483,871	\$ 3,884	\$ 165,058	\$ 652,813
Accrued wages and benefits	95,082	2,011		97,093
Due to other funds	64,035	273,017	37,419	374,471
Unearned revenue	<u>40,067</u>			<u>40,067</u>
Total liabilities	<u>683,055</u>	<u>278,912</u>	<u>202,477</u>	<u>1,164,444</u>
Deferred Inflows of Resources:				
Deferred inflows of resources	<u>228,003</u>		<u>63,052</u>	<u>291,055</u>
Total deferred inflows of resources	<u>228,003</u>	<u>-0-</u>	<u>63,052</u>	<u>291,055</u>
Fund Balance:				
Non-Spendable:				
Notes receivable	6,639,208			6,639,208
Restricted:				
Tourism			25,504	25,504
Debt service			51,870	51,870
Construction			54,029	54,029
Municipal court security	21,260			21,260
Municipal court technology	2,342			2,342
Assigned:				
Beach maintenance			6,617	6,617
Narcotics operations	63,517			63,517
Main street	2,795			2,795
Unassigned	<u>4,808,735</u>	<u>(278,912)</u>	<u>(149,919)</u>	<u>4,379,904</u>
Total fund balances	<u>11,537,857</u>	<u>(278,912)</u>	<u>(11,899)</u>	<u>11,247,046</u>
Total liabilities, deferred inflows of resources and fund balances	<u>\$ 12,448,915</u>	<u>\$ -0-</u>	<u>\$ 253,630</u>	<u>\$ 12,702,545</u>

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

CITY OF FREEPORT

Freeport, Texas

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE GOVERNMENTAL ACTIVITIES STATEMENT OF NET POSITION

September 30, 2013

Total fund balances – governmental funds balance sheet	\$ 11,247,046
Amounts reported for governmental activities in the statement of net position are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. Net Capital assets include \$ 35,185,835 in capital assets less \$ 19,470,654 in accumulated depreciation.	15,715,181
Municipal Court accounts receivables net of related allowance for uncollectible are unavailable to pay for current period expenditures and funds that are uncertain as to availability are not recorded in the funds. Municipal Court receivables \$ 1,102,276 net of allowance for uncollectible accounts \$ 881,821 of the general fund amounted to \$ 220,455.	220,455
Property taxes receivable unavailable to pay for current period expenditures are deferred in the funds. Deferred inflows of resources - property tax revenues for the general fund and debt service funds amounted to \$ 228,003 and \$ 63,052, respectively.	291,055
Receivables for loan interest are not reported in the funds.	1,444,331
Payables for bond principal are not reported in the funds.	(4,956,000)
Payables for capital lease principal are not reported in the funds.	(381,967)
Payables for long-term compensated absences are not reported in the funds.	(697,876)
Payables for bond interest are not reported in the funds.	(<u>99,169</u>)
Net position of governmental activities – statement of net position.	\$ <u><u>22,783,056</u></u>

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

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CITY OF FREEPORT

Freeport, Texas

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS

For the Year Ended September 30, 2013

	General Fund	Marina Operations Fund	Non-Major Governmental Funds	Total Governmental Funds
Revenues:				
Taxes	\$ 1,812,612	\$	\$ 565,152	\$ 2,377,764
Other taxes	2,105,793		14,816	2,120,609
Industrial district	4,884,316			4,884,316
Intergovernmental revenues	605,531		439,903	1,045,434
Revenue producing facilities	1,133,949	318,270	6,617	1,458,836
Fines, licenses and fees	455,960			455,960
Investment income	3,829		143	3,972
Miscellaneous	<u>215,789</u>	<u></u>	<u>205,192</u>	<u>420,981</u>
Total revenues	<u>11,217,779</u>	<u>318,270</u>	<u>1,231,823</u>	<u>12,767,872</u>
Expenditures:				
Current:				
Administration	1,707,096		11,250	1,718,346
Public safety	4,301,234			4,301,234
Streets and drainage	911,440			911,440
Sanitation	760,582			760,582
Service center	133,973			133,973
Marina		399,781		399,781
Library	38,365			38,365
Parks and recreation	1,413,885			1,413,885
Capital outlay	929,000	391,275	672,754	1,993,029
Debt Service:				
Principal	52,323	60,211	555,000	667,534
Interest	<u>3,104</u>	<u>11,662</u>	<u>231,455</u>	<u>246,221</u>
Total expenditures	<u>10,251,002</u>	<u>862,929</u>	<u>1,470,459</u>	<u>12,584,390</u>
Excess of revenues over (under) expenditures	<u>966,777</u>	<u>(544,659)</u>	<u>(238,636)</u>	<u>183,482</u>
Other Financing Sources (Uses):				
Issuance of capital lease		391,275		391,275
Operating transfers out	<u>(503,389)</u>	<u></u>	<u></u>	<u>(503,389)</u>
Total other financing sources (uses)	<u>(503,389)</u>	<u>391,275</u>	<u>-0-</u>	<u>(112,114)</u>
Net changes in fund balance	463,388	(153,384)	(238,636)	71,368
Fund balance – beginning	<u>11,074,469</u>	<u>(125,528)</u>	<u>226,737</u>	<u>11,175,678</u>
Fund balance - ending	<u>\$ 11,537,857</u>	<u>\$ (278,912)</u>	<u>\$ (11,899)</u>	<u>\$ 11,247,046</u>

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

CITY OF FREEPORT

Freeport, Texas

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

For the Year Ended September 30, 2013

Net change in fund balances – total governmental funds	\$ 71,368
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the governmental activities statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlay of \$ 1,993,029 exceeded depreciation of \$ 1,283,446 in the current period.	709,583
Municipal court revenues in the governmental activities statement of activities do not provide current financial resources and are not reported as revenues in the funds. Municipal court receivables, net of allowance, decreased by \$ 39,467.	(39,467)
Property tax revenues in the governmental activities statement of activities do not provide current financial resources and are not reported as revenues in the funds. Deferred inflows of resources – property tax revenues, for the general fund increased by \$ 35,255, and for the debt service increased by \$ 15,145.	50,400
Repayment of long-term debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the governmental activities statement of net position. These amounts were for general obligation bonded debt for \$ 555,000 and capital leases for \$ 112,534.	667,534
Long-term debt proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the governmental activities statement of net position. Long-term proceeds in the governmental fund were \$ 391,275 from capital leases.	(391,275)
Some expenses reported in the governmental activities statement of activities do not require the use of current financial resources, and, therefore, are not reported as expenditures in governmental funds. This is the change in accrued interest on long-term debt of \$ 11,265, and accrued compensated absences of \$ 3,273.	<u>7,992</u>
Change in net position of governmental activities	<u>\$ 1,076,135</u>

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

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF NET POSITION - PROPRIETARY FUNDS

September 30, 2013

	<u>Water and Sewer</u>	<u>Golf Course</u>	<u>Ambulance</u>	<u>Total Proprietary Funds</u>
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES				
Assets:				
Current Assets:				
Cash and temporary investments	\$ 180	\$ 5,783	\$	\$ 5,963
Receivables (Net of Allowance for Uncollectible):				
Accounts	524,553		465,042	989,595
Inventory	<u> </u>	<u>10,249</u>	<u> </u>	<u>10,249</u>
Total unrestricted current assets	<u>524,733</u>	<u>16,032</u>	<u>465,042</u>	<u>1,005,807</u>
Current Restricted Assets:				
Cash and temporary investments	<u>227,744</u>	<u> </u>	<u> </u>	<u>227,744</u>
Total current restricted assets	<u>227,744</u>	<u>-0-</u>	<u>-0-</u>	<u>227,744</u>
Total current assets	<u>752,477</u>	<u>16,032</u>	<u>465,042</u>	<u>1,233,551</u>
Capital Assets:				
Land	56,200	339,430		395,630
Buildings		211,468		211,468
Improvements		553,118		553,118
Utility plant	20,706,932			20,706,932
Furniture, equipment and vehicles	146,765	563,353	529,692	1,239,810
Assets under capital lease		307,416		307,416
Construction in progress	285,053			285,053
Less accumulated depreciation	<u>(14,707,889)</u>	<u>(1,137,657)</u>	<u>(298,985)</u>	<u>(16,144,531)</u>
Total capital assets (net of accumulated depreciation)	<u>6,487,061</u>	<u>837,128</u>	<u>230,707</u>	<u>7,554,896</u>
Total assets	<u>7,239,538</u>	<u>853,160</u>	<u>695,749</u>	<u>8,788,447</u>
Deferred Outflows of Resources:				
Deferred outflows of resources	<u> </u>	<u> </u>	<u> </u>	<u>-0-</u>
Total deferred outflows of resources	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>
Total assets and deferred outflows of resources	<u>\$ 7,239,538</u>	<u>\$ 853,160</u>	<u>\$ 695,749</u>	<u>\$ 8,788,447</u>

(Continued)

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF NET POSITION - PROPRIETARY FUNDS - Continued

September 30, 2013

	Water and Sewer	Golf Course	Ambulance	Total Proprietary Funds
LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION				
Liabilities:				
Current Liabilities:				
Accounts payable	\$ 507,412	\$ 19,818	\$ 20,558	\$ 547,788
Accrued wages and benefits	1,551	6,638	8,402	16,591
Accrued compensated absences	12,752	26,403	12,925	52,080
Due to other funds	566,199	146,962	88,017	801,178
Obligations under capital lease - current		94,259		94,259
Unearned revenue	200			200
	<u>1,088,114</u>	<u>294,080</u>	<u>129,902</u>	<u>1,512,096</u>
Total current liabilities				
Current Liabilities Payable from Restricted Assets:				
Accrued interest payable	11,228			11,228
Customer deposits payable	200,339			200,339
Revenue bonds payable	228,000			228,000
	<u>439,567</u>	<u>-0-</u>	<u>-0-</u>	<u>439,567</u>
Total current liabilities payable from restricted assets				
	<u>1,527,681</u>	<u>294,080</u>	<u>129,902</u>	<u>1,951,663</u>
Total current liabilities				
Noncurrent Liabilities:				
Accrued compensated absences	5,201	10,770	5,273	21,244
Obligations under capital lease – net of current		123,919		123,919
Revenue bonds payable	235,000			235,000
	<u>240,201</u>	<u>134,689</u>	<u>5,273</u>	<u>380,163</u>
Total noncurrent liabilities				
	<u>1,767,882</u>	<u>428,769</u>	<u>135,175</u>	<u>2,331,826</u>
Total liabilities				
Deferred Inflows of Resources:				
Deferred inflows of resources				-0-
	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>
Total deferred inflows of resources				
Net Position:				
Invested in capital assets, net of related debt	6,024,061	618,950	230,707	6,873,718
Reserved for revenue bond debt	16,177			16,177
Unreserved	(568,582)	(194,559)	329,867	(433,274)
	<u>5,471,656</u>	<u>424,391</u>	<u>560,574</u>	<u>6,456,621</u>
Total net position				
	<u>\$ 7,239,538</u>	<u>\$ 853,160</u>	<u>\$ 695,749</u>	<u>\$ 8,788,447</u>
Total liabilities, deferred inflows of resources and net position				

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

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION - PROPRIETARY FUNDS

For the Year Ended September 30, 2013

	Water and Sewer	Golf Course	Ambulance	Total Proprietary Funds
Operating Revenues:				
Water service	\$ 2,228,199	\$	\$	\$ 2,228,199
Sewer service	1,248,148			1,248,148
Charges for other services	61,912		542,224	604,136
Golf course fees and charges		524,578		524,578
Miscellaneous	12,143		86,910	99,053
Total operating revenues	3,550,402	524,578	629,134	4,704,114
Operating Expenses:				
Personnel services	62,790	295,302	378,830	736,922
Employee benefits	25,069	117,242	137,193	279,504
Contract and professional services	2,186,205			2,186,205
Other operating costs	68,308	78,884	67,625	214,817
Supplies	10,414	47,453	52,799	110,666
Cost of sales and services	1,349,656	133,910		1,483,566
Operating expenses before depreciation	3,702,442	672,791	636,447	5,011,680
Depreciation	304,975	87,690	45,334	437,999
Total operating expenses	4,007,417	760,481	681,781	5,449,679
Net operating income (loss)	(457,015)	(235,903)	(52,647)	(745,565)
Non-Operating Revenues (Expenses):				
Interest revenue	22	2	55	79
Interest expense and agent fees	(23,372)	(7,060)		(30,432)
Total non-operating revenues (expenses)	(23,350)	(7,058)	55	(30,353)
Net income (loss) before contributions and operating transfers	(480,365)	(242,961)	(52,592)	(775,918)
Contributions (capital)	285,053			285,053
Transfers in	280,400	151,675	71,314	503,389
Change in net position	85,088	(91,286)	18,722	12,524
Net position - beginning	5,386,568	515,677	541,852	6,444,097
Net position - ending	\$ 5,471,656	\$ 424,391	\$ 560,574	\$ 6,456,621

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

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CITY OF FREEPORT

Freeport, Texas

STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS

For the Year Ended September 30, 2013

	Water and Sewer	Golf Course	Ambulance	Total Proprietary Funds
Cash Flows from Operating Activities:				
Receipts from customers and users	\$ 3,585,246	\$ 524,661	\$ 572,986	\$ 4,682,893
Receipts from other funds		47,738	88,017	135,755
Payments to other funds	(299,980)			(299,980)
Payments to suppliers	(3,346,196)	(256,020)	(115,351)	(3,717,567)
Payments to employees	(91,581)	(410,408)	(514,099)	(1,016,088)
Net cash provided (used) by operating activities	(152,511)	(94,029)	31,553	(214,987)
Cash Flows from Non-Capital Financing Activities:				
Transfers from other funds	280,400	151,675	71,314	503,389
Net cash provided by non-capital financing activities	280,400	151,675	71,314	503,389
Cash Flows from Capital and Related Financing Activities:				
Capital expenditures	(76,100)		(185,903)	(262,003)
Interest payments on capital leases		(6,604)		(6,604)
Principal payments on capital leases		(48,023)		(48,023)
Principal payments on bonds	(215,000)			(215,000)
Interest and fees on bonds	(28,586)			(28,586)
Net cash used by capital and related financing activities	(319,686)	(54,627)	(185,903)	(560,216)
Cash Flows from Investing Activities:				
Interest on investments	22	2	55	79
Net cash provided by investing activities	22	2	55	79
Net increase (decrease) in cash and cash equivalents	(191,775)	3,021	(82,981)	(271,735)
Cash and cash equivalents at the beginning of year	419,699	2,762	82,981	505,442
Cash and cash equivalents at the end of the year	\$ 227,924	\$ 5,783	\$ -0-	\$ 233,707

(Continued)

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF CASH FLOWS -
PROPRIETARY FUNDS - Continued

For the Year Ended September 30, 2013

	<u>Water and Sewer</u>	<u>Golf Course</u>	<u>Ambulance</u>	<u>Total Proprietary Funds</u>
Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities:				
Operating income (loss)	\$ (457,015)	\$ (235,903)	\$ (52,647)	\$ (745,565)
Adjustments to Reconcile Operating Income (Loss) to Net Cash				
Provided (Used) by Operating Activities:				
Depreciation	304,975	87,690	45,334	437,999
(Increase) decrease in accounts receivable	22,582	83	(56,148)	(33,483)
(Increase) decrease in inventory		1,454		1,454
Increase (decrease) in accounts payable	268,387	2,773	5,073	276,233
Increase (decrease) in accrued wages and benefits payable	404	2,438	3,505	6,347
Increase (decrease) in accrued compensated absences payable	(4,126)	(302)	(1,581)	(6,009)
Increase (decrease) in customer deposits	12,262			12,262
Increase (decrease) in due to other funds	(299,980)	47,738	88,017	(164,225)
Total adjustments	<u>304,504</u>	<u>141,874</u>	<u>84,200</u>	<u>530,578</u>
Net cash provided (used) by operating activities	\$ (<u>152,511</u>)	\$ (<u>94,029</u>)	\$ <u>31,553</u>	\$ (<u>214,987</u>)
Non-Cash Investing, Capital and Financing Activities:				
Contributions from other governments	\$ 285,053		\$	\$ 285,053
Assets acquired as a result of contributed assets	(285,053)			(285,053)
Capital lease liability		207,867		207,867
Assets acquired through capital lease		(207,867)		(207,867)
Net effect of non-cash transactions	\$ <u>-0-</u>	\$ <u>-0-</u>	\$ <u>-0-</u>	\$ <u>-0-</u>

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

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CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

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CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General Statement

The City of Freeport (City) operates under a Home Rule Charter adopted in a special election on June 20, 1960. The City operates under a Council-Manager form of government and provides the following services as authorized by its charter: public services, streets and drainage, sanitation, health and building inspections, culture-recreation, public improvements, planning and zoning, and general administrative services.

The City prepares its basic financial statements in conformity with generally accepted accounting principles promulgated by the Governmental Accounting Standards Board (GASB) and other authoritative sources. The City's Financial Statements are in accordance with GASB Statement No. 34, "Basic Financial Statements and Management Discussion and Analysis for State and Local Governments", GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus" which provides additional guidance for the implementation of GASB Statement No. 34, and GASB Statement No. 38 "Certain Financial Statement Disclosures" which changes the note disclosure requirements in the financial statements for governmental entities. GASB Statement No. 34 established a new financial reporting model for state and local governments that included the addition of management's discussion and analysis, government-wide financial statements, required supplementary information and the elimination of the effects of internal service activities and the use of account groups to the already required fund financial statements and notes. The GASB determined that fund accounting has and will continue to be essential in helping governments to achieve fiscal accountability and should, therefore, be retained. The GASB also determined that government-wide financial statements are needed to allow users of financial reports to assess a government's operational accountability. The GASB Statement No. 34 reporting model integrates fund-based financial reporting and government-wide financial reporting as complementary components of a single comprehensive financial reporting model.

The following is a summary of the most significant accounting policies.

Reporting Entity

Primary Government

The City is considered an independent entity for financial reporting purposes and is considered a primary government. As required by generally accepted accounting principles, these basic financial statements have been prepared, based on considerations regarding the potential for inclusion of other entities, organizations, or functions, as part of the City's financial reporting entity. Based on these considerations, the City's basic financial statements do not include any other entities. Additionally, as the City is considered a primary government for financial reporting purposes, its activities are not considered a part of any other governmental or other type of reporting entity.

Considerations regarding the potential for inclusion of other entities, organizations, or functions in the City's financial reporting entity are based on criteria prescribed by generally accepted accounting principles. These same criteria are evaluated in considering whether the City is part of any other governmental or other type of reporting entity. The overriding elements associated with prescribed criteria considered in determining that the City's financial reporting entity status is that of a primary government are: that it has a separately elected governing body; it is legally separate; and it is fiscally independent of other state and local governments.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Reporting Entity - Continued

Primary Government - Continued

Additionally prescribed criteria under generally accepted accounting principles include considerations pertaining to organizations for which the primary government is financially accountable; and considerations pertaining to other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

The members of City council (the "members") are elected by the public and have the authority to make decisions, appoint administrators and managers, and significantly influence operations. It also has the primary accountability for fiscal matters. Therefore, the City is a financial reporting entity as defined by the GASB in its GASB Statement No. 61, "The Financial Reporting Entity: Omnibus - an amendment of GASB Statements No. 14, and No. 34".

Component Unit

The City Council authorized the creation and approved the Articles of Incorporation and the Bylaws of the Freeport Economic Development Corporation (the Corporation). The Articles of Incorporation were filed with the Office of the Secretary of State of Texas on December 20, 1999. The Corporation, a nonprofit corporation, organized under Section 4B of the development Corporation Act of 1979 was created to act on behalf of the City in the promotion and financing of projects so as to promote the public welfare.

The Corporation is governed by a seven member board of directors appointed by the City Council. All projects must have prior approval of the City Council. The voters of Freeport approved collection of a one-half cent sales tax, effective November 2, 1999, to fund the cost of land, buildings, equipment, facilities, improvements and maintenance and operation costs for public park purposes, recreational facilities and infrastructure improvements for development of new or expanded business enterprises. In prior years, the Freeport Economic Development Corporation (the "Corporation") provided services entirely or, almost entirely, to the City or otherwise exclusively or almost exclusively benefited the City even though it did not provide services directly to it and was reported as a blended component unit. However, during the year ended September 30, 2007, the Corporation began construction and entered into a long-term lease for a marina with a company unrelated to the City. Because of this, the City is no longer able to report the Corporation as a blended component unit and has currently reported the Corporation as a discretely presented component unit.

The Financial Statements for the Freeport Economic Development Corporation can be obtained from the Office of the Finance Director, City of Freeport, Texas.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report financial information on all of the nonfiduciary activities of the primary government. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental 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 program 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 or applicants who purchase, use or directly benefit from goods, services, or privileges provided by a given program and 2) operating or capital grants and contributions that are restricted to meeting operational or capital requirements of a particular program. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements. The City has three enterprise funds.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Revenues from property and sales taxes, grants and contracts, charges for services, licenses and permits, fines and forfeitures, and interest associated with the current fiscal period are all considered to be susceptible to accrual. Miscellaneous revenues are recorded as revenue when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned, since they are both measurable and available.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

Revenue from investments, including governmental external investment pools, is based upon fair value. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Most investments are reported at amortized cost when the investments have remaining maturities of one year or less at time of purchase. External investment pools are permitted to report short-term debt investments at amortized cost, provided that the fair value of those investments is not significantly affected by the impairment of the credit standing of the issuer, or other factors. For that purpose, a pool's short-term investments are those with remaining maturities of up to ninety days.

Grant funds are considered earned to the extent of the expenditures made under the provisions of the grant. Accordingly, when such funds are received, they are recorded as deferred revenues until the related and authorized expenditures have been made. If balances have not been expended by the end of the project period, grantors sometimes require the City to refund all or part of the unused amount.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, and 2) operating and capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's enterprise fund are charges to customers for sales and services and rentals.

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

The City has presented the following major governmental fund:

The *General fund* is the City's primary operating fund. It accounts for all financial resources of the City, except those required to be accounted for in another fund. All general tax revenues and other receipts that are not restricted by law or contractual agreement to some other fund are accounted for in this fund. General operating expenditures, fixed charges and capital improvement costs that are not paid through other funds are paid from the general fund.

The *Marina Operations special revenue fund*) accounts for all financial transactions related to the operation of the marina, owned by the Freeport Economic Development Corporation. All rental and general revenues associated with the marina are utilized for the operation of the marina.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Measurement Focus, Basis Of Accounting, and Financial Statement Presentation - continued

The City reports the following major proprietary funds:

The Water and Sewer Enterprise Fund is used to account for the provision of water and sewer services to the residents of the City. Activities of the fund include administration, operations and maintenance of the water and sewer system and billing and collection activities. All costs are financed through charges to utility customers with rates reviewed regularly and adjusted if necessary to ensure integrity of the fund.

The Golf Course Enterprise Fund is used to account for the operation of the golf course to fulfill the recreational needs of the citizens and others. Activities of the fund include administration, operations and maintenance of the golf course activities. All costs are financed through charges to customers with rates reviewed regularly and adjusted if necessary to ensure integrity of the fund.

The Ambulance Enterprise Fund is used to account for the operation of the EMS ambulance service to fulfill the emergency medical needs of the citizens and others. Activities of the fund include administration, operations and maintenance of the EMS and ambulances activities. All costs are financed through charges to customers with rates adjusted in accordance with insurance and regulatory agencies.

New Pronouncements

GASB issues statements on a routine basis with the intent to provide authoritative guidance on the preparation of financial statements and to improve governmental accounting and financial reporting of governmental entities. Management reviews these statements to ensure that preparation of its financial statements are in conformity with generally accepted accounting principles and to anticipate changes in those requirements. The following recent GASB Statements reflect the action and consideration of management regarding these requirements:

GASB No. 61, "The Financial Reporting Entity: Omnibus - an amendment of GASB Statements No. 14 and No. 34", was issued November 2010. The statement was implemented and did not have an impact on the City's financial statements. This statement is effective for periods beginning after June 15, 2012.

GASB No. 62, "Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements", was issued December 2010. The statement was implemented and did not have an impact on the City's financial statements. This statement is effective for periods beginning after December 15, 2011.

GASB No. 63, "Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position", was issued June 2011. The statement was implemented and did not have an impact on the City's financial statements, although it has reclassified certain items previously recorded as assets and liabilities within the City's financial statements as outflow and inflows of resources. This statement is effective for periods beginning after December 15, 2011.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

GASB No. 64, "Derivative Instruments: Application of Hedge Accounting Termination Provisions - an amendment of GASB Statements No. 53", was issued June 2011. The statement was implemented and did not have an impact on the City's financial statements.

GASB No. 65, "Items Previously Reported as Assets and Liabilities", was issued March 2012. The statement was implemented and did have an impact on the City's financial statements (See Note 2 Change in Accounting Principle). This statement is effective for periods beginning after December 15, 2012.

GASB No. 66, "Technical Corrections - 2012 - an amendment of GASB Statements No. 10 and No. 62", was issued March 2012. The statement was implemented and did not have an impact on the City's financial statements. This statement is effective for periods beginning after December 15, 2012.

GASB Statement No. 67, "Financial Reporting for Pension Plans – an amendment of GASB Statement No. 25", was issued June 2012. The management of the City does not believe that the implementation of this statement will have a material effect on the financial statements of the City. This statement is effective for periods beginning after June 15, 2013.

GASB Statement No. 68, "Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27", was issued June 2012. The management of the City does believe that the implementation of this statement will have a material effect on the financial statements of the City. This statement is effective for periods beginning after June 15, 2014.

GASB Statement No. 69, "Government Combinations and Disposals of Government Operations", was issued January 2013. The management of the City does not believe that the implementation of this statement will have a material effect on the financial statements of the City. This statement is effective for periods beginning after December 15, 2013.

GASB Statement No. 70, "Accounting and Financial Reporting for Nonexchange Financial Guarantees", was issued April 2013. The management of the City does not believe that the implementation of this statement will have a material effect on the financial statements of the City. This statement is effective for periods beginning after June 15, 2013.

Budgetary Data

Financial statements in this report are based on legally enacted basis (modified accrual basis with certain exceptions) and the generally accepted accounting principles (GAAP) basis. The financial statements prepared on the legally enacted basis differ from the GAAP basis statements on an individual fund basis as follows:

Enterprise Funds:

- Depreciation is not recorded as expense (Non-GAAP).
- Capital outlays are recorded as current year expense (Non-GAAP) as opposed to being capitalized and depreciated over the estimated useful life of the asset (GAAP).
- Amortization of bond issuance cost is not recorded as expense (Non-GAAP).
- Debt principal is recorded as an expense (Non-GAAP).
- Capital contributions

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Budgetary Data - Continued

The following schedule reconciles the difference between the City's legally enacted basis and the GAAP basis:

	<u>Budgeted Enterprise Funds</u>			
	<u>Water & Sewer</u>	<u>Golf Course</u>	<u>Ambulance</u>	<u>Total</u>
Net income (loss) - GAAP basis	\$ 85,088	\$(91,286)	\$ 18,722	\$ 12,524
Differences:				
Depreciation	304,975	87,690	45,334	437,999
Capital contributions	(285,053)			(285,053)
Capital outlay	(76,100)		(185,903)	(262,003)
Debt principal	(215,000)	(48,023)		(263,023)
Net income (loss) - budget basis	\$(186,090)	\$(51,619)	\$(121,847)	\$(359,556)

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

1. Between sixty (60) and ninety (90) days prior to the beginning of the next fiscal year (October 1), the City Manager submits to council a proposed budget, which includes a complete financial plan for the fiscal year.
2. In September, a public hearing for the proposed budget is held. After the conclusion of the hearing, a vote is taken for adoption of the budget.
3. An ordinance is passed by Council to legally enact the budget.
4. Expenditures may not legally exceed appropriations at the fund level.

Encumbrances

Encumbrances represent commitments related to unperformed contracts for goods or services. Encumbrance accounting - under which purchase orders, contracts and other commitments for the expenditure of resources are recorded to reserve that portion of the applicable appropriation - is utilized in the governmental funds. Encumbrances outstanding at year end do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year. No encumbrances were outstanding at September 30, 2013.

Cash and Investments

Cash and temporary investments include amounts in demand deposits and short-term investments with a maturity date within three months of the date acquired by the City. For purposes of the cash flow statement, cash and temporary investments are considered cash equivalents. In accordance with GASB Statement 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools", investments are stated at fair value. State statutes authorize the government to invest in obligations of the U. S. Treasury, commercial paper, corporate bonds and repurchase agreements, and other such securities or obligations as allowed in the Public Funds Investment Act (PFIA) as amended and approved by the City's Council. The City's management believes it complied with the requirements of the PFIA and the City's investment policies, except for obtaining investment officer training.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Property Taxes

The City levies taxes on or about October 1, of each year. Property taxes attach as an enforceable lien on property as of January 1. These taxes are due by January 31, and are considered delinquent after that date, at which time interest is charged at a rate established by the state property tax code. Collections made on or after July 1, are subject to an additional fifteen percent collection fee.

Property tax revenue is recognized when levied to the extent that they are available. Available includes those property tax receivables expected to be collected within sixty days after year end.

The City is permitted by the State Property Tax Board to levy taxes up to \$ 1.50 per \$ 100 of assessed valuation for general governmental services other than the payment of principal and interest on long-term debt and unlimited amounts for the payment of principal and interest on long-term debt. The tax rates assessed for the year ended September 30, 2013, to finance general fund operations and the payment of principal and interest on general obligation long-term debt were \$ 0.533310 and \$ 0.166690 per \$ 100 valuation, respectively, for a total of \$ 0.700000 per \$ 100 valuation.

Interfund Receivables, Payables and Transfers

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All outstanding balances between funds are reported as "due to/from other funds". The City had no advances between funds. See Note 5 for additional discussion of interfund receivables, payables and transfers.

Capital Assets

Capital assets, which include property, plant, and equipment, are reported in the applicable governmental or business-type activities columns in the government-wide financial statements and in the fund financial statements for proprietary funds. All capital assets are valued at historical cost or estimated historical cost if actual historical is not available. Donated assets are valued at their fair market value on the date donated. Repairs and maintenance are recorded as expenses. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital Assets capitalized have an original cost of \$ 5,000 or more and over three years of useful life. Depreciation has been calculated on each class of depreciable property using the straight-line method. Estimated useful lives are as follows:

Buildings	10-20 Years
Utility Plant	40 Years
Equipment	5-15 Years
Vehicles	5 Years

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Compensated Absences

Eligible City employees accrue vacation time monthly at various rates based on length of service with the City. Employees may elect to carry over a maximum of five (5) days past his/her yearly anniversary date. It is possible for employees to have accrued vacation time at September 30, which has not yet been lost. The City's sick leave policy provides fifteen paid sick days per year for full-time employees. Unused sick leave can be accumulated to a maximum of ninety (90) days. Upon termination, an employee with five years of service or more may be paid for accumulated sick leave to a maximum of two weeks.

The following is a summary of benefits payable as of September 30, 2013:

	<u>2013</u>
Governmental activities	\$ 697,876
Business-type activities	<u>73,324</u>
	<u>\$ 771,200</u>

Pension Plans

It is the policy of the City to fund pension costs annually. Pension costs are composed of normal cost and, where applicable, amortization of unfunded actuarial accrued liability and of unfunded prior service costs. In the fiscal year ended September 30, 1998, the City implemented GASB Statement No. 27 for the Texas Municipal Retirement System (TMRS). At the date of transition and implementation of GASB Statement 27, there was no pension liability or pension asset. Further, in the fiscal year ended September 30, 2008, the City implemented GASB Statement No. 50, *Pension Disclosures* (an amendment of GASB Statements No. 25 and No. 27 (see Note 9)).

Long-Term Debt

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 or proprietary fund type statement of net position. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Fund Equity

The City's council meets on a regular basis to manage and review cash financial activities and to ensure compliance with established policies. The City's Unassigned General Fund Balance is maintained to provide the City with sufficient working capital and a margin of safety to address local and regional emergencies without borrowing. The unassigned General Fund Balance may only be appropriated by resolution of the council. Fund Balance of the City may be committed for a specific source by formal action of the council. Amendments or modifications of the committed fund balance must also be approved by formal action by the council. When it is appropriate for fund balance to be assigned, the City council has delegated authority to the City Manager or the Finance Director. In circumstances where an expenditure is to be made for a purpose for which amounts are available in multiple fund balance classifications, the order in which resources will be expended is as follows: restricted fund balance, followed by committed fund balance, followed by assigned fund balance, and lastly, unassigned fund balance.

The City has implemented GASB 54, "Fund Balance, Reporting and Governmental Fund Type Definitions", for its governmental funds. Under GASB 54, fund balances are required to be reported according to the following classifications:

Non-spendable Fund Balance - Includes amounts that cannot be spent because they are either not in spendable form, or, for legal or contractual reasons, must be kept intact. This classification includes inventories, prepaid amounts, assets held for sale, and long-term receivables.

Restricted Fund Balance - Constraints placed on the use of these resources are either externally imposed by creditors (such as through debt covenants), grantors, contributors or other governments; or are imposed by law (through constitutional provisions enabling legislation).

Committed Fund Balance - Amounts that can only be used for specific purposes because of a formal action (resolution or ordinance) by the government's highest level of decision-making authority.

Assigned Fund Balance - Amounts that are constrained by the City's intent to be used for specific purposes, but that do not meet the criteria to be classified as restricted or committed. Intent can be stipulated by the governing body, another body (such as a Finance Committee), or by an official to whom that authority has been given. With the exception of the General Fund, this is the residual fund balance classification for all government funds with positive balances.

Unassigned Fund Balance - This is the residual classification of the General Fund. Only the General Fund reports a positive unassigned fund balance. Other governmental funds might report a negative balance in this classification, as the result of overspending for specific purposes for which amounts had been restricted, committed, or assigned.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Net Position

Net assets represent the differences between assets and deferred outflows, and liabilities and deferred inflows of resources. Net position invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciations, reduced by the outstanding balances of any borrowing used for the acquisition, construction or improvements of those assets, and adding back unspent proceeds. Restricted net position, as presented in the government-wide Statement of Net Position, are reported when constraints placed on the use of net position are either 1) externally imposed by creditors (such as through debt covenants, grantors, contributors, or laws or regulations of other governments), or 2) imposed by law through constitutional provisions or enabling legislation.

NOTE 2 - CHANGE IN ACCOUNTING PRINCIPLE/PRIOR PERIOD ADJUSTMENT

During the year ended September 30, 2013, the City implemented GASB 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. As a result, bond issuance costs are no longer accounted for as an asset to be amortized over future periods. Accounting changes adopted to conform to the provisions of this Statement have been applied retroactively as required by restating financial statements, for all periods presented.

Additionally, during the year ended September 30, 2013, the City identified \$ 93,792 of expenditures that were not reported as capital assets during the year ended September 30, 2012. To correct the beginning construction in progress at October 1, 2012, the City recorded a prior period adjustment that increased capital assets and decreased non-capital expenses for the year ended September 30, 2012.

The following represents the retroactive restatement of net position and changes in net position as a result of implementation of GASB Statement No. 65 and correction of an error in construction in progress as noted above:

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Water & Sewer Enterprise</u>
Net position, September 30, 2012 previously reported	\$ 21,683,241	\$ 6,474,473	\$ 5,416,944
Prior Period Adjustments:			
Elimination of net bond issuance costs	(70,112)	(30,376)	(30,376)
Increase in construction in progress	<u>93,792</u>	<u> </u>	<u> </u>
Net position, September 30, 2012 restated	<u>\$ 21,706,921</u>	<u>\$ 6,444,097</u>	<u>\$ 5,386,568</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 2 - CHANGE IN ACCOUNTING PRINCIPLE/PRIOR PERIOD ADJUSTMENT – Continued

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Water & Sewer Enterprise</u>
Change in net position for the year ended September 30, 2012, previously reported	\$ 128,753	\$(56,307)	\$(164,965)
Prior Period Adjustments:			
Decrease in bond issuance cost expense	7,356	15,188	15,188
Decrease in non-capital expenses	<u>93,792</u>		
Change in net position for the year ended September 30, 2012, restated	229,901	(41,119)	(149,777)
Net position, September 30, 2011, restated	<u>21,477,020</u>	<u>6,485,216</u>	<u>5,536,345</u>
Net position, September 30, 2012, restated	\$ <u>21,706,921</u>	\$ <u>6,444,097</u>	\$ <u>5,386,568</u>

NOTE 3 - DEPOSITS, INVESTMENTS AND DERIVATIVES

The City classifies deposits and investments for financial statement purposes as cash and temporary investments, and investments based upon both liquidity (demand deposits) and maturity date (deposits and investments) of the asset at the date of purchase. For this purpose a temporary investment is one that when purchased had a maturity date of three months or less. Cash and temporary investments, as reported on the combined balance sheet at September 30, 2013 are as follows:

	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>
Cash and Temporary Investments:			
Cash (petty cash accounts)	\$ 1,482	\$	\$ 1,482
Financial Institution Deposits:			
Demand deposits	98,156	227,744	325,900
State Treasury Investment Pool:			
Texpool	<u>3,981,033</u>		<u>3,981,033</u>
Total cash and temporary investments	\$ <u>4,080,671</u>	\$ <u>227,744</u>	\$ <u>4,308,415</u>

Deposits

All deposits with financial institutions must be collateralized in an amount equal to 100 percent of uninsured balances. At September 30, 2013, in addition to petty cash of \$ 1,482, the carrying amount of the City's deposits were \$ 325,900. The financial institutions balances were \$ 863,712 at September 30, 2013. Bank balances of \$ 250,000 were covered by federal depository insurance and \$ 613,712 was covered by collateral pledged in the City's name.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 3 - DEPOSITS, INVESTMENTS AND DERIVATIVES - Continued

Deposits - continued

Custodial Credit Risk – Deposits. Custodial credit risk is the risk that in the event of a financial institution failure, the City's deposits may not be returned to them. The City requires that all deposits with financial institutions be collateralized in an amount equal to 100 percent of uninsured balances.

Under Texas state law, a bank serving as the City depository must have a bond or in lieu thereof, deposited or pledged securities with the City or an independent third party agent, an amount equal to the highest daily balance of all deposits the City may have during the term of the depository contract, less any applicable FDIC insurance.

Chapter 2256 of the Texas Government Code (the Public Funds Investment Act) authorizes the City to invest its funds under written investment policy (the "investment policy") that primarily emphasizes safety of principal and liquidity, addresses investment diversification, yield, and maturity and addresses the quality and capability of investment personnel. This investment policy defines what constitutes the legal list of investments allowed under the policies, which excludes certain instruments allowed under chapter 2256 of the Texas Government Code.

Investments

The City's deposits and investments are invested pursuant to the investment policy, which is approved by the City Council. The investment policy includes lists of authorized investment instruments and allowable stated maturity of individual investments. In addition it addresses the priorities of preservation of capital, liquidity, diversification and yield. Additionally, the soundness of financial institutions (including broker/dealers) in which the City will deposit funds is addressed. The City's investment policy and types of investments are governed by the Public Funds Investment Act (PFIA). The City's management believes it complied with the requirements of the PFIA and the City's investment policy, except for obtaining investment officer training.

The City's Investment Committee submits an investment report each quarter to the City Council. The report details the investment positions of the City and the compliance of the investment portfolio's as they relate to both the investment strategy and policy approved by City Council and Texas State law.

The City is authorized to invest in the following investment instruments provided that they meet the guidelines of the investment policy:

1. Fully insured or collateralized certificate of deposit of commercial banks;
2. U.S. Treasury Securities maturing in less than three (3) years;
3. Short-term obligations of U.S. Government Agencies which are guaranteed by the full faith and credit of the United States of America as to principle and interest;
4. Repurchase agreements collateralized by U.S. Treasury or U.S. Government Agency Securities in accordance with a master repurchase agreement approved by the Investment Committee;
5. Eligible investment pools authorized by the City Council;
6. Other securities or obligations approved by the Investment Committee and authorized by the Local Government Code, Sections 2256.006 and 2256.016.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 3 - DEPOSITS, INVESTMENTS AND DERIVATIVES - Continued

Investments - Continued

The City participates in one Local Government Investment Pool (LGIP): Texpool. The State Comptroller oversees Texpool with Federated Investors managing the daily operations of the pool under a contract with the State Comptroller.

The City invests in Texpool to provide its liquidity needs. Texpool is a local government investment pool that was established in conformity with the Interlocal Cooperation Act, Chapter 791 of the Texas Government Code and the Public Funds Investment Act, Chapter 2256 of the Code. Texpool is a 2(a)7 like fund, meaning that it is structured similar to a money market mutual fund. Such funds allow shareholders the ability to deposit or withdraw funds on a daily basis. Interest rates are also adjusted on a daily basis. Such funds seek to maintain a constant net asset value of \$ 1.00, although this cannot be fully guaranteed. Texpool is rated AAA and must maintain a dollar weighted average maturity not to exceed 60 days, which is the limit.

At September 30, 2013, Texpool had a weighted average maturity of 60 days. Although Texpool portfolio had a weighted average maturity of 60 days, the City considers holdings in these funds to have a one day weighted average maturity. This is due to the fact that the share position can usually be redeemed each day at the discretion of the shareholder, unless there has been a significant change in value.

All of the City's investments are insured, registered, or the City's agent holds the securities in the City's name; therefore, the City is not exposed to custodial credit risk.

The following table includes the portfolio balances of all investment types of the City at September 30, 2013.

<u>Investment Type</u>	<u>Fair Value</u>	<u>Weighted Average Maturity (Days)</u>
Local government investment pools (LGIP)	\$ <u>3,981,033</u>	60
	\$ <u>3,981,033</u>	60

Credit Risk – As of September 30, 2013, the LGIP (which represents 100% of the City's portfolio) are rated AAAM by Standard and Poor's.

Interest rate Risk – As a means of minimizing risk of loss due to interest rate fluctuations, the Investment Policy the City avoid over-concentration of assets in a specific maturity sector, limiting of average maturities of operating fund investments to one year, and avoiding over-concentrated assets in specific instruments other than U.S. Treasury Securities and insured or collateralized certificates of deposit.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 3 - DEPOSITS, INVESTMENTS AND DERIVATIVES - Continued

Derivatives

Interest in derivative products has increased in recent years. Derivatives are investment products, which may be a security or contract, which derives its value from another security, currency, commodity, or index, regardless of the source of funds used. The City made no direct investments in derivatives during the year ended September 30, 2013, and holds no direct investments in derivatives at September 30, 2013.

NOTE 4 - DEFERRED INFLOWS OF RESOURCES AND UNEARNED REVENUE

Governmental funds report unearned revenue in connection with receivables for revenues that are considered to be available to liquidate liabilities of the current period. Governmental funds also report deferred inflows of resources with resources that have been received, but not yet earned.

As of September 30, 2013, the various components of deferred inflows of resources and unearned revenue reported in the governmental funds were as follow.

	<u>Deferred Inflows of Resources</u>	<u>Unearned Revenue</u>
Delinquent property taxes receivable (General Fund)	\$ 228,003	\$
Delinquent property taxes receivable (Debt Service Fund)	63,052	
Franchise tax receipts (General Fund)	<u> </u>	<u>40,067</u>
Total deferred inflows of resources/unearned revenue from governmental funds	<u>\$ 291,055</u>	<u>\$ 40,067</u>

As of September 30, 2013, the various components of unearned revenue reported in the proprietary funds were as follow.

	<u>Unearned Revenue</u>
Deposits	\$ <u>200</u>
Total unearned revenue from proprietary funds	\$ <u>200</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 5 - INTERFUND RECEIVABLES, PAYABLES AND TRANSFERS

Interfund balances at September 30, 2013 consisted of the following individual fund receivables and payables:

<u>Fund</u>	<u>Receivable</u>	<u>Payable</u>
General Fund:		
Special Revenue Fund:		
Streets, Drainage and Sidewalk	\$ 5,769	\$ 11,432
Marina Operations	273,017	
Debt Service Fund:		
Series 2003A	300	
Series 2003B	26,910	280
Series 2008	4,440	
Capital Projects Fund:		
2008 Bond Construction		52,323
Enterprise Fund:		
Water and Sewer Fund	566,199	
Golf Course Fund	146,962	
Ambulance Fund	88,017	
	<u>1,111,614</u>	<u>64,035</u>
Special Revenue Fund:		
Street, Drainage and Sidewalk Fund:		
General	11,432	5,769
Marina Operations Fund:		
General		<u>273,017</u>
	<u>11,432</u>	<u>278,786</u>
Debt Service Fund:		
Series 2003A Fund:		
General Fund		300
Series 2003B Fund:		
General Fund	280	26,910
Series 2008 Fund:		
General		<u>4,440</u>
	<u>280</u>	<u>31,650</u>

(continued)

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 5 - INTERFUND RECEIVABLES, PAYABLES AND TRANSFERS - Continued

Capital Projects Fund:		
2008 Bond Construction Fund:		
General	\$ <u>52,323</u>	\$ _____
Enterprise Fund:		
Water and Sewer Fund:		
General		566,199
Golf Course Fund:		
General		146,962
Ambulance Fund:		
General	_____	<u>88,017</u>
	<u>-0-</u>	<u>801,178</u>
Total	\$ <u>1,175,649</u>	\$ <u>1,175,649</u>

Interfund transfers for the year ended September 30, 2013 consisted of the following individual fund transfers in and transfers out:

<u>Fund</u>	<u>Transfers In</u>	<u>Transfers Out</u>
General Fund:		
Enterprise Funds:		
Water and Sewer Fund	\$	\$ 280,400
Golf Course Fund		151,675
Ambulance Fund	_____	<u>71,314</u>
	<u>-0-</u>	<u>503,389</u>
Enterprise Funds:		
Water & Sewer Fund:		
General	280,400	
Golf Course:		
General Fund	151,675	
Ambulance:		
General Fund	<u>71,314</u>	_____
	<u>503,389</u>	<u>-0-</u>
Total	\$ <u>503,389</u>	\$ <u>503,389</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 6 - CAPITAL ASSETS

Capital assets activity for the year ended September 30, 2013 was as follows:

	<u>Restated Balance 10/01/12</u>	<u>Additions</u>	<u>Retirements & Transfers</u>	<u>Balance 09/30/13</u>
Governmental Activities:				
Capital Assets, Not Depreciated:				
Land	\$ 3,024,568	\$ 23,980	\$	\$ 3,048,548
Construction in progress	<u>144,336</u>	<u>707,312</u>	<u> </u>	<u>851,648</u>
Total capital assets not being depreciated	<u>3,168,904</u>	<u>731,292</u>	<u>-0-</u>	<u>3,900,196</u>
Capital Assets, Being Depreciated:				
Improvements	18,464,373	616,208		19,080,581
Buildings	4,774,243			4,774,243
Furniture, equipment and vehicles	6,785,286	254,254		7,039,540
Assets under lease	<u> </u>	<u>391,275</u>	<u> </u>	<u>391,275</u>
Total capital assets being depreciated	<u>30,023,902</u>	<u>1,261,737</u>	<u>-0-</u>	<u>31,285,639</u>
Less Accumulated Depreciation For:				
Improvements	10,694,380	615,688		11,310,068
Buildings	2,725,919	171,485		2,897,404
Furniture, equipment and vehicles	4,766,909	470,188		5,237,097
Assets under lease	<u> </u>	<u>26,085</u>	<u> </u>	<u>26,085</u>
Total accumulated depreciation	<u>18,187,208</u>	<u>1,283,446</u>	<u>-0-</u>	<u>19,470,654</u>
Total capital assets being depreciated, net	<u>11,836,694</u>	<u>(21,709)</u>	<u>-0-</u>	<u>11,814,985</u>
Governmental activities capital assets, net	<u>\$15,005,598</u>	<u>\$ 709,583</u>	<u>\$ -0-</u>	<u>\$15,715,181</u>
Combined Business-type Activities:				
Capital Assets, Not Depreciated:				
Land	\$ 395,630	\$	\$	\$ 395,630
Construction in progress	<u> </u>	<u>285,053</u>	<u> </u>	<u>285,053</u>
Total capital assets not being depreciated	<u>395,630</u>	<u>285,053</u>	<u>-0-</u>	<u>680,683</u>
Capital Assets, Being Depreciated:				
Buildings	211,468			211,468
Improvements	553,118			553,118
Utility plant	20,630,832	76,100		20,706,932
Furniture, equipment and vehicles	1,053,907	185,903		1,239,810
Assets under capital lease	<u>99,549</u>	<u>207,867</u>	<u> </u>	<u>307,416</u>
Total capital assets being depreciated	<u>22,548,874</u>	<u>469,870</u>	<u>-0-</u>	<u>23,018,744</u>

(continued)

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 6 - CAPITAL ASSETS - Continued

	Balance 10/01/12	Additions	Retirements & Transfers	Balance 09/30/13
Less Accumulated Depreciation For:				
Buildings	\$ 97,766	\$ 8,313	\$	\$ 106,079
Improvements	420,676	28,232		448,908
Utility plant	14,280,780	298,943		14,579,723
Furniture, equipment and vehicles	888,135	68,246		956,381
Assets under capital lease	<u>19,175</u>	<u>34,265</u>		<u>53,440</u>
Total accumulated depreciation	<u>15,706,532</u>	<u>437,999</u>	<u>-0-</u>	<u>16,144,531</u>
Total capital assets being depreciated, net	<u>6,842,342</u>	<u>31,871</u>	<u>-0-</u>	<u>6,874,213</u>
Business-type activities capital assets, net	<u>\$ 7,237,972</u>	<u>\$ 316,924</u>	<u>\$ -0-</u>	<u>\$ 7,554,896</u>
Business-type Activities:				
<u>Water and Sewer Enterprise Fund:</u>				
Capital Assets, Not Depreciated:				
Land	\$ 56,200	\$	\$	\$ 56,200
Construction in progress		<u>285,053</u>		<u>285,053</u>
Total capital assets not being depreciated	<u>56,200</u>	<u>285,053</u>	<u>-0-</u>	<u>341,253</u>
Capital Assets, Being Depreciated:				
Utility plant	20,630,832	76,100		20,706,932
Furniture, equipment and vehicles	<u>146,765</u>			<u>146,765</u>
Total capital assets being depreciated	<u>20,777,597</u>	<u>76,100</u>	<u>-0-</u>	<u>20,853,697</u>
Less Accumulated Depreciation For:				
Utility plant	14,280,780	298,943		14,579,723
Furniture, equipment and vehicles	<u>122,134</u>	<u>6,032</u>		<u>128,166</u>
Total accumulated depreciation	<u>14,402,914</u>	<u>304,975</u>	<u>-0-</u>	<u>14,707,889</u>
Total capital assets being depreciated, net	<u>6,374,683</u>	<u>(228,875)</u>	<u>-0-</u>	<u>6,145,808</u>
Business-type activities capital assets, net	<u>\$ 6,430,883</u>	<u>\$ 56,178</u>	<u>\$ -0-</u>	<u>\$ 6,487,061</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 6 - CAPITAL ASSETS - Continued

	Balance 10/01/12	Additions	Retirements & Transfers	Balance 09/30/13
Business-type Activities:				
<u>Golf Course Enterprise Fund:</u>				
Capital Assets, Not Depreciated:				
Land	\$ 339,430	\$ _____	\$ _____	\$ 339,430
Total capital assets not being depreciated	<u>339,430</u>	<u>-0-</u>	<u>-0-</u>	<u>339,430</u>
Capital Assets, Being Depreciated:				
Buildings	211,468			211,468
Improvements	553,118			553,118
Furniture, equipment and vehicles	563,353			563,353
Assets under capital lease	<u>99,549</u>	<u>207,867</u>		<u>307,416</u>
Total capital assets being depreciated	<u>1,427,488</u>	<u>207,867</u>	<u>-0-</u>	<u>1,635,355</u>
Less Accumulated Depreciation For:				
Buildings	97,766	8,313		106,079
Improvements	420,676	28,232		448,908
Furniture, equipment and vehicles	512,350	16,880		529,230
Assets under capital lease	<u>19,175</u>	<u>34,265</u>		<u>53,440</u>
Total accumulated depreciation	<u>1,049,967</u>	<u>87,690</u>	<u>-0-</u>	<u>1,137,657</u>
Total capital assets being depreciated, net	<u>377,521</u>	<u>120,177</u>	<u>-0-</u>	<u>497,698</u>
Business-type activities capital assets, net	\$ <u>716,651</u>	\$ <u>120,177</u>	\$ <u>-0-</u>	\$ <u>837,128</u>
Business-type Activities:				
<u>Ambulance Enterprise Fund:</u>				
Capital Assets, Being Depreciated:				
Furniture, equipment and vehicles	\$ 343,789	\$ 185,903	\$ _____	\$ 529,692
Total capital assets being depreciated	<u>343,789</u>	<u>185,903</u>	<u>-0-</u>	<u>529,692</u>
Less Accumulated Depreciation For:				
Furniture, equipment and vehicles	<u>253,651</u>	<u>45,334</u>		<u>298,985</u>
Total accumulated depreciation	<u>253,651</u>	<u>45,334</u>	<u>-0-</u>	<u>298,985</u>
Business-type activities capital assets, net	\$ <u>90,138</u>	\$ <u>140,569</u>	\$ <u>-0-</u>	\$ <u>230,707</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 6 - CAPITAL ASSETS - Continued

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

Governmental Activities:

Administration	\$ 328,631
Public safety	300,438
Service center	16,543
Streets and drainage	424,710
Marina	28,494
Library	19,599
Parks and recreation	<u>165,031</u>
Total depreciation expense-governmental activities	<u>\$ 1,283,446</u>

Business-type Activities:

Water and sewer	\$ 304,975
Golf Course	87,690
Ambulance	<u>45,334</u>
Total depreciation expense-business-type activities	<u>\$ 437,999</u>

Total	<u>\$ 1,721,445</u>
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NOTE 7 - ALLOWANCE FOR UNCOLLECTIBLE ACCOUNTS

Taxes - Ad valorem taxes receivable are reserved based on historical experience and evaluation of collectability within the near future. The allowance for uncollectible taxes as of September 30, 2013, for the General Fund was \$ 49,925 and for the Debt Service Funds was \$ 5,020.

Garbage Customer Receivables - The allowance for uncollectible receivables related to garbage service is determined using twenty-five percent of the accounts thirty days past due and one hundred percent of the accounts over sixty days. The allowance for uncollectible receivables for the year ended September 30, 2013 was \$ 10,536.

Paving Assessments - Receivables for special paving assessments have been fully reserved due to the uncertainty of collections within the near future. Revenue as related to paving assessments is reported as collected. The allowance for uncollectible assessments as of September 30, 2013 was \$ 144,284.

Utility Customer Receivables - The allowance for uncollectible receivables related to utility services is determined using twenty-five percent of the accounts thirty days past due and one hundred percent of the accounts over sixty days. The allowance for uncollectible receivables for the year ended September 30, 2013 was \$ 34,431.

Ambulance Customer Receivables - The allowance for uncollectible receivables related to ambulance service is determined using sixty-seven percent of all accounts based on current historical data. The allowance for uncollectible receivables for the year ended September 30, 2013 was \$ 849,077.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 7 - ALLOWANCE FOR UNCOLLECTIBLE ACCOUNTS - Continued

Municipal Court Receivables - Municipal court receivables are reported in the governmental activities statement of net position. Since these receivables do not represent current available resources, they are not reported in the governmental funds balance sheet. The allowance for uncollectible receivables related to municipal court assessments is determined based on historical experience and evaluation of collection in relation to the aging of customer accounts. The allowance for uncollectible receivables for the year ended September 30, 2013 was \$ 881,821.

NOTE 8 - CONTINGENT LIABILITIES

The City is contingently liable in respect to lawsuits and other claims in the ordinary course of its operations. The potential settlement (if any) of such contingencies under the budgetary process would require appropriation of revenues yet to be realized and would not materially affect the financial position of the City at September 30, 2013.

NOTE 9 - PENSION AND OPEB-SUPPLEMENTAL DEATH BENEFITS PLAN

Plan Description

The City provides pension benefits for all of its eligible employees through a non-traditional, joint contributory, hybrid defined benefit plan in the state-wide Texas Municipal Retirement System (TMRS), an agent multiple-employer public employee retirement system. The plan provides 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. This report may be obtained from TMRS' website at www.TMRS.com.

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

	<u>Plan Year 2012</u>	<u>Plan Year 2013</u>
Employee deposit rate	7%	7%
Matching ratio (city to employee)	2 to 1	2 to 1
Years required for vesting	5	5
Service retirement eligibility (expressed as age/years of service)	60/5, 0/20	60/5, 0/20
Updated Service Credit	100%	100%
	Repeating, Transfers	Repeating, Transfers
Annual Increase (to retirees)	70% of CPI	70% of CPI

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 9 - PENSION AND OPEB-SUPPLEMENTAL DEATH BENEFITS PLAN - Continued

Contributions:

Under the state law governing TMRS, the contribution rate for each city is determined annually by the actuary, using the Protected Unit Credit actuarial cost method. This rate consists of the normal cost contribution rate and the prior service cost contributions rate, which is calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the portion of an active member's projected benefit allocated annually; the prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the applicable period for the 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 Annual Increases.

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

The annual pension cost and net pension obligation (asset) are as follows:

Three-Year Trend Information

Fiscal Year Ending	Annual Pension Cost (APC)	Actual Contribution Made	Percentage of APC Contributed	Net Pension Obligation/ (Asset)
2011	\$ 564,034	\$ 564,034	100%	\$ -0-
2012	565,439	565,439	100%	-0-
2013	571,460	571,460	100%	-0-

The required contribution rates for fiscal year 2013 were determined as part of the December 31, 2010 and 2011 actuarial valuations. Additionally information as of the latest actuarial valuation, December 31, 2012, also follows:

Valuation date	12-31-10 Prior to Restructuring	12-31-10 Restructured	12-31-11	12-31-12
Actuarial Cost Method	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit	Projected unit Credit
Amortization Method	Level Percent of payroll	Level Percent of payroll	Level Percent of payroll	Level Percent of payroll
GASB 25 Equivalent Single Amortization Period	27.3 years; closed period	27.3 years; closed period	26.3 years; closed period	25.3 years; closed period

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 9 - PENSION AND OPEB-SUPPLEMENTAL DEATH BENEFITS PLAN - Continued

Amortization Period for new Gains/Losses	30 years	30 years	30 years	30 years
Asset Valuation Method	10-year Smoothed Market	10-year Smoothed Market	10-year Smoothed Market	10-year Smoothed Market
Actuarial Assumptions:				
Investment Rate of Return*	7.5%	7.0%	7.0%	7.0%
Projected Salary Increases*	Varies by age & service	Varies by age & service	Varies by age & service	Varies by age and service
*Includes Inflation rate at Cost-of-Living Adjustments	3.00%	3.00%	3.00%	3.00%
	2.10%	2.10%	2.10%	2.10%

Funded Status and Funding Progress –

The funding status of December 31, 2012, the most recent actuarial valuation date, is presented, is presented as follows:

Actuarial Valuation Date	Actuarial Value of Assets (1)	Actuarial Accrued Liability (AAL) (2)	Funded Ratio (3) (1) / (2)	Unfunded AAL (UAAL) (4) (2) – (1)	Covered Payroll (5)	UAAL as a Percentage of Covered (6) (4) / (5)
12-31-10	\$12,689,121	\$ 16,586,761	76.5%	\$ 3,897,640	\$ 4,703,129	82.9%
12-31-11	13,664,468	17,542,600	77.9%	3,878,132	5,018,818	77.3%
12-31-12	14,744,043	18,505,472	79.7%	3,761,429	4,943,961	76.1%

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.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 9 - PENSION AND OPEB-SUPPLEMENTAL DEATH BENEFITS PLAN - Continued

OPEB Supplemental Death Benefits Fund

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

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

The city contributes to the SDBF at a contractually required rate as determined by an annual actuarial valuation. The rate is equal to the cost of providing on-year term life insurance. The funding policy for the SDBF program is to assure that adequate resources are available to meet all death benefit payments for the coming year; the intent is not to pre-fund retiree term life insurance during employee's entire careers.

The city's contributions to the TMRS SDBF for the years ended 2013, 2012, and 2011 were \$ 11,542, \$ 10,435 and \$ 10,045, respectively, which equaled the required contributions each year.

Schedule of Contribution Rates (Retiree-only portion of the rate):

Plan/Calendar Year	Actual Required Contribution (Rate)	Actual Contribution Made (Rate)	Percentage of ARC Contributed
2011	0.05%	0.05%	100.0%
2012	0.05%	0.05%	100.0%
2013	0.05%	0.05%	100.0%

NOTE 10 - TEXAS STATEWIDE EMERGENCY SERVICES PERSONNEL RETIREMENT FUND

Plan Description

The Fire Fighters' Pension Commissioner is the administrator of the Texas Statewide Emergency Services Personnel Retirement Fund (TESRS), a cost-sharing multiple employer pension system established and administered by the State of Texas to provide pension benefits for emergency services personnel who serve without significant monetary remuneration. At August 31, 2012, there were 199 member fire or emergency services departments actively participating in TESRS. Eligible participants include volunteer emergency services personnel who are members in good standing of a participating department.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 10 - TEXAS STATEWIDE EMERGENCY SERVICES PERSONNEL RETIREMENT FUND -
Continued

Plan Description - Continued

At August 31, 2012, TESRS membership consisted of:

Retirees and beneficiaries currently receiving benefits	2,750
Terminated participants entitled to benefits but not yet receiving them	2,250
Current active participants (vested and non-vested)	<u>4,448</u>
	<u>9,448</u>

Senate Bill 411, 65th Legislature, Regular Session (1977) created TESRS and established the applicable benefit provisions. The 79th Legislature, Regular Session (2005), recodified the provisions and gave the TESRS Board of Trustees authority to establish vesting requirements, contribution levels, benefit formulas, and eligibility requirements by board rule. The benefit provisions include retirement benefits as well as death and disability benefits. Member are 50% vested after the tenth year of service, with the vesting percent increasing 10% for each of the next five years of service so that a member becomes 100% vested with 15 years of service.

Upon reaching age 55, each vested member may retire and receive a monthly pension equal to his vested percent multiplied by six times the governing body's average monthly contribution over the member's years of qualified service. For years of service in excess of 15 years, this monthly benefit is increased at the rate of 6.2% compounded annually.

On and off duty death benefits and on-duty disability benefits are dependent on whether or not the member was engaged in the performance of duties at the time of death or disability. Death benefits include a lump-sum amount and continuing monthly payments to a member's surviving spouse and dependent children.

Funding Policy

Contribution provisions were established by S.B. 411, 65th Legislative, Regular Session (1977) and were amended by board rule in 2006. No contributions are required by individual members of participating departments. The governing bodies of participating departments are required to contribute at least the minimum prescribed amount per month for each active member and may contribute more. Additional contributions may be made by a governing body to pay for granting credit for service before the department began participating in TESRS (prior service). The State may also be required to make annual contributions up to a limited amount to make TESRS actuarially sound.

Annual Required Contributions

The contribution requirement per active emergency services personnel member per month is not actuarially determined. Rather, the minimum contribution provisions were set by board rule. For the fiscal year ending August 31, 2012 total contributions (dues and prior service) of \$ 3,517,455 were paid into TESRS by the political subdivisions served by the member volunteer emergency services personnel. The state did not appropriate any maximum state contribution for the fiscal years ending August 31, 2012 and 2013. Total contributions made were less than the contributions required by the state statute and required based on the August 31, 2010 actuarial valuation.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 10 - TEXAS STATEWIDE EMERGENCY SERVICES PERSONNEL RETIREMENT FUND - Continued

Annual Required Contributions - Continued

The purpose of the biennial actuarial valuation is to test the adequacy of the contribution arrangement to determine if it is adequate to pay the benefits that are promised. The actuarial valuation as of August 31, 2012 revealed the inadequacy of the expected contributions from the political subdivisions (dues and prior service contributions) even together with the actual state appropriations for the fiscal year ending August 31, 2013 (\$ 528,538 to pay for part of the System's administrative expenses) and with the assumed legislative appropriations of (1) the maximum state contributions amount in future years for up to 30 years as is necessary for the System to have a 30-year amortization period, and (2) approximately \$ 530,000 each year to help pay for part of the System's administrative expenses.

Required Supplementary Information - Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) ¹ - Entry Age (b)	Unfunded AAL (UAAL) (b)-(a)	Funded Ratio (a/b)	Total Members Covered (c)	UAAL Per Member Covered (b-a)/(c)
8/31/08 ²	\$ 60,987,157	\$ 64,227,341	\$ 3,240,184	95.0%	8,254	\$ 393
8/31/10 ³	64,113,803	81,264,230	17,150,427	78.9%	8,644	1,984
8/31/12 ²	67,987,487	101,856,042	33,868,555	66.7%	9,448	3,585

Notes:

- ¹ The actuarial accrued liability is based upon the entry age actuarial cost method.
- ² Changes in actuarial assumptions were reflected in this valuation.
- ³ Changes in actuarial assumptions and method were reflected in this valuation.

Fiscal Year Ending	Three-Year Trend Information		
	Annual Required Contributions (ARC)	Actual Contributions	Percentage of ARC Contributed
August 31, 2010	\$ 2,875,103 ¹	\$ 2,875,103	100%
August 31, 2011	3,125,329 ²	3,125,329	100%
August 31, 2012	4,423,898 ²	3,517,455	80%

- ¹ Based on the August 31, 2008 actuarial valuation.
- ² Based on the revised August 31, 2010 actuarial valuation.
- ³ Includes a requested state contribution of \$ 906,443.

A report may be obtained by contacting the Texas Comptroller, Post Office Box 13528, Capitol Station, Austin, Texas 78711-3528.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 11 - INDUSTRIAL DISTRICT CONTRACTS

In 2011, the City of Freeport in conjunction with the cities of Lake Jackson and Clute entered into an industrial contract with the Dow Chemical Company and BASF Corporation. A formula using Dow Chemical Company's and BASF Corporation's assets determine how much the City of Freeport will receive each year. The amount received under this contract and various other industrial district contracts during the year ended September 30, 2013 was \$ 4,884,316 and is reported in the General Fund.

NOTE 12 - WATER SUPPLY CONTRACT

The City entered into a water supply contract with the Brazosport Water Authority on February 20, 1987. The contract term is forty years and may not be terminated as long as bonds are outstanding. The City agrees to take and pay for, whether taken or not, 2 million gallons of water per day. The actual supply of water under this contract started in March, 1989.

NOTE 13 - JOINT VENTURE

The City is party to an agreement with the City of Oyster Creek to share costs associated with the operation of a sewer treatment plant. The plant went on-line during the fiscal year ended September 30, 1989. The percentage for sharing the operating expenses is determined based upon meter flow calibrations. For the year ended September 30, 2013, the City of Freeport's portion of these expenses was \$ 36,719. The City of Oyster Creek maintains both budgetary and accounting responsibility over these operations.

During the year ended September 30, 2003, the City began a joint venture with the City of Clute, City of Lake Jackson, and the SPCA for an animal shelter. The shelter is located in Lake Jackson and provides programs for the claiming and adoption of lost or abandoned animals for the three cities. The term of the agreement is from March 1, 2003 through February 28, 2023. The City and Clute contributed \$ 150,000 each and the SPCA contributed \$ 250,000 for a total of \$ 550,000 to Lake Jackson for the design, construction, and furnishing of the \$ 1,100,000 facility. The City pays each year for administrative operating costs. For the year ended September 30, 2013, the City paid \$ 66,029 for their portion of the operating costs.

NOTE 14 - LONG-TERM DEBT

General Long-Term Debt:

On October 24, 2003, the City issued \$ 3,000,000 and \$ 2,185,000 of Series 2003 Certificate of Obligation Bonds and Series 2003 Refunding Bonds. The Refunding Bonds effectively defeased the Series 2001 Certificates of Obligation Bonds.

On March 13, 2008, the City issued \$ 3,350,000 of Series 2008 Certificates of Obligation for authorized construction projects.

The general obligation bonds payable at September 30, 2013 are summarized as follows:

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 14 - LONG-TERM DEBT - Continued

General Long-Term Debt - Continued

Purpose	Interest Rate (%)	Series Dates			Bonds Outstanding 09/30/13
		Issued	Maturity	Callable	
Certificate Obligation					
Bonds Series 2008	3.79%	2008	2023		\$ 2,435,000
Bonds Series 2003	4.84%	2003	2018	2014	1,459,000
Refunding Bonds Series 2003	4.84%	2003	2018	2014	<u>1,062,000</u>
					<u>\$ 4,956,000</u>

General obligation bond transactions for the year ended September 30, 2013 were as follows:

	<u>2013</u>
Bonds outstanding, October 1,	\$ 5,511,000
Maturities	<u>(555,000)</u>
Bonds outstanding, September 30,	<u>\$ 4,956,000</u>

Aggregate maturities of certificate of obligation bonds for the five years subsequent to September 30, 2013 are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014	\$ 577,000	\$ 205,300	\$ 782,300
2015	605,000	179,091	784,091
2016	629,000	151,606	780,606
2017	659,000	122,989	781,989
2018	689,000	93,024	782,024
2019-2023	<u>1,797,000</u>	<u>165,865</u>	<u>1,962,865</u>
Total	<u>\$ 4,956,000</u>	<u>\$ 917,875</u>	<u>\$ 5,873,875</u>

Proprietary Fund Debt:

In August 2004, the City issued \$ 1,943,000 in Revenue Refunding Bonds. Long term debt of the proprietary fund, which consists of serially maturing bonds for waterworks and sewer system improvements, is payable from the operations of the water and sewer utility operations. The revenue bonds payable at September 30, 2013 are summarized as follows:

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 14 - LONG-TERM DEBT - Continued

Proprietary Fund Debt - Continued

Purpose	Interest Rate (%)	Series Dates			Bonds Outstanding 09-30-13
		Issued	Maturity	Callable	
Waterworks and Sewer System Revenue Bonds Series 2004	4.85%	2004	2015		\$ <u>463,000</u>
					\$ <u>463,000</u>

Revenue bond transactions for the year ended September 30, 2013 are as follows:

	2013
Bonds outstanding, October 1, Maturities	\$ 678,000 (215,000)
Bonds outstanding, September 30,	\$ <u>463,000</u>

Aggregate maturities of revenue bonds for the years subsequent to September 30, 2013 are as follows:

	Principal	Interest	Total
2014	\$ 228,000	\$ 16,926	\$ 244,926
2015	<u>235,000</u>	<u>5,699</u>	<u>240,699</u>
Total	\$ <u>463,000</u>	\$ <u>22,625</u>	\$ <u>485,625</u>

These bonds are due on October 1st each year and the City normally pays principal and interest on September 30th, however, payment was not made until October 1, 2013. Therefore, the reserve requirement for these bonds, in the amount of \$ 244,926, at September 30, 2013 was underfunded by \$ 228,749. Both payments for October 1, 2013 and April 1, 2014 were made without incident and the final payment is due on October 1, 2014.

Changes in Long-Term Debt

Transactions for the year ended September 30, 2013 are summarized as follows:

	Balance 10/01/12	Issues or Additions	Payments or Expenditures	Balance 09/30/13	Due Within One Year
Governmental Type Activities:					
General obligation bonds	\$ 5,511,000	\$	\$ 555,000	\$ 4,956,000	\$ 577,000
Capital lease	103,226	391,275	112,534	381,967	144,742
Compensated absences	694,603	404,414	401,141	697,876	400,000
Component of Long-Term Debt:					
Accrued interest payable	<u>110,434</u>	<u>99,169</u>	<u>110,434</u>	<u>99,169</u>	<u>99,169</u>
Total governmental activities	<u>6,419,263</u>	<u>894,858</u>	<u>1,179,109</u>	<u>6,135,012</u>	<u>1,220,911</u> (continued)

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 14 - LONG-TERM DEBT - Continued

Changes in Long-Term Debt - Continued

	<u>Balance</u> <u>10/01/12</u>	<u>Issues or</u> <u>Additions</u>	<u>Payments or</u> <u>Expenditures</u>	<u>Balance</u> <u>09/30/13</u>	<u>Due Within</u> <u>One Year</u>
Business Type Activities:					
Revenue bonds payable	678,000		215,000	463,000	228,000
Capital leases	58,334	207,867	48,023	218,178	94,259
Compensated absences	79,333	46,190	52,199	73,324	52,080
Component of Long-Term Debt:					
Accrued interest	<u>16,442</u>	<u>11,228</u>	<u>16,442</u>	<u>11,228</u>	<u>11,228</u>
Total business type activities	<u>832,109</u>	<u>265,285</u>	<u>331,664</u>	<u>765,730</u>	<u>385,567</u>
Total government (net)	<u>\$ 7,251,372</u>	<u>\$ 1,160,143</u>	<u>\$ 1,510,773</u>	<u>\$ 6,900,742</u>	<u>\$ 1,606,478</u>

Debt Issuances and Defeased Debt

General Long-Term Debt:

During the year ended September 30, 2004, the City issued \$ 2,185,000 in Certificate of Obligation Refunding Bonds, Series 2003 for refunding of previously issued and outstanding \$ 2,135,000 Economic Development Corporation Certificate of Obligation Bonds – Series 2001. The City placed \$ 2,142,889 from the proceeds of the refunding in an escrow fund. The escrow fund is irrevocably pledged to the payment of principal and interest on the issue being refunded. The difference between the cash flow required to service the old debt and that required to service the new debt and complete the refunding was a decrease of \$ 216,580. The economic gain resulting from the transaction was \$ 252,180. The outstanding balance of these defeased bonds at September 30, 2013 was \$ 1,270,000 and the balance held in escrow was \$ 1,270,851.

NOTE 15 - LEASES

Operating leases

Lessor (Governmental)

The City leases various office space as well as park and community house rentals as lessor. These leases are considered operating leases for accounting purposes and are reported as income in the General Fund. The office leases are annual leases that are renewed each year as of January 1st or multi-year leases for up to ten years. The park and community house rentals are based upon usage.

Aggregate maturities of operating lease receivables for the five years subsequent to September 30, 2013 are as follows:

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 15 - LEASES - ContinuedOperating leases - ContinuedLessor (Governmental) - Continued

Year Ended <u>September 30,</u>	<u>Total</u>
2014	\$ 120,000
2015	120,000
2016	120,000
2017	<u>30,000</u>
Minimum payments under operating leases	\$ <u><u>390,000</u></u>

Operating lease and rental income for the year ended September 30, 2013 was as follows:

Office lease income	\$ 130,216
Other rental income	<u>94,176</u>
Total	\$ <u><u>224,392</u></u>

During the year ended September 30, 2008, the City entered into an operating lease for a postage machine through June 30, 2014, sixty-three monthly payments of \$ 156.00. Further, on October 1, 2012, the City entered into two operating leases for copy machines, which calls for monthly payments, through September 30, 2017, of \$ 388 and \$ 239, respectively.

Aggregate maturities of operating lease obligations for the five years subsequent to September 30, 2013 are as follows:

Year Ended <u>September 30,</u>	<u>Total</u>
2014	\$ 8,928
2015	7,524
2016	7,524
2017	<u>7,524</u>
Minimum payments under operating leases	\$ <u><u>31,500</u></u>

Operating lease expenditures for the year ended September 30, 2013 were \$ 11,184.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 15 - LEASES - Continued

Operating leases - Continued

Lessee (Proprietary)

During the year ended September 30, 2009, the City's Golf Course fund entered into an operating lease for forty-five (45) golf carts from February 1, 2009 through January 1, 2013, which called for forty-eight payments of \$ 2,635.20. This lease was terminated on January 1, 2013, with the return of the golf carts.

During the year ended September 30, 2010, the City's Golf Course fund entered into an operating lease for ten (10) golf carts from October 1, 2009 through September 1, 2013, which called for forty-eight payments of \$ 585.60. This lease was terminated on February 1, 2013, with the return of the golf carts.

These leases were replaced with capital leases for the same number of golf carts on March 15, 2013. \$ 10,248 was charged to the Gold Course Fund as cost of sales.

Capital Leases (Governmental)

During the year ended September 30, 2008, the City purchased a digital copier under a capital lease, with an effective interest rate of 5.62%. Current requirements for principal and interest expenditures accounted for in the General Fund were \$ 3,040 and \$ 64, respectively. During the year ended September 30, 2011, the City purchased an air sweeper under a capital lease, with an effective interest rate of 2.79%. Current requirements for principal and interest expenditures accounted for in the General Fund were \$ 49,283 and \$ 3,040, respectively. During the year ended September 30, 2013, the City purchased a Toyota Lift for use in the Marina (special revenue fund) under capital lease, with a cost of \$ 391,275 and an effective interest rate of 4.79%. Current requirements for principal and interest expenditures accounted for in the Marina Fund were \$ 60,111 and \$ 11,662, respectively.

The leased assets and related obligations are accounted for in the governmental activities column of the government-wide financial statements as capital assets and noncurrent liabilities. Current year depreciation on leased assets totaled \$ 26,085 and has been included in depreciation expense.

The capital assets acquired through capital leases are as follows:

Asset:	
Machinery and equipment	\$ 391,275
Less accumulated depreciation	<u>26,085</u>
Total	<u>\$ 365,190</u>

The following is a schedule of future minimum lease payments under capital leases, together with the net present value of the minimum lease payments, as of September 30, 2013:

CITY OF FREEPORT
Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 15 - LEASES - Continued

Capital Leases (Governmental) - Continued

Year Ended September 30,	Amount
2014	\$ 159,983
2015	107,660
2016	107,660
2017	35,888
	411,191
Less amount representing interest	29,224
Net present value of minimum lease payments	\$ 381,967

Capital Leases (Proprietary)

During the year ended September 30, 2012, the City purchased a John Deere precision cut fairway mower under capital lease, with an effective interest rate of 4.67%. Current requirements for principal and interest expenses accounted for in the Golf Course fund were \$ 7,428 and \$ 347, respectively.

During the year ended September 30, 2010, the City purchased a John Deere PROGATOR 2030A Diesel, a John Deere HD200 SELECTSPRAY, and a Rogers Airfoil Boom FGF11 under capital lease, with an effective interest rate of 4.74%. Current requirements for principal and interest expense accounted for in the Golf Course fund were \$ 8,084 and \$ 517, respectively. During the year ended September 30, 2010, the City purchased a John Deere Terrain Cut Trim Mower under capital lease, with an effective interest rate of 4.74%. Current requirements for principal and interest expense accounted for in the Golf Course fund were \$ 9,700 and \$ 1,127, respectively. On March 15, 2013, the City purchased forty-five (45) Toyota golf cars for \$ 170,378, under capital lease, with an effective interest rate of 4.792%. This lease calls for thirty-six monthly payments of \$ 3,330 with a \$ 67,500 balloon payment on March 15, 2016. Current requirements for principal and interest expense accounted for in the Golf Course fund were \$ 19,468 and \$ 3,842, respectively. On March 15, 2013, the City purchased ten (10) Toyota golf cars for \$ 37,489, under capital lease, with an effective interest rate of 4.792%. This lease calls for thirty-six monthly payments of \$ 600 with a \$ 20,000 balloon payment on March 15, 2016. Current requirements for principal and interest expense accounted for in the Golf Course fund were \$ 3,343 and \$ 857, respectively.

The leased assets and related obligations are accounted for in the business-type activities column of the government wide financial statements as capital assets and noncurrent liabilities. Current year depreciation on leased assets totaled \$ 34,265 and has been included in depreciation expense.

The capital assets acquired through capital leases are as follows:

Asset:	
Machinery and equipment	\$ 307,416
Less accumulated depreciation	53,440
Total	\$ 253,976

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 15 - LEASES - Continued

Capital Leases (Proprietary) - Continued

The following is a schedule of future minimum lease payments under capital leases, together with the net present value of the minimum lease payments, as of September 30, 2013:

<u>Year Ended September 30,</u>	<u>Amount</u>
2014	\$ 69,751
2015	57,990
2016	<u>108,052</u>
	235,793
Less amount representing interest	<u>17,615</u>
Net present value of minimum lease payments	<u>\$ 218,178</u>

NOTE 16 - LONG-TERM RECEIVABLES

During prior years, the City loaned the Freeport Economic Development Corporation (the "Corporation"), a component unit of the City, funds in connection with the acquisition of land and preliminary construction plans for the marina project. During the year ended September 30, 2007, the City consolidated these loans in the amount of \$ 734,090. No payments have been received on this loan since September 30, 2008.

During the year ended September 30, 2007, the City loaned the Corporation, a component unit of the City, \$ 6,000,000 to finance the development of the marina project to be located in the City on approximately four acres of land owned or leased by the Corporation. No payments on this loan have been paid since inception.

Effective October 1, 2011, the Freeport Economic Development Corporation and the City of Freeport agreed to freeze the payment of scheduled note payments and the accrual of interest until such time as the Marina is complete and a determination of value and the ability to pay has been made.

The notes receivable at September 30, 2013 are summarized as follows:

<u>Purpose</u>	<u>Interest Rate (%)</u>	<u>Dates</u>			<u>Bonds Outstanding 09/30/13</u>
		<u>Issued</u>	<u>Maturity</u>	<u>Callable</u>	
Note to Freeport EDC 2007	4.84	2007	Undetermined		\$ 6,000,000
Consolidated note to Freeport EDC 2006	5.00	2006	Undetermined		<u>639,208</u>
					<u>\$ 6,639,208</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 16 - LONG-TERM RECEIVABLES - Continued

Notes receivable transactions for the year ended September 30, 2013 are summarized as follows:

	<u>2013</u>
Notes receivable, October 1, Maturities	\$ 6,639,208
Notes outstanding, September 30,	\$ <u>6,639,208</u>

Aggregate maturities of frozen notes receivable at September 30, 2013 are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Total	\$ <u>6,639,208</u>	\$ <u>5,168,991</u>	\$ <u>11,808,199</u>

Changes in Long-Term Receivables

Transactions for the year ended September 30, 2013 are summarized as follows:

	<u>Balance 10/01/12</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance 09/30/13</u>	<u>Due Within One Year</u>
Governmental Type Activities:					
Notes receivable	\$ 6,639,208	\$	\$	\$ 6,639,208	\$
Component of Long-Term Receivable:					
Accrued interest receivable	<u>1,444,331</u>			<u>1,444,331</u>	
Total governmental activities	\$ <u>8,083,539</u>	\$ <u>-0-</u>	\$ <u>-0-</u>	\$ <u>8,083,539</u>	\$ <u>-0-</u>

NOTE 17 - RISK POOL PARTICIPATION

The City is a participant in the Texas Municipal League Intergovernmental Risk Pool for coverage of liability, property and worker's compensation claims. The City pays annual premiums to the pool for the coverage stated. The agreement with the Texas Municipal League Intergovernmental Risk Pool requires the pool to be self-sustaining. Therefore, the City's exposure for claims is designed to be limited to their deductible.

NOTE 18 - GRANTS, ENTITLEMENTS AND SHARED REVENUES

During the year ended September 30, 2013, the City applied for and received federal grants related to various activities. The operations of these grants are reported in the General fund, the Streets, Drainage and Sidewalk (special revenue fund), and the Water and Sewer (enterprise fund). For the most part, these grants are reimbursement type grants, therefore, revenues equal expenditures. Grant revenues are classified as intergovernmental revenues and capital contributions. The federal grants are covered by the requirements of the Single Audit Act and OMB Circular A-133. The state grants are covered by the State of Texas Single Audit Circular. Since the total federal revenues exceeded \$ 500,000, a Single Audit was performed.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 19 - DEFICIT FUND BALANCES/NET UNRESTRICTED POSITION

The following funds reported a fund balance deficit as of September 30, 2013:

Deficit Fund Balances:

Streets Drainage and Sidewalk (special revenue fund)	\$	136,882
Marina Operations (special revenue fund)		278,912
Series 2003B (debt service fund)		13,037

Deficit Unrestricted Net Position:

Water and Sewer (enterprise fund)		568,582
Golf Course (enterprise fund)		194,559

Property tax revenues in the Series 2003B Funds were not sufficient to cover debt payments during the current year. The Series 2003B (debt service fund) had a net decrease of \$ 7,847, which increased the deficit in fund balance to \$ 13,037 at September 30, 2013.

NOTE 20 – EXPENDITURES/EXPENSES IN EXCESS OF APPROPRIATIONS

Expenditures exceeded appropriations for the year ended September 30, 2013 for the following funds:

Special Revenue Funds:

Streets, Drainage and Sidewalks	\$	86,890
Marina Operations		363,138

Debt Service Fund:

Series 2003B		221
--------------	--	-----

Enterprise Funds:

Water and Sewer		14,565
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The expenditures and expenses were approved by City Council; however, the budget was not amended.

NOTE 21 - EVALUATION OF SUBSEQUENT EVENTS

The City has evaluated subsequent events through June 23, 2014, the date which the financial statements were available to be issued.

NOTE 22 - LITIGATION

The City is involved in the following legal actions, and is represented by legal counsel. The stated probable outcome and the possible effect are the opinion of legal counsel based upon conditions existing as of June 23, 2014.

Trevino v. City of Freeport (EEOC Charge No. 846-2013-52047). Ms. Trevino IS currently employed as a Recreation Attendant for the City and has been in that position since February of 2012. She started as a part-time Recreation Attendant on February 8, 2012. She transitioned to full-time Recreation Attendant on October 22, 2012. Trevino was physically able to perform all the duties assigned to her but on or about September 17, 2013, she provided the City with a doctor's statement that raised concerns about her ability to perform certain essential functions of her job. Trevino was placed on protected FMLA leave while the City sought further information from her doctor regarding her ability to safely perform her job with or without a reasonable accommodation. She filed an EEOC charge asserting pregnancy and gender discrimination and was issued a right to sue letter by the EEOC on December 5, 2013. Currently she has not filed suit.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2013

NOTE 22 - LITIGATION - Continued

FEDC v. Royall, et. al.; Cause No. 55780; in the 239th District Court of Brazoria County, Texas; Appeal No. 01-11-01108-CV in the Court of Appeals for the First District of Texas. This matter involves two separate lawsuits that have now been consolidated. The first lawsuit was filed by Briarwood Holdings, LLC (“Briarwood Holdings”), against the Freeport Economic Development Corporation (the “FEDC”) and the City of Freeport (the “City”). In that lawsuit Briarwood Holdings alleges that the FEDC was required to sell Briarwood a tract of water-front property for an agreed sum and that, instead, the FEDC sold the property to the City. Briarwood alleges, among other things, that the FEDC and the City are guilty of fraud. In the second lawsuit, the FEDC sued Briarwood Holdings, Hiram Walker Royall (“Royall”) Freeport Waterfront Properties, L.P. (“FWP”), Freeport Marina, L.P. (“FM”), Freeport Marina GP, LLC (“FMGP”, and Briarwood Capital Corporation (“BCC”), alleging that the defendants are liable for the breach of various agreements concerning the development and operation of the Freeport Marina, a publicly owned pleasure boat marina in downtown Freeport. The City filed a plea to jurisdiction contending that it is immune from the claims asserted against it by the plaintiffs. The trial court denied that motion and the City filed an interlocutory appeal. On March 19, 2013, the First Court of Appeals dismissed the Plaintiffs’ claims against the City other than Briarwood’s breach of contract claim. The appellate court remanded to give Briarwood the opportunity to replead. On November 7, 2013, the Plaintiff’s filed a third amended pleading alleging that FWP assigned its contract rights to Briarwood. The City is now seeking discovery regarding the alleged assignment. We are unable, at this time, to express an opinion on the degree or amount of risk imposed by the claims against the City.

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REQUIRED SUPPLEMENTARY INFORMATION

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL GENERAL FUND AND MARINA SPECIAL REVENUE FUND

For the Year Ended September 30, 2013

	General Fund			Variance with Final Budget Positive (Negative)
	Budgeted Amounts		Actual	
	Original	Final		
Revenues:				
Taxes	\$ 1,984,011	\$ 1,984,011	\$ 1,812,612	\$(171,399)
Other taxes	1,970,484	1,970,484	2,105,793	135,309
Industrial district	4,673,835	4,673,835	4,884,316	210,481
Intergovernmental	94,500	606,207	605,531	(676)
Revenue producing facilities	1,107,484	1,107,484	1,133,949	26,465
Fines, licenses and fees	485,082	485,082	455,960	(29,122)
Investment income	3,653	3,653	3,829	176
Miscellaneous	130,375	189,536	215,789	26,253
Total revenues	<u>10,449,424</u>	<u>11,020,292</u>	<u>11,217,779</u>	<u>197,487</u>
Expenditures:				
Current:				
Administration	1,519,773	1,632,773	1,707,096	(74,323)
Public safety	4,448,060	4,522,738	4,301,234	221,504
Streets and drainage	1,056,654	1,056,654	911,440	145,214
Sanitation	842,550	842,550	760,582	81,968
Service center	137,876	137,876	133,973	3,903
Marina operations				-0-
Library	47,385	47,385	38,365	9,020
Parks and recreation	1,468,213	1,525,170	1,413,885	111,285
Capital outlay	431,351	1,028,128	929,000	99,128
Debt Service:				
Principal	56,026	56,026	52,323	3,703
Interest and fees	547	547	3,104	(2,557)
Total expenditures	<u>10,008,435</u>	<u>10,849,847</u>	<u>10,251,002</u>	<u>598,845</u>
Excess of revenues over (under) expenditures	<u>440,989</u>	<u>170,445</u>	<u>966,777</u>	<u>796,332</u>
Other Financing Sources (Uses):				
Issuance of capital leases				-0-
Transfers out	(440,989)	(503,389)	(503,389)	-0-
Total other financing sources (uses)	<u>(440,989)</u>	<u>(503,389)</u>	<u>(503,389)</u>	<u>-0-</u>
Net change in fund balance	-0-	(332,944)	463,388	796,332
Fund balance - beginning	<u>11,074,469</u>	<u>11,074,469</u>	<u>11,074,469</u>	<u>-0-</u>
Fund balance - ending	<u>\$ 11,074,469</u>	<u>\$ 10,741,525</u>	<u>\$ 11,537,857</u>	<u>\$ 796,332</u>

Marina Operations Special Revenue Fund

Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
Original	Final		
\$	\$	\$	\$
			-0-
			-0-
			-0-
			-0-
475,497	487,631	318,270	(169,361)
			-0-
			-0-
			-0-
<u>475,497</u>	<u>487,631</u>	<u>318,270</u>	<u>(169,361)</u>
			-0-
			-0-
			-0-
			-0-
			-0-
224,103	266,560	791,056	(524,496)
			-0-
			-0-
			-0-
223,481	223,481	60,211	163,270
<u>9,750</u>	<u>9,750</u>	<u>11,662</u>	<u>(1,912)</u>
<u>457,334</u>	<u>499,791</u>	<u>862,929</u>	<u>(363,138)</u>
<u>18,163</u>	<u>(12,160)</u>	<u>(544,659)</u>	<u>(532,499)</u>
		391,275	391,275
			-0-
<u>-0-</u>	<u>-0-</u>	<u>391,275</u>	<u>391,275</u>
18,163	(12,160)	(153,384)	(141,224)
<u>(125,528)</u>	<u>(125,528)</u>	<u>(125,528)</u>	<u>-0-</u>
<u>\$(107,365)</u>	<u>\$(137,688)</u>	<u>\$(278,912)</u>	<u>\$(141,224)</u>

CITY OF FREEPORT

Freeport, Texas

**TEXAS MUNICIPAL RETIREMENT SYSTEM
SCHEDULE OF FUNDING PROGRESS
LAST THREE FISCAL YEARS**

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets**</u>	<u>Actuarial Accrued Liability* (AAL)-</u>	<u>Unfunded AAL (UAAL)</u>	<u>Percentage Funded</u>	<u>Annual Covered Payroll</u>	<u>UAAL as a Percentage of Covered Payroll</u>
	(a)	(b)	(b-a)	(a/b)	(c)	(b-a)/(c)
12-31-10	\$ 12,689,121	\$ 16,586,761	\$ 3,897,640	76.5%	\$ 4,703,129	82.9%
12-31-11	13,664,468	17,542,600	3,878,132	77.9%	5,018,818	77.3%
12-31-12	14,744,043	18,505,472	3,761,429	79.7%	4,943,961	76.1%

* As of December 31 of the preceding year, the date of the actuarial valuation.

** Assets are stated at cost as of December 31 of the preceding year.

CITY OF FREEPORT

Freeport, Texas

TEXAS STATEWIDE EMERGENCY SERVICES PERSONNEL RETIREMENT FUND
SCHEDULE OF FUNDING PROGRESS
LAST THREE ACTUARIAL PERIODS

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL)* - Entry Age (b)	Unfunded AAL (UAAL) (b)-(a)	Funded Ratio (a/b)	Total Members Covered (c)	UAAL Per Member Covered (b-a)/(c)
8/31/08**	\$ 60,987,157	\$ 64,227,341	\$ 3,240,184	95.0%	8,254	\$ 393
8/31/10***	64,113,803	81,264,230	17,150,427	78.9%	8,644	1,984
8/31/12***	67,987,487	101,856,042	33,868,555	66.7%	9,448	3,585

* The actuarial accrued liability is based upon the entry age actuarial cost method.

** Changes in actuarial assumptions were reflected in this valuation.

*** Changes in an actuarial assumption and method were reflected in this valuation.

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OTHER SCHEDULES

CITY OF FREEPORT

Freeport, Texas

COMBINING BALANCE SHEET- NONMAJOR GOVERNMENTAL FUNDS

September 30, 2013

	Special Revenue Funds			
	Streets, Drainage and Sidewalks	Hotel/ Motel Tax	Beach Maintenance	Total
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES				
Assets:				
Cash and temporary investments	\$ 50	\$ 21,299	\$ 6,617	\$ 27,966
Receivables (Net of Allowance for Uncollectable):				
Taxes				-0-
Accounts		4,205		4,205
Due from other governments	22,463			22,463
Due from other funds	<u>11,432</u>			<u>11,432</u>
Total assets	<u>33,945</u>	<u>25,504</u>	<u>6,617</u>	<u>66,066</u>
Deferred Outflows of Resources:				
Total deferred outflows of resources				<u>-0-</u>
Total assets and deferred outflows of resources	<u>\$ 33,945</u>	<u>\$ 25,504</u>	<u>\$ 6,617</u>	<u>\$ 66,066</u>
LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCE				
Liabilities:				
Accounts payable	\$ 165,058	\$	\$	\$ 165,058
Due to other funds	<u>5,769</u>			<u>5,769</u>
Total liabilities	<u>170,827</u>	<u>-0-</u>	<u>-0-</u>	<u>170,827</u>
Deferred Inflows of Resources:				
Deferred inflows of resources – property taxes				<u>-0-</u>
Total deferred inflows of resources	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>
Fund Balances:				
Restricted:				
Tourism		25,504		25,504
Debt Service				-0-
Construction				-0-
Assigned:				
Beach maintenance			6,617	6,617
Unassigned	<u>(136,882)</u>			<u>(136,882)</u>
Total fund balances	<u>(136,882)</u>	<u>25,504</u>	<u>6,617</u>	<u>(104,761)</u>
Total liabilities, deferred inflows of resources and fund balances	<u>\$ 33,945</u>	<u>\$ 25,504</u>	<u>\$ 6,617</u>	<u>\$ 66,066</u>

Debt Service Funds				Capital Projects Fund	Total Nonmajor Governmental Funds
Debt Service Series 2003A	Debt Service Series 2003B	Debt Service Series 2008	Total	2008 Bond Construction	
\$ 11,999	\$ 10,855	\$ 41,790	\$ 64,644	\$ 1,706	\$ 94,316
	33,398	33,983	67,381		67,381
	595	635	1,230		4,205
	280		280	52,323	23,693
<u>11,999</u>	<u>45,128</u>	<u>76,408</u>	<u>133,535</u>	<u>54,029</u>	<u>64,035</u>
			-0-		-0-
<u>\$ 11,999</u>	<u>\$ 45,128</u>	<u>\$ 76,408</u>	<u>\$ 133,535</u>	<u>\$ 54,029</u>	<u>\$ 253,630</u>
\$ 300	\$ 26,910	\$ 4,440	\$ -0-	\$	\$ 165,058
<u>300</u>	<u>26,910</u>	<u>4,440</u>	<u>31,650</u>		<u>37,419</u>
				-0-	202,477
	31,255	31,797	63,052		63,052
<u>-0-</u>	<u>31,255</u>	<u>31,797</u>	<u>53,052</u>	<u>-0-</u>	<u>63,052</u>
11,699		40,171	-0-		25,504
			51,870		51,870
			-0-	54,029	54,029
	(13,037)		-0-		6,617
<u>11,699</u>	<u>(13,037)</u>	<u>40,171</u>	<u>(13,037)</u>	<u>54,029</u>	<u>(149,919)</u>
<u>\$ 11,999</u>	<u>\$ 45,128</u>	<u>\$ 76,408</u>	<u>\$ 133,535</u>	<u>\$ 54,029</u>	<u>\$ 253,630</u>

CITY OF FREEPORT

Freeport, Texas

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES - NONMAJOR GOVERNMENTAL FUNDS

For the Year Ended September 30, 2013

	Special Revenue Funds			
	Streets, Drainage and Sidewalks	Hotel/ Motel Tax	Beach Maintenance	Total
Revenues:				
Property taxes	\$	\$	\$	\$ -0-
Hotel-motel tax		14,816		14,816
Intergovernmental revenues	439,903			439,903
Revenue producing facilities			6,617	6,617
Investment income	37	9		46
Miscellaneous				-0-
Total revenues	439,940	14,825	6,617	461,382
Expenditures:				
Current:				
Administrative		11,250		11,250
Capital outlay	672,754			672,754
Debt Service:				
Principal				-0-
Interest				-0-
Total expenditures	672,754	11,250	-0-	684,004
Excess of revenues over (under) expenditures	(232,814)	3,575	6,617	(222,622)
Other Financing Sources (Uses):				
Total other financing sources (uses)				-0-
Net changes in fund balance	(232,814)	3,575	6,617	(222,622)
Fund balance - beginning	95,932	21,929	-0-	117,861
Fund balance - ending	\$(136,882)	\$ 25,504	\$ 6,617	\$(104,761)

Debt Service Funds				Capital Projects Fund	Total Nonmajor Governmental Funds
Debt Service Series 2003A	Debt Service Series 2003B	Debt Service Series 2008	Total	2008 Bond Construction	
\$	\$ 273,210	\$ 291,942	\$ 565,152	\$	\$ 565,152
			-0-		14,816
			-0-		439,903
			-0-		6,617
17	40	40	97		143
<u>205,192</u>			<u>205,192</u>		<u>205,192</u>
<u>205,209</u>	<u>273,250</u>	<u>291,982</u>	<u>770,441</u>	<u>-0-</u>	<u>1,231,823</u>
			-0-		11,250
			-0-		672,754
150,000	205,000	200,000	555,000		555,000
<u>55,492</u>	<u>76,097</u>	<u>99,866</u>	<u>231,455</u>		<u>231,455</u>
<u>205,492</u>	<u>281,097</u>	<u>299,866</u>	<u>786,455</u>	<u>-0-</u>	<u>1,470,459</u>
<u>(283)</u>	<u>(7,847)</u>	<u>(7,884)</u>	<u>(16,014)</u>	<u>-0-</u>	<u>(238,636)</u>
			-0-		-0-
<u>(283)</u>	<u>(7,847)</u>	<u>(7,884)</u>	<u>(16,014)</u>	<u>-0-</u>	<u>(238,636)</u>
<u>11,982</u>	<u>(5,190)</u>	<u>48,055</u>	<u>54,847</u>	<u>54,029</u>	<u>226,737</u>
<u>\$ 11,699</u>	<u>\$(13,037)</u>	<u>\$ 40,171</u>	<u>\$ 38,833</u>	<u>\$ 54,029</u>	<u>\$(11,899)</u>

CITY OF FREEPORT

Freeport, Texas

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES - BUDGET AND ACTUAL
STREETS, DRAINAGE AND SIDEWALKS SPECIAL REVENUE FUND**

For the Year Ended September 30, 2013

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Intergovernmental revenues	\$	\$ 383,885	\$ 439,903	\$ 56,018
Investment income			37	37
Total revenues	-0-	383,885	439,940	56,055
Expenditures:				
Capital outlay		585,864	672,754	(86,890)
Total expenditures	-0-	585,864	672,754	(86,890)
Excess of revenues over (under) expenditures	-0-	(201,979)	(232,814)	(30,835)
Other Financing Sources (Uses):				
Total other financing sources (uses)				-0-
Net change in fund balance	-0-	(201,979)	(232,814)	(30,835)
Fund balance - beginning	95,932	95,932	95,932	-0-
Fund balance - ending	\$ 95,932	\$(106,047)	\$(136,882)	\$(30,835)

CITY OF FREEPORT

Freeport, Texas

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES - BUDGET AND ACTUAL
HOTEL/MOTEL TAX SPECIAL REVENUE FUND**

For the Year Ended September 30, 2013

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Other taxes	\$ 11,250	\$ 11,250	\$ 14,816	\$ 3,566
Investment income			9	9
Total revenues	<u>11,250</u>	<u>11,250</u>	<u>14,825</u>	<u>3,575</u>
Expenditures:				
Current:				
Administration	<u>11,250</u>	<u>11,250</u>	<u>11,250</u>	<u>-0-</u>
Total expenditures	<u>11,250</u>	<u>11,250</u>	<u>11,250</u>	<u>-0-</u>
Excess of revenues over expenditures	<u>-0-</u>	<u>-0-</u>	<u>3,575</u>	<u>3,575</u>
Other Financing Sources (Uses):				
Total other financing sources (uses)				<u>-0-</u>
Net change in fund balance	-0-	-0-	3,575	3,575
Fund balance - beginning	<u>21,929</u>	<u>21,929</u>	<u>21,929</u>	<u>-0-</u>
Fund balance - ending	<u>\$ 21,929</u>	<u>\$ 21,929</u>	<u>\$ 25,504</u>	<u>\$ 3,575</u>

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES - BUDGET AND ACTUAL
BEACH MAINTENANCE SPECIAL REVENUE FUND

For the Year Ended September 30, 2013

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Revenue producing facilities	\$ _____	\$ _____	\$ 6,617	\$ 6,617
Total revenues	-0-	-0-	6,617	6,617
Expenditures:				
Total expenditures	-0-	-0-	-0-	-0-
Excess of revenues over expenditures	-0-	-0-	6,617	6,617
Other Financing Sources (Uses):				
Total other financing sources (uses)	_____	_____	_____	-0-
Net change in fund balance	-0-	-0-	6,617	6,617
Fund balance - beginning	_____	_____	_____	-0-
Fund balance - ending	\$ <u>-0-</u>	\$ <u>-0-</u>	\$ <u>6,617</u>	\$ <u>6,617</u>

CITY OF FREEPORT

Freeport, Texas

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES - BUDGET AND ACTUAL
SERIES 2003A DEBT SERVICE FUND**

For the Year Ended September 30, 2013

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Investment income	\$	\$	\$ 17	\$ 17
Miscellaneous	<u>382,204</u>	<u>382,204</u>	<u>205,192</u>	<u>(177,012)</u>
Total revenues	<u>382,204</u>	<u>382,204</u>	<u>205,209</u>	<u>(176,995)</u>
Expenditures:				
Debt Service:				
Principal	229,648	229,648	150,000	79,648
Interest	<u>152,947</u>	<u>152,947</u>	<u>55,492</u>	<u>97,455</u>
Total expenditures	<u>382,595</u>	<u>382,595</u>	<u>205,492</u>	<u>177,103</u>
Excess of revenues over (under) expenditures	<u>(391)</u>	<u>(391)</u>	<u>(283)</u>	<u>108</u>
Other Financing Sources (Uses):				
Total other financing sources (uses)				<u>-0-</u>
Net change in fund balance	<u>(391)</u>	<u>(391)</u>	<u>(283)</u>	<u>108</u>
Fund balance - beginning	<u>11,982</u>	<u>11,982</u>	<u>11,982</u>	<u>-0-</u>
Fund balance - ending	<u>\$ 11,591</u>	<u>\$ 11,591</u>	<u>\$ 11,699</u>	<u>\$ 108</u>

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES - BUDGET AND ACTUAL
SERIES 2003B DEBT SERVICE FUND

For the Year Ended September 30, 2013

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Property taxes	\$ 280,876	\$ 280,876	\$ 273,210	\$ (7,666)
Investment income			40	40
Total revenues	<u>280,876</u>	<u>280,876</u>	<u>273,250</u>	<u>(7,626)</u>
Expenditures:				
Debt Service:				
Principal	205,000	205,000	205,000	-0-
Interest	<u>75,876</u>	<u>75,876</u>	<u>76,097</u>	<u>(221)</u>
Total expenditures	<u>280,876</u>	<u>280,876</u>	<u>281,097</u>	<u>(221)</u>
Excess of revenues over (under) expenditures	<u>-0-</u>	<u>-0-</u>	<u>(7,847)</u>	<u>(7,847)</u>
Other Financing Sources (Uses):				
Total other financing sources (uses)				<u>-0-</u>
Net change in fund balance	-0-	-0-	(7,847)	(7,847)
Fund balance - beginning	<u>(5,190)</u>	<u>(5,190)</u>	<u>(5,190)</u>	<u>-0-</u>
Fund balance - ending	<u><u>\$(5,190)</u></u>	<u><u>\$(5,190)</u></u>	<u><u>\$(13,037)</u></u>	<u><u>\$(7,847)</u></u>

CITY OF FREEPORT

Freeport, Texas

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES - BUDGET AND ACTUAL
SERIES 2008 DEBT SERVICE FUND**

For the Year Ended September 30, 2013

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Property taxes	\$ 300,166	\$ 300,166	\$ 291,942	\$(8,224)
Investment income			40	40
Total revenues	<u>300,166</u>	<u>300,166</u>	<u>291,982</u>	<u>(8,184)</u>
Expenditures:				
Debt Service:				
Principal	200,000	200,000	200,000	-0-
Interest	<u>100,166</u>	<u>100,166</u>	<u>99,866</u>	<u>300</u>
Total expenditures	<u>300,166</u>	<u>300,166</u>	<u>299,866</u>	<u>300</u>
Excess of revenues over (under) expenditures	<u>-0-</u>	<u>-0-</u>	<u>(7,884)</u>	<u>(7,884)</u>
Other Financing Sources (Uses):				
Total other financing sources (uses)				<u>-0-</u>
Net change in fund balance	-0-	-0-	(7,884)	(7,884)
Fund balance - beginning	<u>48,055</u>	<u>48,055</u>	<u>48,055</u>	<u>-0-</u>
Fund balance - ending	<u>\$ 48,055</u>	<u>\$ 48,055</u>	<u>\$ 40,171</u>	<u>\$(7,884)</u>

CITY OF FREEPORT

Freeport, Texas

SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN NET POSITION - BUDGET AND ACTUAL WATER AND SEWER ENTERPRISE FUND

For the Year Ended September 30, 2013

	Budgeted Amounts		Actual GAAP Basis	Adjustments to Budgetary Basis
	Original	Final		
Operating Revenues:				
Water service	\$ 2,285,000	\$ 2,285,000	\$ 2,228,199	\$
Sewer service	1,340,000	1,340,000	1,248,148	
Charges for other services	69,536	69,536	61,912	
Miscellaneous	10,900	10,900	12,143	
Total operating revenues	<u>3,705,436</u>	<u>3,705,436</u>	<u>3,550,402</u>	<u>-0-</u>
Operating Expenses:				
Personnel services	76,719	76,919	62,790	
Employee benefits	27,576	27,576	25,069	
Contract and professional services	2,182,494	2,209,382	2,186,205	
Other operating costs	23,500	23,500	68,308	
Supplies			10,414	
Cost of sales	1,314,988	1,350,500	1,349,656	
Operating expenses before depreciation	<u>3,625,477</u>	<u>3,687,877</u>	<u>3,702,442</u>	<u>-0-</u>
Depreciation			304,975	(304,975)
Total operating expenses	<u>3,625,477</u>	<u>3,687,877</u>	<u>4,007,417</u>	<u>(304,975)</u>
Net operating income (loss)	<u>79,959</u>	<u>17,559</u>	<u>(457,015)</u>	<u>304,975</u>
Non-Operating Revenues (Expenses):				
Interest revenue	10	10	22	
Capital outlay	(55,000)	(55,000)		(76,100)
Debt principal	(215,000)	(215,000)		(215,000)
Interest expense and agent fees	(27,969)	(27,969)	(23,372)	
Total non-operating revenues (expenses)	<u>(297,959)</u>	<u>(297,959)</u>	<u>(23,350)</u>	<u>(291,100)</u>
Net income (loss) before contributions and operating transfers	<u>(218,000)</u>	<u>(280,400)</u>	<u>(480,365)</u>	<u>13,875</u>
Contribution (capital)			285,053	(285,053)
Transfers in	218,000	280,400	280,400	-0-
Change in net position	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ 85,088</u>	<u>\$ (271,178)</u>

Actual Budgetary Basis	Variance on Final Budget - Positive (Negative)
\$ 2,228,199	\$(56,801)
1,248,148	(91,852)
61,912	(7,624)
<u>12,143</u>	<u>1,243</u>
<u>3,550,402</u>	<u>(155,034)</u>
62,790	14,129
25,069	2,507
2,186,205	23,177
68,308	(44,808)
10,414	(10,414)
<u>1,349,656</u>	<u>844</u>
3,702,442	(14,565)
<u> </u>	<u>-0-</u>
<u>3,702,442</u>	<u>(14,565)</u>
<u>(152,040)</u>	<u>(169,599)</u>
22	12
(76,100)	(21,100)
(215,000)	-0-
<u>(23,372)</u>	<u>4,597</u>
<u>(314,450)</u>	<u>(16,491)</u>
(466,490)	(186,090)
-0-	-0-
<u>280,400</u>	<u>-0-</u>
<u>\$(186,090)</u>	<u>\$(186,090)</u>

CITY OF FREEPORT

Freeport, Texas

SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL GOLF COURSE ENTERPRISE FUND

For the Year Ended September 30, 2013

	Budgeted Amounts		Actual GAAP Basis	Adjustments to Budgetary Basis
	Original	Final		
Operating Revenues:				
Golf course fees and charges	\$ 595,150	\$ 595,150	\$ 524,578	\$
Total operating revenues	595,150	595,150	524,578	-0-
Operating Expenses:				
Personnel services	330,283	330,283	295,302	
Employee benefits	127,151	127,151	117,242	
Contract and professional services	73,850	73,850	78,884	
Supplies	51,750	51,750	47,453	
Cost of sales and services	136,500	136,500	133,910	
Operating expenses before depreciation	719,534	719,534	672,791	-0-
Depreciation			87,690	(87,690)
Total operating expenses	719,534	719,534	760,481	(87,690)
Net operating income (loss)	(124,384)	(124,384)	(235,903)	87,690
Non-Operating Revenues (Expenses):				
Interest revenue			2	
Lease principal	(27,291)	(265,031)		(48,023)
Interest expense and agent fees		(7,060)	(7,060)	
Total non-operating revenues (expenses)	(27,291)	(272,091)	(7,058)	(48,023)
Net income (loss) before operating transfers	(151,675)	(396,475)	(242,961)	39,667
Transfers in (out)	151,675	151,675	151,675	
Change in net position	-0-	\$(244,800)	\$(91,286)	\$ 39,667

Actual Budgetary Basis	Variance on Final Budget - Positive (Negative)
\$ <u>524,578</u>	\$ (<u>70,572</u>)
<u>524,578</u>	(<u>70,572</u>)
295,302	34,981
117,242	9,909
78,884	(5,034)
47,453	4,297
<u>133,910</u>	<u>2,590</u>
672,791	46,743
<u>672,791</u>	<u>-0-</u>
(<u>148,213</u>)	(<u>23,829</u>)
2	2
(48,023)	217,008
(<u>7,060</u>)	<u>-0-</u>
(<u>55,081</u>)	<u>217,010</u>
(203,294)	193,181
<u>151,675</u>	<u>-0-</u>
\$ (<u>51,619</u>)	\$ <u>193,181</u>

CITY OF FREEPORT

Freeport, Texas

SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL AMBULANCE ENTERPRISE FUND

For the Year Ended September 30, 2013

	Budgeted Amounts		Actual GAAP Basis	Adjustments to Budgetary Basis
	Original	Final		
Operating Revenues:				
Charges for other services	\$ 585,039	\$ 585,039	\$ 542,224	\$
Miscellaneous	<u>86,500</u>	<u>86,500</u>	<u>86,910</u>	<u> </u>
Total operating revenues	<u>671,539</u>	<u>671,539</u>	<u>629,134</u>	<u>-0-</u>
Operating Expenses:				
Personnel services	404,602	404,602	378,830	
Employee benefits	139,761	139,761	137,193	
Other operating	71,500	71,500	67,625	
Supplies	<u>57,000</u>	<u>57,000</u>	<u>52,799</u>	<u> </u>
Operating expenses before depreciation	672,863	672,863	636,447	-0-
Depreciation	<u> </u>	<u> </u>	<u>45,334</u>	<u>(45,334)</u>
Total operating expenses	<u>672,863</u>	<u>672,863</u>	<u>681,781</u>	<u>(45,334)</u>
Net operating income (loss)	<u>(1,324)</u>	<u>(1,324)</u>	<u>(52,647)</u>	<u>45,334</u>
Non-Operating Revenues (Expenses):				
Interest revenue	10	10	55	
Capital outlay	<u>(70,000)</u>	<u>(177,024)</u>	<u> </u>	<u>(185,903)</u>
Total non-operating revenues (expenses)	<u>(69,990)</u>	<u>(177,014)</u>	<u>55</u>	<u>(185,903)</u>
Net income (loss) before operating transfers	(71,314)	(178,338)	(52,592)	(140,569)
Transfers in	<u>71,314</u>	<u>71,314</u>	<u>71,314</u>	<u> </u>
Change in net position	<u>\$ -0-</u>	<u>\$ (107,024)</u>	<u>\$ 18,722</u>	<u>\$ (140,569)</u>

Actual Budgetary Basis	Variance on Final Budget - Positive (Negative)
\$ 542,224	\$(42,815)
<u>86,910</u>	<u>410</u>
629,134	(42,405)
378,830	25,772
137,193	2,568
67,625	3,875
<u>52,799</u>	<u>4,201</u>
636,447	36,416
<u> </u>	<u>-0-</u>
<u>636,447</u>	<u>36,416</u>
(7,313)	(5,989)
55	45
(185,903)	(8,879)
(185,848)	(8,834)
(193,161)	(14,823)
<u>71,314</u>	<u>-0-</u>
<u>\$(121,847)</u>	<u>\$(14,823)</u>

CITY OF FREEPORT

Freeport, Texas

SCHEDULE OF AD VALOREM TAX LEVY AND COLLECTIONS

September 30, 2013

Levy Year	Balance 10-01-12	Current Year Levy	Collections	Adjustments	Balance 09-30-13
2003 & Prior	\$ 47,219	\$	\$ 1,871	\$(11,512)	\$ 33,836
2004	9,000		326	(278)	8,396
2005	7,927		492	(271)	7,164
2006	8,695		764	(124)	7,807
2007	11,199		1,337	(131)	9,731
2008	11,844		3,097	(183)	8,564
2009	19,267		7,790	(171)	11,306
2010	42,012		18,681	(4,952)	18,379
2011	156,801		47,957	(5,188)	103,656
2012	<u> </u>	<u>2,395,772</u>	<u>2,240,087</u>	<u> </u>	<u>155,685</u>
	<u>\$ 313,964</u>	<u>\$ 2,395,772</u>	<u>\$ 2,322,402</u>	<u>\$(22,810)</u>	364,524
Less reserve for uncollectible taxes					<u>54,945</u>
Net delinquent ad valorem taxes receivable					<u>\$ 309,579</u>

CITY OF FREEPORT

Freeport, Texas

DEBT SERVICE REQUIREMENTS TO MATURITY CERTIFICATES OF OBLIGATION BONDS

September 30, 2013

(Unaudited)

Year Ending 09-30	\$ 3,000,000 Series 2003		\$ 2,185,000 Series 2003		\$ 3,350,000 Series 2008		Total Principal & Interest
	Principal	Interest	Principal	Interest	Principal	Interest	
2014	\$ 215,000	\$ 65,413	\$ 157,000	\$ 47,601	\$ 205,000	\$ 92,287	782,301
2015	226,000	54,740	164,000	39,833	215,000	84,517	784,090
2016	237,000	43,536	172,000	31,702	220,000	76,368	780,606
2017	248,000	31,799	181,000	23,159	230,000	68,031	781,989
2018	260,000	19,505	189,000	14,205	240,000	59,313	782,023
2019	273,000	6,607	199,000	4,816	245,000	50,217	778,640
2020					255,000	40,932	295,932
2021					265,000	31,268	296,268
2022					275,000	21,224	296,224
2023					285,000	10,802	295,802
TOTAL	\$ 1,459,000	\$ 221,600	\$ 1,062,000	\$ 161,316	\$ 2,435,000	\$ 534,959	\$ 5,873,875

CITY OF FREEPORT

Freeport, Texas

**DEBT SERVICE REQUIREMENTS TO MATURITY
REVENUE BONDS**

September 30, 2013
(Unaudited)

Year Ending 09/30	\$ 1,943,000 Series 2004		Total Principal & Interest
	Principal	Interest	
2014	\$ 228,000	\$ 16,926	\$ 244,926
2015	235,000	5,699	240,699
2016			
2017			
2018			
2019			
2020			
2021			
2022			
2023			
TOTAL	<u>\$ 463,000</u>	<u>\$ 22,625</u>	<u>\$ 485,625</u>

FEDERAL AWARD SECTION

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Kennemer, Masters & Lunsford

CERTIFIED PUBLIC ACCOUNTANTS

Limited Liability Company

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Lake Jackson, Texas 77566

El Campo Office:
201 W. Webb
El Campo, Texas 77437

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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 Major, City Council, and Management
City of Freeport
Freeport, Texas 77531

We have audited, in accordance with the 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, the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Freeport (the "City"), Texas, as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise the City's basic financial statements and have issued our report thereon dated June 23, 2014.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be material weaknesses. See finding reference numbers 2013-001, 2013-002, 2013-003, and 2013-004.

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Honorable Major, City Council,
and Management
City of Freeport
Page 2

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from 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 an instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of findings and questioned costs as item 2013-005.

City of Freeport, Texas's Response to Findings

The City's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The City's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Kennemer, Masters & Hunzford, LLC

Certified Public Accountants
Lake Jackson, Texas
June 23, 2014

Kennemer, Masters & Lunsford

CERTIFIED PUBLIC ACCOUNTANTS
Limited Liability Company

Lake Jackson Office:
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Independent Auditor's Report
On Compliance for Each Major Program and on Internal Control Over
Compliance Required by OMB Circular A-133

To the Honorable Major, City
Council and Management
City of Freeport
Freeport, Texas 77531

Report on Compliance for Each Major Federal Program

We have audited the City of Freeport (the "City"), Texas's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended September 30, 2013. The City's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the City's compliance.

Opinion on Each Major Federal Program

In our opinion, the City, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended September 30, 2013.

Report on Internal Control over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on

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Honorable Major, City
Council and Management
City of Freeport
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Report on Internal Control over Compliance - Continued

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

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be a material weakness and significant deficiency.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 2013-001, 2013-002, 2013-003 and 2013-004 to be material weaknesses.

The City's response to the internal control over compliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The City's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Kennemer, Masters & Kingford, LLC

Certified Public Accountants
Lake Jackson, Texas 77566
June 23, 2014

I. Summary of Auditor's Results

1. Type of auditor's report issued on the financial statements: Unmodified.
2. Four (4) significant internal control deficiencies, which were considered a material weakness that is required to be reported in this schedule, were disclosed in the audit of the financial statements.
3. Noncompliance, which is material to the financial statements: None.
4. Four (4) internal control deficiencies that are required to be reported in this schedule were disclosed in the audit of major programs.
5. Type of auditor's report on compliance for major programs: Unmodified.
6. Did the audit disclose findings, which are required to be reported under Sec. 5 I O (a): No.
7. Major Programs Include:
Federal:
 - Community Development Block Grant – CFDA #14.228
 - Port Security Grant – CFDA #97.056
8. Dollar threshold used to distinguish between Type A and Type B programs: \$ 300,000.
9. Low Risk Auditee: No.

II. Findings related to the financial statements

1. Schedule reference number 2013-001; Balance Sheet Year-end Accruals - Numerous year-end accruals were not accurately recorded requiring recommended audit adjustments (accepted by the City) to ensure the financial statements were fairly presented for the year ended September 30, 2013.

Criteria: Generally accepted accounting principles require the City to accrue receivables and related revenues, and accounts payable and accrued liabilities and related expenditures and expenses, both during the year and at year-end.

Condition: During our audit procedures we performed tests of the year-end accruals as of September 30, 2013 and determined that audit adjustments were required to present fairly stated financial statements.

Effect: Due to the significance of audit accrual adjustments, this control deficiency was considered to be material to the financial statements.

Cause: These circumstances stem from the lack of time as prioritized by the City's accounting staff to accurately record year-end accruals.

Recommendations: The City accounting personnel should review its accounting duties as well as its resources and adjust its priorities to ensure that year-end accruals are made, and that the financial statements will be fairly presented without significant audit adjustments.

II. Findings related to the financial statements - Continued

1. Schedule reference number 2013-001; Balance Sheet Year-end Accruals - Continued

Questioned Cost/Basis: None.

2. Schedule reference number 2013-002; Grant Accounting for Revenues and Expenditures/Expenses at Gross – Grant revenue and expenditure/expense accounts were netted and failed to accurately report the grant revenue and expenditures/expenses.

Criteria: Generally accepted accounting principles require the City to record grant revenues and expenditures/expenses at gross. Grant revenue and expenditure/expense accounts were netted and failed to accurately report the grant revenue and expenditures/expenses.

Condition: During our audit procedures we performed reconciliations and tests of grant receipts and disbursements and determined that revenues were netted with expenditures/expenses and vice versa, and required significant audit adjustments (accepted by the City) to correct.

Effect: Due to the significance of audit accrual adjustments, this control deficiency was considered to be material to the financial statements.

Cause: These circumstances stem from the lack internal control over grant accounting as well as training of the City's accounting staff to accurately record grant transactions.

Recommendations: Controls over grant accounting should be reviewed and adjusted to ensure grant revenues and expenditures/expenses are properly recorded at gross.

Questioned Cost/Basis: None.

3. Schedule reference number 2013-003; Purchasing Bid Requirements. The City failed to obtain competitive bids in three of thirty-one vendors (twelve requiring competitive bid) with expenditures/expenses in excess of \$ 50,000, as follows: 1) The City contracted a single vendor for the purchase of gasoline and diesel, with expenditures/expenses totaling \$ 239,396, and was unaware that this product required competitive bidding, although the City acquired quotes for each purchase; 2) the City acquired \$ 54,000 and \$ 50,578 in products (consistently the same in nature) from two vendors, that had not exceeded the \$ 50,000 in the previous years. All expenditures/expenses related to federal financial assistance programs were bid appropriately.

Criteria: State and local policies require the City to bid expenditures/expenses that exceed \$ 50,000 individually and in the aggregate, assuming a homogeneous product, acquired during the City's fiscal year.

Criteria: Procedures should be established to identify purchases that require competitive bidding, including cumulative projects.

II. Findings related to the financial statements – Continued

3, Schedule reference number 2013-003: Purchasing Bid Requirements – Continued.

Instances/universe: These bidding violations were noted during the testing of internal controls over purchasing.

Effect: The City failed to comply with its purchasing policy and that of the State.

Recommendation: We recommend that the City evaluate its control procedures for identifying purchases that require competitive bidding. A procedure should be established to prevent multiple purchases, each under the bid limit, from cumulatively exceeding the bid limit. Each year a listing of vendors with purchases over the \$ 50,000 limit should be reviewed to identify those that may require bidding in future periods.

Questioned Cost/Basis: None.

4. Schedule reference number 2013-004; Cash Disbursement and Purchasing Requirements. The City failed to comply with the City's internal control procedures over cash disbursements and purchasing in the following areas (based upon a tests of controls of forty transactions) as follows: 1) One invoice failed to match the check number; 2) five purchase orders approvals were noted as verbal and lacked the required authorization documentation required by policy, and 3) three transactions were incorrectly coded and required adjustment. None of these expenditures/expenses were charged to a federal financial assistance program.

Criteria: Generally accepted accounting principles require the City to maintain internal controls over cash disbursements and purchasing to ensure the accuracy of the related financial statements.

Criteria: Verification that cash disbursement and purchasing procedures be followed to ensure the accuracy of the City's financial statements.

Instances/universe: These cash disbursement and purchasing violations were noted during the testing of internal controls over cash disbursement and purchasing.

Effect: The City failed to comply with its cash disbursement and purchasing policy.

Recommendation: We recommend that the City evaluate its review and authorization of cash disbursement and purchasing procedures. All City personnel should be aware of the cash disbursement and purchasing procedures and the importance for compliance. The City should review its procedures for verifying and approving cash disbursement and purchasing in accordance with City policy.

II. Findings related to the financial statements - Continued

5. Schedule reference number 2013-005; The City's investment officer failed to obtain the training required by the Public Funds Investment Act ("PFIA").

Criteria: The PFIA requires that governmental investment officers obtain ten (10) hours every two years to maintain the knowledge required to comply with the PFIA.

Condition: During our audit procedures to test compliance with the PFIA we noted that the City's Investment Officer failed to obtain the necessary hours required to comply with the PFIA.

Effect: In not obtaining the necessary training, the City has not complied with all parts of the PFIA.

Cause: This circumstance appears to be an oversight on the part of the City's investment officer. The City only invests in a public investment pool (Texpool) and has performed other required functions of the PFIA.

Recommendations: The City's investment officer should schedule the required training as soon as possible and schedule future requirements in advance to ensure compliance with the PFIA.

Questioned Cost/Basis: None.

III. Findings and questioned costs related to the federal awards.

1. Schedule reference number 2013-001; (Both the Community Development Block Grant, CFDA #14.228, and the Port Security Grant, CFDA #97.056) Balance sheet year-end accruals.

See Finding in Section II above.

2. Schedule reference number 2013-002, (Both the Community Development Block Grant, CFDA #14.228, and the Port Security Grant, CFDA #97.056) Grant accounting for revenues and expenditures/expenses at gross.

See Finding in Section II above.

3. Schedule reference number 2013-003, (Both the Community Development Block Grant, CFDA #14.228, and the Port Security Grant, CFDA #97.056) Purchasing Bid Requirements.

See Finding in Section II above.

4. Schedule reference number 2013-004, (Both the Community Development Block Grant, CFDA #14.228, and the Port Security Grant, CFDA #97.056) Cash Disbursement and Purchasing Requirements.

See Finding in Section II above.

CITY OF FREEPORT
SCHEDULE OF STATUS OF PRIOR FINDINGS
FOR THE YEAR ENDED SEPTEMBER 30, 2013

None.

1. Schedule reference number 2013-001; balance sheet year-end accruals.

Corrective Action Planned: The City accounting department personnel plan to review its accounting duties as well as its resources and training to determine if changes in its procedures and priorities are necessary to accomplish the performance of year-end accruals in the future. The Finance Director will monitor the implementation of this corrective action and appropriately report to the City Manager.

2. Schedule reference number 2013-002; Grant accounting for revenues and expenditures/expenses at gross.

Corrective Action Planned: The City's accounting department personnel plan to review its accounting duties as well as its resources and training to determine if changes in its procedures and priorities are necessary to accomplish accurate accounting for grants in the future. The Finance Director will monitor the implementation of this corrective action and appropriately report to the City Manager.

3. Schedule reference number 2013-003; Purchasing Bid Requirements.

Corrective Action Planned: The City's accounting department personnel plan to review the City's and State's purchasing bid requirements as well as its resources and training to determine if changes in its procedures and priorities are necessary to obtain competitive bids on all required purchases. The Finance Director will monitor the implementation of this corrective action and appropriately report to the City Manager.

4. Schedule reference number 2013-004; Cash Disbursement and Purchasing Requirements.

Corrective Action Planned: The City's accounting department personnel plan to review the City's cash disbursement purchasing requirements as well as its resources and training to determine if changes in its procedures and priorities are necessary to maintain internal controls for all cash disbursements and purchases. The Finance Director will monitor the implementation of this corrective action and appropriately report to the City Manager.

5. Schedule reference number 2013-005; The City's investment officer failed to obtain the training required by the Public Funds Investment Act ("PFIA").

Corrective Action Planned: The City's investment officer plans to obtain the required PFIA training and will schedule such training for future periods. The Finance Director will monitor the implementation of this corrective action and appropriately report to the City Manager.

CITY OF FREEPORT**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED AUGUST 31, 2013**

Federal Grantor/ Pass-Through Grantor/ Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Pass-Through Disbursements and Expenditures
U.S. Department of Transportation:			
Passed Through Texas Parks and Wildlife:			
Recreational Trails Program – Freeport Wetlands Recreational Trails	20.219	RT1008	\$ <u>27,543</u>
TOTAL U.S. DEPARTMENT OF TRANSPORTATION			\$ <u><u>27,543</u></u>
U.S. Department of Housing and Urban Development			
Passed Through Texas General Land Office:			
Community Development Block Grant – Disaster Recovery Program – Program 2.1 (1)	14.228	12-215-000-5515	\$ <u>439,903</u>
Passed Through Brazoria County, Texas:			
Community Development Block Grant –			
Freeport Lift Station Improvements	14.218	B-10-UC-48-0005	189,101
Freeport Sewer Study and Sewer Line Replacements	14.218	B-12-UC-48-0005	<u>95,952</u>
			<u>285,053</u>
TOTAL U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT			\$ <u><u>724,956</u></u>
U.S. Department of Justice:			
Direct:			
Edward Byrne Memorial Justice Assistance – Radio Console Upgrade and Interoperability Improvements	16.738	DJ2545001	\$ <u>34,398</u>
TOTAL U.S. DEPARTMENT OF JUSTICE			\$ <u><u>34,398</u></u>
U.S. Department of Homeland Security:			
Passed Through Port Freeport, Texas:			
Port Security Grant – Freeport Police Department Surveillance (1)	97.052	2008-GB-T8-H056	\$ <u>469,290</u>
TOTAL U.S. DEPARTMENT OF HOMELAND SECURITY			\$ <u><u>469,290</u></u>
TOTAL FEDERAL ASSISTANCE			\$ <u><u>1,256,187</u></u>
TOTAL MAJOR PROGRAMS			\$ <u><u>909,193</u></u>
TYPE A PROGRAM			\$ <u><u>300,000</u></u>

(1) – Major Programs

CITY OF FREEPORT

NOTES ON ACCOUNTING POLICIES FOR FEDERAL AWARDS

Year Ended September 30, 2013

1. The City uses funds and account groups to report its financial position and the results of its operations. Fund accounting is designated to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts. An account group, on the other hand, is a financial reporting device designated to provide accountability for certain assets and deferred outflows of resources, and liabilities and deferred inflows of resources that are not recorded in the funds because they do not directly affect net expendable available resources. Funds are classified into three categories: governmental, proprietary, and fiduciary. Each category, in turn is divided into separate "fund types". The following fund types were utilized to account for federal awards.

Governmental Fund Types:

General Fund - is the general operating fund of the City. All financial resources, except those required to be accounted for in another fund, are accounted for in the General Fund. Federal financial assistance not required to be reported in other funds is accounted for in the General Fund.

Special Revenue Funds - used to account for proceeds of specific revenue sources that are legally restricted to expenditures for specific purposes. Federal financial assistance generally is accounted for in a Special Revenue Fund unless required to be reported in a Capital Projects Fund or a proprietary fund type. Generally, unused balances are returned to the grantor at the close of specified project periods.

Proprietary Fund Types:

Enterprise Fund - used to account for activities similar to those found in the private business enterprises, where the intent of the governing body is that costs (expenses, including depreciation) of providing services be financed primarily through user charges, or where periodic determination of net income is appropriate. Federal financial assistance for the benefiting enterprise operations generally is accounted for in the Enterprise Fund. Generally, unused balances are returned to the grantor at the close of specified project periods.

2. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The Governmental Fund types are accounted for using a current financial resources measurement focus. With this measurement focus, only current assets and deferred outflows of resources, and current liabilities and deferred inflows of resources generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in fund balance. Federal and State grant funds were accounted for in the General Fund and Special Revenue Fund, a component of the Governmental Fund type.

CITY OF FREEPORT

NOTES ON ACCOUNTING POLICIES FOR FEDERAL AWARDS - Continued

Year Ended September 30, 2013

2. Continued

The Proprietary Fund Types are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and deferred outflows of resources, and all liabilities and deferred inflows of resources associated with the operation of these funds are included on the balance sheet. Fund equity (total net position) is segregated into contributed capital and retained earnings components for proprietary funds. Proprietary fund type operating statements present increases (revenues) and decreases (expenses) in total net position. Federal grant funds were accounted for in the Enterprise Fund, a component of the Proprietary Fund type.

The modified accrual basis of accounting is used for the Governmental Fund Types. This basis of accounting recognizes revenues in the accounting period in which they become susceptible to accrual, i.e., both measurable and available, and expenditures in the accounting period in which the fund liability is incurred, if measurable, except for unmatured interest on General Long-Term Debt, which is recognized when due, and certain compensated absences and claims and judgments, which are recognized when the obligations are expected to be liquidated with expendable available financial resources.

The accrual basis of accounting is used for the Proprietary Fund Types. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Federal grant funds are considered to be earned to the extent of expenditures/expenses made under the provisions of the grant, and, accordingly, when such funds are received, they are recorded as Unearned revenues until earned.

3. The period of availability for state grant funds for the purpose of liquidation of outstanding obligations made on or before the ending date of the federal project period extended 30 days beyond the federal project period ending date, in accordance with provisions in Section H, Period of Availability of Federal Funds, Part 3, OMB Circular A-133 Compliance Supplement.

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