

CITY OF HITCHCOCK, TEXAS

ANNUAL FINANCIAL REPORT

Year Ended September 30, 2014

CITY OF HITCHCOCK, TEXAS
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FINANCIAL SECTION

INDEPENDENT AUDITOR'S REPORT

To the Honorable Anthony Matranga, Mayor
and Members of the City Commission
City of Hitchcock, Texas

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Hitchcock, 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.

Auditor's Responsibility

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

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

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

To the Honorable Anthony Matranga, Mayor
and Members of the City Commission
City of Hitchcock, Texas

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City, 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.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 7 through 14 budgetary comparison information on pages 48 through 49, and schedule of funding progress on page 50, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide 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 and individual nonmajor fund financial statements 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 and individual nonmajor fund financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the 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 and individual 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.

To the Honorable Anthony Matranga, Mayor
and Members of the City Commission
City of Hitchcock, Texas

Other Reporting Required by *Government Auditing Standards*

In accordance with Government Auditing Standards, we have also issued our reported dated June 22, 2015, on our consideration of the City's internal control over financial reporting 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, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "Whitley Penn LLP". The signature is written in a cursive, flowing style.

Texas City, Texas
June 22, 2015

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MANAGEMENT'S DISCUSSION AND ANALYSIS

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CITY OF HITCHCOCK, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Hitchcock (the "City"), we offer the 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.

Financial Highlights

The assets of the City exceeded its liabilities at the close of the most recent fiscal year by \$14.5 million (net position). Of this amount, \$11.0 million is net investment in capital assets, \$0.5 million is restricted, leaving \$3.0 million in unrestricted net position.

As of the close of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$2.11 million, an increase of \$126 thousand from the prior year.

Overview of the Financial Statements

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

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

The statement of net 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 government's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g. uncollected taxes and earned but unused vacation leave).

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

The government-wide financial statements include the City itself (known as the primary government), but also legally separate component units. Financial information for these component units are reported separately from the financial information presented for the primary government itself.

The government-wide financial statements can be found on pages 17 through 19 of this report.

CITY OF HITCHCOCK, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

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

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

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

The City maintains seven individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures and changes in fund balances for the general fund, debt service fund, and the Community Development Block Grant fund, which are considered to be major funds. Data from the other four governmental funds are combined into a single, aggregated presentation.

The basic governmental fund financial statements can be found on pages 20 through 23 of this report.

Proprietary Funds. The City maintains one type of proprietary fund. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses an enterprise fund to account for its Water and Wastewater utility fund. Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Water and Sewer Operating fund which is considered to be a major fund of the City.

The basic proprietary fund financial statements can be found on pages 24 through 26 of this report.

Notes to the Basic 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 basic financial statements can be found on pages 27 through 46 of this report.

CITY OF HITCHCOCK, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Other Information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the City's progress in funding its obligation to provide pension benefits to its employees and general fund budgetary comparisons. Required supplementary information can be found on pages 48 through 50 of this report.

The combining statements referred to earlier in connection with nonmajor governmental funds are presented immediately following the required supplementary information on pensions. Combining and individual fund statements and schedules can be found on pages 54 through 59 of this report.

Government-wide Financial Analysis

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. In the case of the City, assets exceeded liabilities by \$14.5 million.

By far the largest portion of the City's net position of \$11.0 million reflects its investment in capital assets (e.g., land, buildings, infrastructure, machinery and equipment) less any related debt used to acquire those assets that is still outstanding. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources since the capital assets themselves cannot be used to liquidate these liabilities.

CITY OF HITCHCOCK, TEXAS

Table A-1

Net Position (in thousands)

September 30, 2014

With Comparative Totals for September 30, 2013

	2014			2013		
	Governmental Activities	Business- type Activities	Total	Governmental Activities	Business- type Activities	Total
Current assets	\$ 4,648	\$ 1,674	\$ 6,322	\$ 3,570	\$ 1,746	\$ 5,316
Capital assets	5,455	8,756	14,211	5,171	6,774	11,945
Total Assets	10,103	10,430	20,533	8,741	8,520	17,261
Current liabilities	2,214	587	2,801	1,266	509	1,775
Long-term liabilities	497	2,719	3,216	637	2,317	2,954
Total Liabilities	2,711	3,306	6,017	1,903	2,826	4,729
Net position						
Net investment in capital assets	4,987	6,059	11,046	4,564	4,479	9,043
Restricted	56	400	456	561	405	966
Unrestricted	2,349	665	3,014	1,713	810	2,523
Total Net Position	\$ 7,392	\$ 7,124	\$ 14,516	\$ 6,838	\$ 5,694	\$ 12,532

An additional portion of the City's net position, \$0.5 million, represents resources that are subject to external restrictions on how they may be used. The amount of unrestricted net position is \$3.0 million.

CITY OF HITCHCOCK, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

The government's net position increased by \$2.0 million during the current fiscal year. The following table summarizes the changes in net position for the City for the year ended September 30, 2014:

CITY OF HITCHCOCK, TEXAS
Changes in Net Position (in thousands)
For the Fiscal Year Ended September 30, 2014
With Comparative Totals for September 30, 2013

Table A-2

	2014			2013		
	Governmental Activities	Business- type Activities	Total	Governmental Activities	Business- type Activities	Total
Revenues						
Program Revenues:						
Charges for services	\$ 1,154	\$ 2,279	\$ 3,433	\$ 1,162	\$ 2,380	\$ 3,542
Operating grants and contributions	2,549	64	2,613	1,376	141	1,517
Capital grants and contributions	-	2,162	-	-	-	-
General revenues:						
Property taxes	1,037	-	1,037	966	-	966
Sales taxes	315	-	315	459	-	459
Franchise fees	1,164	-	1,164	665	-	665
Other	61	1	62	55	-	55
Total Revenues	6,280	4,506	10,786	4,683	2,521	7,204
Expenses						
General government	951	-	951	591	-	591
Public safety	1,671	-	1,671	1,668	-	1,668
Public works	2,871	-	2,871	760	-	760
Health, welfare and sanitation	42	-	42	39	-	39
Culture and recreation	97	-	97	96	-	96
Interest on long-term debt	-	-	-	-	-	-
Water	-	1,747	1,747	-	1,418	1,418
Sewer	-	1,423	1,423	-	1,841	1,841
Total Expenses	5,632	3,170	8,802	3,154	3,259	6,413
Transfer in (out)	(94)	94				
Change in net position	554	1,430	1,984	1,529	(738)	791
Beginning Net Position	6,838	5,694	12,532	5,309	6,485	11,794
Prior period adjustment	-	-	-	-	(53)	(53)
Ending Net Position	\$ 7,392	\$ 7,124	\$ 14,516	\$ 6,838	\$ 5,694	\$ 12,532

CITY OF HITCHCOCK, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Governmental activities. Governmental activities increased the City's net position by \$0.55 million. A comparison of program expenses to program revenues and revenues by source for governmental activities follows:

CITY OF HITCHCOCK, TEXAS

Table A-3

Expenses, Program Revenues and Net Cost of Services - Governmental Activities (in thousands)

For the Fiscal Year Ended September 30, 2014

With Comparative Totals for September 30, 2013

Program	2014			2013		
	Expenses	Program Revenues	Net (Cost) of Services	Expenses	Program Revenues	Net (Cost) of Services
General government	\$ 951	\$ -	\$ (951)	\$ 591	\$ -	\$ (591)
Public safety	1,671	673	(998)	1,668	651	(1,017)
Public works	2,871	2,997	126	760	1,818	1,058
Health, welfare and sanitation	42	33	(9)	39	69	30
Culture and recreation	97	-	(97)	96	-	(96)
	<u>\$ 5,632</u>	<u>\$ 3,703</u>	<u>\$ (1,929)</u>	<u>\$ 3,154</u>	<u>\$ 2,538</u>	<u>\$ (616)</u>

Revenue sources for governmental activities were distributed as follows:

CITY OF HITCHCOCK, TEXAS

Table A-4

Revenues by Source- Governmental Activities (in thousands)

For the Fiscal Year Ended September 30, 2014

With Comparative Totals for September 30, 2013

	2014		2013	
	Dollars	Percentage	Dollars	Percentage
Charges for services	\$ 1,154	19%	\$ 1,162	25%
Operating grants and contributions	2,549	41%	1,376	29%
Property taxes	1,037	17%	966	21%
Franchise fees	315	5%	459	10%
Sales tax	1,164	19%	665	14%
Other taxes	61	1%	55	1%
	<u>\$ 6,280</u>	<u>102%</u>	<u>\$ 4,683</u>	<u>100%</u>

CITY OF HITCHCOCK, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Business-type activities. The net position of the City's business-type activities decreased by approximately \$1.4 million. A comparison between expenses relating to water and sewer operations and program revenues (charges for services and operating grants) follows.

CITY OF HITCHCOCK, TEXAS *Table A-5*
Expenses, Program Revenues, and Net Cost of Services - Business Type Activities (in thousands)
For the Fiscal Year Ended September 30, 2014
With Comparative Totals for September 30, 2013

Program	2014		2013	
	Expenses	Program Revenues	Net (Cost) of Services	Net (Cost) of Services
Water	\$ 1,747	\$ 2,589	\$ 842	\$ 147
Sewer	1,423	1,916	493	(885)
Total	\$ 3,170	\$ 4,505	\$ 1,335	\$ (738)

Revenue sources for business-type activities were distributed as follows:

CITY OF HITCHCOCK, TEXAS *Table A-6*
Revenues by Source- Business Type Activities (in thousands)
For the Fiscal Year Ended September 30, 2014
With Comparative Totals for September 30, 2013

	2014		2013	
	Dollars	Percentage	Dollars	Percentage
Charges for services	\$ 2,279	51%	\$ 2,380	94%
Operating grants and contributions	64	1%	141	6%
Capital grants and contributions	2,162	48%		0%
Other revenue	1	0%		0%
Total	\$ 4,506	100%	\$ 2,521	100%

Financial Analysis of the Government's Funds

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

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

As of the end of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$2.11 million.

The General fund is the chief operating fund of the City. At the end of the current fiscal year, the fund balance of the general fund was \$2.04 million. This is approximately \$608 thousand more than September 30, 2013.

CITY OF HITCHCOCK, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

The Debt Service fund had a total fund balance of \$0, since all of the City's general obligation debt has been retired. The net decrease in fund balance from the prior year was approximately \$494 thousand.

The Community Development Block Grant Fund ("CDBG") is used to account for funds associated with the CDBG disaster recovery program. This fund had a total fund balance of \$100, all of which is restricted for the CDBG program. There was no change in fund balance for CDBG from the prior fiscal year.

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

Unrestricted net position of the Water and Sewer Enterprise fund at the end of the year amounted to \$665 thousand or 21% of annual operating and non-operating expenses for the fund.

General Fund Budgetary Highlights

The City amended the general fund budget during the fiscal year in order to appropriate budgetary funds for lease purchase payments in the amount of \$159,068.

Capital Assets and Debt Administration

Capital Assets. The City's investment in capital assets for its governmental and business type activities, as of September 30, 2014, amounted to \$14.2 million (net of accumulated depreciation). This investment in capital assets includes land, construction in progress, buildings, park facilities, water and wastewater plants and service lines, machinery and equipment. The total decrease in the City's investment in capital assets for the current fiscal year was approximately 19.0%.

A summary of capital assets, as of September 30, 2014, is as follows:

CITY OF HITCHCOCK, TEXAS

Table A-7

Capital Assets, net of depreciation where applicable (in thousands)

September 30, 2014

With Comparative Totals for September 30, 2013

	2014			2013		
	Governmental Activities	Business- Type Activities	Total	Governmental Activities	Business- Type Activities	Total
Land	\$ 1,425	\$ 62	\$ 1,487	\$ 1,425	\$ 57	\$ 1,482
Construction in progress	2,809	-	2,809	2,478	-	2,478
Infrastructure	-	7,821	7,821	-	6,311	6,311
Buildings	581	122	703	613	128	741
Equipment and furniture	641	752	1,393	155	280	435
Assets under capital lease	-	-	-	499	-	499
	<u>\$ 5,456</u>	<u>\$ 8,757</u>	<u>\$ 14,213</u>	<u>\$ 5,170</u>	<u>\$ 6,776</u>	<u>\$ 11,946</u>

Additional information on the City's capital assets can be found in Note 7 of the basic financial statements of this report.

CITY OF HITCHCOCK, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Long-Term Debt. At the end of the current fiscal year, the City had total bonded debt outstanding of approximately \$2.14 million which represents revenue bonds secured solely by specified revenue sources.

CITY OF HITCHCOCK, TEXAS

Table A-8

Outstanding Debt (in thousands)

September 30, 2014

With Comparative Totals for September 30, 2013

	2014			2013		
	Governmental Activities	Business- Type Activities	Total	Governmental Activities	Business- Type Activities	Total
Certificates of obligation	\$ -	\$ 1,098	\$ 1,098	\$ -	\$ 1,114	\$ 1,114
Contract revenue bonds	-	1,046	1,046	-	1,117	1,117
Capital lease obligations	468	495	963	607	-	607
	<u>\$ 468</u>	<u>\$ 2,638</u>	<u>\$ 3,106</u>	<u>\$ 607</u>	<u>\$ 2,231</u>	<u>\$ 2,838</u>

The City's total debt decreased by approximately \$268 thousand during the fiscal year.

Additional information on the City's long-term debt can be found in Note 8 of the basic financial statements of this report.

Economic Factors and Next Year's Budgets and Rates

The unemployment rate for the County in which the City is located is currently 4.7 percent, which is an decrease of 3.2 percent from a year ago. This is higher than the state's average unemployment rate of 4.2 percent and the national average rate of 5.5 percent.

The City approved a general fund budget of 3.46 million for the fiscal year 2014 - 2015, which is an increase of 17.7% over the current year. The tax rate of \$.413202 per \$100 valuation was approved.

Requests for Information

This financial report is designed to provide a general overview of the City's finances for all those with an interest in the government's finances. Questions concerning any of the information should be addressed to the Office of the City Secretary, 7423 Highway 6, Hitchcock, Texas 77563.

BASIC FINANCIAL STATEMENTS

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CITY OF HITCHCOCK, TEXAS

STATEMENT OF NET POSITION

September 30, 2014

Exhibit A-1

	<u>Primary Government</u>			
	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>	<u>Component Units</u>
Assets				
Current Assets:				
Cash and temporary investments	\$ 2,374,804	\$ 941,044	\$ 3,315,848	\$ 2,008,548
Receivables	1,880,934	222,268	2,103,202	91,711
Internal balances	38,034	(38,034)	-	-
Prepaid items	1,784	2,381	4,165	-
Restricted Assets:				
Cash and temporary investments	352,500	546,656	899,156	746,190
Total Current Assets	<u>4,648,056</u>	<u>1,674,315</u>	<u>6,322,371</u>	<u>2,846,449</u>
Capital Assets:				
Land	1,424,690	61,776	1,486,466	-
Construction in progress	2,809,351	-	2,809,351	-
Capital assets, net of depreciation/amortization:				
Infrastructure	-	7,821,243	7,821,243	-
Buildings	580,685	122,103	702,788	-
Furniture, equipment and vehicles	640,581	750,810	1,391,391	-
Total Capital Assets	<u>5,455,307</u>	<u>8,755,932</u>	<u>14,211,239</u>	<u>-</u>
Total Assets	<u>10,103,363</u>	<u>10,430,247</u>	<u>20,533,610</u>	<u>2,846,449</u>
Liabilities				
Accounts payable and other current liabilities	2,213,689	545,775	2,759,464	32,229
Due to other governmental agencies	-	5,020	5,020	-
Unearned revenue	-	36,277	36,277	-
Long-term liabilities:				
Due within one year:				
Bonds, capital leases and contracts	143,341	213,016	356,357	500,000
Accrued interest	-	12,220	12,220	83,100
Compensated absences	29,293	9,446	38,739	-
Due in more than one year:				
Bonds, capital leases and contracts	324,679	2,484,117	2,808,796	4,465,000
Total Liabilities	<u>2,711,002</u>	<u>3,305,871</u>	<u>6,016,873</u>	<u>5,080,329</u>
Net Position				
Net investment in capital assets	4,987,287	6,058,799	11,046,086	-
Restricted for:				
Debt service	-	400,241	400,241	-
Public Safety	56,219	-	56,219	-
Grants	100	-	100	-
Unrestricted	2,348,755	665,336	3,014,091	(2,233,880)
Total Net Position	<u>\$ 7,392,361</u>	<u>\$ 7,124,376</u>	<u>\$ 14,516,737</u>	<u>\$ (2,233,880)</u>

See Notes to Basic Financial Statements

CITY OF HITCHCOCK, TEXAS

STATEMENT OF ACTIVITIES

For the Year Ended September 30, 2014

Functions/Programs	Expenses	Program Revenue		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary Government				
Governmental Activities:				
General government	\$ 950,534	\$ -	\$ -	\$ -
Public safety	1,670,772	616,714	56,560	-
Public works	2,870,999	504,350	2,492,665	-
Health, welfare and sanitation	42,330	32,659	-	-
Culture and recreation	97,349	-	-	-
Total Governmental Activities	5,631,984	1,153,723	2,549,225	-
Business-type Activities:				
Water	1,746,735	1,364,744	63,924	1,160,242
Sewer	1,423,046	914,425	-	1,001,387
Total Business-type Activities	3,169,781	2,279,169	63,924	2,161,629
Total Primary Government	\$ 8,801,765	\$ 3,432,892	\$ 2,613,149	\$ 2,161,629
Component Units				
Hitchcock Industrial Development Corporation	\$ 349,219	\$ -	\$ -	\$ -
Reinvestment Zone Number One	324,748	-	-	-
Total component units	\$ 673,967	\$ -	\$ -	\$ -

General revenues:

Taxes:

Property taxes, levied for general purposes

Property taxes, levied for debt service

Property taxes, Reinvestment Zone Number One

Franchise taxes

Public service taxes

Unrestricted investment earnings

Miscellaneous

Transfers

Total general revenues, special items and transfers

Change in net position

Net position - beginning

Net position - ending

See Notes to Basic Financial Statements.

Net (Expense) Revenue and Changes in Net Position			
Primary Government			
Governmental Activities	Business- type Activities	Total	Component Units
\$ (950,534)	\$ -	\$ (950,534)	
(997,498)	-	(997,498)	
126,016	-	126,016	
(9,671)	-	(9,671)	
(97,349)	-	(97,349)	
<u>(1,929,036)</u>	<u>-</u>	<u>(1,929,036)</u>	
-	842,175	842,175	
-	492,766	492,766	
-	1,334,941	1,334,941	
<u>(1,929,036)</u>	<u>1,334,941</u>	<u>(594,095)</u>	
			\$ (349,219)
-	-	-	<u>(324,748)</u>
-	-	-	<u>(673,967)</u>
1,026,911	-	1,026,911	-
10,316	-	10,316	-
-	-	-	736,344
315,131	-	315,131	-
1,163,769	-	1,163,769	387,923
10,113	1,311	11,424	2,719
50,851	-	50,851	-
(94,030)	94,030	-	-
<u>2,483,061</u>	<u>95,341</u>	<u>2,578,402</u>	<u>1,126,986</u>
554,025	1,430,282	1,984,307	453,019
6,838,336	5,694,094	12,532,430	(2,686,899)
<u>\$ 7,392,361</u>	<u>\$ 7,124,376</u>	<u>\$ 14,516,737</u>	<u>\$ (2,233,880)</u>

CITY OF HITCHCOCK, TEXAS

Exhibit B-1

BALANCE SHEET

GOVERNMENTAL FUNDS

September 30, 2014

	<u>General</u>	<u>Debt Service</u>	<u>Community Development Block Grant</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets					
Current assets:					
Cash and temporary investments	\$ 2,306,389	\$ -	\$ 100	\$ 68,315	\$ 2,374,804
Due from other funds	92,994	-	-	-	92,994
Accounts receivable, less allowance for doubtful accounts:					
Property taxes	328,983	-	-	-	328,983
Due from others	308,826	-	1,188,165	54,960	1,551,951
Prepaid Items	1,784	-	-	-	1,784
Restricted Assets:					
Cash and temporary investments	352,500	-	-	-	352,500
Total Assets	<u>\$ 3,391,476</u>	<u>\$ -</u>	<u>\$ 1,188,265</u>	<u>\$ 123,275</u>	<u>\$ 4,703,016</u>
Liabilities, Deferred Inflows of Resources, and Fund Balances					
Liabilities:					
Accounts payable	\$ 429,487	\$ -	\$ -	\$ -	\$ 429,487
Due to other funds	-	-	-	54,960	54,960
Other liabilities	243,537	-	1,188,165	-	1,431,702
Payable from restricted assets:					
Refundable deposits and bonds	352,500	-	-	-	352,500
Total Liabilities	<u>1,025,524</u>	<u>-</u>	<u>1,188,165</u>	<u>54,960</u>	<u>2,268,649</u>
Deferred Inflows of Resources					
Unavailable revenue - property taxes	323,430	-	-	-	323,430
	<u>323,430</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>323,430</u>
Fund Balance:					
Non-spendable:					
Prepaid items	1,784	-	-	-	1,784
Restricted:					
Culture and recreation	-	-	-	12,096	12,096
Grants	-	-	100	-	100
Public safety	-	-	-	56,219	56,219
Unassigned	2,040,738	-	-	-	2,040,738
Total Fund Balance	<u>2,042,522</u>	<u>-</u>	<u>100</u>	<u>68,315</u>	<u>2,110,937</u>
Total Liabilities, Deferred Inflows of Resources and Fund Balances	<u>\$ 3,391,476</u>	<u>\$ -</u>	<u>\$ 1,188,265</u>	<u>\$ 123,275</u>	<u>\$ 4,703,016</u>

CITY OF HITCHCOCK, TEXAS

Exhibit B-2

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET

TO THE STATEMENT OF NET POSITION

September 30, 2014

Total fund balance, governmental funds \$ 2,110,937

Amounts reported for governmental activities in the Statement of Net Position are different because:

Capital assets used in governmental activities are not current financial resources and, therefore, are not reported in this fund financial statement but are reported in the governmental activities of the Statement of Net Position. 5,455,307

Certain other long-term receivables are not available to pay current period expenditures and, therefore, are not reported in this fund financial statement but are reported in the governmental activities of the Statement of Position. 323,430

Some liabilities are not due and payable in the current period and are not included in the fund financial statements but are included in the governmental activities of the Statement of Net Position. These are as follows:

Capital leases payable (468,020)
Compensated absences (29,293)

Net position of governmental activities in the statement of net position \$ 7,392,361

See Notes to Basic Financial Statements.

CITY OF HITCHCOCK, TEXAS

Exhibit B-3

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

GOVERNMENTAL FUNDS

For the Year Ended September 30, 2014

	<u>General</u>	<u>Debt Service</u>	<u>Community Development Block Grant</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenues					
Property taxes	\$ 1,023,580	\$ 10,316	\$ -	\$ -	\$ 1,033,896
Sales, franchise and local taxes	1,478,900	-	-	-	1,478,900
Licenses and permits	504,350	-	-	-	504,350
Charges for services	139,181	-	-	-	139,181
Fines and forfeitures	411,227	-	-	15,974	427,201
Earnings on investments	9,472	641	-	-	10,113
Intergovernmental	83,030	-	2,492,665	54,960	2,630,655
Other	50,812	-	-	1,600	52,412
Total Revenues	<u>3,700,552</u>	<u>10,957</u>	<u>2,492,665</u>	<u>72,534</u>	<u>6,276,708</u>
Expenditures					
Current:					
General government	885,716	-	-	-	885,716
Public safety	1,482,815	-	-	59,846	1,542,661
Public works	612,742	-	-	-	612,742
Health, welfare and sanitation	42,330	-	-	-	42,330
Culture and recreation	95,614	-	-	-	95,614
Capital outlay	225,383	-	2,492,665	-	2,718,048
Debt service:					
Principal retirement	138,777	-	-	-	138,777
Interest and fees	20,292	-	-	-	20,292
Total Expenditures	<u>3,503,669</u>	<u>-</u>	<u>2,492,665</u>	<u>59,846</u>	<u>6,056,180</u>
Excess (deficiency) of revenues over expenditures	196,883	10,957	-	12,688	220,528
Other Financing Sources (Uses)					
Operating transfers in	504,921	-	-	-	504,921
Operating transfers out	(94,030)	(504,921)	-	-	(598,951)
Total Other Financing Sources (Uses)	<u>410,891</u>	<u>(504,921)</u>	<u>-</u>	<u>-</u>	<u>(94,030)</u>
Net change in fund balances	607,774	(493,964)	-	12,688	126,498
Fund balances - beginning of year	<u>1,434,748</u>	<u>493,964</u>	<u>100</u>	<u>55,627</u>	<u>1,984,439</u>
Fund balances - end of year	<u>\$ 2,042,522</u>	<u>\$ -</u>	<u>\$ 100</u>	<u>\$ 68,315</u>	<u>\$ 2,110,937</u>

See Notes to Basic Financial Statements.

CITY OF HITCHCOCK, TEXAS

Exhibit B-4

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
For the Year Ended September 30, 2014**

Net change in fund balances - total governmental funds: \$ 126,498

Amounts reported for Governmental Activities in the Statement of Activities are different because:

Governmental funds report outlays for capital assets as expenditures because such outlays use current financial resources. In contrast, the Statement of Activities reports only a portion of the outlay as expense. The outlay is allocated over the assets' estimated useful lives as depreciation expense for the period. This is the amount by which capital outlay \$2,718,048 exceeded depreciation 272,187 and capital contribution to enterprise fund \$2,161,629 in the current period. 284,232

Property tax revenues in the statement of activities that do not provide current financial resources are reported as unavailable revenue in the fund statements. 3,331

Governmental funds report repayment of long-term debt as an expenditure. In contrast, the Statement of Activities treats such repayments as a reduction in long-term liabilities. This is the amount of repayments made on long-term debt during the current year. 138,777

Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.

Decrease in accrued compensated absences. 1,187

Change in net position of governmental activities \$ 554,025

See Notes to Basic Financial Statements.

CITY OF HITCHCOCK, TEXAS*Exhibit C-1**STATEMENT OF NET POSITION**PROPRIETARY FUND**September 30, 2014*

	<u>2014</u>
Assets	
Current assets:	
Cash and temporary investments	\$ 941,042
Customer receivables (net of allowance for uncollectibles)	222,268
Prepaid items	2,381
Total current assets	<u>1,165,691</u>
Non-current assets:	
Restricted cash and temporary investments	546,656
Total non-current assets	<u>546,656</u>
Capital assets (net of depreciation):	
Land	61,776
Buildings	122,103
Infrastructure	7,821,243
Machinery and equipment	750,810
Total capital assets (net of depreciation)	<u>8,755,932</u>
Total Assets	<u>10,468,279</u>
Liabilities	
Current liabilities:	
Accounts payable and accrued expenses	416,598
Unearned revenues	36,277
Due to other funds	38,034
Total current liabilities	<u>490,909</u>
Current liabilities (payable from restricted assets):	
Customer deposits	134,195
Current portion of long-term debt payable	213,016
Current portion of capital leases payable	53,833
Accrued interest payable	12,220
Compensated absences	9,446
Total current liabilities (payable from restricted assets)	<u>422,710</u>
Non-current liabilities:	
Long term debt payable	1,989,614
Capital leases payable	440,670
Total non-current liabilities (net of current portion)	<u>2,430,284</u>
Total Liabilities	<u>3,343,903</u>
Net Position:	
Net investment in capital assets	6,058,799
Restricted for debt service	400,241
Unrestricted	665,336
Total Net Position	<u>\$ 7,124,376</u>

See notes to basic financial statements.

CITY OF HITCHCOCK, TEXAS*Exhibit C-2***STATEMENT OF REVENUES, EXPENSES AND CHANGES IN****FUND NET POSITION****PROPRIETARY FUND***Year Ended September 30, 2014*

	<u>2014</u>
Operating Revenues	
Charges for services	\$ 2,279,169
Operating Expenses	
Personnel services	599,161
Contract Services	1,048,730
Supplies	187,731
Repair and maintenance	445,767
Depreciation	827,607
Total Operating Expenses	<u>3,108,996</u>
Operating income (loss)	<u>(829,827)</u>
Non-Operating Revenues (Expenses)	
Investment earnings	1,311
Interest expense and fiscal agent fees	(60,785)
Total Non-Operating Revenues (Expenses)	<u>(59,474)</u>
Income (loss) before contributions	(889,301)
Capital contributions	2,225,553
Operating transfers in	94,030
Change in net position	1,430,282
Total Net Position - beginning	<u>5,694,094</u>
Total Net Position - ending	<u>\$ 7,124,376</u>

See notes to basic financial statements.

CITY OF HITCHCOCK, TEXAS

Exhibit C-3

STATEMENT OF CASH FLOWS

PROPRIETARY FUND

Year Ended September 30, 2014

	2014
Cash flows from operating activities	
Receipts from customers and users	\$ 2,328,547
Payments to suppliers	(1,598,589)
Payments to employees	(597,148)
Net cash provided (used) by operating activities	<u>132,810</u>
 Cash flows from capital and related activities	
Proceeds from capital leases	574,547
Capital contributions	63,924
Purchase of assets	(646,016)
Principal payments on debt	(86,842)
Payments on capital leases	(80,590)
Interest and fiscal agent fees paid	(68,175)
Net cash provided (used) by capital and related activities	<u>(243,152)</u>
 Cash Flows from Noncapital Financing Activities	
Operating transfers	94,030
Net cash (used) by noncapital financing activities	<u>94,030</u>
 Cash flows from investing activities	
Interest earned on investments	1,311
Net cash provided by investing activities	<u>1,311</u>
 Net increase (decrease) in cash and cash equivalents	(15,001)
 Cash and cash equivalents, beginning	<u>1,502,699</u>
Cash and cash equivalents, ending	<u>\$ 1,487,698</u>
 Cash and temporary investments per balance sheet	
Unrestricted	\$ 941,042
Restricted	546,656
Cash and cash equivalents at end of year	<u>\$ 1,487,698</u>
 Reconciliation of operating income (loss) to net cash provided by operating activities:	
Operating income (loss)	\$ (829,827)
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	827,607
Changes in current assets and liabilities:	
(Increase) decrease in accounts receivable	42,020
(Increase) decrease in prepaid items	17,757
Increase (decrease) in accounts payable and accrued expenses	71,071
Increase (decrease) in customer deposits	7,358
Increase (decrease) in compensated absences	2,013
Increase (decrease) in interfund payables	(5,189)
Total adjustments	<u>962,637</u>
Net cash provided (used) by operating activities	<u>\$ 132,810</u>

See notes to basic financial statements.

Note 1 - Organization

The City of Hitchcock, Texas (the “City”) is a political subdivision of the State of Texas governed by an elected mayor and four member City Commission. The Mayor, as the official head of City government, resides at all meetings of Council and signs all official documents.

The City provides the following services: public safety, public works, parks and recreation, water and sewer and general administrative services.

Note 2 - Summary of Significant Accounting Policies

The financial statements of the City have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. The GASB is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the government's accounting policies are described as follows.

A. Reporting Entity

In conformity with GAAP, the financial statements of component units have been included in the financial reporting entity as discretely presented component units.

Hitchcock Industrial Development Corporation (the “Corporation”)

The mission of the Corporation is to provide economic development within the City and surrounding areas. The members of the Corporation are appointed by the City’s Commissioners. The Corporation’s budget requires the approval of the City’s Commissioners.

Reinvestment Zone Number One (the “TIRZ”)

The City designated approximately 850 acres of which at least 400 acres is designated wetlands, comprising the Harborwalk Development as a reinvestment zone in December 1999. A board of directors was established to make recommendations to the City Commission concerning administration of the TIRZ. A final project and financing plan was approved in February 2000. All project costs are to be advanced by the Developer, who will be reimbursed from proceeds of bonds issued by the City and payable from tax increments.

The component units identified above are included in the City's reporting entity because of the significance of their operational or financial relationships with the City. The City appoints the organizations' boards and is either able to impose its will on them or a financial benefit/burden exists.

Complete financial statements of the individual component units are not prepared.

The financial reporting entity consists of the primary government and other organizations for which the primary government is financially accountable.

The definition of the reporting entity is based primarily on the notion of financial accountability. A primary government is financially accountable for the organizations that make up its legal entity. It is also financially accountable for legally separate organizations if its officials appoint a voting majority of an organization's governing body and either it is able to impose its will on that organization or there is a potential for the organization to provide specific financial benefits to, or to impose specific financial burdens on, the primary government. A primary government may also be financially accountable for governmental organizations that are fiscally dependent on it.

Note 2 - Summary of Significant Accounting Policies (continued)

B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the Statement of Net Position and the Statement of Changes in Net Position) report information about the City as a whole. These statements include all nonfiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

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

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

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation

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

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

General property taxes are recorded as receivables when levied and as revenue in the period for which they were levied and become available. Property taxes receivable have been recorded as deferred inflows of resources at year end. Property taxes collected within 60 days subsequent to September 30, 2014, have not been recorded as revenue as the amount is not considered material. Franchise taxes and Sales taxes relating to underlying transactions that occurred prior to September 30, 2014, have been recorded as receivables and revenue. Licenses, permits and fines are not susceptible to accrual since they are not measurable until received. Revenue on federal and state cost-reimbursement grants is accrued when the related expenditures are incurred. Interest is recorded when earned.

Note 2 - Summary of Significant Accounting Policies (continued)

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation (continued)

The City reports the following major governmental funds:

The *General Fund* is used to account for all financial transactions that are not accounted for in another fund. The principal sources of revenue of the General Fund are property taxes, sales and use taxes, franchise taxes, licenses, permits, fines and forfeitures. Expenditures are for general government, public safety, public works and other community services.

The *Debt Service Fund* is used to account for the payment of interest and principal on all general long-term debt of the City except for capital leases which are accounted for in the General Fund. The primary source of revenue for the Debt Service Fund is general property taxes.

The *Community Development Block Grant ("CDBG") Fund* is used to account for a federal disaster recovery grant from the United States Department of Housing and Urban Development. The CDGB Fund is used for water and sewer improvements necessary as a result of Hurricane Ike.

The City has one major proprietary fund:

The *Water and Sewer Operating Fund* is used to account for operations of the water and wastewater division and the construction of related facilities. The fund is financed and operated in a manner similar to private business enterprises - where the intent of the City 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 acquisition, maintenance and improvement of the physical plant facilities required to provide these goods and services are financed from existing cash resources, the issuance of bonds (revenue or general obligation) and other City funds.

Amounts reported as program revenues include: 1) charges to customers or applicants for goods, services or privileges provided; 2) operating grants and contributions; and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenues rather than program revenues. Likewise, general revenues include all taxes.

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

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

Note 2 - Summary of Significant Accounting Policies (continued)

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation (continued)

GASB Statement No. 34 established standards for external financial reporting for all state and local governmental entities, which includes a statement of net position and a statement of activities. It requires the reclassification of net position into three components - invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are as follows:

- Net investment in capital assets - This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, notes or other borrowings.
- Restricted - This component of net position consists of constraints placed on net asset use through external constraints imposed by creditors, grantors, contributors, laws, regulations of other governments, constraints imposed by law through contractual provisions or enabling legislation.
- Unrestricted net position - This component of net position consists of net position that does not meet the definition of “restricted” or “net investment in capital assets.”

D. Cash and temporary investments (Cash Equivalents)

The City’s cash and temporary investments consist of cash on hand, amounts in demand deposits and short-term investments with a maturity date within three months of the date acquired by the City.

E. Receivables

All receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible. Estimated unbilled revenues from the Water and Sewer fund have not been recognized as of the end of the year as they are considered immaterial.

F. Due to and from other funds

Interfund receivables and payables arise from interfund transactions and are recorded by all funds affected in the period in which transactions are executed. These receivable and payables are, for the most part, eliminated from the Government-Wide Statement of Net Position and are recorded as “due from other funds” or “due to other funds” in the fund financial statements.

Note 2 - Summary of Significant Accounting Policies (continued)

G. Capital Assets

Capital assets are reported in the applicable governmental or business-type activities column in the government-wide financial statements. The government defines capital assets as assets with an initial, individual cost of \$5,000 or more and an estimated useful life in excess of one year. All purchased fixed assets are valued at cost where historical records exist. Donated fixed assets are valued at their estimated fair value on the date received.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Improvements, including public domain and equipment are capitalized and Proprietary Fund fixed assets are depreciated over the remaining useful lives of the related fixed assets using the straight line method, as applicable.

<u>Asset</u>	<u>Estimated Useful Life</u>
Building	40 years
Improvements	20-40 years
Water and sewer system	33 years
Heavy Equipment	10 years
Automobiles, trucks and equipment	5 years

H. Compensated absences

Employees earn vacation based on years of service with the City and may accumulate unused time. Sick leave is accrued at the rate of eight hours per month of employment. In accordance with GAAP, the liability for accumulated vacation, as of September 30, 2014, has been recorded as a liability in the Government-Wide Statement of Net Position.

I. General property taxes

All taxes due to the City on real or personal property are payable at the Office of the County Tax Assessor-Collector and may be paid at any time after the tax rolls for the year have been completed and approved, which is October 1, or as soon thereafter as practical. Taxes are due upon receipt and all taxes not paid prior to February 1 are deemed delinquent and are subject to such penalty and interest set forth by the Property Tax Code. All property located within the City limits on the first day of January of each year are charged with a special lien in favor of the City from such date for taxes due thereon.

J. Restricted assets

Certain proceeds of bonds, as well as other resources set aside for specific purposes, are classified as restricted assets on the balance sheet because their use is limited by applicable bond covenants or contractual agreements.

Note 2 - Summary of Significant Accounting Policies (continued)

K. Fund equity

Beginning with fiscal year 2011, the City implemented GASB Statement No. 54 “Fund Balance Reporting and Governmental Fund Type Definitions.” This Statement provides more clearly defined fund balance categories to make the nature and extent of the constraints placed on a government’s fund balances more transparent. The following classifications describe the relative strength of the spending constraints:

Non-spendable fund balance – amounts that are not in spendable form or are required to be maintained intact. As such, the inventory and prepaid items have been properly classified in the Governmental Funds Balance Sheet.

Restricted fund balance - amounts that can be spent only for specific purposes because of local, state or federal laws, or externally imposed conditions by grantors or creditors. Restrictions for capital acquisitions and contractual obligations, retirement of fund indebtedness and other state restrictions have been properly classified in the Governmental Funds Balance Sheet.

Committed fund balance – amounts constrained to specific purposes by the City itself, using its highest level of decision-making authority (i.e. the City Council). To be reported as committed, amounts cannot be used for any other purposes unless the City takes the same highest level of action to remove or change the constraint.

Assigned fund balance – amounts the City intends to use for a specific purpose. Intent can be expressed by the City or by an official or body to which the City Council delegates the authority.

Unassigned fund balance – amounts that are available for any purpose.

Beginning fund balances for the City’s governmental funds have been restated to reflect the above classifications.

The City establishes (and modifies and rescinds) fund balance commitments by passage of a resolution.

When multiple categories of fund balance are available for expenditure, the City will first spend the most restricted funds before moving down to the next most restrictive category with available funds.

L. Net Position

Net position represents the difference between assets and liabilities. Net position for net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowing used for the acquisition, construction or improvements of those assets, and adding back unspent proceeds. Net position is reported as restricted when there are limitations imposed on their use either through the enabling legislations adopted by the City or through external restrictions imposed by creditors, grantors or laws or regulations of other governments. When an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available, the City considers restricted funds to have been spent first.

Note 2 - Summary of Significant Accounting Policies (continued)

M. Revenues and expenditures/expenses

In the fund financial statements, revenues for governmental funds are recorded when they are determined to be both measurable and available. Generally, tax revenues, fees and non-tax revenues are recognized when received. Grants from other governments are recognized when qualifying expenditures are incurred. Expenditures for governmental funds are recorded when the related liability is incurred.

Revenues and expenses in the Government-Wide Statement of Activities are recognized in essentially the same manner as used in commercial accounting.

N. Use of estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual amounts could vary from those estimates.

O. Deferred outflows/inflows of resources

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then The City did not report any deferred outflows of resources for the year ending September 30, 2014.

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, deferred inflows of resources, 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 only one type of item that fits in this category, which is reported only in the governmental funds balance sheet. The governmental funds report unavailable revenues for uncollected property taxes. This amount is deferred and recognized as an inflow of resources in the period that the amount becomes available.

Note 3 - Cash and Temporary Investments (Cash Equivalents)

The City’s cash and temporary investments include demand accounts and certificates of deposits.

The City’s agent bank is required to pledge securities in an amount sufficient to protect City funds on a day-to-day basis during the period of the contract. The pledge of approved securities is waived only to the extent of the depository bank’s dollar amount of Federal Deposit Insurance Corporation (FDIC) insurance. At year end, not all deposits of the City and its component units were fully insured or collateralized by government obligation held in the City’s name by the City’s agent in accordance with Texas Law.

Investments (Cash Equivalents)

State statutes authorize the City to invest in: 1) obligations of the U.S. or its agencies and instrumentalities; 2) obligations of the State of Texas or its agencies; 3) other obligations guaranteed by the U.S., the State of Texas or their agencies and instrumentalities; 4) obligations of states, agencies, counties, cities and other political subdivisions of any state having been rated as to investment quality by a nationally recognized investment rating firm and having received a rating of not less than “A” or its equivalent; 5) guaranteed or secured certificates of deposit issued by state or national banks domiciled in Texas; 6) fully collateralized repurchase agreements; 7) a public funds investment pool meeting the requirements of Government Code 2256.016-2256.019; and, 8) commercial paper having received a rating of A1/P1 from a nationally recognized investment rating firm.

The Public Funds Investment Act (PFIA) governs the City’s investment policies and types of investment.

Currently, the City Commission has not adopted a written investment policy regarding the investment of funds as defined by the PFIA. However, the City’s investments (cash equivalents) are in compliance with the authorized investments provided by the PFIA. It is the City’s policy to invest all excess funds only in certificates of deposit (time deposits).

The City’s deposits and investments (cash equivalents), including those of the component units, as of September 30, 2014, are summarized below.

	Cash	Certificates	US Treasury	
	Equivalents	of Deposit	Money	Total
	Market			
Primary government	\$ 3,110,543	\$ 1,104,461	\$ -	\$ 4,215,004
Component units	1,676,999	195,280	882,459	2,754,738
	<u>\$ 4,787,542</u>	<u>\$ 1,299,741</u>	<u>\$ 882,459</u>	<u>\$ 6,969,742</u>

“Custodial Credit Risk” is the risk that in the event of a bank failure, the City’s deposits may not be returned to it. As of September 30, 2014, the City’s deposits were subject to custodial credit risk, as \$53,149 of the HICDC’s total deposits of \$303,149 was potentially uninsured and uncollateralized.

Note 4 - Restricted Assets

As of September 30, 2014, the City held restricted cash and temporary investments for the following purposes:

	<u>Governmental Activities</u>	<u>Business Type Activities</u>	<u>Component Units</u>
Restricted for:			
Customer deposits	\$ -	\$ 134,195	\$ -
Debt service	-	412,461	746,190
Bond escrow deposits	352,500	-	-
	<u>\$ 352,500</u>	<u>\$ 546,656</u>	<u>\$ 746,190</u>

Note 5 - Property Tax

Property taxes attach as an enforceable lien on property as of January 1. Taxes are levied on October 1 and are payable on or before January 31. No penalties or interest shall be collected if payment in full is made by January 31. City property taxes are recognized as current receivables when levied; however, such amounts are reported as deferred inflows of resources, and not reported as revenues until collections are received. At year end, all property taxes receivable are classified as delinquent. Penalties and interest accrued at September 30 are also recognized as receivables.

Within these guidelines, the tax rate per \$100 of assessed valuation, for the year ended September 30, 2014, was 41.3202 cents based on an assessed property valuation of approximately of \$288.8 million resulting in a tax levy of approximately \$1.2 million, all of which was to finance general governmental services.

Property taxes receivable, as of September 30, 2014, includes penalty and interest on delinquent accounts and an estimated allowance for uncollectible as follows:

<u>Tax Year</u>	<u>Taxes</u>	<u>Penalty and Interest</u>	<u>Less Allowance for Uncollectible Accounts</u>	<u>Net Property Taxes Receivable - Governmental Funds</u>
Prior	\$ 60,105	\$ 105,674	\$ (142,599)	\$ 23,180
2005	10,897	12,641	(471)	23,067
2006	13,170	13,697	(537)	26,330
2007	13,119	12,069	(504)	24,684
2008	13,874	11,098	(499)	24,473
2009	18,042	12,269	(606)	29,705
2010	22,759	12,744	(710)	34,793
2011	22,498	9,899	(648)	31,749
2012	34,628	11,081	(914)	44,795
2013	56,298	11,260	(1,351)	66,207
	<u>\$ 265,390</u>	<u>\$ 212,432</u>	<u>\$ (148,839)</u>	<u>\$ 328,983</u>

Note 6 - Receivables

Amounts recorded as receivables, as of September 30, 2014, for the government's individual major and nonmajor funds, including the applicable allowance for uncollectible accounts, are as follows:

	General	Debt Service	Community Development Block Grant	Other Governmental Funds	Water and Wastewater	Component Units
Receivables:						
Property taxes	\$ 477,822	\$ -	\$ -	\$ -	\$ -	\$ -
Franchise taxes	24,999	-	-	-	-	-
Sales taxes	275,133	-	-	-	-	91,711
Intergovernmental						
Accounts	8,694	-	1,188,165	54,960	335,683	-
Other	-	-	-	-	10,314	-
Gross receivables	786,648	-	1,188,165	54,960	345,997	91,711
Less: allowance for uncollectibles	(148,839)	-	-	-	(123,729)	-
Net Total Receivables	<u>\$ 637,809</u>	<u>\$ -</u>	<u>\$ 1,188,165</u>	<u>\$ 54,960</u>	<u>\$ 222,268</u>	<u>\$ 91,711</u>

Note 7 - Capital Assets

A summary of activity for capital assets, for the year ended September 30, 2014, follows:

	Balance October 1, 2013	Additions	Deletions/ Adjustments	Balance September 30, 2014
Governmental activities				
Capital assets, not being depreciated:				
Land	\$ 1,424,690	\$ -	\$ -	\$ 1,424,690
Construction in progress	2,478,315	2,492,665	(2,161,629)	2,809,351
Total capital assets not being depreciated	<u>3,903,005</u>	<u>2,492,665</u>	<u>(2,161,629)</u>	<u>4,234,041</u>
Capital assets being depreciated:				
Buildings and improvements	1,291,115	-	-	1,291,115
Machinery and equipment	1,729,527	225,383	-	1,954,910
Total capital assets being depreciated	<u>3,020,642</u>	<u>225,383</u>	<u>-</u>	<u>3,246,025</u>
Less accumulated depreciation for:				
Building and improvements	(677,658)	(32,772)	-	(710,430)
Machinery and equipment	(1,074,914)	(239,415)	-	(1,314,329)
Total accumulated depreciation	<u>(1,752,572)</u>	<u>(272,187)</u>	<u>-</u>	<u>(2,024,759)</u>
Total capital assets being depreciated, net	<u>1,268,070</u>	<u>(46,804)</u>	<u>-</u>	<u>1,221,266</u>
Governmental activities capital assets, net	<u>\$ 5,171,075</u>	<u>\$ 2,445,861</u>	<u>\$ (2,161,629)</u>	<u>\$ 5,455,307</u>

Note 7 - Capital Assets (continued)

	Balance October 1, 2013	Additions	Deletions/ Adjustments	Balance September 30, 2014
Business-type activities:				
Capital assets, not being depreciated:				
Land	\$ 57,276	\$ 4,500	\$ -	\$ 61,776
Total capital assets, not being depreciated	<u>57,276</u>	<u>4,500</u>	<u>-</u>	<u>61,776</u>
Capital assets being depreciated:				
Water/sewer system	19,631,075	2,161,629	-	21,792,704
Buildings and improvements	130,853	-	-	130,853
Machinery and equipment	1,092,037	642,061	-	1,734,098
Total capital assets being depreciated	<u>20,853,965</u>	<u>2,803,690</u>	<u>-</u>	<u>23,657,655</u>
Less accumulated depreciation for:				
Water/sewer system	(13,320,012)	(651,451)	-	(13,971,461)
Buildings and improvements	(2,917)	(5,833)	-	(8,750)
Machinery and equipment	(812,965)	(170,323)	-	(983,288)
Total accumulated depreciation	<u>(14,135,894)</u>	<u>(827,607)</u>	<u>-</u>	<u>(14,963,499)</u>
Total capital assets being depreciated, net	<u>6,718,071</u>	<u>1,976,083</u>	<u>-</u>	<u>8,694,156</u>
Business-type activities capital assets, net	<u>\$ 6,775,347</u>	<u>\$ 1,980,583</u>	<u>\$ -</u>	<u>\$ 8,755,932</u>

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

Governmental activities:

General	\$ 8,165
Garage	13,426
Public safety	167,673
Public works	81,188
Culture and recreation	1,735
Total Governmental activities	<u>\$ 272,187</u>

Business-type activities:

Water	\$ 319,063
Sewer	508,544
Total Business-type activities	<u>\$ 827,607</u>

As of September 30, 2014, the City had the following construction contract commitments outstanding related to construction in progress in the governmental activities:

	Total Commitment	Construction in Progress	Remaining Commitment
Sanitary Sewer System Improvements	\$ 2,002,466	\$ 1,116,331	\$ 886,135
Sewer Facilities	2,846,271	1,693,020	1,153,251
Water Facilities	1,093,701	-	1,093,701
Flood & Drainage Facilities	1,205,691	-	1,205,691
	<u>\$ 7,148,129</u>	<u>\$ 2,809,351</u>	<u>\$ 4,338,778</u>

Note 8 - Long-Term Debt

The City issues a variety of long-term debt instruments in order to acquire and/or construct major capital facilities and equipment for governmental and business-type activities. These instruments include general obligation bonds, certificates of obligation, notes payable and revenue bonds. Future ad valorem tax revenues, water and sewer system revenues or liens on property and equipment secure these debt obligations.

During the year ended September 30, 2014, the following changes occurred in long-term liabilities:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Governmental Activities					
Capital leases	\$ 606,797	\$ -	\$ (138,777)	\$ 468,020	\$ 53,797
Compensated absences	30,480	61,345	(62,532)	29,293	29,293
Long-term liabilities	<u>\$ 637,277</u>	<u>\$ 61,345</u>	<u>\$ (201,309)</u>	<u>\$ 497,313</u>	<u>\$ 83,090</u>
Business-type Activities					
Certificates of obligation	\$ 1,114,000	\$ -	\$ (16,000)	\$ 1,098,000	\$ 17,000
Contract revenue bonds	1,116,526	-	(70,842)	1,045,684	104,424
Less amounts:					
For issuance premiums/discounts	66,314	-	(7,368)	58,946	-
Capital leases	-	574,547	(80,590)	494,503	82,146
Compensated absences	7,433	20,808	(18,795)	9,446	9,446
Long-term liabilities	<u>\$ 2,304,273</u>	<u>\$ 595,355</u>	<u>\$ (193,595)</u>	<u>\$ 2,706,579</u>	<u>\$ 213,016</u>
Component Units					
Tax increment bonds	<u>\$ 5,435,000</u>	<u>\$ -</u>	<u>\$ (470,000)</u>	<u>\$ 4,965,000</u>	<u>\$ 500,000</u>

Annual debt service requirements to retire outstanding certificates of obligation are as follows:

Fiscal Year Ending September 30	<u>Business-type Activities</u>	
	<u>Principal</u>	<u>Interest</u>
2015	\$ 17,000	\$ 46,665
2016	17,000	45,943
2017	18,000	45,220
2018	19,000	44,455
2019	20,000	43,648
2020 - 2024	112,000	204,765
2025 - 2029	138,000	179,010
2030 - 2034	170,000	147,008
2035 - 2039	209,000	107,738
2040 - 2044	257,000	59,458
2045 - 2046	121,000	7,820
	<u>\$ 1,098,000</u>	<u>\$ 931,730</u>

Note 8 - Long-Term Debt (continued)

Annual debt service requirements to retire outstanding contract revenue bonds are as follows:

Fiscal Year Ending September 30	Business-type Activities	
	Principal	Interest
2015	\$ 104,424	\$ 35,413
2016	106,256	32,280
2017	109,920	29,092
2018	113,584	24,695
2019	119,080	20,152
2020-2022	492,420	31,217
	<u>\$ 1,045,684</u>	<u>\$ 172,849</u>

The following is a summary of the terms of certificates of obligation and revenue bonds outstanding as of September 30, 2014:

Business-type Activities

Series	Original Issue	Interest Rate	Matures	Principal Outstanding
Contract Revenue Bonds				
2011-B Contract Revenue Refunding Bonds	\$ 1,286,064	2.00 - 4.00%	2012 - 2022	\$ 1,045,684
Certificates of Obligation				
2006 Tax and Revenue Certificates of Obligations	1,185,000	4.25%	2011-2050	1,098,000
Total Business-Type Activities				<u>\$ 2,143,684</u>

Long-Term Contract Revenue Bonds

On July 1, 1998, the City of Hitchcock entered into a long-term contract with the Gulf Coast Water Authority (GCWA) to build and improve facilities for potable water transportation to the City of Hitchcock. The GCWA is a conservation and reclamation district created by Chapter 712, Acts of the 59th Texas Legislature, 1965, as amended (compiled as Article 8280-339, Vernon's Texas Civil Statutes, as amended). The GCWA issued bonds totaling \$4,835,000 in 1998 under the title "Gulf Coast Water Authority Water System Contract Revenue Bonds (South Project), Series 1998 B." Under the contract, the City of Hitchcock agrees to provide sufficient sums to retire the bonds.

On May 12, 2011, the GCWA redeemed the Series 1998 B Water System Contract Revenue Bonds and issued Water System Contract Revenue Refunding Bonds, Series 2011-B totaling \$3,510,000, of which the City was responsible for 36.64%, or \$1,286,064.

The balances for GCWA activity are presented as of their fiscal year end, August 31, 2014. Any amounts related to the timing of the fiscal year end between GCWA and the City are not considered material to the financial statements.

Note 8 - Long-Term Debt (continued)

Component Units

The City of Hitchcock Reinvestment Zone Number One issued bonds in 2006. The proceeds are for the economic development inside the zone's boundary. Substantially all the project costs have been advanced by the developer for projects related to Harborwalk community and marina. Harborwalk community is a waterfront residential and commercial development on the West Galveston, Texas Bay. These bonds are payable from tax collections resulting from increases to the zone's tax base.

Fiscal Year Ending September 30	City of Hitchcock Tax Reinvestment Zone #1		
	Principal	Interest	Total
2015	\$ 500,000	\$ 251,360	\$ 751,360
2016	525,000	227,360	752,360
2017	555,000	201,110	756,110
2018	585,000	173,360	758,360
2019	615,000	144,110	759,110
2020-2024	1,615,000	359,520	1,974,520
2025-2026	570,000	44,980	614,980
	<u>\$ 4,965,000</u>	<u>\$ 1,401,800</u>	<u>\$ 6,366,800</u>

The following is a summary of the Tax Increment Bonds outstanding as of September 30, 2014:

Series	Original Issue	Interest Rate	Matures	Principal Outstanding
Tax Increment Bonds				
2006 Tax Increment Bonds	\$ 7,800,000	4.50% - 5.25%	2012-2026	\$ 4,965,000
Total Component Units				<u>\$ 4,965,000</u>

Capital Leases

Governmental Activities

During fiscal year 2012, the City entered into capital lease agreements totaling \$832,150 for the purchase of vehicles and other equipment. In fiscal year 2014, the City entered into a capital lease agreement in the amount of \$66,376 for the purchase of a utility backhoe. Additional information on the leases is as follows:

	Interest Rate	Original Balance	Maturity
Police vehicles	3.237%	\$ 358,532	2015
Tractor/mowing equipment	3.100%	78,819	2017
Police radio equipment	3.420%	394,799	2022
		<u>\$ 832,150</u>	

General fund revenues are used to retire these capital lease obligations.

Note 8 - Long-Term Debt (continued)

The following presents capital lease payment requirements to maturity for the Governmental Activities:

Fiscal Year Ending September 30	Governmental Activities		
	Principal	Interest	Total
2015	\$ 143,341	\$ 15,727	\$ 159,068
2016	53,797	11,013	64,810
2017	55,706	9,218	64,924
2018	40,191	7,359	47,550
2019	41,565	5,985	47,550
2020 - 2022	133,420	9,228	142,648
	<u>\$ 468,020</u>	<u>\$ 58,530</u>	<u>\$ 526,550</u>

Business-type Activities

In fiscal year 2013, the City entered into capital lease agreements in the amount of \$508,717 for the purchase of water meters and \$66,376 for the purchase of a utility backhoe. Additional information on the leases is as follows:

	Interest Rate	Original Balance	Maturity
Utility backhoe	2.890%	\$ 66,376	2017
Water meters	2.35%	508,171	2020
		<u>\$ 574,547</u>	

General fund revenues are transferred to the water and sewer operating fund to retire these lease obligations

The following presents capital lease payment requirements to maturity for the Business-Type Activities:

Fiscal Year Ending September 30	Business-type Activities		
	Principal	Interest	Total
2015	\$ 82,146	\$ 11,884	\$ 94,030
2016	84,139	9,890	94,029
2017	86,180	7,850	94,030
2018	88,274	5,756	94,030
2019	75,989	3,613	79,602
2020	77,775	1,828	79,603
	<u>\$ 494,503</u>	<u>\$ 40,821</u>	<u>\$ 535,324</u>

Note 9 - Interfund Receivables, Payables and Transfers

The composite of the interfund balances as of September 30, 2014, is as follows.

<u>Receivable Fund</u>	<u>Payable Fund</u>		<u>Total</u>
	<u>Grant Fund</u>	<u>Utility Fund</u>	
General Fund	\$ 54,960	\$ 38,034	\$ 92,994
Totals	<u>\$ 54,960</u>	<u>\$ 38,034</u>	<u>\$ 92,994</u>

All interfund balances are expected to be repaid within one year.

<u>Transfer in fund</u>	<u>Transfer out fund</u>		<u>Total</u>
	<u>Debt Service Fund</u>	<u>General Fund</u>	
General Fund	\$ 504,921	\$ -	\$ 504,921
Enterprise Fund		94,030	94,030
Totals	<u>\$ 504,921</u>	<u>\$ 94,030</u>	<u>\$ 598,951</u>

A transfer from the debt service fund to the general fund in the amount of \$504,921 was made to eliminate the debt service fund, since all of the City's general obligation debt has been retired. A transfer from the general fund to the water and sewer operating fund in the amount of \$94,030 was made for capital lease payments.

Note 10 - Employment Retirement System

The City provides pension benefits for all of its full-time employees through a non-traditional, joint contributory, hybrid defined benefit plan in the statewide Texas Municipal Retirement System (TMRS), an agent multiple-employer public employee retirement system.

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

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

Note 10 - Employment Retirement System (continued)

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

	<u>Plan Year 2014</u>	<u>Plan Year 2013</u>
Employee deposit rate	5.0%	5.0%
Matching ratio (city to employee)	2 to 1	1 to 1
Years required for vesting	5	5
Service retirement eligibility (expressed)	60/5,0/25	60/5,0/25
Updated Service Credit	50%, Transfers	0%
Annuity Increase (to retirees)	0% of CPI	0% of CPI

Members can retire at certain ages, based on the years of service with the City. The Service Retirement Eligibilities for the City are 5 years at age 60 and 25 years at any age.

Contributions

Under the state law governing TMRS, the contribution rate for each city is determined annually by the actuary, using the Entry Age Normal actuarial cost method (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 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, it 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. Both the normal cost and prior service contribution rates include recognition of the projected impact of annually repeating benefits, such as Updated Service Credits and Annuity Increases.

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

Three-year trend information for the Pension Plan is presented below:

Fiscal Year	<u>2014</u>	<u>2013</u>	<u>2012</u>
Annual required contribution	\$ 60,519	\$ 14,319	22,846
Percentage of Contributions made	100%	100%	100%
NPO at the End of Period	-	-	-

Because the actuary determines contribution rates on an annual basis and the City pays the calculated rate each month, the City will always have a net pension obligation (NPO) of zero at the beginning and end of the period, and the annually required contributions (ARC) will always equal contributions made.

Note 10 - Employment Retirement System (continued)

Funded Status and Funding Progress

In October 2013, the TMRS Board 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, actuarial valuation.

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

	<u>12/31/13</u>
Actuarial Value of Assets	\$ 3,015,918
Actuarial Accrued Liability (AAL)	\$ 3,087,439
Percentage funded	97.7%
Underfunded (Overfunded) AAL (UAAL)	\$ 71,521
Annual covered payroll	\$ 1,562,641
UAAL as a percentage of covered payroll	4.6%

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 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.

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

	<u>12/31/2011</u>	<u>12/31/2012</u>	<u>12/31/2013</u>
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	24.8 Years - Closed Period	25.1 Years - Closed Period	7.1 Years - Closed Period
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
Includes Inflation At	3.0%	3.0%	3.0%
Cost-of-Living Adjustments	None	None	None

Note 11 - Risk Management

General Liability

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's risk management program encompasses various means of protecting the City against loss by obtaining property, casualty and liability coverage through commercial insurance carriers and from participation in a risk pool. The participation of the City in the risk pool is limited to the payment of premiums. There has not been any significant reduction in insurance coverage in the past three years.

Workers' Compensation

The City is a member of the Texas Municipal League (TML) Workers' Compensation Intergovernmental Risk Pool, an unincorporated association of political subdivision of the State of Texas. The company is not intended to operate as an insurance company but rather a contracting mechanism by which the City provides self-insurance benefits to its employees. The fund contracts with a third party administrator for administration, investigation and adjustment services in the handling of claims. Premiums are based on the estimated City payroll by risk factor and rates. The premiums are adjusted by the City's experience modifier. All loss contingencies, including claims incurred but not reported, if any, are recorded and accounted for by the TML Pool.

Note 12 - Amounts Due To Developer

In a prior year the City created Reinvestment Zone One (the "Zone"). The development and financing agreement between the City, the Zone and the developer provides that the developer will advance the funds to provide for construction costs that will be reimbursed from proceeds of bonds issued by the City and payable from tax increments, as provided in the agreement.

The property included in the Zone is adjacent to West Bay and the Highland Bayou Diversionary Canal. Originally, the only vehicular access to this waterfront land was via 2nd Street. Now, primary vehicular access to this waterfront property is via Harbor Drive from State Highway 6. The construction of a bridge over the Diversionary Canal and reconstruction of Basford Bayou Bridge are completed. The public improvement and associated cost are estimated at \$13.56 million, while the estimated appraised value is estimated by the Galveston Central Appraisal District to be \$71.9 million as of January 1, 2014. Since the Zone's creation in 1999, \$13.9 million in expenses have been paid or advanced to finance the development expenses, engineering cost, environmental studies, land surveys, bridge construction/repairs, regional lift station, road improvements and tax zone expenses.

Note 13 - Economic Development Agreements

The City and Hitchcock Industrial Development Corporation (“HDC”) entered into an economic development agreement with a developer in May, 2014. The agreement by the City and HIDC would provide funding to an entity involved, which will be utilized to defray a portion of the costs of infrastructure projects in the new developed area of the City. Under the terms of the agreement, the developer will be reimbursed as follows:

<u>Years</u>	<u>Amount</u>
Year 1 - Year 5	65% of the eligible 2% sales tax collected at the project
Year 6	62% of the eligible 2% sales tax collected at the project
Year 7	59% of the eligible 2% sales tax collected at the project
Year 8	56% of the eligible 2% sales tax collected at the project
Year 9	53% of the eligible 2% sales tax collected at the project
Year 10	50% of the eligible 2% sales tax collected at the project

If the project meets a minimum revenue amount contributes \$6,500,000 to the City in the first ten years, the City will extend the agreement for five years and will reimburse the developer 50% of the eligible 2% sales tax collected during the life of the new agreement. Upon completion of year fifteen, if the City has collected \$4,000,000 during the term of the new agreement, the City will extend the agreement for another five years and reimburse the developer 35% of the eligible 2% sales tax collected during the life of the new agreement.

During the fiscal year ended September 30, 2014, the City and HIDC reimbursed the developer a total of \$272,685. In addition, the City agreed to give the developer a 50% property tax abatement for ten years on the project improvements that are subject to ad valorem taxation as well as all business personal property.

Note 14 - Segment Information

The City issues separate revenue bonds to finance its water and sewer departments. The two departments are accounted for in a single fund, but investors in those bonds rely solely on the revenue generated by the individual activities for repayment. Summary financial information for each department is presented below. The Water Department operates the City’s water supply system. The Sewer Department operates the City’s sewage treatment plant, sewage pumping stations, and collection systems.

Condensed Statement of Revenues, Expenses, and Changes in Net Position	Water Department	Sewer Department
Operating revenues	\$ 1,364,744	914,425
Depreciation expense	(319,062)	(508,545)
Other operating expenses	(1,367,830)	(913,559)
Operating income (loss)	(322,148)	(507,679)
Nonoperating revenues (expenses):		
Investment income	1,311	-
Interest expense	(59,843)	(942)
Capital contributions	1,224,166	1,001,387
Transfers in	7,214	86,816
Change in net position	<u>\$ 850,700</u>	<u>\$ 579,582</u>

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF HITCHCOCK, TEXAS

Exhibit G-1

GENERAL FUND

SCHEDULE OF REVENUES, EXPENDITURES AND

CHANGES IN FUND BALANCE - BUDGET AND ACTUAL - BUDGETARY BASIS

For the Year Ended September 30, 2014

	Budgeted Amounts		Actual - Budgetary Basis	Variance with Final Budget Positive / (Negative)
	Original	Final		
Revenues				
Property taxes	\$ 885,372	\$ 885,372	\$ 1,023,580	\$ 138,208
Sales, franchise and local taxes	980,000	980,000	1,178,600	198,600
Licenses and permits	318,680	318,680	504,350	185,670
Charges for services	155,000	155,000	139,181	(15,819)
Fines and forfeitures	426,600	426,600	411,227	(15,373)
Earnings on investments	6,500	6,500	9,472	2,972
Intergovernmental	74,596	74,596	83,030	8,434
Other	83,458	83,458	50,812	(32,646)
Total Revenues	<u>2,930,206</u>	<u>2,930,206</u>	<u>3,400,252</u>	<u>470,046</u>
Expenditures				
Current:				
General government	600,020	600,020	585,416	14,604
Public safety	1,525,024	1,666,832	1,482,815	184,017
Public works	663,337	680,597	612,742	67,855
Health, welfare and sanitation	43,725	43,725	42,330	1,395
Culture and recreation	98,100	98,100	95,614	2,486
Capital outlay			225,383	(225,383)
Debt service:				
Principal retirement			138,777	(138,777)
Interest and fees			20,292	(20,292)
Total Expenditures	<u>2,930,206</u>	<u>3,089,274</u>	<u>3,203,369</u>	<u>(114,095)</u>
Excess (deficiency) of revenues over expenditures	-	(159,068)	196,883	355,951
Other Financing Sources (Uses)				
Operating transfers in	-	159,068	504,921	504,921
Operating transfer out	-	-	(94,030)	(94,030)
Total Other Financing Sources (Uses)	<u>-</u>	<u>159,068</u>	<u>410,891</u>	<u>410,891</u>
Net change in fund balance	-		607,774	766,842
Fund Balance (Budgetary Basis), Beginning of Year	<u>1,434,748</u>	<u>1,434,748</u>	<u>1,434,748</u>	<u>-</u>
Fund Balance (Budgetary Basis), End of Year	<u>\$ 1,434,748</u>	<u>\$ 1,434,748</u>	<u>\$ 2,042,522</u>	<u>\$ 766,842</u>

A. Legal Compliance - Budgets

Prior to October 1, the departments and agencies of the City transmit their estimates of their budgetary requirements to the Mayor. The Commission may revise, alter, increase or decrease the items of the budget, provided that when it shall increase the total proposed expenditures, it shall also increase the total anticipated income. At least ten days before the beginning of the fiscal year, the Commission approves the budget plan. One or more public hearings are conducted to obtain taxpayer comments. The budget is legally enacted prior to October 1. The Commission may transfer unencumbered appropriated balances, or portion thereof, from one department to another. During the year, the Commission approved amendments to the original budget in the amount of \$159,068 for the payment of capital leases.

B. Excess of Expenditures over Appropriations

At September 30, 2014, expenditures exceeded appropriations at the department level (the legal level of compliance) in the following departments.

<u>Fund / Department</u>	<u>Amount</u>
General Fund:	
Capital outlay	\$ 225,383
Debt service:	
Principal retirement	138,777
Interest and fees	20,292

C. Revenue and Expenditures Analysis in Comparison to Budget

	<u>General Fund</u>		
	<u>Budgetary Basis</u>	<u>Unbudgeted Activities</u>	<u>GAAP Basis</u>
Revenues	\$ 3,400,252	\$ 300,300	\$ 3,700,552
Expenditures	<u>3,203,369</u>	<u>300,300</u>	<u>3,503,669</u>
Revenues over (under) expenditures	196,883	-	196,883
Other financing sources (uses)	<u>410,891</u>	<u>-</u>	<u>410,891</u>
Revenues and other financing sources over (under) expenditures and other financing (uses)	607,774	-	607,774
Fund balance at beginning of year	<u>1,434,748</u>	<u>-</u>	<u>1,434,748</u>
Fund balance at end of year	<u><u>\$ 2,042,522</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 2,042,522</u></u>

CITY OF HITCHCOCK, TEXAS
REQUIRED PENSION SYSTEM SUPPLEMENTARY INFORMATION
Year Ended September 30, 2014

Exhibit G-3

Texas Municipal Retirement System (Unaudited)

Schedule of Funding Progress

	<u>12/31/13</u>	<u>12/31/12</u>	<u>12/31/11</u>
Actuarial Value of Assets	\$ 3,015,918	\$ 2,778,587	\$ 2,579,686
Actuarial Accrued Liability (AAL)	\$ 3,087,439	\$ 2,493,077	\$ 2,337,561
Percentage funded	97.7%	111.5%	110.4%
Underfunded (Overfunded) AAL (UAAL)	\$ 71,521	\$ (285,510)	\$ (242,125)
Annual covered payroll	\$ 1,562,641	\$ 1,436,229	\$ 1,367,796
UAAL as a percentage of covered payroll	4.6%	-19.9%	-17.7%

**COMBINING AND INDIVIDUAL FUND
STATEMENTS AND SCHEDULES**

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NON MAJOR GOVERNMENTAL

SPECIAL REVENUE FUNDS

These funds are used to account for the proceeds of revenue sources that are legally restricted or committed for certain activities.

CITY OF HITCHCOCK, TEXAS
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
September 30, 2014

	<i>Special Revenue Funds</i>		
	Court Security and Technology Fund	Parks and Recreation	Donation Fund
Assets			
Cash and cash equivalents	\$ 51,945	\$ 5,273	\$ 6,823
Accounts receivable	-	-	-
Total Assets	<u>\$ 51,945</u>	<u>\$ 5,273</u>	<u>\$ 6,823</u>
 Liabilities and Fund Balances			
Liabilities:			
Due to other funds	\$ -	\$ -	\$ -
Total Liabilities	<u>-</u>	<u>-</u>	<u>-</u>
 Fund Balance:			
Restricted:			
Public safety	51,945	-	-
Culture and recreation	-	5,273	6,823
Total Fund Balance	<u>51,945</u>	<u>5,273</u>	<u>6,823</u>
 Total Liabilities and Fund Balance	 <u>\$ 51,945</u>	 <u>\$ 5,273</u>	 <u>\$ 6,823</u>

Exhibit H-1

Seizure Fund	Public Safety Grant Fund	Total NonMajor Governmental Funds
\$ 4,274	\$ -	\$ 68,315
-	54,960	54,960
<u>\$ 4,274</u>	<u>\$ 54,960</u>	<u>\$ 123,275</u>
<u>\$ -</u>	<u>\$ 54,960</u>	<u>\$ 54,960</u>
-	54,960	54,960
4,274	-	56,219
-	-	12,096
<u>4,274</u>	<u>-</u>	<u>68,315</u>
<u>\$ 4,274</u>	<u>\$ 54,960</u>	<u>\$ 123,275</u>

CITY OF HITCHCOCK, TEXAS

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND

CHANGES IN FUND BALANCES

NONMAJOR GOVERNMENTAL FUNDS

For the Year Ended September 30, 2014

	<i>Special Revenue Funds</i>		
	<u>Court Security and Technology Fund</u>	<u>Parks and Recreation</u>	<u>Donation Fund</u>
Revenues			
Fines and forfeitures	\$ 14,736	\$ -	\$ -
Intergovernmental	-	-	-
Other	-	-	1,600
Total Revenues	<u>14,736</u>	<u>-</u>	<u>1,600</u>
Expenditures			
Current:			
Public safety	<u>2,006</u>	<u>-</u>	<u>-</u>
Total Expenditures	<u>2,006</u>	<u>-</u>	<u>-</u>
Revenues Over (Under) Expenditures	12,730	-	1,600
Fund Balances, Beginning of Year	<u>39,215</u>	<u>5,273</u>	<u>5,223</u>
Fund Balances, End of Year	<u>\$ 51,945</u>	<u>\$ 5,273</u>	<u>\$ 6,823</u>

Exhibit H-2

<u>Seizure Fund</u>	<u>Public Safety Grant Fund</u>	<u>Total NonMajor Governmental Funds</u>
\$ 1,238	\$ -	\$ 15,974
-	54,960	54,960
-	-	1,600
<u>1,238</u>	<u>54,960</u>	<u>72,534</u>
2,880	54,960	59,846
<u>2,880</u>	<u>54,960</u>	<u>59,846</u>
(1,642)	-	12,688
<u>5,916</u>	<u>-</u>	<u>55,627</u>
<u>\$ 4,274</u>	<u>\$ -</u>	<u>\$ 68,315</u>

CITY OF HITCHCOCK
ANALYSIS OF TAXES LEVIED AND RECEIVABLE
September 30, 2014

<u>Tax Rate/\$100 Valuation</u>					
<u>Tax Year</u>	<u>Maintenance and Operations</u>	<u>Debt Service</u>	<u>Total</u>	<u>Beginning Balance</u>	<u>Taxes Levied</u>
Prior	Various	Various	Various	\$ 74,217	\$ -
2005	0.348740	0.18582	0.534560	11,884	-
2006	0.375140	0.17991	0.555050	14,428	-
2007	0.395350	0.11573	0.511080	14,933	-
2008	0.370790	0.10244	0.473230	18,275	-
2009	0.325910	0.14732	0.473230	21,525	-
2010	0.335700	0.13660	0.472300	28,199	-
2011	0.396460	-	0.396460	31,872	-
2012	0.396105	-	0.396105	56,470	-
2013	0.413202	-	0.413202	-	1,193,244
				<u>\$ 271,803</u>	<u>\$ 1,193,244</u>

Exhibit H-3

<u>Collections</u>	<u>Adjustments and Refunds</u>	<u>Ending Balance</u>
\$ (5,515)	\$ (8,597)	\$ 60,105
(861)	(126)	10,897
(1,058)	(200)	13,170
(1,661)	(154)	13,118
(4,289)	(112)	13,874
(6,352)	2,869	18,042
(8,095)	2,655	22,759
(11,271)	1,898	22,499
(23,568)	1,726	34,628
<u>(1,187,198)</u>	<u>50,252</u>	<u>56,298</u>
<u>\$ (1,249,868)</u>	<u>\$ 50,211</u>	<u>\$ 265,390</u>

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FEDERAL AWARDS SECTION

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

To the Honorable Anthony Matranga, Mayor
and Members of the City Commission
Hitchcock, 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, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Hitchcock, 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, and have issued our report thereon dated June 22, 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. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs that we consider to be a significant deficiency and is identified as item # 2014-001.

To the Honorable Anthony Matranga, Mayor
and Members of the City Commission
City of Hitchcock, Texas

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as items #2013-002, and 2013-003.

The City's Response to Findings

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

Purpose of this Report

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

Whitley Penn LLP

Texas City, Texas
June 22, 2015

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

To the Honorable Anthony Matranga, Mayor
and Members of the City Commission
Hitchcock, Texas

Report on Compliance for Each Major Program

We have audited the City of Hitchcock, 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.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City's major federal programs based on our audit of the types of compliance referred to above. We conducted our audit of the compliance in accordance with auditing 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.

To the Honorable Anthony Matranga, Mayor
and Members of the City Commission
City of Hitchcock, Texas

Other Matters

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as item #2013-004. Our opinion on each major program is not modified with respect to these matters.

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

Report on Internal Control Over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on 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 item #2013-004, that we consider to be a significant deficiency.

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

To the Honorable Anthony Matranga, Mayor
and Members of the City Commission
City of Hitchcock, Texas

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 A-133. Accordingly, this report is not suitable for any other purpose.

Whitley Penn LLP

Texas City, Texas
June 22, 2015

CITY OF HITCHCOCK, 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
Internal Control over financial reporting:	
• Material weakness(es) identified?	No
• Significant deficiencies identified that are not considered to be material weaknesses?	Yes, Item #2014-001
Noncompliance material to financial statements noted?	Yes, Items #2013-002, #2013-003

Federal Awards

Internal control over major programs:	
• Material weakness(es) identified?	No
• Significant deficiencies identified that are not considered to be material weaknesses?	Yes, Item #2013-004
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 OMB Circular A-133?	No

Identification of Major Programs:

CFDA Number	Name of Federal Program
14.228	Community Development Block Grant-Small Cities-Disaster Recovery

Dollar threshold used to distinguish between type A and type B federal programs:	\$300,000
Auditee qualified as low-risk auditee?	No

CITY OF HITCHCOCK, TEXAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
For the Year Ended September 30, 2014

Section II. - Financial Statement Findings

Significant Deficiency

Finding #2014-001-Water and Sewer Adjustments

Criteria: The City is responsible for maintaining internal controls over utility revenues.

Condition: The City is not maintaining supporting documentation for utility billing adjustments.

Context: During our walkthrough procedures of the utility department, we noted that supporting documentation for billing adjustments is not being maintained.

Effect: Failure to establish and maintain internal controls over utility billing can result in fraud or errors occurring, and not being detected in a timely manner.

Recommendation: The City should establish procedures to monitor utility billing adjustments and supporting documentation for all adjustments should be maintained.

Compliance

Finding #2013-002 - Competitive Procurement Procedures

Criteria: Competitive procurement procedures are required for making purchases involving dollar amounts in excess of \$50,000 or more, in the aggregate, over a twelve month period.

Condition: The City is not monitoring cumulative purchases of similar items, which in the aggregate over a twelve month period, could be subject to State bidding requirements.

Context: During our audit, we noted instances of purchases of similar items aggregating amounts in excess of \$50,000 which were not purchased through competitive procurement procedures.

Effect: This condition may cause the City to be in technical noncompliance with the state bidding requirements for some purchases. In addition, competitive procurement procedures may result in lower costs per unit or in the aggregate.

Recommendation: The City should establish procedures to monitor purchases of similar commodities on a regular basis to identify items which should be purchased under competitive procurement procedures.

CITY OF HITCHCOCK, TEXAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
For the Year Ended September 30, 2014

Section II. - Financial Statement Findings (continued)

Finding #2013-003 Expenditures in Excess of Appropriations

Criteria: State law mandates that expenditures do not exceed appropriations at the functional level.

Condition: Expenditures exceeded appropriations in the general fund as follows:

<u>Fund / Department</u>	<u>Amount</u>
General Fund:	
Capital outlay	\$ 225,383
Debt service:	
Principal retirement	138,777
Interest and fees	20,292

Context: During the course of the audit, we noted that expenditures exceeded appropriations at the departmental level.

Effect: Noncompliance with state law.

Recommendation: The City should implement procedures to review budget to actual comparisons, and budget amendments should be presented and approved prior to expending funds for which appropriations are not available.

CITY OF HITCHCOCK, TEXAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
For the Year Ended September 30, 2014

Section III. - Federal Award Findings and Questioned Costs

Finding #2013-004 – Cash Management

Program: Community Development Block Grant (“CDBG”)
CFDA: 14.228
Federal Award #12-203-5044/010069; 12-203-5503/210069; 12-608-000-6995/22069; 713229
Department of Housing and Urban Development
Passed Through: Texas General Land Office

Criteria: When federal funds are advanced, recipients must follow procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury and disbursement. Interest earned in excess of \$100 on advances is required to be submitted promptly, but at least quarterly, to the federal agency.

Condition: The City draws CDGB funds once an invoice is submitted by the vendor for payment. The City disburses funds to the vendor upon receipt of the payment from the federal agency. Often times, the City will pay the vendor one week after receipt of funds from the federal agency.

Context: We noted this while performing a test of disbursements for the CDBG program.

Questioned Costs: None

Effect: Failure to follow internal controls over the cash management process could result in noncompliance with the Cash Management compliance requirement as established in OMB Circular A-133. It was noted that the funds were not left in an interest bearing account long enough to earn interest in excess of \$100.

Recommendation: The City should have written policies to ensure that all requirements listed in the OMB Circular A-133 compliance supplement are met. Management should be aware of all applicable compliance requirements per OMB Circular A-133 and should communicate those requirements to the appropriate personnel.

CITY OF HITCHCOCK, TEXAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
For the Year Ended September 30, 2014

Section IV. - Status of Prior Year Findings and Questioned Costs

Finding #2013-001 **Resolved:** The City adopted an investment policy in FY2014.
Investment Policy

Finding #2013-002 **Not Resolved:** See current year finding 2013-002
Competitive Procurement
Procedures

Finding #2013-003 **Not Resolved:** See current year finding 2013-003
Expenditures in Excess of
Appropriations

Finding #2013-004 **Not Resolved:** See current year finding 2013-004
Cash Management

CITY OF HITCHCOCK, TEXAS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS (continued)
For the Year Ended September 30, 2014

Section V. - Views of Responsible Officials and Planned Corrective Action

- Finding #2014-001**
Water and Sewer
Adjustments
- Description:** The City will develop formal policies and procedures regarding utility adjustments. These will include situations that warrant an adjustment and a regular review of the adjustments. The Customer Service Supervisor will have authority to make adjustments with review by the City Secretary.
- Responsible party:** Anthony Matranga, Mayor
- Estimated completion date:** September 2015
-
- Finding #2013-002**
Competitive Procurement
Procedures
- Description:** To the extent possible, the City will consider approving interlocal agreements with other governmental entities to utilize their contract to purchase similar commodities. In addition, the City will utilize other cooperative purchasing arrangements to purchase needed commodities.
- Responsible party:** Anthony Matranga, Mayor
- Estimated completion date:** September 2015
-
- Finding #2013-003**
Expenditures in Excess of
Appropriations
- Description:** The City will implement procedures to review budget to actual comparisons, and amend the budget prior to expending funds for which appropriations are not available.
- Responsible party:** Anthony Matranga, Mayor
- Estimated completion date:** September 2015
-
- Finding #2013-004**
Cash Management
- Description:** As of the date of this report, the City has implemented procedures to ensure that federal funds are disbursed within three days after the funds are received from the U.S. Treasury.
- Responsible party:** Anthony Matranga, Mayor
- Estimated completion date:** September 2015

CITY OF HITCHCOCK, TEXAS
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended September 30, 2014

Exhibit K-1

Federal Grantor/Pass-through Grantor/Program Title	Federal CFDA Number	Pass Through Grantors Number	Disbursement/ Expenditures
U.S. Department of Housing and Urban Development			
Passed through the General Land Office			
<i>Community Development Block Grant - Small Cities Program - Disaster Recovery*</i>	14.228	12-203-5044/010069	\$ 295,515
<i>Community Development Block Grant - Small Cities Program - Disaster Recovery*</i>	14.228	12-203-5503/210069	472,256
<i>Community Development Block Grant - Small Cities Program - Disaster Recovery*</i>	14.228	12-608-000-6995/22069	1,693,019
<i>Community Development Block Grant - Small Cities Program - Disaster Recovery*</i>	14.228	713229	<u>31,875</u>
Total U.S. Department of Housing and Urban Development			<u>2,492,665</u>
U.S. Department of Homeland Security			
Passed through Texas Department of Public Safety:			
<i>State Homeland Security Grant</i>	97.073	10-SR-34220-01	<u>54,960</u>
Total U.S. Department of Homeland Security			<u>54,960</u>
Total Federal Awards			<u>\$ 2,547,625</u>

* Denotes Major Program

Note 1 - Basis of Accounting

City of Hitchcock, Texas accounts for federal funding using the modified accrual method of accounting. This basis of accounting recognizes revenues in the accounting period in which they become susceptible to accrual, i.e. both measurable and available, and expenditures in the accounting period in which the liability is incurred, if measurable, except for certain compensated absences, claims and judgments, which are recognized when the obligations are expected to be liquidated with expendable available financial resources. Equipment purchases for grant purposes are treated as expenditures in the schedule of expenditures of federal awards and typically capitalized for financial statement purposes.

Federal grant funds are considered to be earned to the extent of expenses made under the provisions of the grant, and, accordingly, when such funds are received, they are recorded as unearned revenues until earned. Generally, unused balances are returned to the grantor at the close of specified project periods.

Note 2 - U.S.D.A. Rural Development Loan

The City in prior fiscal years received proceeds from a U.S.D.A. Rural Development Loan. At September 30, 2014, the loan balance was \$1,098,000. In accordance with OMB Circular A-133, the prior loan balances are not considered to have continuing compliance requirements.