

CITY OF ELKHART, TEXAS
AUDITED FINANCIAL STATEMENTS
AND REPORTS ON COMPLIANCE
SEPTEMBER 30, 2014

INTRODUCTORY SECTION

**CITY OF ELKHART, TEXAS
TABLE OF CONTENTS**

| | PAGE NO. |
|---|----------|
| INTRODUCTORY SECTION | |
| Table of Contents | 1-2 |
| Principal City Officials..... | 3 |
| FINANCIAL SECTION | |
| Independent Auditors' Report | 5-6 |
| Management's Discussion and Analysis (unaudited)..... | 7-12 |
| Basic Financial Statements | |
| Government-wide Financial Statements | |
| Statement of Net Position | 15 |
| Statement of Activities | 16 |
| Fund Financial Statements | |
| Balance Sheet – Governmental Funds..... | 18 |
| Reconciliation of the Balance Sheet – Governmental Funds to the Statement of Net Position..... | 19 |
| Statement of Revenues, Expenditures, and Changes in Fund Balance – Governmental Funds..... | 20 |
| Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balance – Governmental Funds to the Statement of Activities..... | 21 |
| Statement of Net Position – Proprietary Funds | 22 |
| Statement of Revenues, Expenses, and Changes in Fund Net Position – Proprietary Funds..... | 23 |
| Statement of Cash Flows – Utility Fund | 24 |
| Notes to the Financial Statements..... | 25-40 |
| Required Supplementary Information (unaudited) | |
| Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual – General Fund | 42 |
| Schedule of Funding Progress of Pension Plan – Texas Municipal Retirement System..... | 43 |
| Combining Statements | |
| Combining Balance Sheet – Nonmajor Governmental Funds | 45 |
| Combining Statement of Revenues, Expenditures, and Changes in Fund Balance – Nonmajor Governmental Funds | 46 |

**CITY OF ELKHART, TEXAS
TABLE OF CONTENTS**

| | PAGE NO. |
|---|----------|
| COMPLIANCE SECTION | |
| Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Governmental Auditing Standards</i> | 48-49 |
| Independent Auditors' Report on Compliance for Each Major Program and on Internal Control over Compliance Required by OMB Circular A-133 | 50-51 |
| Schedule of Expenditures of Federal Awards | 52 |
| Notes to the Schedule of Expenditures of Federal Awards | 53 |
| Schedule of Findings and Questioned Costs | |
| Section I – Summary of Auditors' Results | 54 |
| Section II – Financial Statements Audit Findings | 55 |
| Section III – Major Federal Award Programs Audit Findings and Questioned Costs | 56-57 |
| Summary Schedule of Prior Audit Findings | 58 |

**CITY OF ELKHART, TEXAS
PRINCIPAL CITY OFFICIALS
SEPTEMBER 30, 2014**

Honorable Raymond DunlapMayor
Randy McCoyMayor Pro Tem
Karen Bridges Councilmember
Lucia Butler Councilmember
Billy Jack Wright Councilmember
Erroll Tatum..... Councilmember
Jan Stuteville..... City Secretary

FINANCIAL SECTION

Todd, Hamaker & Johnson, LLP

CERTIFIED PUBLIC ACCOUNTANTS

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

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

INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and Members of the City Council
City of Elkhart, Texas

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Elkhart, Texas, (the "City") as of and for the year ended September 30, 2014, 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.

Auditors' 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 auditors' 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.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Elkhart, Texas, as of September 30, 2014, 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.

INDEPENDENT AUDITORS' REPORT – CONTINUED

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison information, and schedule of funding progress of pension plan on pages 7 – 12 and 42 – 43, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate 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 combining nonmajor fund financial statements 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 combining nonmajor fund financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the 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 combining nonmajor fund financial statements 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.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated January 30, 2015, 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 the City's internal control over financial reporting and compliance.

Todd, Hamaker & Johnson, LLP

Todd, Hamaker & Johnson, LLP
Lufkin, Texas

January 30, 2015

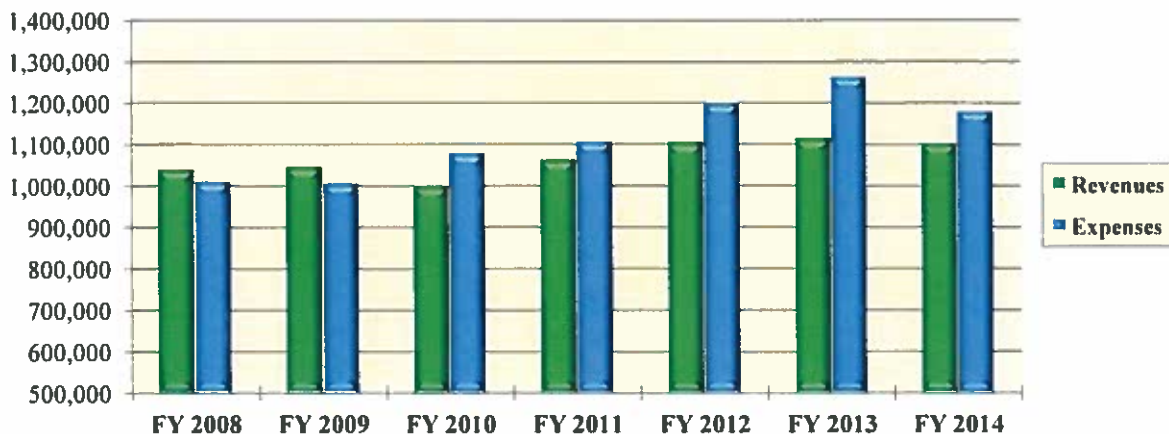
**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2014
(UNAUDITED)**

As management of City of Elkhart, Texas (the City), we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended September 30, 2014. We encourage readers to consider information presented here as well as the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The overall assets of the City increased by \$528,319 during the fiscal year. Cash and other current assets increased by \$23,892; capital assets increased by \$504,427.
- The City's total long-term debt obligations decreased by \$78,943 during the current fiscal year. Total debt outstanding at year end was \$719,060; \$660,000 in bond obligations and \$59,060 in notes payable and capital lease obligations. New debt in the amount of \$27,310 was incurred during the year for the purchase of tractor.
- The City's overall assets exceeded its total liabilities by \$2,991,329 (*net position*) at September 30, 2014. Of this amount, \$295,900 (*unrestricted net position*) may be used to meet the on-going obligations to citizens and creditors.
- Excluding grant revenues received, overall revenues decreased by \$13,032 from the prior year. Decreases in sales tax revenues accounted for the majority of the change.
- Excluding grant expenditures, overall expenses decreased by \$83,396 from the prior year. Major contributors to the reduction were decreases in personnel and related costs and street maintenance.
- Overall revenues exceeded expenses (or an increase in net position) by \$571,193. Net position increased by \$613,262 in the governmental fund and decreased by \$42,069 in the proprietary fund.

**Total Revenues and Expenses
(Excluding Grants)
Governmental and Business-type Activities**



**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2014
(UNAUDITED)**

OVERVIEW OF THE FINANCIAL STATEMENTS

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

Government-wide Financial Statements. The *government-wide financial statements*, which begin on page 14 of this report, are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

The *statement of net position* presents information on all of the City's assets and liabilities, 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. Revenues are recorded when earned and expenses are recorded when the liability is incurred, regardless of the timing of related cash flows.

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

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Revenues are recognized when they are both measurable and available. Expenditures are recorded when the related fund liability is incurred, except for general obligation bond principal and interest, which are reported as expenditures in the year due.

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

The basic governmental and proprietary fund financial statements can be found on pages 18 - 24 of this report.

Notes to the Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 25 - 40 of this report.

**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2014
(UNAUDITED)**

THE CITY'S NET POSITION

Over time, net position may serve as a useful indicator of a government's financial position. At September 30, 2014, the City's assets exceeded its liabilities by \$2,991,329.

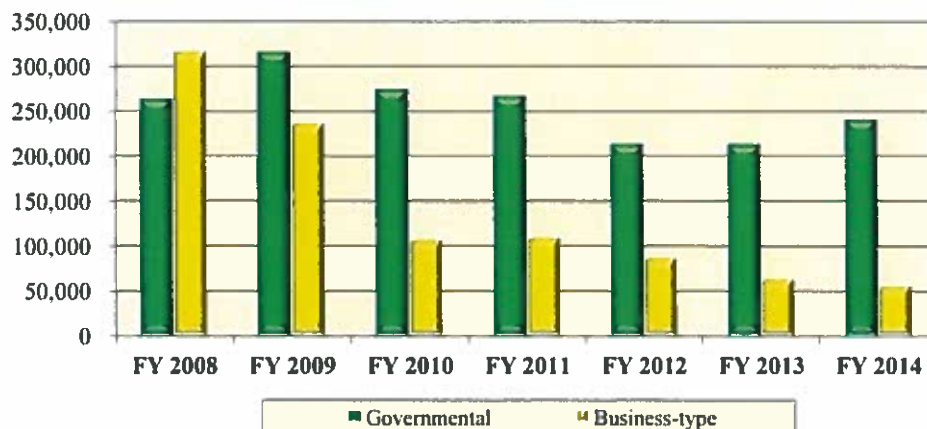
The City has a large investment in capital assets (e.g., land, buildings, equipment, and construction in progress) and related debt used to acquire those assets that remains outstanding. The City uses these capital assets to provide services to citizens; consequently, these assets are not available for 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. At year end, net position invested in capital assets, net of related debt, totaled \$2,679,633.

An additional portion of the City's net position, \$15,796, represents resources that are subject to external restriction on how they may be used. The remaining balance is \$295,900 and unrestricted in nature.

The City's Net Position

| | <u>Governmental Activities</u> | | <u>Business-type Activities</u> | | <u>Total</u> | |
|--|--------------------------------|---------------------|---------------------------------|---------------------|---------------------|---------------------|
| | 2014 | 2013 | 2014 | 2013 | 2014 | 2013 |
| Current and other assets | \$ 300,736 | \$ 274,237 | \$ 189,552 | \$ 192,159 | \$ 490,288 | \$ 466,396 |
| Capital assets | 819,284 | 217,710 | 2,579,409 | 2,676,556 | 3,398,693 | 2,894,266 |
| Total assets | <u>1,120,020</u> | <u>491,947</u> | <u>2,768,961</u> | <u>2,868,715</u> | <u>3,888,981</u> | <u>3,360,662</u> |
| Long-term liabilities | 683,915 | 700,000 | 35,145 | 98,003 | 719,060 | 798,003 |
| Other liabilities | 44,544 | 13,648 | 134,048 | 128,875 | 178,592 | 142,523 |
| Total liabilities | <u>728,459</u> | <u>713,648</u> | <u>169,193</u> | <u>226,878</u> | <u>897,652</u> | <u>940,526</u> |
| Net position | | | | | | |
| Invested in capital assets, net of related debt | 135,369 | (482,290) | 2,544,264 | 2,578,553 | 2,679,633 | 2,096,263 |
| Restricted | 15,796 | 47,413 | - | - | 15,796 | 47,413 |
| Unrestricted | 240,396 | 213,176 | 55,504 | 63,284 | 295,900 | 276,460 |
| Total net position | <u>\$ 391,561</u> | <u>\$ (221,701)</u> | <u>\$ 2,599,768</u> | <u>\$ 2,641,837</u> | <u>\$ 2,991,329</u> | <u>\$ 2,420,136</u> |

**Unrestricted Net Position
Governmental and Business-type Activities**

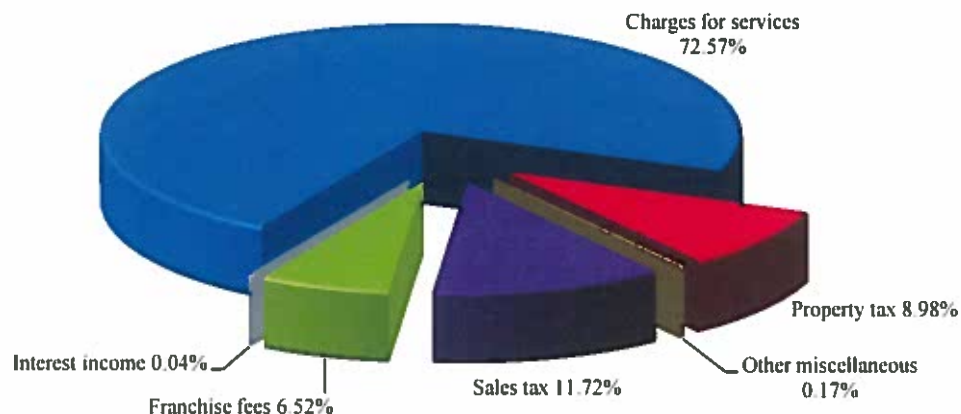


**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2014
(UNAUDITED)**

Change in Net Position

| | <u>Governmental Activities</u> | | <u>Business-type Activities</u> | | <u>Total</u> | |
|--|--------------------------------|---------------------|---------------------------------|---------------------|---------------------|---------------------|
| | <u>2014</u> | <u>2013</u> | <u>2014</u> | <u>2013</u> | <u>2014</u> | <u>2013</u> |
| Revenues | | | | | | |
| Charges for services | \$ - | \$ - | \$ 797,318 | \$ 799,827 | \$ 797,318 | \$ 799,827 |
| Property taxes | 98,629 | 102,928 | - | - | 98,629 | 102,928 |
| Sales taxes | 128,755 | 138,000 | - | - | 128,755 | 138,000 |
| Franchise fees | 71,667 | 68,875 | - | - | 71,667 | 68,875 |
| Interest income | 343 | 957 | 102 | 77 | 445 | 1,034 |
| Grants and contributions | 830,292 | 260,566 | 100,202 | 915,522 | 930,494 | 1,176,088 |
| Other miscellaneous | 1,827 | 1,009 | - | - | 1,827 | 1,009 |
| Total revenues | 1,131,513 | 572,335 | 897,622 | 1,715,426 | 2,029,135 | 2,287,761 |
| Expenses | | | | | | |
| General government | 122,549 | 174,099 | - | - | 122,549 | 174,099 |
| Streets and drainage | 64,575 | 99,803 | - | - | 64,575 | 99,803 |
| Fire protection | 14,763 | 12,748 | - | - | 14,763 | 12,748 |
| Municipal court | 1,100 | 2,062 | - | - | 1,100 | 2,062 |
| Health and welfare | 10,834 | 2,000 | - | - | 10,834 | 2,000 |
| Pass-through expenditures | 269,804 | 157,724 | - | - | 269,804 | 157,724 |
| Water, sewer, sanitation | - | - | 687,109 | 708,661 | 687,109 | 708,661 |
| Depreciation | 26,765 | 8,662 | 225,079 | 214,133 | 251,844 | 222,795 |
| Interest on long-term debt | 31,379 | 32,183 | 3,985 | 6,349 | 35,364 | 38,532 |
| Total expenses | 541,769 | 489,281 | 916,173 | 929,143 | 1,457,942 | 1,418,424 |
| Transfers | | | | | | |
| In (out) | 23,518 | (300) | (23,518) | 300 | - | - |
| Total transfers | 23,518 | (300) | (23,518) | 300 | - | - |
| Increase (decrease) in net position | 613,262 | 82,754 | (42,069) | 786,583 | 571,193 | 869,337 |
| Net position at beginning of year | (221,701) | (304,455) | 2,641,837 | 1,857,874 | 2,420,136 | 1,553,419 |
| Prior period adjustment | - | - | - | (2,620) | - | (2,620) |
| Net position at end of year | \$ 391,561 | \$ (221,701) | \$ 2,599,768 | \$ 2,641,837 | \$ 2,991,329 | \$ 2,420,136 |

**Revenue by Major Category (Excluding Grants)
Governmental and Business-type Activities
For the Year Ended September 30, 2014**



**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2014
(UNAUDITED)**

FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

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

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

As of September 30, 2014, the City's governmental funds reported a total fund balance of \$259,266. This fund balance is comprised of \$5,853 that is restricted for payment of debt service and \$9,943 that is restricted for street repair/maintenance. The remaining balance, \$243,470, is unassigned. During the year, the fund balance in the City's governmental funds decreased by \$5,148.

General Fund Budget. A comparison of the general fund budget and actual results is presented as required supplementary information on page 42. Actual revenues were lower than budgeted amounts by \$11,832. Actual expenditures were lower than budgeted amounts by \$37,559. The General fund balance increased by \$34,589 during the fiscal year; a decrease of \$4,975 in fund balance was budgeted.

CAPITAL ASSETS

The City's investment in capital assets as of September 30, 2014, totaled \$3,398,693 (net of accumulated depreciation). This investment includes land, buildings and improvements, streets and drainage, equipment, and construction work in progress.

Current year expenditures during the current year included:

- New Holland Tractor and attachments
- Water well project (grant funded and in progress at year end)
- Building addition to the fire station
- Drainage project was completed (grant funded)
- Sidewalk project was completed (grant funded)
- Newsome well generator project was completed (grant funded)
- Various water/sewer plant improvements and upgrades

Capital Assets (Net of Depreciation)

| | Governmental Activities | | Business-type Activities | | Total | |
|------------------------------|-------------------------|-------------------|--------------------------|---------------------|---------------------|---------------------|
| | 2014 | 2013 | 2014 | 2013 | 2014 | 2013 |
| Land | \$ 2,350 | \$ 2,350 | \$ 61,203 | \$ 61,203 | \$ 63,553 | \$ 63,553 |
| Buildings and improvements | 94,374 | 65,561 | - | - | 94,374 | 65,561 |
| Plant and equipment | - | - | 2,248,082 | 2,306,652 | 2,248,082 | 2,306,652 |
| Machinery and equipment | 36,584 | 14,668 | 260,146 | 291,965 | 296,730 | 306,633 |
| Transportation equipment | - | - | 8,371 | 13,553 | 8,371 | 13,553 |
| Office equipment & furniture | 6,626 | 9,020 | 1,607 | 3,183 | 8,233 | 12,203 |
| Streets and drainage | 660,638 | - | - | - | 660,638 | - |
| Construction in progress | 18,712 | 126,111 | - | - | 18,712 | 126,111 |
| Total net assets | <u>\$ 819,284</u> | <u>\$ 217,710</u> | <u>\$ 2,579,409</u> | <u>\$ 2,676,556</u> | <u>\$ 3,398,693</u> | <u>\$ 2,894,266</u> |

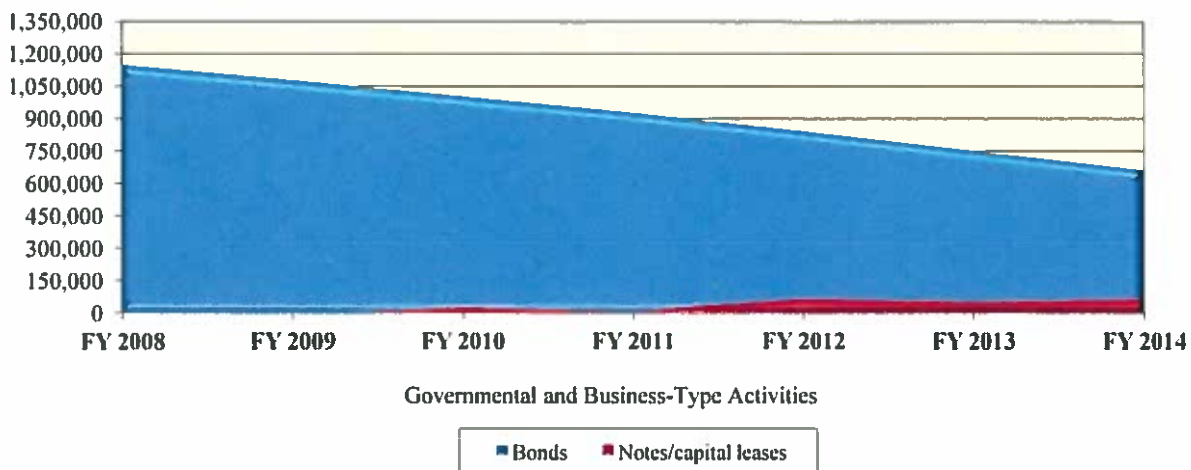
**CITY OF ELKHART, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2014
(UNAUDITED)**

DEBT ADMINISTRATION

At the end of the current fiscal year, the City had total debt outstanding of \$719,060.

Debt Outstanding

| | <u>Governmental Activities</u> | | <u>Business-type Activities</u> | | <u>Total</u> | |
|---------------------------|--------------------------------|-------------------|---------------------------------|------------------|-------------------|-------------------|
| | <u>2014</u> | <u>2013</u> | <u>2014</u> | <u>2013</u> | <u>2014</u> | <u>2013</u> |
| Notes payable | \$ 23,915 | \$ - | \$ - | \$ - | \$ 23,915 | \$ - |
| Capital lease obligations | - | - | 35,145 | 48,003 | 35,145 | 48,003 |
| Bonds payable | <u>660,000</u> | <u>700,000</u> | <u>-</u> | <u>50,000</u> | <u>660,000</u> | <u>750,000</u> |
| Total | <u>\$ 683,915</u> | <u>\$ 700,000</u> | <u>\$ 35,145</u> | <u>\$ 98,003</u> | <u>\$ 719,060</u> | <u>\$ 798,003</u> |



ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

In September, 2014, the Council approved the 2014/2015 budget. The City adopted a property tax rate of 0.2972 per \$100, an increase from the prior year. No increases in utility rates were projected. With slight variances, the overall revenues and expenses of the City were budgeted to remain at prior year levels.

REQUESTS FOR INFORMATION

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

Basic Financial Statements

Government-wide Financial Statements

CITY OF ELKHART, TEXAS
STATEMENT OF NET POSITION
SEPTEMBER 30, 2014

| | Primary Government | | |
|---|----------------------------|-----------------------------|---------------------|
| | Governmental Activities | Business-type Activities | Total |
| ASSETS | | | |
| Cash and cash equivalents | \$ 258,323 | \$ 74,121 | \$ 332,444 |
| Receivables | | | |
| Customers, net of allowance | - | 76,584 | 76,584 |
| Unbilled receivables | - | 13,235 | 13,235 |
| Property taxes, net of allowance | 439 | - | 439 |
| Sales taxes | 9,760 | - | 9,760 |
| Due from other governments | 27,857 | - | 27,857 |
| Inventory | - | 16,041 | 16,041 |
| Internal balances | (9,571) | 9,571 | - |
| Restricted assets | | | |
| Cash and cash equivalents | 13,928 | - | 13,928 |
| Capital assets | | | |
| Nondepreciable | 21,062 | 61,203 | 82,265 |
| Depreciable, net of accumulated depreciation | 798,222 | 2,518,206 | 3,316,428 |
| TOTAL ASSETS | 1,120,020 | 2,768,961 | 3,888,981 |
| LIABILITIES | | | |
| Accounts payable | 4,565 | 25,510 | 30,075 |
| Accrued expenses | 36,547 | - | 36,547 |
| Accrued interest | 3,432 | - | 3,432 |
| Customer deposits payable | - | 96,407 | 96,407 |
| Insurance proceeds refundable | - | 12,131 | 12,131 |
| Noncurrent liabilities | | | |
| Due within one year | 104,904 | 13,290 | 118,194 |
| Due in more than one year | 579,011 | 21,855 | 600,866 |
| TOTAL LIABILITIES | 728,459 | 169,193 | 897,652 |
| NET POSITION | | | |
| Invested in capital assets, net of related debt | 135,369 | 2,544,264 | 2,679,633 |
| Restricted for: | | | |
| Debt service | 5,853 | - | 5,853 |
| Street maintenance | 9,943 | - | 9,943 |
| Unrestricted | 240,396 | 55,504 | 295,900 |
| TOTAL NET POSITION | \$ 391,561 | \$ 2,599,768 | \$ 2,991,329 |

See accompanying notes to the financial statements.

CITY OF ELKHART, TEXAS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2014

| Functions/Programs | Program Revenues | | | Net (Expenses) Revenues and Changes in Net Position | | |
|--------------------------------------|------------------|---|--|--|----------------------------|-----------------------------|
| | Expenses | Fees, Fines, Charges for Services | Operating Grants and Contributions | Capital Grants and Contributions | Primary Government | |
| | | | | | Governmental Activities | Business-type Activities |
| Primary government | | | | | | |
| Governmental activities | | | | | | |
| General government | \$ 126,015 | \$ - | \$ - | \$ 18,712 | \$ (107,303) | \$ - |
| Streets | 85,532 | - | - | 523,432 | 437,900 | - |
| Fire protection | 17,105 | - | - | - | (17,105) | - |
| Municipal court | 1,100 | - | - | - | (1,100) | - |
| Health and welfare | 10,834 | - | 18,524 | - | 7,690 | - |
| Pass-through expenditures | 269,804 | - | - | 269,624 | (180) | - |
| Interest on long-term debt | 31,379 | - | - | - | (31,379) | - |
| Total governmental activities | 541,769 | - | 18,524 | 811,768 | 288,523 | - |
| Business-type activities | | | | | | |
| Water, sewer, garbage | 912,188 | 797,318 | - | 100,202 | - | (14,668) |
| Interest on long-term debt | 3,985 | - | - | - | - | (3,985) |
| Total business-type activities | 916,173 | 797,318 | - | 100,202 | - | (18,653) |
| Total primary government | \$ 1,457,942 | \$ 797,318 | \$ 18,524 | \$ 911,970 | \$ 288,523 | \$ 269,870 |
| | | | | | | |
| General revenues | | | | | | |
| Property taxes | | | | | 98,629 | - |
| Sales taxes | | | | | 128,755 | - |
| Franchise taxes | | | | | 71,667 | - |
| Investment income | | | | | 343 | 102 |
| Miscellaneous income | | | | | 1,827 | - |
| Transfers in (out) | | | | | 23,518 | (23,518) |
| Total general revenues and transfers | | | | | 324,739 | (23,416) |
| Change in net position | | | | | 613,262 | (42,069) |
| Net position - beginning | | | | | (221,701) | 2,641,837 |
| Net position - ending | | | | | \$ 391,561 | \$ 2,599,768 |
| | | | | | | \$ 2,991,329 |

See accompanying notes to the financial statements.

Fund Financial Statements

**CITY OF ELKHART, TEXAS
BALANCE SHEET
GOVERNMENTAL FUNDS
SEPTEMBER 30, 2014**

| | General Fund | Governmental Grants Fund | Nonmajor Governmental Funds (Page 45) | Total |
|--|-------------------|--------------------------------|--|-------------------|
| ASSETS | | | | |
| Cash and cash equivalents | \$ 254,448 | \$ 3,875 | \$ - | \$ 258,323 |
| Receivables | | | | |
| Property taxes, net of allowance | 439 | - | - | 439 |
| Sales taxes | 7,808 | - | 1,952 | 9,760 |
| Due from other governments | - | 27,857 | - | 27,857 |
| Restricted assets | | | | |
| Cash and cash equivalents | - | - | 13,928 | 13,928 |
| TOTAL ASSETS | \$ 262,695 | \$ 31,732 | \$ 15,880 | \$ 310,307 |
| LIABILITIES | | | | |
| Accounts payable | \$ 4,565 | \$ - | \$ - | \$ 4,565 |
| Accrued expenses | 7,864 | 28,683 | - | 36,547 |
| Due to other funds | 5,612 | 3,875 | 84 | 9,571 |
| Total liabilities | 18,041 | 32,558 | 84 | 50,683 |
| DEFERRED INFLOWS OF RESOURCES | | | | |
| Unavailable revenue - property taxes | 358 | - | - | 358 |
| Total deferred inflows of resources | 358 | - | - | 358 |
| FUND BALANCES | | | | |
| Restricted for: | | | | |
| Debt service | - | - | 5,853 | 5,853 |
| Street maintenance | - | - | 9,943 | 9,943 |
| Unassigned | 244,296 | (826) | - | 243,470 |
| Total fund balances | 244,296 | (826) | 15,796 | 259,266 |
| TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND FUND BALANCES | \$ 262,695 | \$ 31,732 | \$ 15,880 | \$ 310,307 |

See accompanying notes to the financial statements.

**CITY OF ELKHART, TEXAS
RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL
FUNDS TO THE STATEMENT OF NET POSITION
FOR THE YEAR ENDED SEPTEMBER 30, 2014**

| | |
|--|-------------------|
| Total fund balances - governmental funds balance sheet | \$ 259,266 |
| Amounts reported for governmental activities in the statement of net position are different because: | |
| Certain revenues are not available to pay current period expenditures and therefore, are reported as deferred inflows in the governmental funds. | 358 |
| Capital assets used in governmental activities are not financial resources and therefore, are not reported in the governmental funds. | 819,284 |
| Payables for long-term liabilities, including certificates of obligations and capital leases, are not due in the current period and therefore, are not reported in the governmental funds. | (683,915) |
| Payables for accrued interest on long-term liabilities are not due in the current period and therefore, are not reported in the governmental funds. | <u>(3,432)</u> |
| Net position of governmental activities | <u>\$ 391,561</u> |

See accompanying notes to financial statements.

CITY OF ELKHART, TEXAS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2014

| | General Fund | Governmental Grants Fund | Nonmajor Governmental Funds (Page 46) | Total |
|---|-------------------|--------------------------------|--|-------------------|
| REVENUES | | | | |
| Property taxes, penalty and interest | \$ 98,271 | \$ - | \$ - | \$ 98,271 |
| Sales taxes | 103,004 | - | 25,751 | 128,755 |
| Franchise taxes | 71,667 | - | - | 71,667 |
| Intergovernmental | - | 811,768 | - | 811,768 |
| Interest income | - | - | 343 | 343 |
| Donations | 18,524 | - | - | 18,524 |
| Other revenues | 1,827 | - | - | 1,827 |
| Total revenues | <u>293,293</u> | <u>811,768</u> | <u>26,094</u> | <u>1,131,155</u> |
| EXPENDITURES | | | | |
| General government | 122,549 | - | - | 122,549 |
| Streets | 46,954 | - | 17,621 | 64,575 |
| Fire protection | 14,763 | - | - | 14,763 |
| Municipal court | 1,100 | - | - | 1,100 |
| Health and welfare | 10,834 | - | - | 10,834 |
| Pass-through expenditures | - | 269,804 | - | 269,804 |
| Capital outlay | 59,228 | 569,110 | - | 628,338 |
| Debt service | | | | |
| Principal retired | 3,395 | - | 40,000 | 43,395 |
| Interest | 871 | - | 30,902 | 31,773 |
| Total expenditures | <u>259,694</u> | <u>838,914</u> | <u>88,523</u> | <u>1,187,131</u> |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES | | | | |
| | <u>33,599</u> | <u>(27,146)</u> | <u>(62,429)</u> | <u>(55,976)</u> |
| OTHER FINANCING SOURCES (USES) | | | | |
| Loan proceeds | 27,310 | - | - | 27,310 |
| Transfers in (out) | (26,320) | 26,320 | 23,518 | 23,518 |
| Net other financing sources (uses) | <u>990</u> | <u>26,320</u> | <u>23,518</u> | <u>50,828</u> |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES AND OTHER USES | | | | |
| | 34,589 | (826) | (38,911) | (5,148) |
| FUND BALANCES - BEGINNING OF YEAR | <u>209,707</u> | <u>-</u> | <u>54,707</u> | <u>264,414</u> |
| FUND BALANCES - END OF YEAR | <u>\$ 244,296</u> | <u>\$ (826)</u> | <u>\$ 15,796</u> | <u>\$ 259,266</u> |

See accompanying notes to the financial statements.

**CITY OF ELKHART, TEXAS
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCE -
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2014**

| | | |
|---|----|---------|
| Net change in fund balance - governmental funds | \$ | (5,148) |
|---|----|---------|

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

| | | |
|--|--|---------|
| Governmental funds report capital outlay as expenditures. In the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period. | | 601,574 |
|--|--|---------|

| | | |
|---|--|-----|
| Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the governmental funds. | | 358 |
|---|--|-----|

| | | |
|---|--|--------|
| The issuance of long-term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. This amount is the net effect of these differences in the treatment of long-term debt and related items. | | 16,085 |
|---|--|--------|

| | | |
|---|--|-----|
| Accrued interest expense on long-term debt is reported in the government-wide statement of activities and changes in net position, but does not require the use of current financial resources; therefore, accrued interest expense is not reported as expenditures in governmental funds. This amount is the change in accrued interest. | | 393 |
|---|--|-----|

| | | |
|---|----|----------------|
| Change in net position of governmental activities | \$ | <u>613,262</u> |
|---|----|----------------|

CITY OF ELKHART, TEXAS
STATEMENT OF NET POSITION
PROPRIETARY FUNDS
SEPTEMBER 30, 2014

| | Utility Fund | Proprietary Grants Fund | Total |
|---|---------------------|-------------------------------|---------------------|
| ASSETS | | | |
| Current assets | | | |
| Cash and cash equivalents | \$ 74,103 | \$ 18 | \$ 74,121 |
| Receivables, net of allowance | 76,584 | - | 76,584 |
| Unbilled receivables | 13,235 | - | 13,235 |
| Due from other funds | 9,487 | 84 | 9,571 |
| Inventory | 16,041 | - | 16,041 |
| Total current assets | <u>189,450</u> | <u>102</u> | <u>189,552</u> |
| Noncurrent assets | | | |
| Capital assets | | | |
| Nondepreciable | 61,203 | - | 61,203 |
| Depreciable, net of accumulated depreciation | 2,518,206 | - | 2,518,206 |
| Total noncurrent assets | <u>2,579,409</u> | <u>-</u> | <u>2,579,409</u> |
| TOTAL ASSETS | <u>2,768,859</u> | <u>102</u> | <u>2,768,961</u> |
| LIABILITIES | | | |
| Current liabilities | | | |
| Accounts payable | 25,510 | - | 25,510 |
| Customer deposits payable | 96,407 | - | 96,407 |
| Insurance proceeds refundable | 12,131 | - | 12,131 |
| Capital leases - current maturities | 13,290 | - | 13,290 |
| Total current liabilities | <u>147,338</u> | <u>-</u> | <u>147,338</u> |
| Noncurrent liabilities | | | |
| Capital leases | 21,855 | - | 21,855 |
| Total noncurrent liabilities | <u>21,855</u> | <u>-</u> | <u>21,855</u> |
| TOTAL LIABILITIES | <u>169,193</u> | <u>-</u> | <u>169,193</u> |
| NET POSITION | | | |
| Invested in capital assets, net of related debt | 2,544,264 | - | 2,544,264 |
| Unrestricted | 55,402 | 102 | 55,504 |
| TOTAL NET POSITION | <u>\$ 2,599,666</u> | <u>\$ 102</u> | <u>\$ 2,599,768</u> |

See accompanying notes to the financial statements.

CITY OF ELKHART, TEXAS
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
PROPRIETARY FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2014

| | Utility Fund | Proprietary Grants Fund | Total |
|---|---------------------|-------------------------------|---------------------|
| OPERATING REVENUES | | | |
| Water sales | \$ 408,493 | \$ - | \$ 408,493 |
| Sewer income | 204,955 | - | 204,955 |
| Garbage income | 156,802 | - | 156,802 |
| Late charges and other income | 27,068 | - | 27,068 |
| Total operating revenues | <u>797,318</u> | <u>-</u> | <u>797,318</u> |
| OPERATING EXPENSES | | | |
| Personnel and related costs | 344,872 | - | 344,872 |
| Supplies and materials | 56,510 | - | 56,510 |
| Repairs and maintenance | 22,232 | - | 22,232 |
| Garbage expense | 144,259 | - | 144,259 |
| Professional fees | 50,307 | - | 50,307 |
| Insurance | 13,039 | - | 13,039 |
| Utilities | 43,850 | - | 43,850 |
| Office expense | 4,544 | - | 4,544 |
| Other expense | 7,496 | - | 7,496 |
| Depreciation | 225,079 | - | 225,079 |
| Total operating expenses | <u>912,188</u> | <u>-</u> | <u>912,188</u> |
| INCOME (LOSS) FROM OPERATIONS | (114,870) | - | (114,870) |
| NONOPERATING REVENUES (EXPENSES) | | | |
| Capital contributions | - | 100,202 | 100,202 |
| Interest income | 102 | - | 102 |
| Interest expense | (3,985) | - | (3,985) |
| Total nonoperating revenues (expenses) | <u>(3,883)</u> | <u>100,202</u> | <u>96,319</u> |
| INCOME (LOSS) BEFORE CONTRIBUTIONS AND TRANSFERS | (118,753) | 100,202 | (18,551) |
| Transfers in (out) | 76,684 | (100,202) | (23,518) |
| CHANGE IN NET POSITION | (42,069) | - | (42,069) |
| NET POSITION AT BEGINNING OF YEAR | <u>2,641,735</u> | <u>102</u> | <u>2,641,837</u> |
| NET POSITION AT END OF YEAR | <u>\$ 2,599,666</u> | <u>\$ 102</u> | <u>\$ 2,599,768</u> |

See accompanying notes to the financial statements.

CITY OF ELKHART, TEXAS
STATEMENT OF CASH FLOWS
UTILITY FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2014

CASH FLOWS FROM OPERATING ACTIVITIES

| | |
|---|------------------|
| Cash received from customers and users | \$ 814,402 |
| Cash payments to suppliers | (353,780) |
| Cash payments to employees | <u>(345,184)</u> |
| Net cash provided by operating activities | <u>115,438</u> |

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

| | |
|--|---------------|
| Operating transfers in | <u>76,684</u> |
| Net cash provided by noncapital financing activities | <u>76,684</u> |

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

| | |
|---|------------------|
| Acquisition of capital assets | (127,932) |
| Principal payments on long-term debt | (62,858) |
| Interest payments on long-term debt | <u>(3,985)</u> |
| Net cash used by capital and related financing activities | <u>(194,775)</u> |

CASH FLOWS FROM INVESTING ACTIVITIES

| | |
|---|------------|
| Interest received | <u>102</u> |
| Net cash provided by investing activities | <u>102</u> |

NET DECREASE IN CASH AND CASH EQUIVALENTS (2,551)

CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR 76,654

CASH AND CASH EQUIVALENTS AT END OF YEAR \$ 74,103

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

| | |
|---|----------------|
| Operating loss before nonoperating revenues | \$ (114,870) |
| Adjustments to reconcile operating loss to net cash provided by operating activities: | |
| Depreciation and amortization | 225,079 |
| Changes in assets and liabilities | |
| (Increase) decrease in accounts receivable | 15,012 |
| (Increase) decrease in inventory | 1,927 |
| Increase (decrease) in accounts payable | 3,413 |
| Increase (decrease) in accrued interest | (312) |
| Increase (decrease) in due from other funds | (9,487) |
| (Increase) decrease in due to other funds | (7,396) |
| Increase (decrease) in customer deposits payable | <u>2,072</u> |
| Total adjustments | <u>230,308</u> |

NET CASH PROVIDED BY OPERATING ACTIVITIES \$ 115,438

See accompanying notes to the financial statements.

Notes to the Financial Statements

**CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014**

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Introduction

The financial statements of the City of Elkhart, Texas (the "City") have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") as applied to government units. The Governmental Accounting Standards Board ("GASB") is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant accounting and reporting policies used by the City are discussed below.

Reporting Entity

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

For financial reporting purposes, based on standards established by GASB Statement No. 61, *The Financial Reporting Entity: Omnibus*, these financial statements should present the City (the primary government) and its component units. Component units generally are legally separate entities for which the primary government is financially accountable or for which the nature and significance of their relationship with a primary government are such that exclusion would cause the reporting entity's financial statements to be misleading. The City does not have any blended or discretely presented component units.

Government-wide and Fund Financial Statements

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

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

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

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

New Accounting Pronouncements

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions* ("GASB 68"), establishes reporting standards for public employee pensions by state and local governments. The requirements of

CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014

this statement are effective for financial statements for periods beginning after June 15, 2014. The City has not determined the impact, if any, upon its financial position, results of operations or cash flows upon adoption.

GASB Statement No. 69, *Government Combinations and Disposals of Government Operations* ("GASB 69"), establishes accounting and financial reporting standards related to government combinations and disposals of government operations. The requirements of this statement are effective for financial statements for periods beginning after December 15, 2013. The City has not determined the impact, if any, upon its financial position, results of operations or cash flows upon adoption.

GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees* ("GASB 70"), establishes accounting and financial reporting standards related to local governments that extend and receive nonexchange financial guarantees. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2014. The City has not determined the impact, if any, upon its financial position, results of operations or cash flows upon adoption.

GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date* ("GASB 71"), eliminates the source of a potential understatement of restated beginning net position and expense in the first year of implementation of GASB 68 in the accrual-basis financial statements of employers and nonemployer contributing entities. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2014. The City has not determined the impact, if any, upon its financial position, results of operations or cash flows upon adoption.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

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

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized when they are both measurable and available. Available means collectible within the current period or soon enough thereafter to pay current liabilities. The City considers revenues to be available if they are collected within 60 days of the end of the fiscal year. Expenditures are recorded when the related liability is incurred, as under accrual accounting. Debt service expenditures, both principal and interest, are recorded only when payment is due.

Major governmental fund revenue sources susceptible to accrual include: sales and use taxes, property taxes, franchise taxes, and investment income. In general, all other revenue items are considered to be measurable and available only when cash is received. Expenditure driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other grant requirements have been met.

Proprietary funds distinguish between operating revenues and expenses from non-operating items. Operating income reported in proprietary fund financial statements include revenues and expenses related to the primary, continuing operations of the fund. Principal operating revenues for proprietary funds are charges to customers for sales or services. Principal operating expenses are the costs of providing goods

**CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014**

or services and include administrative expense and depreciation of capital assets. Revenues and expenses not meeting this definition are classified as non-operating in the financial statements.

The City's funds are classified as either governmental or enterprise and are described below.

Governmental Funds. Governmental funds are used to account for all or most of a government's general activity.

The *general fund* is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund. The principal sources of revenue include local property taxes, fees, licenses and permits, and intergovernmental revenue and grants. Expenditures include general government, streets, fire, municipal court, and health and welfare.

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

Governmental grants funds are used to account for grant resources received from various local, state, and federal sources. The use of these resources is restricted to a particular function of the City by each grantor.

Special revenue funds are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for specific purposes.

Enterprise Funds. Enterprise funds (or proprietary funds) are used to account for the City's business-type activities.

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

Proprietary grants funds are used to account for the expenditures of resources accumulated from debt issued by the city or from grants received by the city, as well as related interest earnings for capital improvement projects.

The general fund, governmental grants fund, and utility fund are all reported as major funds.

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

All expenses incurred by the City are properly segregated and accounted for in the fund to which the expenses apply. Certain general and administrative expenses are allocated to the proprietary fund and to the governmental fund based on the level of services rendered through each fund as estimated by management.

**CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014**

Assets, Liabilities, and Net Position or Fund Balance

Deposits and Investments

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

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

The City is required by the Public Funds Collateral Act (Government Code, chapter 2257) to maintain security for all deposits of funds that exceed coverage provided by the Federal Deposit Insurance Corporation (FDIC). As of the balance sheet date, the City's cash deposits were fully collateralized by securities pledged by the depository banks. Based on audit procedures conducted in conjunction with the audit of the basic financial statements, the City complied with the requirements of the Public Funds Collateral Act.

The City is required by the Public Funds Investment Act (Government Code, chapter 2256) (the "Act") to adopt, implement, and publicize a written investment policy which primarily emphasizes safety of principal and liquidity, and addresses investment diversification, yield, and maturity. Additionally, the policy must address the quality and capability of investment management and include the types of investments in which the entity may invest its funds, as well as the maximum allowable stated maturity of any individual investment, the maximum dollar-weighted average maturity allowed based on the stated maturity date for the portfolio of pooled fund groups, and bid requirements for certificates of deposit.

The City is authorized to invest in financial instruments, as authorized by the Act, including:

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

The Act also requires an annual audit of investment practices. The City did not have any investments at year end or at any time during the current fiscal year.

**CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014**

Fair Value of Financial Instruments

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

Receivables

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

Restricted Assets

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

Inventories

Inventories are valued at cost which approximates market, using the first-in/first-out method. Inventories consist of expendable supplies and repair parts held for consumption. The cost of inventory is recorded as an expenditure when used (consumption method).

Capital Assets and Depreciation

Capital assets, which include land, buildings and improvements, furniture and equipment, and infrastructure assets are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Contributed capital assets are recorded at estimated fair market value at the date received.

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

Infrastructure assets are a subset of capital assets and primarily consist of roads and bridges. GASB No. 34 encourages but does not require Phase 3 governments (cities with revenues of less than \$10 million) to retroactively report major general infrastructure assets. New roads and bridges acquired after October 1, 2003 are required to be reported.

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

The estimated useful lives are as follows:

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

**CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014**

Deferred Inflows of Resources

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The City has one type of item, which arises only under a modified accrual basis of accounting, that qualifies for reporting in this category. Accordingly, the item, unavailable revenue – property taxes, is reported only on the governmental funds balance sheet. This amount is deferred and recognized as an inflow of resources in the period that the amount becomes available.

Compensated Absences

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

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

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

Long-term Obligations

In the government-wide and proprietary fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net position. Bond premiums and discounts are deferred and amortized over the life of the bonds using the straight-line method that approximates the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

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

Net Position and Fund Balances

In the government-wide financial statements, the difference between the City's total assets and total liabilities represents net position. Net position is displayed in three components – invested in capital assets, net of related debt; restricted; and unrestricted. At September 30, 2014, restricted net position represents monies that are legally restricted for payment of debt service. Unrestricted net position represents the net position available for future operations.

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

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

**CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014**

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

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

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

Unassigned – all other spendable amounts.

Proprietary fund net position is classified the same as in government-wide statements.

Estimates

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

STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Budgets and Budgetary Process

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

Restricted Balances

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

Deficit Balances

Generally accepted accounting principles require disclosure of individual funds that have deficit balances at year end. At September 30, 2014, the governmental grants fund had a deficit balance. This deficit was the result of timing of transfers between funds.

CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014

DETAILED NOTES ON ALL FUNDS

ASSETS

Deposits and Investments

Interest Rate Risk. In accordance with its investment policy, the City manages its exposure to declines in fair value by diversifying investments in terms of maturity.

Credit Risk. State law and the City's investment policy limit investments to obligations of states, agencies, counties, cities and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent. As of September 30, 2014, the City did not have any investments.

Custodial Credit Risk – Deposits. In the case of deposits, this is the risk that in the event of a bank failure, the City's deposits may not be returned. The City's investment policy requires funds on deposit at depository banks to be collateralized to the extent that the deposits exceed FDIC coverage. As of September 30, 2014, the City's cash deposits with depository banks totaled \$588,336. All deposits were fully collateralized by securities pledged by the depository banks with total collateral value of \$563,041, in addition to FDIC coverage.

Elkhart Volunteer Fire Department ("EVFD") Donations

The City receives donations for the EVFD, generally through utility collections. These donations are transacted through a separate cash account and remitted to the EVFD on a periodic basis. Both the cash and offsetting liability are excluded from these financial statements. At September 30, 2014, the balance of collections to be remitted to the EVFD totaled \$100.

Receivables

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

| | <u>Customer Accounts</u> | <u>Property Taxes</u> | <u>Sales Taxes</u> | <u>Other</u> | <u>Totals</u> |
|------------------------------|------------------------------|---------------------------|------------------------|------------------|-------------------|
| Receivables by activity | | | | | |
| Governmental | \$ - | \$ 20,718 | \$ 9,760 | \$ 27,857 | \$ 58,335 |
| Business-type | <u>105,081</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>105,081</u> |
| Receivables, gross | <u>105,081</u> | <u>20,718</u> | <u>9,760</u> | <u>27,857</u> | <u>163,416</u> |
| Allowance for uncollectibles | | | | | |
| Governmental | - | (20,279) | - | - | (20,279) |
| Business-type | <u>(15,262)</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>(15,262)</u> |
| Total allowance | <u>(15,262)</u> | <u>(20,279)</u> | <u>-</u> | <u>-</u> | <u>(35,541)</u> |
| Total receivables, net | <u>\$ 89,819</u> | <u>\$ 439</u> | <u>\$ 9,760</u> | <u>\$ 27,857</u> | <u>\$ 127,875</u> |

CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014

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

The property tax rate to finance general governmental services for the year ended September 30, 2014, was \$.29486 per \$100 of assessed valuation. The total taxable value and total tax levy assessed for the year was \$33,557,526 and \$101,363, respectively. The City has contracted with the Anderson County Central Appraisal District for the collection of property taxes.

Capital Assets

A summary of changes in capital assets for the year ended September 30, 2014 is as follows:

Governmental activities

| | Balance 09/30/2013 | Additions | Deletions/ Placed in Svc | Balance 09/30/2014 |
|---------------------------------------|-----------------------|---|-----------------------------|-----------------------|
| Capital assets, not being depreciated | | | | |
| Land | \$ 2,350 | \$ - | \$ - | \$ 2,350 |
| Construction in progress | 126,111 | 569,110 | (676,509) | 18,712 |
| Total not being depreciated | <u>128,461</u> | <u>569,110</u> | <u>(676,509)</u> | <u>21,062</u> |
| Capital assets, being depreciated | | | | |
| Buildings and improvements | 87,657 | 32,228 | - | 119,885 |
| Machinery and equipment | 22,140 | 27,000 | - | 49,140 |
| Office equipment and furniture | 17,329 | - | - | 17,329 |
| Streets | 140,656 | 676,509 | - | 817,165 |
| Total being depreciated | <u>267,782</u> | <u>735,737</u> | <u>-</u> | <u>1,003,519</u> |
| Less accumulated depreciation: | | | | |
| Buildings and improvements | (22,096) | (3,415) | - | (25,511) |
| Machinery and equipment | (7,472) | (5,084) | - | (12,556) |
| Office equipment and furniture | (8,309) | (2,394) | - | (10,703) |
| Streets | (140,656) | (15,871) | - | (156,527) |
| Total accumulated depreciation | <u>(178,533)</u> | <u>(26,764)</u> | <u>-</u> | <u>(205,297)</u> |
| Total being depreciated, net | <u>89,249</u> | <u>708,937</u> | <u>-</u> | <u>798,222</u> |
| Total capital assets, net | <u>\$ 217,710</u> | <u>\$ 1,278,083</u> | <u>\$ (676,509)</u> | <u>\$ 819,284</u> |
| | | Less associated debt | | <u>(683,915)</u> |
| | | Invested in capital assets, net of related debt | | <u>\$ 135,369</u> |

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

| | |
|--------------------|------------------|
| General government | \$ 3,467 |
| Fire protection | 2,341 |
| Streets | <u>20,956</u> |
| Total | <u>\$ 26,764</u> |

CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014

Business-type activities

| | Balance 09/30/2013 | Additions | Deletions/ Placed in Svc | Balance 09/30/2014 |
|---------------------------------------|-----------------------|---|-----------------------------|-----------------------|
| Capital assets, not being depreciated | | | | |
| Land | \$ 61,203 | \$ - | \$ - | \$ 61,203 |
| Total not being depreciated | <u>61,203</u> | <u>-</u> | <u>-</u> | <u>61,203</u> |
| Capital assets, being depreciated | | | | |
| Plant and equipment | 4,728,257 | 127,932 | - | 4,856,189 |
| Transportation equipment | 76,534 | - | - | 76,534 |
| Machinery and equipment | 430,627 | - | - | 430,627 |
| Office equipment | 7,586 | - | - | 7,586 |
| Total being depreciated | <u>5,243,004</u> | <u>127,932</u> | <u>-</u> | <u>5,370,936</u> |
| Less accumulated depreciation: | | | | |
| Plant and equipment | (2,421,605) | (186,502) | - | (2,608,107) |
| Transportation equipment | (62,981) | (5,182) | - | (68,163) |
| Machinery and equipment | (138,662) | (31,819) | - | (170,481) |
| Office equipment | (4,403) | (1,576) | - | (5,979) |
| Total accumulated depreciation | <u>(2,627,651)</u> | <u>(225,079)</u> | <u>-</u> | <u>(2,852,730)</u> |
| Total being depreciated, net | <u>1,615,353</u> | <u>(97,147)</u> | <u>-</u> | <u>2,518,206</u> |
| Total capital assets, net | <u>\$ 1,676,556</u> | <u>\$ (97,147)</u> | <u>\$ -</u> | <u>\$ 2,579,409</u> |
| | | Less associated debt | | <u>(35,145)</u> |
| | | Invested in capital assets, net of related debt | | <u>\$ 2,544,264</u> |

Depreciation expense of \$225,079 was charged to the proprietary fund.

LIABILITIES

Interfund Receivables, Payables, and Transfers

The following interfund receivable and payable balances are the result of cash needed by the utility fund until the fund is able to generate sufficient revenues to cover expenditures. These receivables and payables are netted and eliminated on the government-wide statement of net assets.

At September 30, 2014, these internal balances consisted of the following:

| | Receivable | Payable | Net Totals |
|---------------------------------|-----------------|--------------------|-------------------|
| <i>Governmental activities</i> | | | |
| General Fund | \$ 5,578 | \$ (11,190) | \$ (5,612) |
| Debt Service Fund | - | (84) | (84) |
| Governmental Grants Fund | - | (3,875) | (3,875) |
| Total governmental activities | <u>\$ 5,578</u> | <u>\$ (15,149)</u> | <u>\$ (9,571)</u> |
| <i>Business-type activities</i> | | | |
| Utility Fund | \$ 9,582 | \$ (95) | \$ 9,487 |
| Proprietary Grants Fund | 84 | - | 84 |
| Total business-type activities | <u>\$ 9,666</u> | <u>\$ (95)</u> | <u>\$ 9,571</u> |

CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014

Interfund transfers are indicative of re-allocation of revenues between funds with no anticipation of repayment.

Net interfund transfers during the year consisted of the following:

| | Transfers Out | Transfers In | Net Totals |
|---------------------------------|-------------------|---------------------|--------------------|
| <i>Governmental activities</i> | | | |
| General Fund | \$ 26,320 | \$ - | \$ 26,320 |
| Debt Service Fund | - | (23,518) | (23,518) |
| Governmental Grants Fund | - | (26,320) | (26,320) |
| Total governmental activities | <u>\$ 26,320</u> | <u>\$ (49,838)</u> | <u>\$ (23,518)</u> |
| <i>Business-type activities</i> | | | |
| Utility Fund | \$ 23,518 | \$ (100,202) | \$ (76,684) |
| Proprietary Grants Fund | 100,202 | - | 100,202 |
| Total business-type activities | <u>\$ 123,720</u> | <u>\$ (100,202)</u> | <u>\$ 23,518</u> |

Capital Leases

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

The asset acquired through a capital lease is as follows:

| | General Fund | Utility Fund |
|-------------------------------|-----------------|------------------|
| Asset: | | |
| Machinery and equipment | \$ - | \$ 70,703 |
| Less accumulated depreciation | - | (11,391) |
| Total | <u>\$ -</u> | <u>\$ 59,312</u> |

The future minimum lease obligations and the net present value of these minimum lease payments as of September 30, 2014, were as follows:

| Year ending September 30, | General Fund | Utility Fund |
|---|-----------------|------------------|
| 2015 | \$ - | \$ 14,175 |
| 2016 | - | 14,175 |
| 2017 | - | 8,268 |
| Total minimum lease payments | \$ - | \$ 36,618 |
| Less amount representing interest | - | (1,473) |
| Present value of minimum lease payments | <u>\$ -</u> | <u>\$ 35,145</u> |

CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014

Long-Term Debt

Long-term debt activity for the year ended September 30, 2014, was as follows:

Governmental activities

| | Balance 09/30/13 | Additions | Reductions | Balance 09/30/14 | Due Within One Year |
|----------------------|---------------------|------------------|--------------------|---------------------|------------------------|
| Series 2005 bonds | \$ 700,000 | \$ - | \$ (40,000) | \$ 660,000 | \$ 100,000 |
| Note payable | - | 27,310 | (3,395) | 23,915 | 4,904 |
| Total long-term debt | <u>\$ 700,000</u> | <u>\$ 27,310</u> | <u>\$ (43,395)</u> | <u>\$ 683,915</u> | <u>\$ 104,904</u> |

Business-type activities

| | Balance 09/30/13 | Additions | Reductions | Balance 09/30/14 | Due Within One Year |
|----------------------|---------------------|-------------|--------------------|---------------------|------------------------|
| Series 1999 bonds | \$ 50,000 | \$ - | \$ (50,000) | \$ - | \$ - |
| Capital lease | 48,003 | - | (12,858) | 35,145 | 13,290 |
| Total long-term debt | <u>\$ 98,003</u> | <u>\$ -</u> | <u>\$ (62,858)</u> | <u>\$ 35,145</u> | <u>\$ 13,290</u> |

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

| Year Ending September 30, | Governmental Activities | | Business-type Activities | |
|---------------------------|-------------------------|------------------|--------------------------|-----------------|
| | Principal | Interest | Principal | Interest |
| 2015 | \$ 104,904 | \$ 28,945 | \$ 13,290 | \$ 885 |
| 2016 | 105,253 | 24,096 | 13,698 | 476 |
| 2017 | 110,627 | 19,110 | 8,157 | 112 |
| 2018 | 116,027 | 13,872 | - | - |
| 2019 | 122,104 | 8,355 | - | - |
| 2020-2024 | 125,000 | 2,812 | - | - |
| Total | <u>\$ 683,915</u> | <u>\$ 97,190</u> | <u>\$ 35,145</u> | <u>\$ 1,473</u> |

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

Note payable to CNH Industrial Capital. During the year, the City financed the purchase of a new tractor and related accessories for \$27,310. The note bears interest at 6.89% annually and is payable in 58 (fifty-eight) monthly installments. The note matures in 2019 and is collateralized by the equipment that the note serves to finance.

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

**CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014**

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

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

At September 30, 2014, the City had \$5,937 available in the debt service fund to service bond debt.

OTHER INFORMATION

Pension Plan

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

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

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

| | <u>Plan Year 2013</u> | <u>Plan Year 2014</u> |
|---|------------------------------|------------------------------|
| Employee deposit rate | 5% | 5% |
| Matching ratio (city to employee) | 1 to 1 | 1 to 1 |
| Years required for vesting | 5 | 5 |
| Service retirement eligibility (expressed as age/years of service) | 60/5, 0/25 | 60/5, 0/25 |
| Updated Service Credit | 100% Repeating, Transfers | 100% Repeating, Transfers |
| Annuity Increase (to retirees) | 70% of CPI | 70% of CPI |

Contributions and Actuarial Information. Under the state law governing TMRS, the contribution rate for each City is determined annually by the actuary, using the Entry Age Normal (EAN) cost method (EAN was first used in the December 31, 2013 valuation; previously, the Projected Unit Credit actuarial cost method had been used). This rate consists of the normal cost contribution rate and the prior service cost contribution rate, which is calculated to be a level percent of payroll from year to year. The normal cost

CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014

contribution rate for an employee is the contribution rate which, if applied to a member's compensation throughout their period of anticipated covered service with the municipality, would be sufficient to meet all benefits payable on their behalf. The salary-weighted average of the individual rates is the total normal cost rate. The prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the applicable period for that city. Both the normal cost and prior service contribution rates include recognition of the projected impact of annually repeating benefits, such as Updated Service Credits and Annuity Increases.

The City contributes to the TMRS Plan at an actuarially determined rate. Both the employees and the City make contributions monthly. Since the City needs to know its contribution rate in advance for budgetary purposes, there is a one-year delay between the actuarial valuation that serves as the basis for the rate and the calendar year when the rate goes into effect. (i.e., the December 31, 2013 valuation will determine the contribution rate beginning January 1, 2015).

The City's Annual Pension Cost for the year was \$15,843.

Three-Year Trend Information

| Accounting Year Ending: | Annual Pension Cost ("APC") | Percentage of APC Contributed | Net Pension Obligation |
|-------------------------|--------------------------------|----------------------------------|---------------------------|
| 09/30/12 | \$17,966 | 100% | - |
| 09/30/13 | \$18,259 | 100% | - |
| 09/30/14 | \$15,843 | 100% | - |

The required contribution rates for fiscal year 2014 were determined as part of the December 31, 2011 and 2012 actuarial valuations. Additional information as of the latest actuarial valuation, December 31, 2013, also follows:

Contribution Information

| | 12/31/2011 | 12/31/2012 | 12/31/2013 |
|--|------------------------------|------------------------------|------------------------------|
| Actuarial Cost Method | Projected Unit Credit | Projected Unit Credit | Entry Age Normal |
| Amortization Method | Level Percent of Payroll | Level Percent of Payroll | Level Percent of Payroll |
| GASB 25 Equivalent Single Amortization Period | 26.1 years; Closed Period | 25.1 years; Closed Period | 23.0 years; Closed Period |
| Amortization Period for new Gains/Losses | 17 years | 19 years | 18 years |
| Asset Valuation Method | 10-year Smoothed Market | 10-year Smoothed Market | 10-year Smoothed Market |

Actuarial Assumptions

| | | | |
|----------------------------|------------------------------|------------------------------|------------------------------|
| Investment Rate of Return | 7.0% | 7.0% | 7.0% |
| Projected Salary Increases | Varies by age and service | Varies by age and service | Varies by age and service |
| Inflation Rate | 3.00% | 3.00% | 3.00% |
| Cost-of-Living Adjustments | 2.1% | 2.1% | 2.1% |

CITY OF ELKHART, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2014

Funded Status and Funding Progress. In October 2013, the TMRS Board approved actuarial changes in (a) the funding method from Projected Unit Credit to Entry Age Normal, (b) the post-retirement mortality assumptions used in calculating liabilities and contribution rates and in the development of the Annuity Purchase Rate factors, and (c) the amortization policy. These actuarial changes were effective with the December 31, 2013 actuarial valuation. For a complete description of the new actuarial cost method and assumptions, please see the December 31, 2013 TMRS Comprehensive Annual Financial Report (CAFR)

The funded status as of December 31, 2013, the most recent actuarial valuation date, is presented as follows:

| Actuarial Valuation Date | Actuarial Value of Assets | Actuarial Accrued Liability (AAL) | Funded Ratio | Unfunded AAL (UAAL) | Covered Payroll | UAAL as a Percentage of Covered Payroll |
|--------------------------------|---------------------------------|--|-----------------|---------------------------|--------------------|--|
| | (1) | (2) | (3) | (4) | (5) | (6) |
| | | | (1) / (2) | (2) - (1) | | (4) / (5) |
| 12/31/13 | \$ 534,304 | \$ 636,316 | 84.0 % | \$ 102,012 | \$ 300,634 | 33.9 % |

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

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

Risk Management

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

Contingent Liabilities

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

Subsequent Events

Management has evaluated subsequent events through January 30, 2015, the date when the financial statements were available to be issued.

**Required Supplementary Information
(unaudited)**

CITY OF ELKHART, TEXAS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
BUDGET AND ACTUAL
GENERAL FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2014

| | Original Appropriated Budget | Final Appropriated Budget | Actual Amounts | Variances Favorable (Unfavorable) |
|--|------------------------------------|---------------------------------|-------------------|---|
| REVENUES | | | | |
| Property taxes, penalty and interest | \$ 99,000 | \$ 99,000 | \$ 98,271 | \$ (729) |
| Sales taxes | 105,000 | 105,000 | 103,004 | (1,996) |
| Franchise taxes | 100,000 | 100,000 | 71,667 | (28,333) |
| Other revenues | 1,125 | 1,125 | 20,351 | 19,226 |
| Total revenues | <u>305,125</u> | <u>305,125</u> | <u>293,293</u> | <u>(11,832)</u> |
| EXPENDITURES | | | | |
| General government | 167,100 | 167,100 | 122,549 | 44,551 |
| Fire protection | 7,000 | 7,000 | 14,763 | (7,763) |
| Streets | 99,153 | 99,153 | 46,954 | 52,199 |
| Municipal court | 2,500 | 2,500 | 1,100 | 1,400 |
| Health and welfare | - | - | 10,834 | (10,834) |
| Capital outlay | 21,500 | 21,500 | 59,228 | (37,728) |
| Debt service | | | | |
| Principal retired | - | - | 3,395 | (3,395) |
| Interest | - | - | 871 | (871) |
| Total expenditures | <u>297,253</u> | <u>297,253</u> | <u>259,694</u> | <u>37,559</u> |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES | <u>7,872</u> | <u>7,872</u> | <u>33,599</u> | <u>25,727</u> |
| OTHER FINANCING SOURCES (USES) | | | | |
| Loan proceeds | - | - | 27,310 | 27,310 |
| Transfers in (out) | (12,847) | (12,847) | (26,320) | (13,473) |
| Net other financing sources | <u>(12,847)</u> | <u>(12,847)</u> | <u>990</u> | <u>13,837</u> |
| NET CHANGE IN FUND BALANCE | <u>(4,975)</u> | <u>(4,975)</u> | <u>34,589</u> | <u>39,564</u> |
| FUND BALANCE - BEGINNING OF YEAR | <u>209,707</u> | <u>209,707</u> | <u>209,707</u> | <u>-</u> |
| FUND BALANCE - END OF YEAR | <u>\$ 204,732</u> | <u>\$ 204,732</u> | <u>\$ 244,296</u> | <u>\$ 39,564</u> |

See Independent Auditors' Report.

CITY OF ELKHART, TEXAS
SCHEDULE OF FUNDING PROGRESS OF PENSION PLAN -
TEXAS MUNICIPAL RETIREMENT SYSTEM
FOR THE YEAR ENDED SEPTEMBER 30, 2014

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

| Actuarial Valuation Date | Actuarial Value of Assets | Actuarial Accrued Liability (AAL) | Funded Ratio | Unfunded AAL (UAAL) | Covered Payroll | UAAL as a Percentage of Covered Payroll |
|--------------------------------|---------------------------------|--|-----------------|---------------------------|--------------------|--|
| | (1) | (2) | (3) | (4) | (5) | (6) |
| | | | (1) / (2) | (2) - (1) | | (4) / (5) |
| 12/31/2004 | \$ 204,522 | \$ 293,000 | 69.8 % | \$ 88,488 | \$ 113,966 | 64.6 % |
| 12/31/2005 | 234,238 | 321,273 | 72.9 | 87,035 | 166,553 | 52.2 |
| 12/31/2006 | 263,795 | 369,664 | 71.4 | 105,869 | 170,091 | 62.2 |
| 12/31/2007 | 295,505 | 447,407 | 66.0 | 151,902 | 227,957 | 66.6 |
| 12/31/2008 | 331,711 | 473,805 | 70.0 | 142,094 | 206,043 | 69.0 |
| 12/31/2009 | 382,117 | 506,778 | 75.4 | 124,661 | 233,976 | 53.3 |
| 12/31/2010 | 429,537 | 549,823 | 78.1 | 120,286 | 227,371 | 52.9 |
| 12/31/2011 | 438,601 | 531,054 | 82.6 | 92,453 | 232,916 | 39.7 |

Combining Statements

**CITY OF ELKHART, TEXAS
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
SEPTEMBER 30, 2014**

| | <u>Debt Service Fund</u> | <u>Street Maintenance Fund</u> | <u>Total</u> |
|--|----------------------------------|--|-------------------------|
| ASSETS | | | |
| Receivables | | | |
| Sales taxes | \$ - | \$ 1,952 | \$ 1,952 |
| Restricted assets | | | |
| Cash and cash equivalents | <u>5,937</u> | <u>7,991</u> | <u>13,928</u> |
| TOTAL ASSETS | <u>\$ 5,937</u> | <u>\$ 9,943</u> | <u>\$ 15,880</u> |
| LIABILITIES | | | |
| Due to other funds | <u>\$ 84</u> | <u>\$ -</u> | <u>\$ 84</u> |
| Total liabilities | <u>84</u> | <u>-</u> | <u>84</u> |
| FUND BALANCES | | | |
| Restricted for: | | | |
| Debt service | 5,853 | - | 5,853 |
| Street maintenance | - | 9,943 | 9,943 |
| Unassigned | <u>-</u> | <u>-</u> | <u>-</u> |
| Total fund balances | <u>5,853</u> | <u>9,943</u> | <u>15,796</u> |
| TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND FUND BALANCES | <u>\$ 5,937</u> | <u>\$ 9,943</u> | <u>\$ 15,880</u> |

CITY OF ELKHART, TEXAS
COMBINING STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES - NONMAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2014

| | Debt Service Fund | Street Maintenance Fund | Total |
|---|-------------------------|-------------------------------|------------------|
| REVENUES | | | |
| Sales taxes | \$ - | \$ 25,751 | \$ 25,751 |
| Interest income | <u>343</u> | <u>-</u> | <u>343</u> |
| Total revenues | <u>343</u> | <u>25,751</u> | <u>26,094</u> |
| EXPENDITURES | | | |
| Streets | - | 17,621 | 17,621 |
| Debt service | | | |
| Principal retired | 40,000 | - | 40,000 |
| Interest | <u>30,902</u> | <u>-</u> | <u>30,902</u> |
| Total expenditures | <u>70,902</u> | <u>17,621</u> | <u>88,523</u> |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES | <u>(70,559)</u> | <u>8,130</u> | <u>(62,429)</u> |
| OTHER FINANCING SOURCES (USES) | | | |
| Transfers in (out) | <u>23,518</u> | <u>-</u> | <u>23,518</u> |
| Net other financing sources (uses) | <u>23,518</u> | <u>-</u> | <u>23,518</u> |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES AND OTHER USES | (47,041) | 8,130 | (38,911) |
| FUND BALANCES - BEGINNING OF YEAR | <u>52,894</u> | <u>1,813</u> | <u>54,707</u> |
| FUND BALANCES - END OF YEAR | <u>\$ 5,853</u> | <u>\$ 9,943</u> | <u>\$ 15,796</u> |

COMPLIANCE SECTION

Todd, Hamaker & Johnson, LLP

CERTIFIED PUBLIC ACCOUNTANTS

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

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

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Honorable Mayor and Members of the City Council
City of Elkhart, Texas

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, each major fund, and the aggregate remaining fund information of the City of Elkhart, Texas (the "City"), as of and for the year ended September 30, 2014, and the related notes to the financial statements, which collectively comprise the City of Elkhart, Texas' basic financial statements, and have issued our report thereon dated January 30, 2015.

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.

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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section 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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs as 2014-001, that we consider to be significant deficiencies.

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,

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT
AUDITING STANDARDS - CONTINUED**

contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

City of Elkhart, Texas' Response to Findings

City of Elkhart, Texas' 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.

Todd, Hamaker & Johnson, LLP

Todd, Hamaker & Johnson, LLP
Lufkin, Texas

January 30, 2015

Todd, Hamaker & Johnson, LLP

CERTIFIED PUBLIC ACCOUNTANTS

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

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

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

To the Honorable Mayor and Members of the City Council
City of Elkhart, Texas

Report on Compliance for Each Major Federal Program

We have audited the City of Elkhart, Texas' (the "City") 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, 2014. 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.

Auditors' 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, 2014.

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

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED
BY OMB CIRCULAR A-133 – CONTINUED**

auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on 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.

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.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we identified certain deficiencies in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as items 2014-002 and 2014-003, that we consider to be significant deficiencies.

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

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.

Todd, Hamaker & Johnson, LLP

Todd, Hamaker & Johnson, LLP
Lufkin, Texas

January 30, 2015

CITY OF ELKHART, TEXAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED SEPTEMBER 30, 2014

| Federal Grantor/ Pass-through Grantor/Other Grantor Program Title/Grant Title | Federal CFDA Number | Grant Number | Expenditures |
|---|---------------------------|-------------------------------|--------------------------|
| <u>U.S. Department of Housing and Urban Development</u> | | | |
| Passed through Texas Department of Agriculture | | | |
| Community Development Block Grant/State's Program and Non-Entitlement Grants in Hawaii | 14.228 | 713151 | \$ 18,712 |
| Community Development Block Grant/State's Program and Non-Entitlement Grants in Hawaii | 14.228 | 712172 | 115,533 |
| Passed through Texas General Land Office | | | |
| Community Development Block Grant/State's Program and Non-Entitlement Grants in Hawaii | 14.228 | DRS210044/ 12-285-000-5633 | <u>508,101</u> |
| Total for CFDA 14.228 | | | <u>642,346</u> |
| Passed through Texas Department of Housing and Community Affairs | | | |
| Home Investments Partnerships Program | 14.239 | 1001801 | <u>269,624</u> |
| Total for CFDA 14.239 | | | <u>269,624</u> |
| Total U.S. Department of Housing and Urban Development: | | | <u>911,970</u> |
| Total Federal Awards Expended: | | | <u>\$ 911,970</u> |

See accompanying notes to the schedule of expenditures of federal awards.

CITY OF ELKHART, TEXAS
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED SEPTEMBER 30, 2014

NOTE 1 – Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards ("Schedule") includes the federal grant activity of the City of Elkhart, Texas under programs of the federal government for the year ended September 30, 2014. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of the City of Elkhart, Texas, it is not intended to and does not present the financial position, changes in net position, or cash flows of the City of Elkhart, Texas.

NOTE 2 – Summary of Significant Accounting Policies

Expenditures shown on the Schedule are reported on the accrual basis of accounting and accordingly, all significant receivables, payables, and other liabilities are included. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

NOTE 3 – Presentation of Expenditures

Expenditures included in the Schedule are reported exclusive of non-federal matching funds.

NOTE 4 – Other

Pass-through entity identifying numbers are presented where available.

**CITY OF ELKHART, TEXAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED SEPTEMBER 30, 2014**

Section I – Summary of Auditors' Results

Financial Statements

Type of auditors' report issued:

unmodified

- Material weakness(es) identified? _____ yes ☒ no
- Significant deficiency(ies) identified that are not considered to be material weakness(es)? ☒ yes _____ none reported

Non-compliance material to financial statements noted?

_____ yes ☒ no

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? _____ yes ☒ no
- Significant deficiency(ies) identified that are not considered to be material weakness(es)? ☒ yes _____ none reported

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

unmodified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133?

_____ yes ☒ no

Identification of major programs:

CFDA Number(s)

Name of Federal Program or Cluster

14.228

Community Development Block Grants

Dollar threshold used to distinguish between type A and type B federal programs:

\$ 300,000

Auditee qualified as a low-risk auditee?

_____ yes ☒ no

**CITY OF ELKHART, TEXAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED SEPTEMBER 30, 2014**

Section III – Major Federal Award Programs Audit Findings and Questioned Costs

2014-002 Significant Control Deficiency and Non-compliance: Grant Management

CFDA 14.228 – Community Development Block Grants

CFDA 14.239 – Home Investments Partnerships Program

Condition. A complete, accurate schedule of expenditures of federal awards (“SEFA”) was not provided by the City.

Criteria or Specific Requirements. OMB Circular A-133 requires grantees to prepare a SEFA which properly identifies all federal awards expended and includes for each federal award:

- The federal granting agency and program;
- The five-digit Catalog of Federal Domestic Assistance (CFDA) number;
- The grant’s name (as specified by the grant award);
- The total expenditures of funds provided by the *American Recovery and Reinvestment Act of 2009* (ARRA);
- Any identifying numbers assigned by pass-through entities; and
- The expenditures.

Effect. Failure to provide a complete and accurate SEFA can lead to a failure to identify the need for an annual financial audit in accordance with the standards outlined in OMB Circular A-133 (“Single Audit”). Additionally, an inaccurate SEFA could lead to an improperly planned and executed single audit.

Questioned Costs. None.

Context. Our audit procedures revealed grant revenues/expenditures that were either not recorded in the financial statements or not properly identified as grant-related. In several instances, accounting for grant transactions was inconsistent and grant documents were not readily available at the city office. In at least one instance, the City had paid a vendor prior to having the expenditure approved by the granting agency, necessitating a refund to the City by the vendor.

Recommendation. The City should review and revise, as needed, the policies and procedures in place to ensure that a SEFA is prepared annually and that all federal grants are properly included. We also recommend that the City implement a policy whereby the compiled SEFA is subjected to a secondary review by a party with proper knowledge of the City’s grants and grant policies. The City should consider obtaining additional training as needed, on grant management and other OMB Circular A-133 reporting requirements for those involved in the grant process and preparation of the SEFA.

Views of Responsible Officials and Corrective Action. Management agrees with the observation and recommendation. For fiscal year 2015, a schedule listing all current grants as outlined above will be provided. Additionally, we will have the SEFA reviewed by our grant administrator prior to submission to our auditors.

**CITY OF ELKHART, TEXAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED SEPTEMBER 30, 2014**

2014-003 Significant Control Deficiency and Non-compliance: Equipment Management

CFDA 14.228 – Community Development Block Grants

Federal Agency: Department of Housing and Urban Development

Passed Through: Texas Department of Agriculture, Awards 713151 and 712172

Texas General Land Office, Award DRS210044/12-285-000-5633

Condition. The City does not have a written fixed asset management policy consistent with guidelines for federally funded projects.

Criteria or Specific Requirements. As required by OMB Circular A-87, an entity that acquires equipment with federal funds must implement an appropriate control system to safeguard and maintain the equipment and to provide for final disposal once the equipment is no longer needed. Further, grant agreements between the City of Elkhart and the grantors listed above reference and require an asset control system.

Effect. Failure to implement the required policies and procedures could result in improper fixed asset tracking, potential loss or theft of assets, denial of future federal funding, and could subject the City to other penalties imposed by the federal agency.

Questioned Costs. None.

Context. Historically, the City has relied on its external auditors to maintain a detailed listing of assets. This listing is sufficient for financial accounting purposes, does not include all of the elements required by grant management standards.

Recommendation. We recommend that the City develop a written fixed asset management policy, to be approved by the city council, consistent with criteria as noted above (and consistent with the criteria listed in finding 2014-001) so as to ensure compliance with all state and/or federal funding requirements.

Views of Responsible Officials and Corrective Action. Management agrees with the observation and recommendation. The City will develop and approve a written fixed asset management policy to be consistent with criteria required by OMB Circular A-87.

**CITY OF ELKHART, TEXAS
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED SEPTEMBER 30, 2014**

There were no findings reported in the prior year.