

CITY OF FREEPORT
FREEPORT, TEXAS

ANNUAL FINANCIAL REPORT

FOR THE YEAR ENDED
SEPTEMBER 30, 2016

FINAL

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

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CITY OF FREEPORT

Freeport, Texas

*Annual Financial Report
For the Year Ended September 30, 2016*

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FINANCIAL SECTION

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Kennemer, Masters & Lunsford

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Independent Auditor's Report

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

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Freeport, Texas (the "City") as of and for the year ended September 30, 2016, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

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Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Freeport, as of September 30, 2016, 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 11 through 22, and the Statement of Revenues, Expenditures, and Changes in Fund Balances – Budget and Actual – General Fund, Schedule of TMRS Contributions – For the Last Ten Years, Schedule of TMRS Changes in Net Pension Liability and Related Ratios – For the Last Ten Years, Schedule of TESRS Changes in Net Pension Liability and Related Ratios – For the Last Ten Years, and Schedule of TESRS Investment Returns – For the Last Ten Years on pages 88 through 92, 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 presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by Title 2 U.S. *Code of Federal Regulations*, Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, and is also not a required part of the basic financial statements.

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

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

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated February 24, 2017, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering City's internal control over financial reporting and compliance.

Kennemer, Masters & Hunsford, LLC

Certified Public Accountants
Lake Jackson, Texas
February 24, 2017

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CITY OF FREEPORT, TEXAS

Management's Discussion and Analysis For the Year Ended September 30, 2016

As management of the City of Freeport (the "City"), we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended September 30, 2016. We encourage readers to consider the information presented here in conjunction with the City's financial statements, which follow this section.

Financial Highlights

- The assets and deferred outflows of resources of the City exceeded its liabilities and deferred inflows of resources at the close of the most recent fiscal year by \$ 25,745,673 (net position). Of this amount, \$ 5,212,901 (unrestricted net position) may be used to meet the government's ongoing obligations to citizens and creditors in accordance with the City's fund designation.
- The City's net position of \$ 25,745,673 increased by \$ 869,958 from the prior year.
- As of the close of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$ 9,757,478. 90.93% of this total amount, \$ 8,872,715 (unassigned fund balance) is available for use within the City's fund designation.
- At the end of the current fiscal year, total fund balance for the general fund was \$ 9,329,804 and the unassigned fund balance was \$ 8,872,715. These amounts were 70.36% and 66.91% of the total general fund expenditures.

Overview of the Financial Statements

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

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

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

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

CITY OF FREEPORT, TEXAS

*Management's Discussion and Analysis
For the Year Ended September 30, 2016*

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The *governmental activities* of the City include general government and administration, economic development, public safety, streets and drainage, sanitation, service center, marina operations, library, and parks and recreation. The *business-type activities* of the City include the operations of water and sewer, golf course, and ambulance. The government-wide financial statements can be found on pages 24 through 25 of this report.

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

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

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

The City maintains nine (9) 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, which is considered to be the major fund. Data from the other eight (8) funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of combining statements on pages 94 through 97 of this report.

CITY OF FREEPORT, TEXAS

Management's Discussion and Analysis For the Year Ended September 30, 2016

- **Proprietary Funds.** The City maintains three individual *proprietary funds* - Enterprise Funds. Information is presented separately in the proprietary fund's statement of net position, statement of revenues, expenses and changes in net position, and statement of cash flows on pages 34 through 39 of the report for the Water and Sewer Enterprise Fund, Golf Course Enterprise Fund, and Ambulance Enterprise Fund; which are considered to be major funds. Enterprise funds are used to report the same functions presented as business-type activities in government-wide financial statements. The City uses enterprise funds to account for its water and sewer, golf course, and ambulance operations. Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 41 through 86 of this report.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information that further explains and supports the information in the financial statements. Required supplementary information can be found on pages 88 through 92 of this report. The combining statements referred to earlier in connection with non-major governmental funds are presented following the required supplementary information on pensions. Combining and individual statements and schedules can be found on pages 94 through 112 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 of Freeport, assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources by \$ 25,745,673 as of September 30, 2016.

A large portion of the City's net position, in the amount of \$ 20,130,874 (78.19%) reflects its investments in capital assets (e.g., land, buildings, improvements, equipment, machinery, construction in progress), less any debt used to acquire those assets that is still outstanding. The City uses capital assets to provide service to citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the City's net position of \$ 401,898 (1.56%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net position of \$ 5,212,901 (20.25%) may be used to meet the government's ongoing obligations to citizens and creditors.

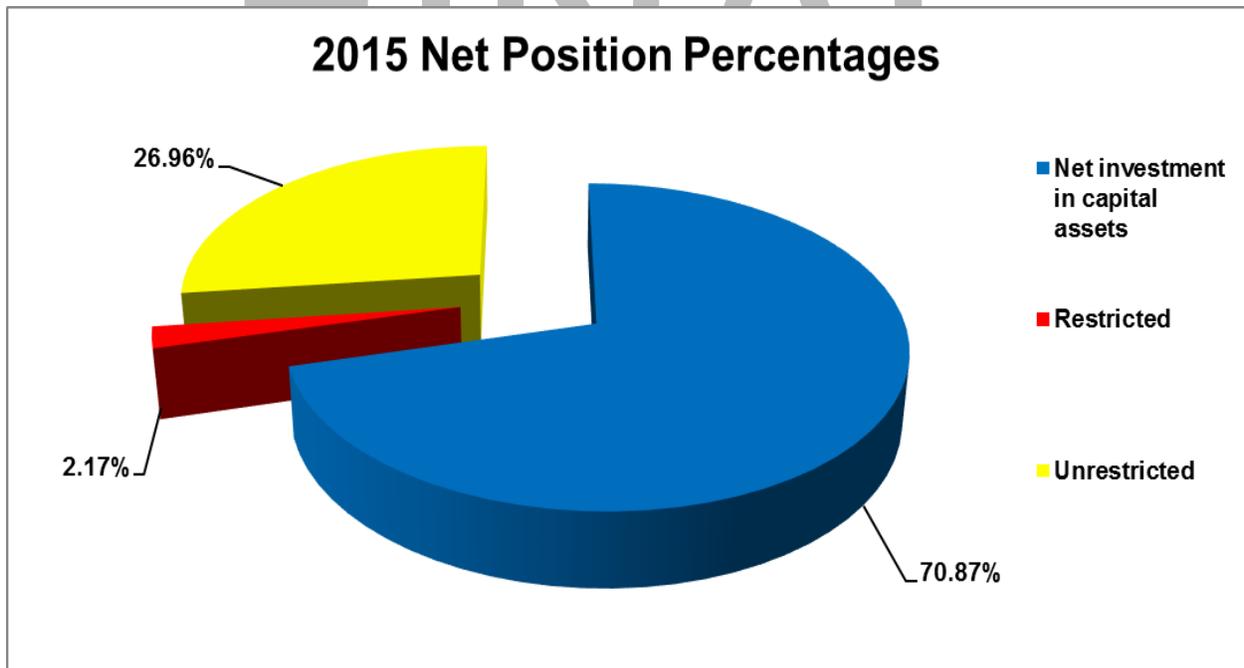
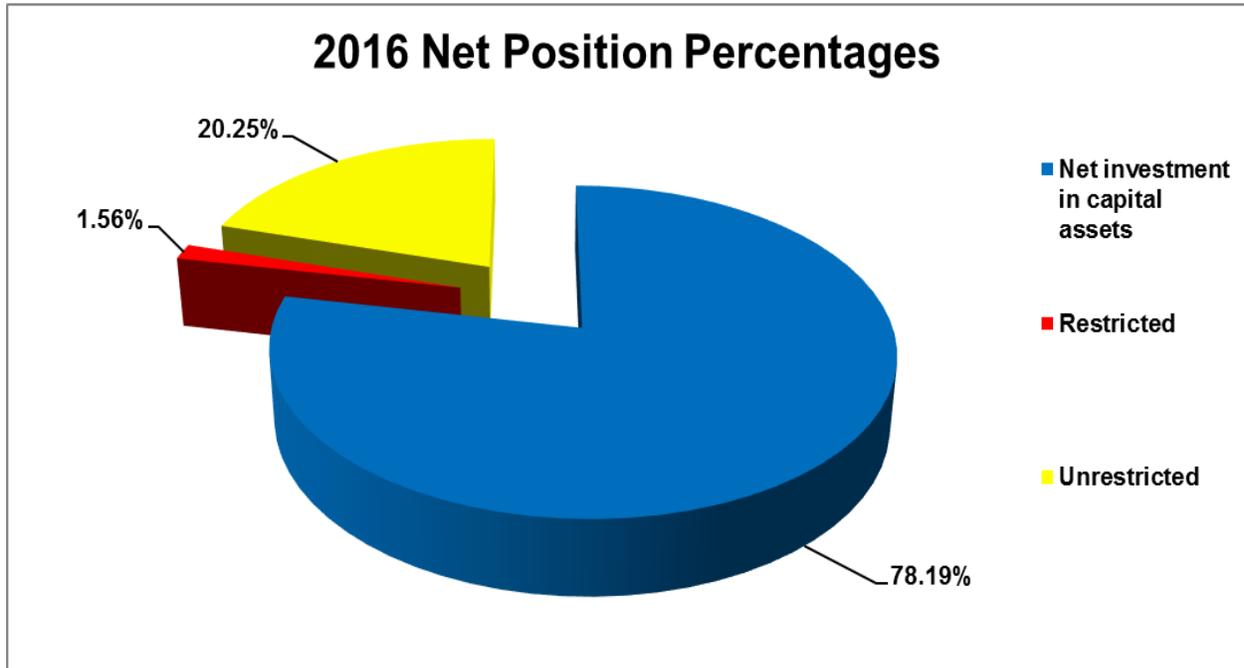
As of September 30, 2016, the City is able to report positive balances in all categories of net position for the government as a whole. The business-type activities reported a negative amount in unrestricted net position.

CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2016

CITY OF FREEPORT'S NET POSITION

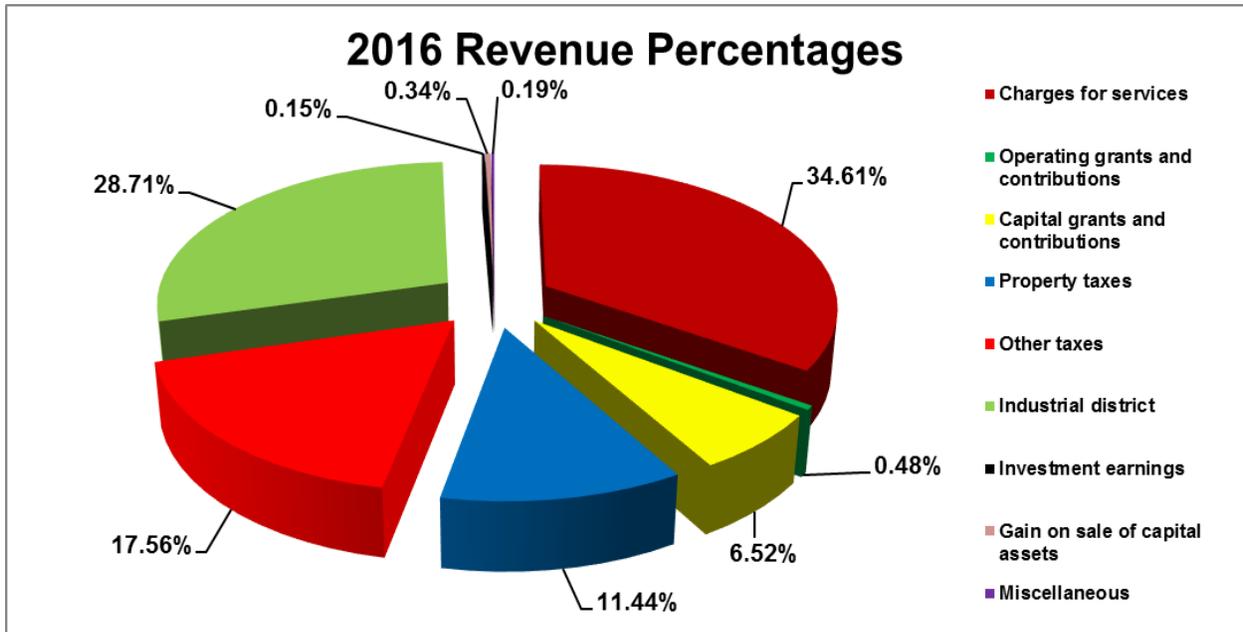
	Governmental Activities		Business-type Activities		Totals	
	September 30,		September 30		September 30,	
	2016	2015	2016	2015	2016	2015
ASSETS						
Current and other assets	\$ 11,222,246	\$ 11,892,064	\$ 1,463,816	\$ 1,487,075	\$ 12,686,062	\$ 13,379,139
Capital assets	<u>17,306,684</u>	<u>17,038,809</u>	<u>8,507,516</u>	<u>7,302,869</u>	<u>25,814,200</u>	<u>24,341,678</u>
Total assets	<u>28,528,930</u>	<u>28,930,873</u>	<u>9,971,332</u>	<u>8,789,944</u>	<u>38,500,262</u>	<u>37,720,817</u>
DEFERRED OUTFLOWS OF RESOURCES						
Deferred outflows of resources	<u>1,650,676</u>	<u>541,875</u>	<u>289,023</u>	<u>95,475</u>	<u>1,847,415</u>	<u>637,350</u>
Total deferred outflows of resources	<u>1,650,676</u>	<u>541,875</u>	<u>289,023</u>	<u>95,475</u>	<u>1,939,699</u>	<u>637,350</u>
LIABILITIES						
Current and other liabilities	1,101,584	1,084,587	1,259,194	938,152	2,360,778	2,022,739
Long-term liabilities	<u>11,282,936</u>	<u>10,638,242</u>	<u>997,579</u>	<u>768,476</u>	<u>12,280,515</u>	<u>11,406,718</u>
Total liabilities	<u>12,384,520</u>	<u>11,722,829</u>	<u>2,256,773</u>	<u>1,706,628</u>	<u>14,641,293</u>	<u>13,429,457</u>
DEFERRED INFLOWS OF RESOURCES						
Deferred inflows of resources	<u>45,056</u>	<u>45,056</u>	<u>7,939</u>	<u>7,939</u>	<u>52,995</u>	<u>52,995</u>
Total deferred inflows of resources	<u>45,066</u>	<u>45,056</u>	<u>7,939</u>	<u>7,939</u>	<u>52,995</u>	<u>52,995</u>
NET POSITION						
Net investment in capital assets	11,665,882	10,431,051	8,464,992	7,198,627	20,130,874	17,629,678
Restricted	401,898	538,482			401,898	538,482
Unrestricted	<u>5,682,250</u>	<u>6,735,330</u>	<u>(469,349)</u>	<u>(27,775)</u>	<u>5,212,901</u>	<u>6,707,555</u>
Total net position	<u>\$ 17,750,030</u>	<u>\$ 17,704,863</u>	<u>\$ 7,995,643</u>	<u>\$ 7,170,852</u>	<u>\$ 25,745,673</u>	<u>\$ 24,875,715</u>

CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2016

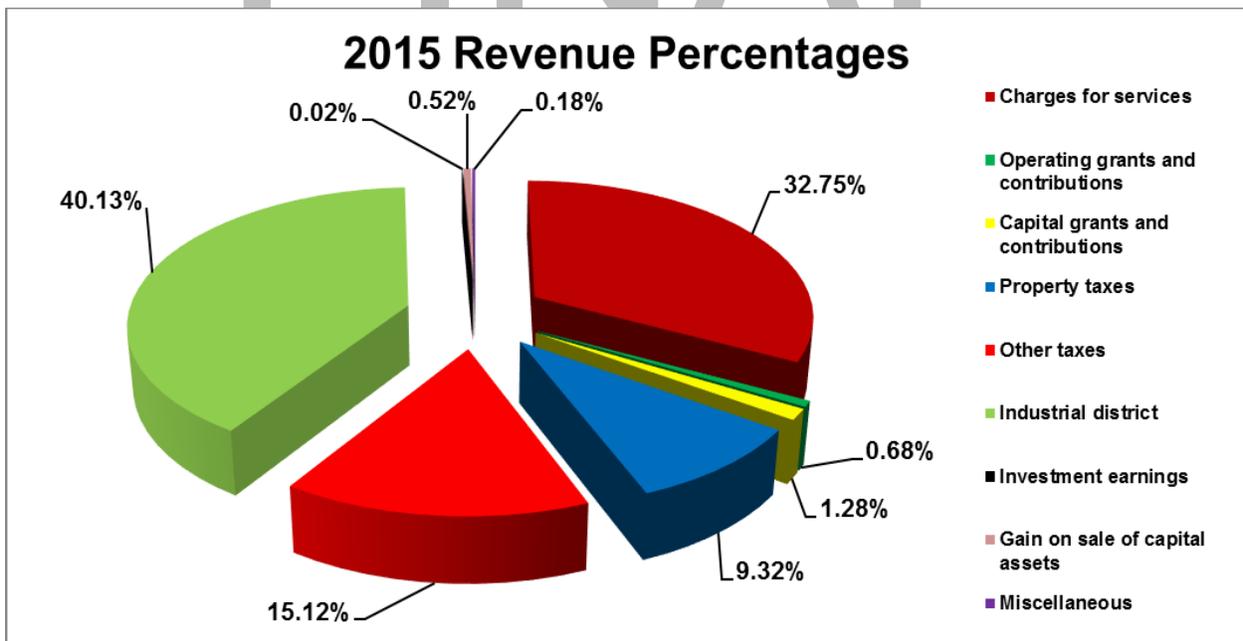


Analysis of the City's Operations. The following graphs provide a summary of the City's operations for the years ended September 30, 2016. Governmental activities increased the City of Freeport's net position by \$ 45,167 and the business-type activities increased the City's net position by \$ 824,791.

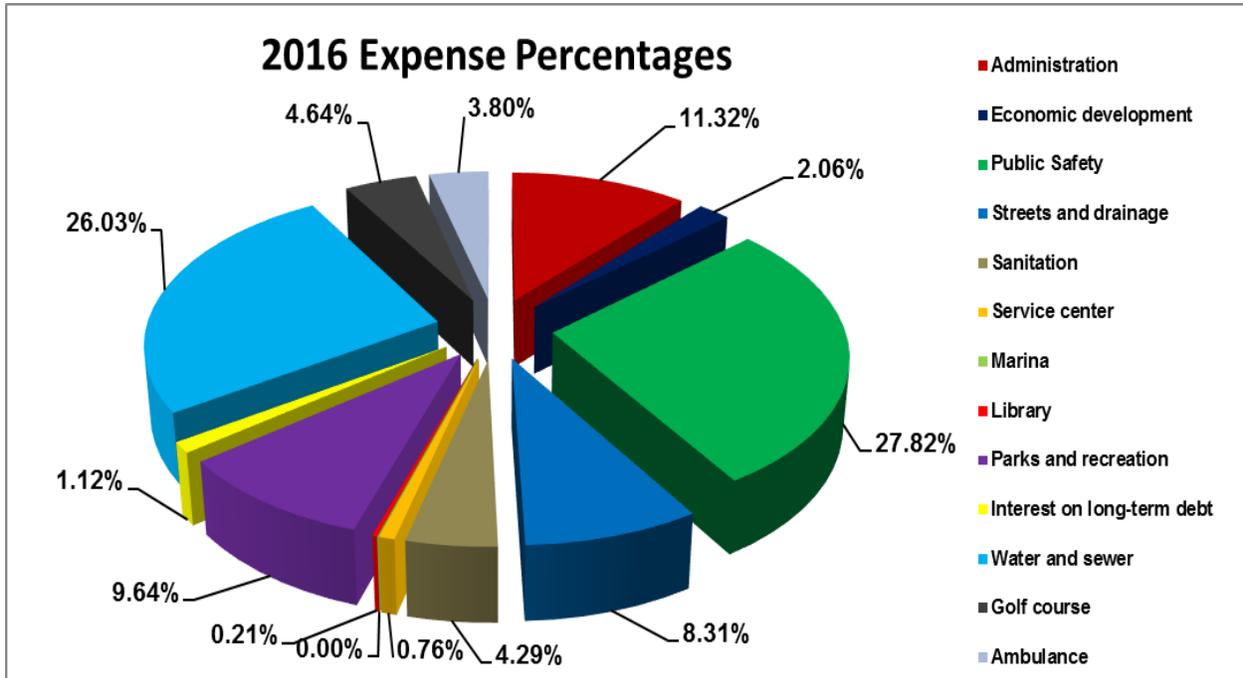
CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2016



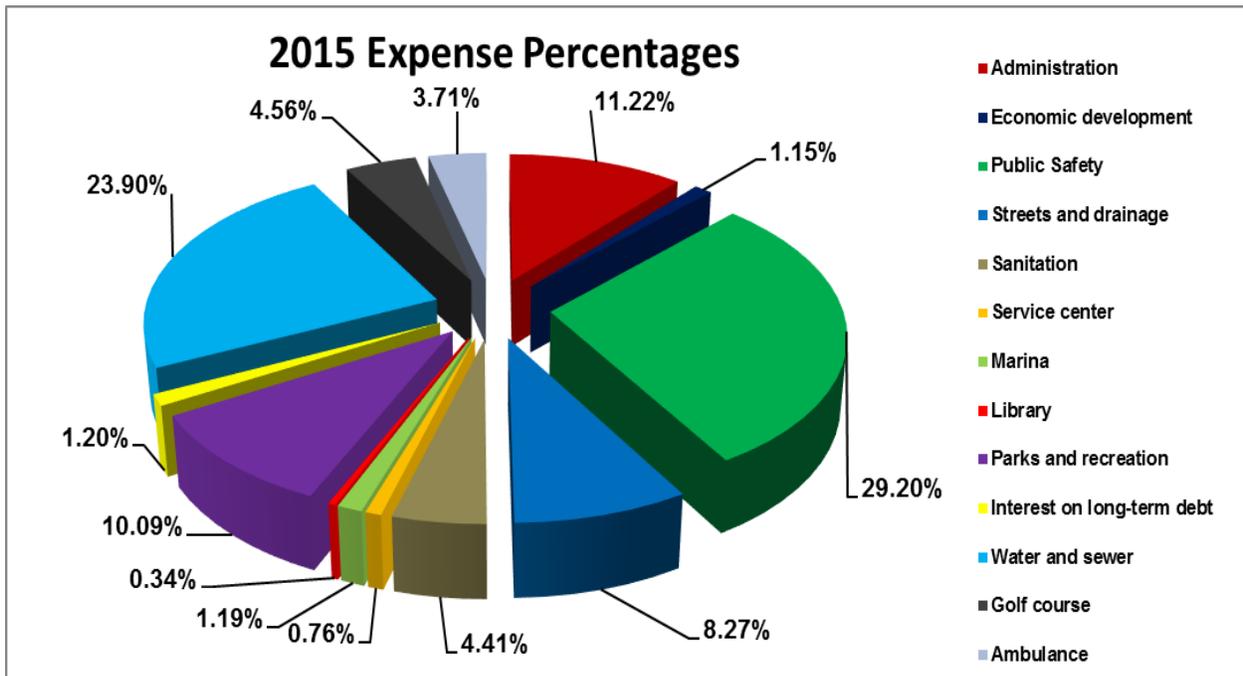
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Management's Discussion and Analysis
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CITY OF FREEPORT'S CHANGES IN NET POSITION

	Governmental Activities		Business-type Activities		Totals	
	September 30,		September 30,		September 30,	
	2016	2015	2016	2015	2016	2015
Revenues:						
Program Revenues:						
Charges for services	\$ 1,742,930	\$ 1,935,358	\$ 5,938,069	\$ 6,252,729	\$ 7,680,999	\$ 8,188,087
Operating grants and contributions	105,476	81,689		89,457	105,476	171,146
Capital grants and contributions	263,407	140,558	1,184,220	179,000	1,447,627	319,558
General Revenues:						
Taxes:						
Property taxes	2,539,494	2,328,836			2,539,494	2,328,836
Other taxes	3,896,907	3,778,677			3,896,907	3,778,677
Industrial district	6,370,196	10,032,955			6,370,196	10,032,955
Investment earnings	30,785	5,105	1,937	52	32,722	5,157
Gain on disposition of capital assets	75,795	129,871			75,795	129,871
Miscellaneous	42,000	45,620			42,000	45,620
Total revenues	<u>15,066,990</u>	<u>18,478,669</u>	<u>7,124,226</u>	<u>6,521,238</u>	<u>22,191,216</u>	<u>24,999,907</u>
Expenses:						
General government and administration	2,414,504	2,063,459			2,414,504	2,063,459
Economic development	438,353	210,816			438,353	210,816
Public safety	5,931,778	5,373,438			5,931,778	5,373,438
Streets and drainage	1,771,064	1,521,757			1,771,064	1,521,757
Sanitation	914,275	810,919			914,275	810,919
Service center	161,099	139,371			161,099	139,371
Marina		219,735				219,735
Library	44,783	63,439			44,783	63,439
Parks and recreation	2,056,169	1,855,714			2,056,169	1,855,714
Interest on long-term debt	239,139	221,279			239,139	221,279
Water and sewer			5,549,230	4,398,015	5,549,230	4,398,015
Golf course			990,176	838,297	990,176	838,297
Ambulance			810,688	683,060	810,688	683,060
Total expenses	<u>13,971,164</u>	<u>12,479,927</u>	<u>7,350,094</u>	<u>5,919,372</u>	<u>21,321,258</u>	<u>18,399,299</u>
Increase (decrease) in net Position before transfers	1,095,826	5,998,742	(225,868)	601,866	869,958	6,600,608
Transfers	(1,050,659)	(750,952)	1,050,659	750,952	-0-	-0-
Change in net position	45,167	5,247,790	824,791	1,352,818	869,958	6,600,608
Net position - beginning	<u>17,704,863</u>	<u>12,457,073</u>	<u>7,170,852</u>	<u>5,818,034</u>	<u>24,875,715</u>	<u>18,275,107</u>
Net position - ending	<u>\$ 17,750,030</u>	<u>\$ 17,704,863</u>	<u>\$ 7,995,643</u>	<u>\$ 7,170,852</u>	<u>\$ 25,745,673</u>	<u>\$ 24,875,715</u>

CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2016

Financial Analysis of the City's Funds

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

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

As of the end of the current fiscal year, the City of Freeport's governmental funds reported combined ending fund balances of \$ 9,757,478. 90.93% of this total amount (\$ 8,872,715) constitutes unassigned fund balance. The remainder of the fund balance is restricted to indicate that it is not available for new spending 1) restricted for economic development \$ 265,836, 2) restricted for debt service \$ 107,057, 3) restricted for construction \$ 54,029, 4) restricted for municipal court security \$ 5,248, 5) restricted for municipal court technology \$ 16,822, 6) assigned for beach maintenance \$ 752; 7) assigned to main street \$ 2,795, 8) assigned to capital projects \$ 420,726, and 9) assigned to LNG boat maintenance \$ 11,498.

The General Fund balance decreased by \$ 414,972 and the other governmental funds decreased \$ 114,906.

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

Net position at September 30, 2016 amounted to \$ 7,995,643. Total net position increased by \$ 824,791 (or 11.50%).

General Fund Budgetary Highlights. Differences between the original budget and the final amended budget resulted in an increase of \$ 487,176 in estimated revenues and \$ 1,152,855 increase in appropriations which involved a number of budget items. The most significant item was \$ 399,840 increase in public safety appropriations for capital outlay.

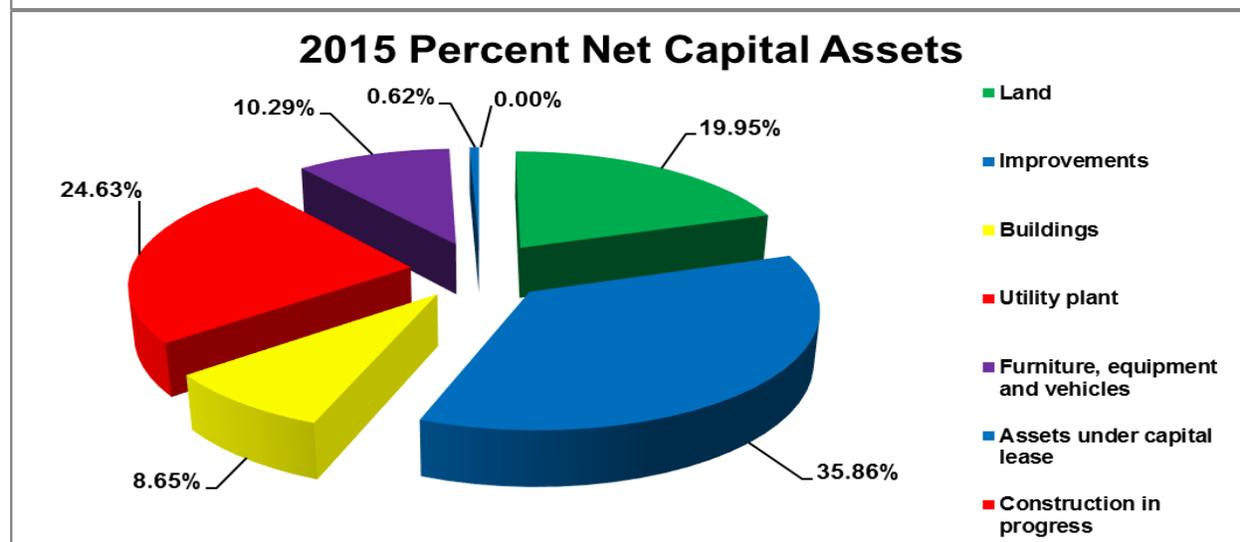
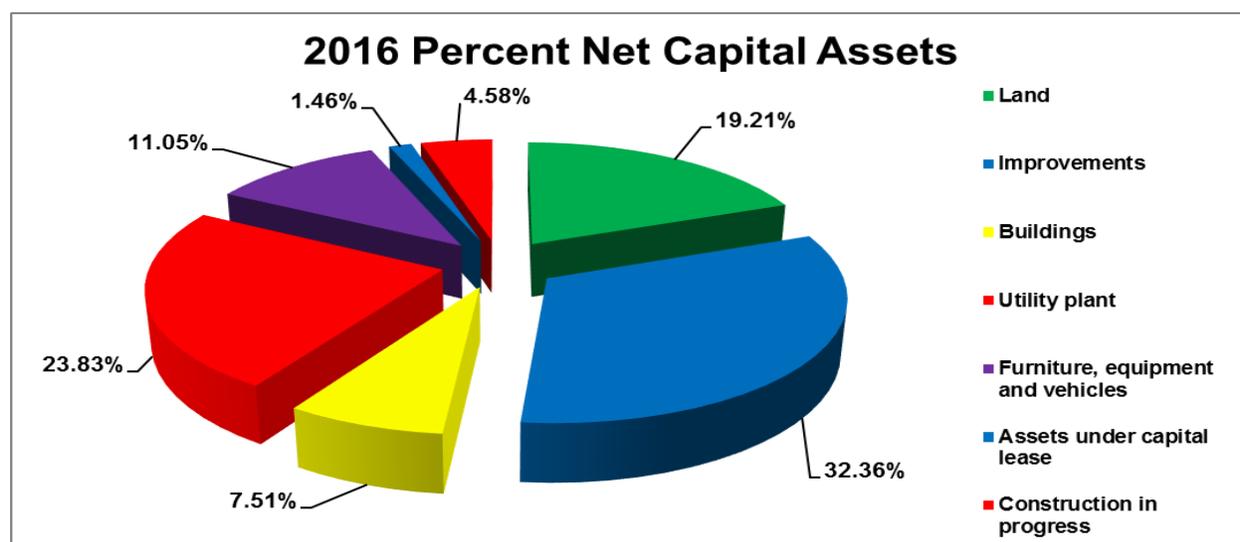
Capital Assets

The City of Freeport's investment in capital assets for its governmental and business-type activities as of September 30, 2016, amounts to \$ 25,814,200 (net of accumulated depreciation). This investment in capital assets includes land, improvements, buildings, utility plant, furniture, and equipment and vehicles.

CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2016

Capital Assets
Net of Accumulated Depreciation

	Governmental Activities		Business-type Activities		Totals	
	September 30,		September 30,		September 30,	
	2016	2015	2016	2015	2016	2015
Land	\$ 4,563,814	\$ 4,458,504	\$ 395,630	\$ 395,630	\$ 4,959,444	\$ 4,854,134
Improvements	8,285,504	8,681,645	67,946	47,747	8,353,450	8,729,392
Buildings	1,854,221	2,016,397	85,320	90,438	1,939,541	2,106,835
Utility plant			6,150,435	5,995,327	6,150,435	5,995,327
Furniture, equipment and vehicles	2,274,421	1,882,263	577,666	622,621	2,852,087	2,504,884
Assets under capital lease	328,724		46,956	151,106	375,680	151,106
Construction in progress			1,183,563		1,183,563	-0-
Total	\$ 17,306,684	\$ 17,038,809	\$ 8,507,516	\$ 7,302,869	\$ 25,814,200	\$ 24,341,678



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

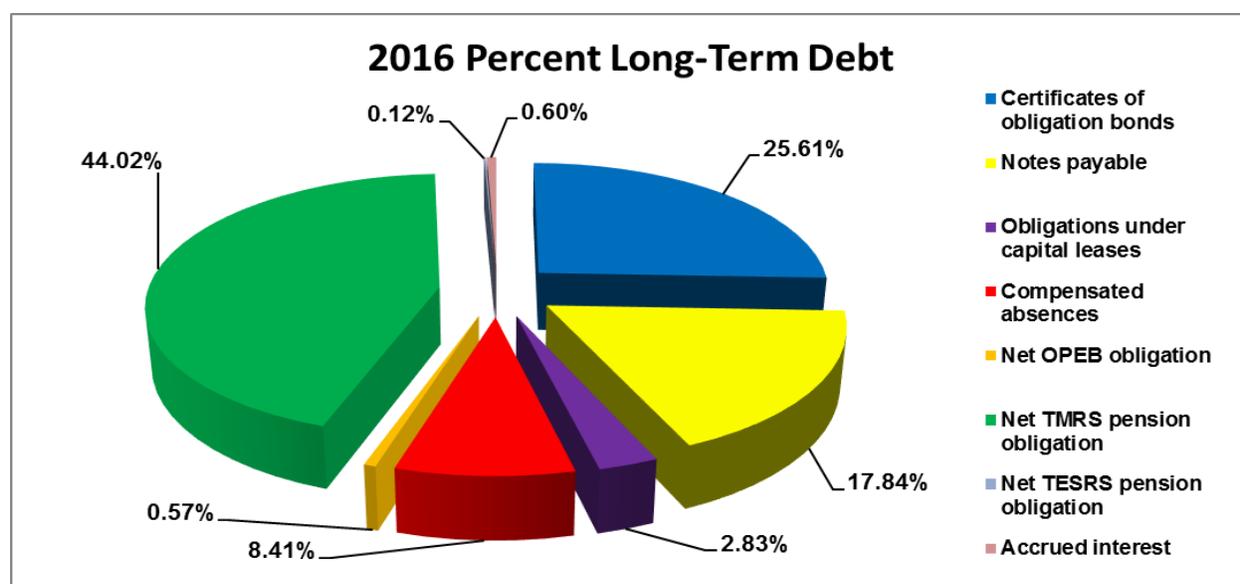
CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2016

Debt Administration

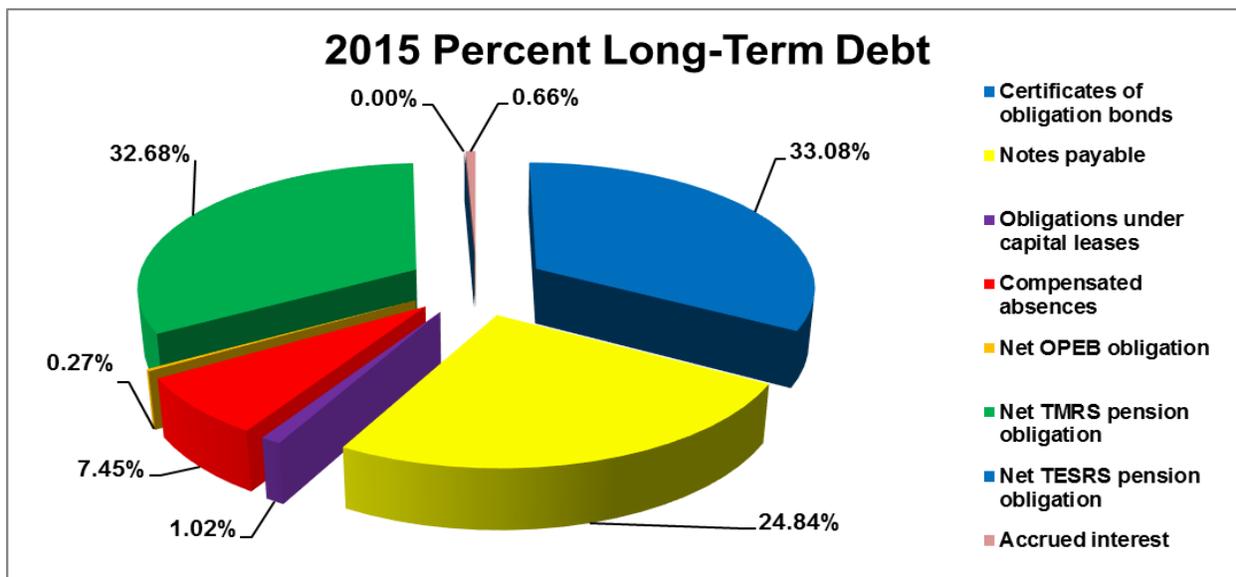
At the end of the current fiscal year, the City of Freeport had a total bonded debt and certificates of obligation payable of \$ 3,145,000, which is comprised of bonded debt backed by the full faith and credit of the City. The notes payable, in the amount of \$ 2,190,344 will be retired with revenues from sales taxes of the Freeport Economic Development Corporation. The remaining \$ 347,982 represents capital lease obligations secured by the assets purchased and the revenues of the General Fund and the Golf Course Enterprise Fund.

Long-Term Debt Outstanding

	Governmental Activities		Business-type Activities		Totals	
	2016	2015	2016	2015	2016	2015
Certificates of obligation bonds	\$ 3,145,000	\$ 3,774,000	\$	\$	\$ 3,145,000	\$ 3,774,000
Notes payable	2,190,344	2,833,758			2,190,344	2,833,758
Obligations under capital leases	305,458		42,524	116,185	347,982	116,185
Compensated absences	898,634	760,247	134,782	89,089	1,033,416	849,336
Net OPEB obligation	59,241	26,103	10,438	4,599	69,679	30,702
Net TMRS pension obligation	4,595,839	3,168,968	809,807	558,400	5,405,646	3,727,368
Net TESRS pension obligation	14,877				14,877	-0-
Components of Long-Term Debt:						
Accrued interest	73,543	75,166	28	203	73,571	75,369
Total	\$ 11,282,936	\$ 10,638,242	\$ 997,579	\$ 768,476	\$ 12,280,515	\$ 11,406,718



CITY OF FREEPORT, TEXAS
Management's Discussion and Analysis
For the Year Ended September 30, 2016



Additional information on the City of Freeport's long-term debt can be found in Note 14 on pages 77 through 80 of this report.

Economic Factors and Next Year's Budgets and Rates

Certified assessed valuations increased 5% over the preceding year. The property tax rate decreased from \$ 0.645642 to \$ 0.628005 with \$ 0.142090 as interest and sinking component and \$ 0.485915 as the maintenance and operation component. From the interest and sinking component, \$ 0.4842 was used to pay the Certificates of Obligations, Series 2003 issued on October 23, 2003 and \$ 0.5158 was used to pay the Certificates of Obligations, Series 2008 issued on March 3, 2008.

The price of water from the Brazosport Water Authority increased from \$ 2.63 to \$ 2.94 per thousand gallons and become effective October 1, 2016.

Request for Information

This financial report is designed to provide a general overview of the City's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Office of Finance, 200 West Second Street, Freeport, Texas, 77541, or call (979) 233-3526.

FINAL

BASIC FINANCIAL STATEMENTS

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF NET POSITION

September 30, 2016

	Governmental Activities	Business- Type Activities	Total
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES			
Assets:			
Cash and cash equivalents	\$ 9,569,872	\$ 611,765	\$ 10,181,637
Receivables (Net of Allowance for Uncollectible):			
Taxes	628,380		628,380
Accounts	418,152	1,062,067	1,480,219
Other	45,422		45,422
Due from other governments	625	100,087	100,712
Interfund balances	559,795	(559,795)	
Inventory		12,772	12,772
Restricted Assets:			
Temporarily Restricted:			
Cash and cash equivalents		236,920	236,920
Capital Assets (Net of Accumulated Depreciation):			
Land	4,563,814	395,630	4,959,444
Improvements	8,285,504	67,946	8,353,450
Buildings	1,854,221	85,320	1,939,541
Utility plant		6,150,435	6,150,435
Furniture, equipment and vehicles	2,274,421	577,666	2,852,087
Assets under capital lease	328,724	46,956	375,680
Construction in progress		1,183,563	1,183,563
Total assets	<u>28,528,930</u>	<u>9,971,332</u>	<u>38,500,262</u>
Deferred Outflows of Resources:			
Pension:			
Net difference between expected and actual earnings	163,824	28,865	192,689
Changes in assumptions	69,168	12,187	81,355
Net difference between projected and actual investment earnings	945,527	166,057	1,111,584
Subsequent contributions	<u>472,157</u>	<u>81,914</u>	<u>554,071</u>
Total deferred outflows of resources	<u>1,650,676</u>	<u>289,023</u>	<u>1,939,699</u>

	Governmental Activities	Business- Type Activities	Total
	<u> </u>	<u> </u>	<u> </u>
LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION			
Liabilities:			
Accounts payable	\$ 744,388	\$ 967,580	\$ 1,711,968
Accrued wages and benefits	292,250	54,494	346,744
Liabilities payable from restricted assets		236,920	236,920
Unearned revenue	64,946	200	65,146
Noncurrent Liabilities:			
Due within one year	1,849,135	58,826	1,907,961
Due in more than one year	<u>9,433,801</u>	<u>938,753</u>	<u>10,372,554</u>
Total liabilities	<u>12,384,520</u>	<u>2,256,773</u>	<u>14,641,293</u>
Deferred Inflows of Resources:			
Pension:			
Net difference between expected and actual experience	<u>45,056</u>	<u>7,939</u>	<u>52,995</u>
Total deferred inflows of resources	<u>45,056</u>	<u>7,939</u>	<u>52,995</u>
Net Position:			
Net investment in capital assets	11,665,882	8,464,992	20,130,874
Restricted For:			
Economic development	262,535		262,535
Debt service	63,264		63,264
Capital projects	54,029		54,029
Municipal court security	5,248		5,248
Municipal court technology	16,822		16,822
Unrestricted	<u>5,682,250</u>	<u>(469,349)</u>	<u>5,212,901</u>
Total net position	<u>\$ 17,750,030</u>	<u>\$ 7,995,643</u>	<u>\$ 25,745,673</u>

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

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF ACTIVITIES

For the Year Ended September 30, 2016

Functions/Programs	Expenses	Program Revenues		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary Government:				
Governmental Activities:				
General government and administration	\$ 2,414,504	\$ 518,169	\$ 3,600	\$
Economic development	438,353			
Public safety	5,931,778	218,013	97,245	263,407
Streets and drainage	1,771,064			
Sanitation	914,275	868,912		
Service center	161,099			
Library	44,783			
Parks and recreation	2,056,169	137,836	4,631	
Interest on long-term debt	239,139			
Total governmental activities	13,971,164	1,742,930	105,476	263,407
Business-type Activities:				
Water and sewer	5,549,230	5,110,748		1,184,220
Golf course (\$ 2,146 interest on long-term debt)	990,176	350,690		
Ambulance	810,688	476,631		
Total business-type activities	7,350,094	5,938,069	-0-	1,184,220
Total	\$ 21,321,258	\$ 7,680,999	\$ 105,476	\$ 1,447,627
General Revenue:				
Taxes:				
Property taxes				
Other taxes				
Industrial district				
Investment earnings				
Miscellaneous				
Gain on disposal of capital assets				
Transfers				
Total general revenues and transfers				
Change in net position				
Net position – beginning				
Net position – ending				

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

Net (Expense) Revenue and Changes in Net Position		
Governmental Activities	Business- Type Activities	Total
\$(1,892,735)	\$	\$(1,892,735)
(438,353)		(438,353)
(5,353,113)		(5,353,113)
(1,771,064)		(1,771,064)
(45,363)		(45,363)
(161,099)		(161,099)
(44,783)		(44,783)
(1,913,702)		(1,913,702)
(239,139)		(239,139)
<u>(11,859,351)</u>	<u>-0-</u>	<u>(11,859,351)</u>

	745,738	745,738
	(639,486)	(639,486)
	<u>(334,057)</u>	<u>(334,057)</u>
<u>-0-</u>	<u>(227,805)</u>	<u>(227,805)</u>
<u>(11,859,351)</u>	<u>(227,805)</u>	<u>(12,087,156)</u>

2,539,494		2,539,494
3,896,907		3,896,907
6,370,196		6,370,196
30,785	1,937	32,722
75,795		75,795
42,000		42,000
(1,050,659)	1,050,659	-0-
<u>11,904,518</u>	<u>1,052,596</u>	<u>12,957,114</u>
45,167	824,791	869,958
<u>17,704,863</u>	<u>7,170,852</u>	<u>24,875,715</u>
<u>\$ 17,750,030</u>	<u>\$ 7,995,643</u>	<u>\$ 25,745,673</u>

CITY OF FREEPORT

Freeport, Texas

**BALANCE SHEET
GOVERNMENTAL FUNDS**

September 30, 2016

	<u>General Fund</u>	<u>Non-Major Governmental Funds</u>	<u>Total Governmental Funds</u>
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES			
<u>Assets</u>			
Cash and temporary investments	\$ 9,383,819	\$ 186,053	\$ 9,569,872
Receivables (Net of Allowance for Uncollectible):			
Property taxes	75,624	20,643	96,267
Sales tax	354,742	177,371	532,113
Accounts	131,150	3,560	134,710
Other receivables	45,422		45,422
Due from other governments		625	625
Due from other funds	<u>624,254</u>	<u>116,195</u>	<u>740,449</u>
 Total assets	 <u>10,615,011</u>	 <u>504,447</u>	 <u>11,119,458</u>
Deferred Outflows of Resources:			
Deferred outflows of resources			-0-
 Total deferred outflows of resources	 <u>-0-</u>	 <u>-0-</u>	 <u>-0-</u>
 Total assets and deferred outflows of resources	 <u>\$ 10,615,011</u>	 <u>\$ 504,447</u>	 <u>\$ 11,119,458</u>

	General Fund	Non-Major Governmental Funds	Total Governmental Funds
LIABILITIES, DEFERRED INFLOWS OF RESOURCES			
<u>Liabilities and Fund Balances</u>			
Liabilities:			
Accounts payable	\$ 702,940	\$ 41,448	\$ 744,388
Accrued wages and benefits	289,688	2,562	292,250
Due to other funds	166,483	14,171	180,654
Unearned revenue	<u>64,946</u>		<u>64,946</u>
Total liabilities	<u>1,224,057</u>	<u>58,181</u>	<u>1,282,238</u>
Deferred Inflows of Resources:			
Deferred inflows of resources	<u>61,150</u>	<u>18,592</u>	<u>79,742</u>
Total deferred inflows of resources	<u>61,150</u>	<u>18,592</u>	<u>79,742</u>
Fund Balance:			
Restricted:			
Economic development		265,836	265,836
Debt service		107,057	107,057
Construction		54,029	54,029
Municipal court security	5,248		5,248
Municipal court technology	16,822		16,822
Assigned:			
Beach maintenance		752	752
Main street	2,795		2,795
Capital projects	420,726		420,726
LNG boat maintenance	11,498		11,498
Unassigned	<u>8,872,715</u>		<u>8,872,715</u>
Total fund balances	<u>9,329,804</u>	<u>427,674</u>	<u>9,757,478</u>
Total liabilities, deferred inflows of resources and fund balances	<u>\$ 10,615,011</u>	<u>\$ 504,447</u>	<u>\$ 11,119,458</u>

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

CITY OF FREEPORT

Freeport, Texas

Exhibit C-1R

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

September 30, 2016

Total fund balances – governmental funds balance sheet	\$ 9,757,478
Amounts reported for governmental activities in the statement of net position are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. Capital assets include \$ 41,750,291 in assets less \$ 24,443,607 in accumulated depreciation.	17,306,684
Municipal Court accounts receivables net of related allowance for uncollectible are unavailable to pay for current period expenditures and funds that are uncertain as to availability are not recorded in the funds. Municipal Court receivables \$ 1,417,212 net of allowance for uncollectible accounts \$ 1,133,770 of the general fund amounted to \$ 283,442.	283,442
Property taxes receivable unavailable to pay for current period expenditures are deferred in the funds. Deferred inflows of resources - property tax revenues for the general fund and debt service funds amounted to \$ 61,150 and \$ 18,592, respectively.	79,742
Deferred outflows of resources are not reported in the funds. These amounted to \$ 1,650,676 (\$ 163,824 for the net difference between expected and actual experience, \$ 69,168 for changes in assumptions, \$ 945,527 for the net difference between projected and actual investment earnings, and \$ 472,157 for subsequent contributions).	1,650,676
Deferred outflows of resources are not reported in the funds. These amounted to \$ 45,056 (for the net difference between expected and actual experience).	(45,056)
Payables for TMRS net pension obligation are not reported in the funds.	(4,595,839)
Payables for TESRS net pension obligation are not reported in the funds.	(14,877)
Payables for Net OPEB obligation.	(59,241)
Payables for bond principal are not reported in the funds.	(3,145,000)
Payables for note principal are not reported in the funds.	(2,190,344)
Payables for obligations under capital lease principal not reported in the funds.	(305,458)
Payables for long-term compensated absences are not reported in the funds.	(898,634)
Payables for bond interest are not reported in the funds.	(<u>73,543</u>)
Net position of governmental activities – statement of net position.	\$ <u>17,750,030</u>

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

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FINAL

CITY OF FREEPORT

Freeport, Texas

Exhibit C-2

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

For the Year Ended September 30, 2016

	General Fund	Non-Major Governmental Funds	Total Governmental Funds
	<u> </u>	<u> </u>	<u> </u>
Revenues:			
Taxes	\$ 2,096,452	\$ 619,753	\$ 2,716,205
Other taxes	2,821,956	1,074,951	3,896,907
Industrial district	6,370,196		6,370,196
Intergovernmental revenues	345,812		345,812
Revenue producing facilities	1,075,084		1,075,084
Fines, licenses and fees	615,826		615,826
Investment income	30,089	696	30,785
Miscellaneous	<u>129,035</u>	<u>2,077</u>	<u>131,112</u>
Total revenues	<u>13,484,450</u>	<u>1,697,477</u>	<u>15,181,927</u>
Expenditures:			
Current:			
General government and administration	2,146,337		2,146,337
Economic development		298,666	298,666
Public safety	5,940,988		5,940,988
Streets and drainage	2,008,648		2,008,648
Sanitation	914,275		914,275
Service center	171,530		171,530
Library	18,933		18,933
Parks and recreation	1,977,510	15,731	1,993,241
Capital outlay		2,810	2,810
Debt Service:			
Principal	82,090	1,272,414	1,354,504
Interest		<u>240,762</u>	<u>240,762</u>
Total expenditures	<u>13,260,311</u>	<u>1,830,383</u>	<u>15,090,694</u>
Excess (deficiency) of revenues over (under) expenditures	<u>224,139</u>	<u>(132,906)</u>	<u>91,233</u>
Other Financing Sources (Uses):			
Sale of capital assets	42,000		42,000
Proceed from issuance of capital leases	387,548		387,548
Operating transfers in		395,071	395,071
Operating transfers out	<u>(1,068,659)</u>	<u>(377,071)</u>	<u>(1,445,730)</u>
Total other financing sources (uses)	<u>(639,111)</u>	<u>18,000</u>	<u>(621,111)</u>
Net changes in fund balance	<u>(414,972)</u>	<u>(114,906)</u>	<u>(529,878)</u>
Fund balance – beginning	<u>9,744,776</u>	<u>542,580</u>	<u>10,287,356</u>
Fund balance - ending	<u>\$ 9,329,804</u>	<u>\$ 427,674</u>	<u>\$ 9,757,478</u>

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

CITY OF FREEPORT

Freeport, Texas

Exhibit C-2R

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

For the Year Ended September 30, 2016

Net change in fund balances – total governmental funds	\$(529,878)
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Amounts reported for governmental activities in the statement of activities are different because:

Governmental funds report capital outlays as expenditures. However, in the governmental activities statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlay of \$ 2,005,578 exceeded depreciation of \$ 1,737,703 in the current period.	267,875
Municipal court revenues in the governmental activities statement of activities do not provide current financial resources and are not reported as revenues in the funds. Municipal court receivables, net of allowance, increased by \$ 19,775.	19,775
Property tax revenues in the governmental activities statement of activities do not provide current financial resources and are not reported as revenues in the funds. Deferred inflows of resources – property tax revenues, for the general fund decreased by \$ 136,595, and for the debt service decreased by \$ 40,116.	(176,711)
Repayment of long-term debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the governmental activities statement of net position. These amounts were for general obligation bonded debt of \$ 629,000 and capital leases of \$ 82,090 and note payable of \$ 643,414.	1,354,504
Long-term debt proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the governmental activities statement of net assets. Long-term Proceeds in the governmental fund were \$ 387,548 in capital leases.	(387,548)
Some expenses reported in the governmental activities statement of activities do not require the use of current financial resources, and, therefore, are not reported as expenditures in governmental funds. This is the change in accrued interest on long-term debt of \$ 1,623, accrued compensated absences of \$(138,387), TMRS net pension obligation of \$(322,105), TESRS net pension obligation of \$(10,842), and net OPEB pension obligation of \$(33,138).	<u>502,850</u>
Change in net position of governmental activities	<u>\$ 45,167</u>

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

CITY OF FREEPORT

Freeport, Texas

STATEMENT OF NET POSITION - PROPRIETARY FUNDS

September 30, 2016

	<u>Water and Sewer</u>	<u>Golf Course</u>	<u>Ambulance</u>	<u>Total Proprietary Funds</u>
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES				
Assets:				
Current Assets:				
Cash and temporary investments	\$ 577,811	\$ 6,491	\$ 27,463	\$ 611,765
Receivables (Net of Allowance for Uncollectible):				
Accounts	749,398		312,669	1,062,067
Due from other governments	100,087			100,087
Due from other funds	56,607		7,552	64,159
Inventory		<u>12,772</u>		<u>12,772</u>
Total unrestricted current assets	<u>1,483,903</u>	<u>19,263</u>	<u>347,684</u>	<u>1,850,850</u>
Current Restricted Assets:				
Cash and temporary investments	<u>236,920</u>			<u>236,920</u>
Total current restricted assets	<u>236,920</u>	<u>-0-</u>	<u>-0-</u>	<u>236,920</u>
Total current assets	<u>1,720,823</u>	<u>19,263</u>	<u>347,684</u>	<u>2,087,770</u>
Capital Assets:				
Land	56,200	339,430		395,630
Construction in progress	1,183,563			1,183,563
Buildings		211,468		211,468
Improvements		601,549		601,549
Utility plant	21,674,409			21,674,409
Furniture, equipment and vehicles	146,765	760,191	799,448	1,706,404
Assets under capital lease		48,985		48,985
Less accumulated depreciation	<u>(15,670,236)</u>	<u>(1,337,902)</u>	<u>(306,354)</u>	<u>(17,314,492)</u>
Total capital assets (net of accumulated depreciation)	<u>7,390,701</u>	<u>623,721</u>	<u>493,094</u>	<u>8,507,516</u>
Total assets	<u>9,111,524</u>	<u>642,984</u>	<u>840,778</u>	<u>10,595,286</u>
Deferred Outflows of Resources:				
Pension:				
Net difference between expected and actual experience	2,904	11,480	14,481	28,865
Changes in assumptions	1,226	4,847	6,114	12,187
Net difference between projected and actual investment earnings	16,705	66,041	83,311	166,057
Subsequent pension contributions	<u>8,280</u>	<u>32,529</u>	<u>41,105</u>	<u>81,914</u>
Total deferred outflows of resources	<u>29,115</u>	<u>114,897</u>	<u>145,011</u>	<u>289,023</u>
Total assets and deferred outflows of resources	<u>\$ 9,140,639</u>	<u>\$ 757,881</u>	<u>\$ 985,789</u>	<u>\$ 10,884,309</u>

	Water and Sewer	Golf Course	Ambulance	Total Proprietary Funds
LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION				
Liabilities:				
Current Liabilities:				
Accounts payable	\$ 935,726	\$ 21,534	\$ 10,320	\$ 967,580
Accrued wages and benefits	3,934	26,731	23,829	54,494
Accrued compensated absences	10,000	24,000	13,000	47,000
Accrued interest payable		28		28
Due to other funds		623,954		623,954
Obligations under capital lease - current		11,798		11,798
Unearned revenue	<u>200</u>			<u>200</u>
Total current liabilities	<u>949,860</u>	<u>708,045</u>	<u>47,149</u>	<u>1,706,054</u>
Current Liabilities Payable from Restricted Assets:				
Customer deposits payable	<u>236,920</u>			<u>236,920</u>
Total current liabilities payable from restricted assets	<u>236,920</u>	<u>-0-</u>	<u>-0-</u>	<u>236,920</u>
Total current liabilities	<u>1,186,780</u>	<u>708,045</u>	<u>47,149</u>	<u>1,941,974</u>
Noncurrent Liabilities:				
Accrued compensated absences	4,731	33,664	49,387	87,782
Obligations under capital lease – net of current		30,726		30,726
Net OPEB obligation	1,044	3,868	5,526	10,438
Net pension obligation	<u>81,466</u>	<u>322,061</u>	<u>406,280</u>	<u>809,807</u>
Total noncurrent liabilities	<u>87,241</u>	<u>390,319</u>	<u>461,193</u>	<u>938,753</u>
Total liabilities	<u>1,274,021</u>	<u>1,098,364</u>	<u>508,342</u>	<u>2,880,727</u>
Deferred Inflows of Resources:				
Pension:				
Difference between expected and actual experience	<u>799</u>	<u>3,157</u>	<u>3,983</u>	<u>7,939</u>
Total deferred inflows of resources	<u>799</u>	<u>3,157</u>	<u>3,983</u>	<u>7,939</u>
Net Position:				
Net investment in capital assets	7,390,701	581,197	493,094	8,464,992
Unrestricted	<u>475,118</u>	<u>(924,837)</u>	<u>(19,630)</u>	<u>(469,349)</u>
Total net position	<u>7,865,819</u>	<u>(343,640)</u>	<u>473,464</u>	<u>7,995,643</u>
Total liabilities, deferred inflows of resources and net position	<u>\$ 9,140,639</u>	<u>\$ 757,881</u>	<u>\$ 985,789</u>	<u>\$ 10,884,309</u>

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

CITY OF FREEPORT

Freeport, Texas

Exhibit D-2

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

For the Year Ended September 30, 2016

	Water and Sewer	Golf Course	Ambulance	Total Proprietary Funds
Operating Revenues:				
Water service	\$ 3,032,832	\$	\$	\$ 3,032,832
Sewer service	1,793,976			1,793,976
Charges for other services	283,940		475,183	759,123
Golf course fees and charges		344,278		344,278
Grant revenue		6,412		6,412
Miscellaneous			1,448	1,448
	<u>5,110,748</u>	<u>350,690</u>	<u>476,631</u>	<u>5,938,069</u>
Total operating revenues				
Operating Expenses:				
Personnel services	80,194	386,868	490,000	957,062
Employee benefits	38,486	182,018	157,770	378,274
Contract and professional services	2,827,153			2,827,153
Other operating costs	52,827	95,706	24,937	173,470
Supplies	35,432	78,751	45,324	159,507
Cost of sales and services	2,199,757	134,710		2,334,467
	<u>5,233,849</u>	<u>878,053</u>	<u>718,031</u>	<u>6,829,933</u>
Operating expenses before depreciation				
Depreciation	315,381	93,195	90,020	498,596
	<u>5,549,230</u>	<u>971,248</u>	<u>808,051</u>	<u>7,328,529</u>
Total operating expenses				
Net operating income (loss)	(438,482)	(620,558)	(331,420)	(1,390,460)
Non-Operating Revenues (Expenses):				
Interest revenue	1,342	507	88	1,937
Loss on sale of capital assets		(16,782)	(2,637)	(19,419)
Interest expense and agent fees		(2,146)		(2,146)
	<u>1,342</u>	<u>(18,421)</u>	<u>(2,549)</u>	<u>(19,628)</u>
Total non-operating revenues (expenses)				
Net income (loss) before contributions and operating transfers	(437,140)	(638,979)	(333,969)	(1,410,088)
Contributions (capital)	1,184,220			1,184,220
Transfers in	620,893	350,816	78,950	1,050,659
	<u>1,367,973</u>	<u>(288,163)</u>	<u>(255,019)</u>	<u>824,791</u>
Change in net position				
Net position – beginning	6,497,846	(55,477)	728,483	7,170,852
	<u>6,497,846</u>	<u>(55,477)</u>	<u>728,483</u>	<u>7,170,852</u>
Net position - ending	\$ 7,865,819	\$(343,640)	\$ 473,464	\$ 7,995,643
	<u>\$ 7,865,819</u>	<u>\$(343,640)</u>	<u>\$ 473,464</u>	<u>\$ 7,995,643</u>

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

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FINAL

CITY OF FREEPORT

Freeport, Texas

**STATEMENT OF CASH FLOWS -
PROPRIETARY FUNDS**

For the Year Ended September 30, 2016

	Water and Sewer	Golf Course	Ambulance	Total Proprietary Funds
Cash Flows from Operating Activities:				
Receipts from customers and users	\$ 5,067,384	\$ 350,690	\$ 628,336	\$ 6,046,410
Receipts from other funds		218,426		218,426
Payments to other funds	(56,607)		(7,552)	(64,159)
Payments to suppliers	(4,726,889)	(307,629)	(62,150)	(5,096,668)
Payments to employees	(115,127)	(525,086)	(602,112)	(1,242,325)
Net cash provided (used) by operating activities	<u>168,761</u>	<u>(263,599)</u>	<u>(43,478)</u>	<u>(138,316)</u>
Cash Flows from Non-Capital Financing Activities:				
Transfers from other funds	<u>620,893</u>	<u>350,816</u>	<u>78,950</u>	<u>1,050,659</u>
Net cash provided by non-capital financing activities	<u>620,893</u>	<u>350,816</u>	<u>78,950</u>	<u>1,050,659</u>
Cash Flows from Capital and Related Financing Activities:				
Capital contributions	1,184,220			1,184,220
Capital expenditures	(1,648,020)	(110,181)	(59,164)	(1,817,365)
Proceeds from the sale of capital assets		(61,718)		(61,718)
Interest payments on capital leases		87,151	7,552	94,703
Principal payments on capital leases		(2,321)		(2,321)
Net cash used by capital and related financing activities	<u>(463,800)</u>	<u>(87,069)</u>	<u>(51,612)</u>	<u>(602,481)</u>
Cash Flows from Investing Activities:				
Interest on investments	<u>1,342</u>	<u>507</u>	<u>88</u>	<u>1,937</u>
Net cash provided by investing activities	<u>1,342</u>	<u>507</u>	<u>88</u>	<u>1,937</u>
Net increase (decrease) in cash and cash equivalents	327,196	655	(16,052)	311,799
Cash and cash equivalents at the beginning of year	<u>487,535</u>	<u>5,836</u>	<u>43,515</u>	<u>536,886</u>
Cash and cash equivalents at the end of the year	<u>\$ 814,731</u>	<u>\$ 6,491</u>	<u>\$ 27,463</u>	<u>\$ 848,685</u>

	<u>Water and Sewer</u>	<u>Golf Course</u>	<u>Ambulance</u>	<u>Total Proprietary Funds</u>
Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities:				
Operating income (loss)	\$(438,482)	\$(620,558)	\$(331,420)	\$(1,390,460)
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:				
Depreciation	315,381	93,195	90,020	498,596
(Increase) decrease in accounts receivable	128,594		151,705	280,299
(Increase) decrease in due from other governments	(100,087)			(100,087)
(Increase) decrease in due from other funds	(56,607)		(7,552)	(64,159)
(Increase) decrease in inventory		579		579
(Increase) decrease in deferred outflows of resources	(19,556)	(79,524)	(94,468)	(193,548)
Increase (decrease) in accounts payable	388,280	959	8,111	397,350
Increase (decrease) in accrued wages and benefits payable	(1,951)	(7,281)	(7,148)	(16,380)
Increase (decrease) in accrued compensated absences payable	(1,099)	13,052	33,740	45,693
Increase (decrease) in unearned revenue	(91,941)			(91,941)
Increase (decrease) in customer deposits	20,070			20,070
Increase (decrease) in due to other funds		218,426		218,426
Increase (decrease) in deferred inflows of resources	4	216	(220)	-0-
Increase (decrease) in net OPEB obligation	584	2,164	3,091	5,839
Increase (decrease) in net pension obligation	<u>25,571</u>	<u>115,173</u>	<u>110,663</u>	<u>251,407</u>
Total adjustments	<u>607,243</u>	<u>356,959</u>	<u>287,942</u>	<u>1,252,144</u>
Net cash provided (used) by operating activities	<u>\$ 168,761</u>	<u>\$(263,599)</u>	<u>\$(43,478)</u>	<u>\$(138,316)</u>
Non-Cash Investing, Capital and Financing Activities:				
Proceeds from capital lease	\$	\$ 34,785	\$	\$ 34,785
Assets acquired through capital lease	<u> </u>	<u>(34,785)</u>	<u> </u>	<u>(34,785)</u>
Net effect of non-cash transactions	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>

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

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FINAL

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

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CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General Statement

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

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

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

Reporting Entity

Primary Government

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Reporting Entity - Continued

Primary Government – Continued

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

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

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

Component Unit

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

The Corporation is governed by a seven member board of directors appointed by the City Council. All projects must have prior approval of the City Council. The voters of Freeport approved collection of a one-half cent sales tax, effective November 2, 1999, to fund the cost of land, buildings, equipment, facilities, improvements and maintenance and operation costs for public park purposes, recreational facilities and infrastructure improvements for development of new or expanded business enterprises. In prior years, the Freeport Economic Development Corporation (the "Corporation") provided services entirely or, almost entirely, to the City or otherwise exclusively or almost exclusively benefited the City even though it did not provide services directly to it and is reported as a blended component unit. However, during the years ended September 30, 2007 through 2014, the Corporation constructed and entered into a long-term lease for a marina with a company unrelated to the City. Because of this, the City was reported as a discretely presented component unit until it divested itself of the marina operations. During the current year, it was reported as a blended component unit.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report financial information on all of the nonfiduciary activities of the primary government. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

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

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

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

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

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

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

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

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

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

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

Operating expenses for the enterprise fund includes the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, and then unrestricted resources as they are needed.

The City has presented the following major governmental fund:

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

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

The City reports the following major proprietary funds:

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

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

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

New Pronouncements

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

GASB Statement No. 68, "Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27", was issued June 2012. This statement was implemented during the current year. This statement is effective for periods beginning after June 15, 2014.

GASB Statement No. 71, "Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 69", was issued November 2013. This statement was implemented during the current year. This statement is effective for periods beginning after June 15, 2014.

GASB Statement No. 72, "Fair Value Measurement and Application", was issued February 2015. This statement enhances the transparency and comparability of fair value measurements and disclosures in the state and local governments' financial statements. This statement was implemented during the current year. This statement is effective for periods beginning after June 15, 2015.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

New Pronouncements - Continued

GASB No. 73, “Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of Statements 67 and 68” was issued June 2015. The management of the City does not expect the implementation of this standard to have a material effect on the financial statements of the City. This statement is effective for periods beginning after June 15, 2016.

GASB No. 74, “Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans” was issued June 2015. The management of the City does not expect the implementation of this standard to have a material effect on the financial statements of the City. This statement is effective for periods beginning after June 15, 2016.

GASB No. 75, “Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions” was issued June 2015. The management of the City does not expect the implementation of this standard to have a material effect on the financial statements of the City. This statement is effective for periods beginning after June 15, 2017.

GASB No. 76, “The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments” was issued June 2015. This statement was implemented during the current year. This statement is effective for periods beginning after June 15, 2015.

GASB No. 77 “Tax Abatement Disclosures” was issued in August 2015. The management of the City does not expect the implementation of this standard to have a material effect on the financial statements of the City. This statement is effective for periods beginning after December 15, 2015.

GASB No. 78, “Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans” was issued in December 2015. The management of the City does not expect the implementation of this standard to have a material effect on the financial statements of the City. This statement is effective for periods beginning after December 15, 2015.

GASB No. 79, “Certain External Investment Pools and Pool Participants” was issued in December 2015. The relevant parts of this statement was implemented during the current year. This statement is effective for periods beginning after June 15, 2015, except for the provisions in paragraphs 18, 19, 23-26, and 40, which is effective for reporting periods beginning after December 15, 2015.

GASB No. 80 “Blending Requirements for Certain Component Units and amendment of GASB No. 14” was issued in January 2016. The management of the City does not expect the implementation of this standard to have a material effect on the financial statements of the City. This statement is effective for periods beginning after June 15, 2016.

GASB No. 81 “Irrevocable Split-Interest Agreements” was issued in March 2016. The management of the District does not expect the implementation of this standard to have a material effect on the financial statements of the City. The requirements of this Statement are effective for periods beginning after December 15, 2016.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

New Pronouncements - Continued

GASB No. 82 “Pension Issues – an amendment of GASB No. 67, No. 68, and No. 73” was issued in March 2016. The management of the City does not expect the implementation of this standard to have a material effect on the financial statements of the District. The requirements of this Statement are effective for periods beginning after June 15, 2016.

Budgetary Data

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

Enterprise Funds:

- Depreciation is not recorded as expense (Non-GAAP).
- Gains and losses on sale of capital assets.
- Capital outlays are recorded as current year expense (Non-GAAP) as opposed to being capitalized and depreciated over the estimated useful life of the asset (GAAP).
- Debt principal is recorded as an expense (Non-GAAP).
- Capital contributions

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

	<u>Budgeted Enterprise Funds</u>			
	<u>Water & Sewer</u>	<u>Golf Course</u>	<u>Ambulance</u>	<u>Total</u>
Net income (loss) - GAAP basis	\$ 1,367,973	\$(288,163)	\$(255,019)	\$ 824,791
Differences:				
Depreciation	315,381	93,195	90,019	498,595
Loss on sale of capital assets		16,782	2,637	19,419
Capital contributions	(1,184,220)			(1,184,220)
Capital outlay	(463,800)	(110,181)	(59,164)	(633,145)
Debt principal		(61,719)		(61,719)
Net income (loss) - budget basis	<u>\$ 35,334</u>	<u>\$(350,086)</u>	<u>\$(221,527)</u>	<u>\$(536,279)</u>

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

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Encumbrances

Encumbrances represent commitments related to unperformed contracts for goods or services. Encumbrance accounting - under which purchase orders, contracts and other commitments for the expenditure of resources are recorded to reserve that portion of the applicable appropriation - is utilized in the governmental funds. Encumbrances outstanding at year end do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year. No encumbrances were outstanding at September 30, 2016.

Cash and Investments

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

Property Taxes

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

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

The City is permitted by the State Property Tax Board to levy taxes up to \$ 1.50 per \$ 100 of assessed valuation for general governmental services other than the payment of principal and interest on long-term debt and unlimited amounts for the payment of principal and interest on long-term debt. The tax rates assessed for the year ended September 30, 2016, to finance general fund operations and the payment of principal and interest on general obligation long-term debt were \$ 0.497578 and \$ 0.148064 per \$ 100 valuation, respectively, for a total of \$ 0.645642 per \$ 100 valuation.

Interfund Receivables, Payables and Transfers

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Capital Assets

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

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

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

Compensated Absences

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

The following is a summary of benefits payable as of September 30, 2016:

	<u>2015</u>
Governmental activities	\$ 898,634
Business-type activities	<u>134,782</u>
	<u>\$ 1,033,416</u>

Pension Plans

The fiduciary net position of the Texas Municipal Retirement System (TMRS) and the Texas Emergency Services Retirement System (TESRS) have been determined using the flow of economic resources measurement focus and full accrual basis of accounting. This includes for purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, pension expense, and information about assets, liabilities and additions to/deductions from TMRS's and the TESRS's fiduciary net positions. Benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Long-Term Debt

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities or proprietary fund type statement of net position. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

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

Fund Equity

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

The City has implemented GASB Statement No. 54, "Fund Balance, Reporting and Governmental Fund Type Definitions", for its governmental funds. Under GASB Statement No. 54, fund balances are required to be reported according to the following classifications:

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

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

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Fund Equity - Continued

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

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

Net Position

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

NOTE 2 - PRIOR PERIOD RESTATEMENT

During the year ended September 30, 2016, the City discovered it had understated both capital assets and long-term debt of the governmental activities statement of net position by \$ 1,575,000. On September 4, 2015, the City purchased land from the Western Seafood Company for \$ 2,450,000 and on the same day made a principal payment of \$ 525,000, leaving a balance of \$ 1,575,000. The financial statements understated capital assets (land) and long-term debt (note payable) by the same amount. Although this had no effect on the governmental activities net position, it did in fact misstate the components of net position. The financial statements for the year ended September 30, 2015 (reported in the Management Discussion and Analysis) have been restated to reflect these transactions.

	<u>Governmental Activities</u>
Net position, September 30, 2015 previously reported	\$ 17,704,863
Capital Assets:	
Land	1,575,000
Long-Term Debt:	
Note payable	<u>(1,575,000)</u>
Net position, September 30, 2015 restated	<u>\$ 17,704,863</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 3 - DEPOSITS, INVESTMENTS AND DERIVATIVES

The City classifies deposits and investments for financial statement purposes as cash and temporary investments, and investments based upon both liquidity (demand deposits) and maturity date (deposits and investments) of the asset at the date of purchase. For this purpose a temporary investment is one that when purchased had a maturity date of three months or less. Cash and temporary investments, as reported on the combined balance sheet at September 30, 2015 are as follows:

	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>
Cash and Temporary Investments:			
Cash (petty cash accounts)	\$ 1,482	\$	\$ 1,482
Financial Institution Deposits:			
Demand deposits	662,319	236,920	899,239
State Treasury Investment Pool:			
Texpool	<u>9,517,836</u>	<u> </u>	<u>9,517,836</u>
Total cash and temporary investments	<u>\$ 10,181,637</u>	<u>\$ 236,920</u>	<u>\$ 10,418,557</u>

Deposits

All deposits with financial institutions must be collateralized in an amount equal to 100 percent of uninsured balances. At September 30, 2016, in addition to petty cash of \$ 1,482, the carrying amount of the City's deposits were \$ 899,239. The financial institutions balances were \$ 627,793 at September 30, 2016. Bank balances of \$ 250,000 were covered by federal depository insurance and \$ 377,793 was covered by collateral pledged in the City's name.

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

Under Texas state law, a bank serving as the City depository must have a bond or in lieu thereof, deposited or pledged securities with the City or an independent third party agent, an amount equal to the highest daily balance of all deposits the City may have during the term of the depository contract, less any applicable FDIC insurance. Chapter 2256 of the Texas Government Code (the Public Funds Investment Act) authorizes the City to invest its funds under written investment policy (the "investment policy") that primarily emphasizes safety of principal and liquidity, addresses investment diversification, yield, and maturity and addresses the quality and capability of investment personnel. This investment policy defines what constitutes the legal list of investments allowed under the policies, which excludes certain instruments allowed under chapter 2256 of the Texas Government Code.

Investments

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 3 - DEPOSITS, INVESTMENTS AND DERIVATIVES - Continued

Investments - Continued

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

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

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

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

The City invests in Texpool to provide its liquidity needs. Texpool is a local government investment pool that was established in conformity with the Interlocal Cooperation Act, Chapter 791 of the Texas Government Code and the Public Funds Investment Act, Chapter 2256 of the Code. Texpool is a 2(a)7 like fund, meaning that it is structured similar to a money market mutual fund. Such funds allow shareholders the ability to deposit or withdraw funds on a daily basis. Interest rates are also adjusted on a daily basis. Such funds seek to maintain a constant net asset value of \$ 1.00, although this cannot be fully guaranteed. Texpool is rated AAA and must maintain a dollar weighted average maturity not to exceed 60 days, which is the limit. At September 30, 2016, Texpool had a weighted average maturity of 44 days. Although Texpool portfolio had a weighted average maturity of 44 days, the City considers holdings in these funds to have a one day weighted average maturity. This is due to the fact that the share position can usually be redeemed each day at the discretion of the shareholder, unless there has been a significant change in value.

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

The following table includes the portfolio balances of all investment types of the City at September 30, 2016.

<u>Investment Type</u>	<u>Fair Value</u>	<u>Weighted Average Maturity (Days)</u>
Local government investment pools (LGIP)	\$ <u>9,517,836</u>	44
	\$ <u>9,517,836</u>	44

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 3 - DEPOSITS, INVESTMENTS AND DERIVATIVES - Continued

Credit Risk – As of September 30, 2016, the LGIP (which represents 100% of the City's portfolio) are rated AAAM by Standard and Poor's.

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

Fair Value Measures

GASB No. 72, "Fair Value Measurement and Application" establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy under GASB No. 72 are described below:

- Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Plan has the ability to access.
- Level 2 Inputs to the valuation methodology include:
- Quoted prices for similar assets or liabilities in active markets;
 - Quoted prices for identical or similar assets or liabilities in inactive markets;
 - Inputs other than quoted prices that are observable for the asset or liability;
 - Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

- Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs. At September 30, 2016, the City held no investments required to be reported under the fair value hierarchy.

NOTE 4 - RECEIVABLES, UNCOLLECTIBLE ACCOUNTS, DEFERRED OUTFLOWS AND INFLOWS OF RESOURCES AND UNEARNED REVENUES

Receivables and Allowances

Receivables as of September 30, 2016, for the government's individual governmental major and nonmajor funds, and proprietary major funds, including the applicable allowances for uncollectible accounts, are as follows:

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 4 - RECEIVABLES, UNCOLLECTIBLE ACCOUNTS, DEFERRED OUTFLOWS AND INFLOWS OF RESOURCES AND UNEARNED REVENUES - Continued

Receivables and Allowances - Continued

	Governmental Funds		
	General	Other	Total
	Fund	Governmental Funds	
Receivables:			
Property taxes	\$ 118,277	\$ 28,219	\$ 146,496
Sales taxes	354,742	177,371	532,113
Accounts	150,210	3,560	153,770
Paving assessments	144,244		144,244
Other receivables	45,422		45,422
Due from other governments (Brazoria County Tax Office)	<u> </u>	<u>625</u>	<u>625</u>
Gross receivables	812,895	209,775	1,022,670
Less Allowance for Uncollectible:			
Property taxes	42,653	7,576	50,229
Accounts	19,060		19,060
Paving assessments	<u>144,244</u>		<u>144,244</u>
Net total receivables	<u>\$ 606,938</u>	<u>\$ 202,199</u>	<u>\$ 809,137</u>

	Proprietary Funds		
	Enterprise Funds		
	Water & Sewer Fund	Ambulance Fund	Total
Receivables:			
Accounts	\$ 829,735	\$ 481,107	\$ 1,310,842
Due from other governments	<u>100,087</u>	<u> </u>	<u>100,087</u>
Gross receivables	929,822	481,107	1,410,929
Less Allowance for Uncollectible:			
Accounts	<u>80,337</u>	<u>168,438</u>	<u>248,775</u>
Net receivables	<u>\$ 849,485</u>	<u>\$ 312,669</u>	<u>\$ 1,162,154</u>

Judicial Receivables

Judicial receivables are reported in the governmental activities statement of net position. Since these receivables do not represent current available resources, they are not reported in the governmental funds balance sheet. The allowance for uncollectible receivables related to the County's various court assessments is determined based on historical experience and evaluation of collectability in relation to the aging of customer accounts. The following is a summary of the receivable and allowance for uncollectible as of September 30, 2016:

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 4 - RECEIVABLES, UNCOLLECTIBLE ACCOUNTS, DEFERRED OUTFLOWS AND INFLOWS OF RESOURCES AND UNEARNED REVENUES - Continued

Judicial Receivables - Continued

	<u>Governmental Activities</u>
Judicial Receivables:	
Accounts	\$ 1,417,212
Less allowance for uncollectible accounts	<u>1,133,770</u>
Net judicial receivables	\$ <u>283,442</u>

Deferred Outflows and Inflows of Resources and Unearned Revenue

Governmental funds report deferred inflows of resources in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received, but not yet earned. As of September 30, 2016, the various components of deferred outflows of resources and unearned revenue reported in the governmental and proprietary funds were as follows:

	<u>Governmental Funds</u>		
	General Fund	Other Governmental Funds	Total
Deferred Inflows of Resources:			
Delinquent property taxes receivable	\$ <u>61,150</u>	\$ <u>18,592</u>	\$ <u>79,742</u>
Unearned Revenue:			
Franchise taxes	\$ <u>64,946</u>	\$ <u>-0-</u>	\$ <u>64,946</u>

	<u>Proprietary Funds/Enterprise Funds</u>			
	<u>Water & Sewer</u>	<u>Golf Course</u>	<u>Ambulance</u>	<u>Total</u>
Deferred Outflows of Resources:				
Pension:				
Difference between expected and actual experience	\$ 2,904	\$ 11,480	\$ 14,481	\$ 28,865
Change is assumptions	1,226	4,847	6,114	12,187
Difference between projected and actual investment earnings	16,705	66,041	83,311	166,057
Subsequent contributions	<u>8,280</u>	<u>32,529</u>	<u>41,105</u>	<u>81,914</u>
Total	\$ <u>29,115</u>	\$ <u>114,897</u>	\$ <u>145,011</u>	\$ <u>289,023</u>

Deferred Inflows of Resources:				
Pension:				
Difference between expected and actual experience	\$ <u>799</u>	\$ <u>3,157</u>	\$ <u>3,983</u>	\$ <u>7,939</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 4 - RECEIVABLES, UNCOLLECTIBLE ACCOUNTS, DEFERRED OUTFLOWS AND INFLOWS OF RESOURCES AND UNEARNED REVENUES - Continued

Deferred Outflows and Inflows of Resources and Unearned Revenue - Continued

	<u>Water & Sewer</u>	<u>Golf Course</u>	<u>Ambulance</u>	<u>Total</u>
Unearned Revenue:				
Customer deposits	\$ 236,920	\$	\$	\$ 236,920
Other	<u>200</u>			<u>200</u>
	<u>\$ 237,120</u>	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ 237,120</u>

	<u>Governmental Activities</u>		
	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>	<u>Unearned Revenue</u>
Pension Related:			
Differences between expected and actual experience	\$ 163,824	\$ 45,056	\$
Changes in assumptions	69,168		
Differences between projected and actual investment earnings	945,527		
Subsequent contributions	472,157		
Unearned Revenue:			
Franchise taxes			<u>64,946</u>
	<u>\$ 1,650,676</u>	<u>\$ 45,056</u>	<u>\$ 64,946</u>

	<u>Business-type Activities</u>		
	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>	<u>Unearned Revenue</u>
Pension Related:			
Differences between expected and actual experience	\$ 28,865	\$ 7,939	\$
Changes in assumptions	12,187		
Differences between projected and actual investment earnings	166,057		
Subsequent contributions	81,914		
Unearned Revenue:			
Customer deposits			236,920
Other			<u>200</u>
	<u>\$ 289,023</u>	<u>\$ 7,939</u>	<u>\$ 237,120</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 5 - INTERFUND RECEIVABLES, PAYABLES AND TRANSFERS

Interfund balances at September 30, 2016 consisted of the following individual fund receivables and payables:

<u>Fund</u>	<u>Receivable</u>	<u>Payable</u>
General Fund:		
Debt Service Fund:		
Series 2003A	300	
Series 2003B		7,754
Series 2008		42,247
Capital Projects Fund:		
2008 Bond Construction		52,323
Enterprise Funds:		
Water and Sewer Fund		56,607
Golf Course Fund	623,954	
Ambulance Fund		7,552
	<u>624,254</u>	<u>166,483</u>
Special Revenue Fund:		
Economic Development Corporation Fund:		
Debt Service Fund:		
General Fund		13,871
Debt Service Fund:		
Series 2003A Fund:		
General Fund		300
Economic Development Fund	13,871	
Series 2003B Fund:		
General Fund	7,754	
Series 2008 Fund:		
General Fund	42,247	
	<u>63,872</u>	<u>300</u>
Capital Projects Fund:		
2008 Bond Construction Fund:		
General Fund	52,323	
Enterprise Funds:		
Water and Sewer Fund:		
General Fund	56,607	
Gold Course Fund:		
General Fund		623,954
Ambulance Fund:		
General Fund	7,552	
	<u>64,159</u>	<u>623,954</u>
Total	<u>\$ 804,608</u>	<u>\$ 804,608</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 5 - INTERFUND RECEIVABLES, PAYABLES AND TRANSFERS - Continued

Interfund transfers for the year ended September 30, 2016 consisted of the following individual fund transfers in and transfers out:

<u>Fund</u>	<u>Transfers In</u>	<u>Transfers Out</u>
General Fund:		
Debt Service Funds:		
Series 2003A	\$	\$ 18,000
Enterprise Funds:		
Water and Sewer Fund		620,893
Golf Course Fund		350,816
Ambulance Fund		78,950
	<u>-0-</u>	<u>1,068,659</u>
Special Revenue Funds:		
Economic Development Corporation Fund:		
Debt Service Funds:		
Series 2003A		159,470
EDC Note		217,601
	<u>-0-</u>	<u>377,071</u>
Debt Service Funds:		
Special Revenue Funds:		
Series 2003A Fund:		
General Fund	18,000	
Economic Development Corporation Fund	159,470	
EDC Note Fund:		
Economic Development Corporation Fund	217,601	
	<u>395,071</u>	<u>-0-</u>
Enterprise Funds:		
Water & Sewer Fund:		
General Fund	620,893	
Golf Course Fund:		
General Fund	350,816	
Ambulance Fund:		
General Fund	78,950	
	<u>1,050,659</u>	<u>-0-</u>
 Total	 <u>\$ 1,445,730</u>	 <u>\$ 1,445,730</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 6 - CAPITAL ASSETS

Restatement (See Note 2)

	Balance <u>10-01-15</u>	Prior Period Adjustment	Restated Balance <u>10-01-15</u>
Governmental Activities:			
Capital Assets, Not Depreciated:			
Land	\$ 2,883,504	\$ 1,575,000	\$ 4,458,504
Total capital assets not being depreciated	<u>\$ 2,883,504</u>	<u>\$ 1,575,000</u>	<u>\$ 4,458,504</u>

Capital Transactions

Capital assets activity for the year ended September 30, 2016 was as follows:

	Restated Balance <u>10-01-15</u>	Additions	Retirements & Transfers	Balance <u>09-30-16</u>
Governmental Activities:				
Capital Assets, Not Depreciated:				
Land	\$ 4,458,504	\$ 105,310	\$	\$ 4,563,814
Total capital assets not being depreciated	<u>4,458,504</u>	<u>105,310</u>	<u>-0-</u>	<u>4,563,814</u>
Capital Assets, Being Depreciated:				
Improvements	21,928,816	436,295		22,365,111
Buildings	5,291,753	62,137		5,353,890
Furniture, equipment and vehicles	8,065,640	1,014,288		9,079,928
Assets under lease		<u>387,548</u>		<u>387,548</u>
Total capital assets being depreciated	<u>35,286,209</u>	<u>1,900,268</u>	<u>-0-</u>	<u>37,186,477</u>
Less Accumulated Depreciation For:				
Improvements	13,247,171	832,436		14,079,607
Buildings	3,275,356	224,313		3,499,669
Furniture, equipment and vehicles	6,183,377	622,130		6,805,507
Assets under lease		<u>58,824</u>		<u>58,824</u>
Total accumulated depreciation	<u>22,705,904</u>	<u>1,737,703</u>	<u>-0-</u>	<u>24,443,607</u>
Total capital assets being depreciated, net	<u>12,580,305</u>	<u>162,565</u>	<u>-0-</u>	<u>12,742,870</u>
Governmental activities capital assets, net	<u>\$ 17,038,809</u>	<u>\$ 267,875</u>	<u>\$ -0-</u>	<u>\$ 17,306,684</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 6 - CAPITAL ASSETS - Continued

Capital Transactions - Continued

	<u>Balance</u> <u>10-01-15</u>	<u>Additions</u>	<u>Retirements</u> <u>& Transfers</u>	<u>Balance</u> <u>09-30-16</u>
Combined Business-type Activities:				
Capital Assets, Not Depreciated:				
Land	\$ 395,630	\$	\$	\$ 395,630
Construction in progress		<u>1,183,563</u>		<u>1,183,563</u>
Total capital assets not being depreciated	<u>395,630</u>	<u>1,183,563</u>	<u>-0-</u>	<u>1,579,193</u>
Capital Assets, Being Depreciated:				
Buildings	211,468			211,468
Improvements	553,118	48,431		601,549
Utility plant	21,209,952	464,457		21,674,409
Furniture, equipment and vehicles	1,786,948	71,929	(152,473)	1,706,404
Assets under capital lease	<u>247,545</u>	<u>48,985</u>	<u>(247,545)</u>	<u>48,985</u>
Total capital assets being depreciated	<u>24,009,031</u>	<u>633,802</u>	<u>(400,018)</u>	<u>24,242,815</u>
Less Accumulated Depreciation For:				
Buildings	\$ 121,030	\$ 5,118	\$	\$ 126,148
Improvements	505,371	28,232		533,603
Utility plant	15,214,625	309,349		15,523,974
Furniture, equipment and vehicles	1,164,327	124,173	(159,762)	1,128,738
Assets under capital lease	<u>96,439</u>	<u>31,724</u>	<u>(126,134)</u>	<u>2,029</u>
Total accumulated depreciation	<u>17,101,792</u>	<u>498,596</u>	<u>(285,896)</u>	<u>17,314,492</u>
Total capital assets being depreciated, net	<u>6,907,239</u>	<u>135,206</u>	<u>(114,122)</u>	<u>6,928,323</u>
Business-type activities capital assets, net	<u>\$ 7,302,869</u>	<u>\$ 1,318,769</u>	<u>\$(114,122)</u>	<u>\$ 8,507,516</u>
Business-type Activities:				
<u>Water and Sewer Enterprise Fund:</u>				
Capital Assets, Not Depreciated:				
Land	\$ 56,200	\$	\$	\$ 56,200
Construction in progress		<u>1,183,563</u>		<u>1,183,563</u>
Total capital assets not being depreciated	<u>56,200</u>	<u>1,183,563</u>	<u>-0-</u>	<u>1,239,763</u>
Capital Assets, Being Depreciated:				
Utility plant	21,209,952	464,457		21,674,409
Furniture, equipment and vehicles	<u>146,765</u>			<u>146,765</u>
Total capital assets being depreciated	<u>21,356,717</u>	<u>464,457</u>	<u>-0-</u>	<u>21,821,174</u>
Less Accumulated Depreciation For:				
Utility plant	15,214,625	309,349		15,523,974
Furniture, equipment and vehicles	<u>140,230</u>	<u>6,032</u>		<u>146,262</u>
Total accumulated depreciation	<u>15,354,855</u>	<u>315,381</u>	<u>-0-</u>	<u>15,670,236</u>
Total capital assets being depreciated, net	<u>6,001,862</u>	<u>149,076</u>	<u>-0-</u>	<u>6,150,938</u>
Water and Sewer Fund capital assets, net	<u>\$ 6,058,062</u>	<u>\$ 1,332,639</u>	<u>\$ -0-</u>	<u>\$ 7,390,701</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 6 - CAPITAL ASSETS - Continued

	<u>Balance</u> <u>10-01-15</u>	<u>Additions</u>	<u>Retirements</u> <u>& Transfers</u>	<u>Balance</u> <u>09-30-16</u>
Business-type Activities:				
<u>Golf Course Enterprise Fund:</u>				
Capital Assets, Not Depreciated:				
Land	\$ 339,430	\$ _____	\$ _____	\$ 339,430
Total capital assets not being depreciated	<u>339,430</u>	<u>-0-</u>	<u>-0-</u>	<u>339,430</u>
Capital Assets, Being Depreciated:				
Buildings	211,468			211,468
Improvements	553,118	48,431		601,549
Furniture, equipment and vehicles	707,748	12,765	39,678	760,191
Assets under capital lease	<u>247,545</u>	<u>48,985</u>	<u>(247,545)</u>	<u>48,985</u>
Total capital assets being depreciated	<u>1,719,879</u>	<u>110,181</u>	<u>(207,867)</u>	<u>1,622,193</u>
Less Accumulated Depreciation For:				
Buildings	121,030	5,118		126,148
Improvements	505,371	28,232		533,603
Furniture, equipment and vehicles	625,801	28,121	22,200	676,122
Assets under capital lease	<u>96,439</u>	<u>31,724</u>	<u>(126,134)</u>	<u>2,029</u>
Total accumulated depreciation	<u>1,348,641</u>	<u>93,195</u>	<u>(103,934)</u>	<u>1,337,902</u>
Total capital assets being depreciated, net	<u>371,238</u>	<u>16,986</u>	<u>(103,933)</u>	<u>284,291</u>
Gold Course Fund capital assets, net	\$ <u>710,668</u>	\$ <u>16,986</u>	\$ <u>(103,933)</u>	\$ <u>623,721</u>
Business-type Activities:				
<u>Ambulance Enterprise Fund:</u>				
Capital Assets, Being Depreciated:				
Furniture, equipment and vehicles	\$ 932,435	\$ 59,164	\$ (192,151)	\$ 799,448
Total capital assets being depreciated	<u>932,435</u>	<u>59,164</u>	<u>(192,151)</u>	<u>799,448</u>
Less Accumulated Depreciation For:				
Furniture, equipment and vehicles	<u>398,296</u>	<u>90,020</u>	<u>(181,962)</u>	<u>306,354</u>
Total accumulated depreciation	<u>398,296</u>	<u>90,020</u>	<u>(181,962)</u>	<u>306,354</u>
Total capital assets being depreciated, net	<u>534,139</u>	<u>(30,856)</u>	<u>(10,189)</u>	<u>493,094</u>
Ambulance Fund capital assets, net	\$ <u>534,139</u>	\$ <u>(30,856)</u>	\$ <u>(10,189)</u>	\$ <u>493,094</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 6 - CAPITAL ASSETS - Continued

Depreciation

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

Governmental Activities:

Administration	\$ 286,269
Economic development	135,063
Public safety	425,291
Service center	19,715
Streets and drainage	571,499
Library	25,850
Parks and recreation	<u>274,016</u>
Total depreciation expense-governmental activities	<u>\$ 1,737,703</u>

Business-type Activities:

Water and sewer	\$ 315,381
Golf Course	93,195
Ambulance	<u>90,020</u>
Total depreciation expense-business-type activities	<u>\$ 498,596</u>
Total	<u>\$ 2,236,299</u>

FINAL

NOTE 7 - CONTINGENT LIABILITIES

The City is contingently liable in respect to lawsuits and other claims in the ordinary course of its operations. The potential settlement (if any) of such contingencies under the budgetary process would require appropriation of revenues yet to be realized and would not materially affect the financial position of the City at September 30, 2016.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 8 - DEFINED BENEFIT PENSION AND SUPPLEMENTAL DEATH BENEFIT PLANS - TMRS

Plan Description

The City participates as one of 860 plans in the nontraditional, join contributory, hybrid defined benefit pension plan administered by the Texas Municipal Retirement System (TMRS). TMRS is an agency created by the State of Texas and administered in accordance with the TMRS Act, Subtitle G, Title 8, Texas Government Code (the TMRS Act) as an agent multiple-employer retirement system for municipal employees in the State of Texas. The TMRS Act places the general administration and management of the System with a six-member Board of Trustees. Although the Governor, with the advice and consent of the Senate, appoints the Board, TMRS is not fiscally dependent on the State of Texas. TMRS's defined benefit pension plan is a tax-qualified plan under Section 401(a) of the Internal Revenue Code. TMRS issues a publically available comprehensive annual financial report (CAFR) that can be obtained at www.tmrs.com.

All eligible employees of the city are required to participate in TMRS.

Benefits Provided

TMRS provides retirement, disability, and death benefits. Benefit provisions are adopted by the governing body of the city, within the options available in the state statutes governing TMRS.

At retirement, the benefit is calculated as if the sum of the employee's contributions, with interest, and the city-financed monetary credits with interest were used to purchase an annuity. Members may choose to receive their retirement benefit in one of seven payment options. Member may also choose to receive a portion of their benefit as a Partial Lump Sum Distribution in an amount equal to 12, 24 or 36 monthly payments, which cannot exceed 75% of the member's deposits and interest.

The plan provisions are adopted by the governing body of each city, within the options available in the state statutes governing TMRS. Members in most cities can retire at age 60 and above with 5 or more years of service or with 20 years of service regardless of age. Some cities have elected retirement eligibility with 25 years of service regardless of age. Most plans also provide death benefits and all provide disability benefits. Effective January 1, 2002, members are vested after 5 years, unless a city opted to maintain 10-year vesting. Members may work for more than one TMRS city during their career. If a member is vested in one TMRS city, he or she is immediately vested upon employment with another TMRS city. Similarly, once a member has met the eligibility requirements for retirement in a TMRS city, he or she is eligible in other TMRS cities as well.

Employees covered by benefit terms - At the December 31, 2015 valuation and measurement date, the following employees were covered by the benefit terms:

Inactive employees or beneficiaries currently receiving benefits	67
Inactive employees entitled to but not yet receiving benefits	116
Active employees	<u>115</u>
Total	<u><u>298</u></u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 8 - DEFINED BENEFIT PENSION AND SUPPLEMENTAL DEATH BENEFIT PLANS - TMRS - Continued

Contributions

The contribution rates for employees in TMRS are either 5%, 6%, or 7% of employee gross earnings, and the city matching percentages are either 100%, 150%, or 200%, both as adopted by the governing body of the city. Under the state law governing TMRS, the contribution rate for each city is determined annually by the actuary, using the Entry Age Normal (EAN) actuarial cost method. The actuarially determined rate is the estimated amount necessary to finance the cost of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability.

Employees of the City were required to contribute 7.00% of their annual gross earnings during the fiscal year. The contribution rates for the City were 12.87% and 13.36% in the calendar years 2015 and 2016, respectively. The City's contributions to TMRS for the year ended September 30, 2016, were \$ 746,948, and were equal to the required contributions.

Net Pension Liability

The City's net pension liability was measured as of December 31, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date.

Actuarial Assumptions - The Total Pension Liability in the December 31, 2015 actuarial valuation was determined using the following actuarial assumptions.

Inflation	2.50% per year
Overall payroll growth	3.50% per year
Investment Rate of Return	6.75%, net of pension plan investment expense, including inflation

Salary increases were based on a service-related table. Mortality rates for active members, retirees, and beneficiaries were based on the gender-distinct RP2000 Combined Healthy Mortality Table, with male rates multiplied by 109% and female rates multiplied by 103%. The rates are projected on a fully generational basis by scale BB to account for future mortality improvements. For disabled annuitants, the gender-distinct RP2000 Disabled Retiree Mortality Table is used, with slight adjustments.

Actuarial assumptions used in the December 31, 2015, valuation were based on the results of actuarial experience studies. The experience study in TMRS was for the period December 31, 2010 through December 31, 2014, first used in the December 31, 2015 valuation. Healthy post-retirement mortality rates and annuity purchase rates were updated based on a Mortality Experience Investigation Study covering 2009 through 2011, and dated December 31, 2013. These assumptions were first used in the December 31, 2013 valuation, along with a change to the Entry Age Normal (EAN) actuarial cost method. Assumptions are reviewed annually. No additional changes were made for the 2015 valuation.

The long-term expected rate of return on pension plan investments is 6.75%. The pension plan's policy in regard to the allocation of invested assets is established and may be amended by the TMRS Board of Trustees. Plan assets are managed on a total return basis with an emphasis on both capital appreciation as well as the production of income, in order to satisfy the short-term and long-term funding needs of TMRS.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 8 - DEFINED BENEFIT PENSION AND SUPPLEMENTAL DEATH BENEFIT PLANS - TMRS -
Continued

Net Pension Liability - Continued

The long term-expected rate of return on pension plan investments was determined using a building-block method in which best estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Net Rate of Return
Equities:		
Domestic	17.5%	4.80%
International	17.5%	6.05%
Fixed Income:		
Core	30.0%	1.50%
Non-Core	10.0%	3.50%
Real Return	5.0%	1.75%
Real Estate	10.0%	5.25%
Absolute Return	5.0%	4.25%
Private Equity	5.0%	8.50%
Total	100%	

Discount Rate - The discount rate used to measure the Total Pension Liability was 6.75%. The projection of cash flows used to determine the discount rate assumed that employee and employer contributions will be made at the rates specified in statute. Based on that assumption, the pension plan's Fiduciary Net Position was projected to be available to make all projected future benefits payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the Total Pension Liability.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 8 - DEFINED BENEFIT PENSION AND SUPPLEMENTAL DEATH BENEFIT PLANS - TMRS -
Continued

Net Pension Liability - Continued

	Increase (Decrease)		
	Total Pension Liability (a)	Plan Fiduciary Net Position (b)	Net Pension Liability (a)-(b)
Balance at December 31, 2014	\$ <u>21,593,032</u>	\$ <u>17,865,664</u>	\$ <u>3,727,368</u>
Changes for the Year:			
Service cost	867,502		867,502
Interest (on total pension liability)	1,511,254		1,511,254
Difference between expected and actual experience	276,833		276,833
Changes in assumptions	116,881		116,881
Contributions – employer		699,079	(699,079)
Contributions – employee		385,600	(385,600)
Net investment income		26,362	(26,362)
Benefit payment, including refunds of employee contributions	(874,894)	(874,894)	-0-
Administrative expense		(16,057)	16,057
Other changes		(792)	792
Net changes	<u>1,897,576</u>	<u>219,298</u>	<u>1,678,278</u>
Balance at December 31, 2015	\$ <u>23,490,608</u>	\$ <u>18,084,962</u>	\$ <u>5,405,646</u>

Sensitivity of the net pension liability to changes in the discount rate.

The following presents the net pension liability of the City, calculated using the discount rate of 6.75%, as well as what's the City's net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (5.75%) or 1-percentage-point higher (7.75%) than the current rate:

	1% Decrease In Discount Rate (5.75%)	Discount Rate (6.75%)	1% Increase In Discount Rate (7.75%)
City's Net Pension Liability			
Changes for the Year:	\$ <u>9,176,255</u>	\$ <u>5,405,646</u>	\$ <u>2,385,796</u>

Pension Plan Fiduciary Net Position - Detailed information about the pension plan's Fiduciary Net Position is available in a separately-issues TMRS financial report. That report may be obtained on the Internet at www.tMrs.com.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 8 - DEFINED BENEFIT PENSION AND SUPPLEMENTAL DEATH BENEFIT PLANS - TMRS -
Continued

Net Pension Liability - Continued

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions - For the year ended September 30, 2016, the city recognized pension expense of \$ 467,280.

At September 30, 2016, the city reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between expected and actual economic experience	\$ 192,689	\$ 52,995
Changes in assumptions	81,355	
Difference between projected and actual investment earnings	1,108,521	
Contributions subsequent to the measurement date	<u>553,099</u>	
 Total	 <u>\$ 1,935,664</u>	 <u>\$ 52,995</u>

\$ 553,099 reported as deferred outflows of resources related to pensions relating from contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability for the year ending September 30, 2016. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

<u>Year Ended September 30,</u>	
2017	\$ 368,016
2018	394,113
2019	322,595
2020	<u>244,846</u>
Total	<u>\$ 1,329,570</u>

OPEB Supplemental Death Benefits Fund

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 8 - DEFINED BENEFIT PENSION AND SUPPLEMENTAL DEATH BENEFIT PLANS - TMRS - Continued

OPEB Supplemental Death Benefits Fund - Continued

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

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

The City’s contributions to the TMRS SDBF for the years ended 2016, 2015, and 2014 were \$ 8,991, \$ 8,609 and \$ 12,649, respectively, which equaled the required contributions each year.

Schedule of Contribution Rates (Retiree-only Portion of the Rate):

<u>Plan/Calendar Year</u>	<u>Actual Required Contribution (Rate)</u>	<u>Actual Contribution Made (Rate)</u>	<u>Percentage of ARC Contributed</u>
2014	0.05%	0.05%	100.0%
2015	0.05%	0.05%	100.0%
2016	0.05%	0.05%	100.0%

NOTE 9 - DEFINED BENEFIT PENSION PLAN - TESRS

Plan Description

The Texas Emergency Services Retirement System (TESRS) administers a cost-sharing multiple employer pension system (the “System”) established and administered by the State of Texas to provide pension benefits for emergency services personnel who serve without significant monetary remuneration. Direct financial activity for the System is classified in the financial statements as pension trust funds. Of the nine member Board of Trustees, at least five trustees must be active members of the pension system, one of whom must represent emergency medical services personnel.

One trustee may be a retiree of the pension system and three trustees must be persons who have experience in the fields of finance, securities investment, or pension administration. At August 31, 2015, there were 197 contributing fire and/or emergency services department members participating in TESRS, with. Eligible participants include volunteer emergency services personnel who are members in good standing of a member department.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 9 - DEFINED BENEFIT PENSION PLAN - TESRS - Continued

Plan Description - Continued

On August 31, 2015, The Pension System Membership Consisted Of:

Retirees and beneficiaries currently receiving benefits	2,991
Terminated members entitled to benefits by not yet receiving them	2,211
Active participants (vested and nonvested)	4,016

On August 31, 2015, the City had 5 active participants (vested and nonvested).

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

Upon reaching age 55, each vested member may retire and receive a monthly pension equal to his vested percent multiplied by six times the governing body's average monthly contribution over the member's years of qualified service. For years of service in excess of 15 years, this monthly benefit is increased at the rate of 6.2% compounded annually. There is no provision for automatic postretirement benefit increases.

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

Funding Policy

Contributions are made by governing bodies for the participating departments. No contributions are required from the individuals who are members of the System, nor are they allowed. The governing bodies of each participating department are required to make contributions for each month a member performs emergency services for a department (this minimum contribution is \$ 36 per member and the department may make a higher monthly contribution for its members). This is referred to as a Part One contribution, which is the legacy portion of the System contribution that directly impacts future retiree annuities.

The state is required to contribute an amount necessary to make the System "actuarially sound" each year, which may not exceed one-third of the total of all contributions made by participating governing bodies in a particular year.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 9 - DEFINED BENEFIT PENSION PLAN - TESRS - Continued

Funding Policy - Continued

The board rule defining contributions was amended effective July 27, 2014 to add the potential for actuarially determined Part Two contributions that would be required only if the expected future annual contributions from the state are not enough with the Part One contributions to provide an adequate contribution arrangement as determined by the most recent actuarial valuation. This Part Two portion, which is actuarially adjusted near the end of each even-numbered calendar year based on the most recent actuarial valuation. Based on the actuarial valuation as of August 31, 2014, the Part Two contribution rate is 0% since the first actuarial valuation report after adoption of the rules showed the System to have an adequate contribution arrangement without any Part Two Contributions.

Additional contributions may be made by governing bodies within two years of joining the System, to grant up to ten years of credit for service per member. Prior service purchased must have occurred before the department began participation in the System.

A small subset of participating departments have a different contribution arrangement which is being phased in over time. In this arrangement, contributions made in addition to the monthly contributions for active members, are made by local governing bodies on a pay-as-you-go basis for members who are pensioners when their respective departments merged with the System. There is no actuarial impact associated with this arrangement as the pay-as-you-go contributions made by these governing bodies are always equal to benefit payments paid by the System.

Contributions

The contribution requirement per active emergency services personnel members per month is not actuarially determined. Rather, the minimum contribution provisions were set by board rule, and there is no maximum contribution rate. For the fiscal year ending August 31, 2015, the total contributions (dues, prior service, and interest on prior service financing) of \$ 2,196 were paid into TESRS by the City.

The purpose of the biennial actuarial valuation is to determine if the contribution arrangement is adequate to pay the benefits that are promised. Actuarial assumptions are disclosed in subsection D below.

The actuarial valuation as of August 31, 2015 stated that TESRS has an adequate contribution arrangement for the benefit provisions recognized in the valuation based on the expected total contributions, including the expected contributions both from the governing body of each participating department and from the state. The expected contributions from the state are state appropriations equal to (1) the maximum annual contribution (one-third of all contributions to TESRS by governing bodies of participating departments in a year) as needed in accordance with state law governing TESRS and (2) approximately \$ 625,000 each year to pay for part of the System's administrative expenses. On August 31, 2015, the actuarial liabilities exceeded the actuarial assets by \$ 26,692,531 and \$ 14,877 for the System and the City.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 9 - DEFINED BENEFIT PENSION PLAN - TESRS - Continued

Net Pension Liability

The City's Net Pension Liability (NPL) was measured as of August 31, 2015, and the Total Pension Liability (TPL) used to calculate the Net Pension Liability was determined by an actuarial valuation as of that date.

Actuarial Assumptions - The Total Pension Liability in the August 31, 2015 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.50% per year
Salary increases	N/A
Investment Rate of Return	7.75%, net of pension plan investment expense, including inflation

Mortality rates were based on the RP-2000 Combined Healthy Lives Mortality Tables for males and for females projected to 2018 by scale AA.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which expected future net real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These components are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation (3.50%). In addition, the final 7.75% assumption reflected a reduction of 0.20% for adverse deviation. The target allocation and expected arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Net Rate of Return
Equities:		
Large cap domestic	32%	5.2%
Small cap domestic	10%	5.8%
Developed international	21%	5.5%
Emerging markets	6%	5.4%
Master limited partnerships	5%	7.1%
Fixed Income:		
Domestic	21%	1.4%
International	5%	1.6%
Cash	0%	0.0%
Total	100%	

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 9 - DEFINED BENEFIT PENSION PLAN - TESRS - Continued

Net Pension Liability - Continued

Discount Rate - The discount rate used to measure the total pension liability was 7.75%. No projection of cash flows was used to determine the discount rate because the August 31, 2014 actuarial valuation showed that expected contributions would pay the normal cost and amortize the unfunded actuarial accrued liability (UAAL) in 30 years using the conservative level dollar amortization method. That UAAL was based on an actuarial value of assets that was \$ 7.9 million less than the plan fiduciary net position as of August 31, 2014. Because of the 30-year amortization period with the conservative amortization method and with a lower value of assets, the pension plan's fiduciary net position is expected to be available to make all projected future benefit payments of current active and inactive members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Net Pension Liability to Changes in the Discount Rate - The following presents the net pension liability of the City, calculated using the discount rate of 7.75%, as well as what the City's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.75%) or 1 percentage point higher (8.75%) than the current rate:

	1% Decrease In Discount Rate (6.75%)	Discount Rate (7.75%)	1% Increase In Discount Rate (8.75%)
System's Net Pension Liability	\$ <u>46,704,033</u>	\$ <u>26,692,531</u>	\$ <u>15,160,925</u>
City's Net Pension Liability	\$ <u>27,377</u>	\$ <u>14,877</u>	\$ <u>7,673</u>

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Due to the insignificance of the amounts and the time required to make such calculations, the City has opted not to record the transactions required to implement GASB No. 68 for the TESRS Pension Plan to the current year financial statements.

NOTE 10 - POST-EMPLOYMENT HEALTH CARE PLAN

The City of Freeport maintains, through TML MultiState Intergovernmental Employee Benefits Pool (IEBP), a health risk pool established pursuant to Texas Local Government Code Chapter 172, Texas Government Code Chapter 791, and the Texas Trust Code to provide health care benefits coverage for employees and retirees and dependents of employees and retirees, of Texas political subdivisions under an interlocal agreement. The City is currently offering health benefits coverage through IEBP which allows the extension of benefits to retirees of the City. The City provides health benefits coverage to its retirees through IEBP and the cost of such coverage be paid for by the City to a maximum of \$ 750 per month; any additional amount will be the responsibility of the retiree. An employee who is under 60 years

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 10 - POST-EMPLOYMENT HEALTH CARE PLAN - Continued

of age and has been covered by TMRS (Texas Municipal Retirement System) for at least 20 years, or an employee who is 60 years or older and has been covered by TMRS for at least 5 years. The employee must also work for the City for a period of eight continuous years and meet the definition of retiree for purposes of the ordinance. The Interlocal Agreement in effect between the City and IEBP, adopted September 8, 2014, provides that the Board of Trustees may adopt rules and regulations which may amend this plan in the future. Other coverage's will be as established by the TML MultiState Intergovernmental Employee Benefits Pool Board of Trustees.

Funding Policy - The contribution requirements of the City are established by the City Council and may be amended at any time. For the years ended September 30, 2016 and 2015, the City contributed \$ 9,000 and 2,250, respectively.

Annual Other Post Employment Benefit (OPEB) Cost and Net OPEB Obligation - The City's annual other post-employment benefits (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with parameters established by GASB Statement 45. The ARC represents a level of accrual that, if paid on an ongoing basis, is projected to cover the normal costs each year and to amortize any unfunded actuarial liabilities (or funding excesses) over a period not to exceed thirty years. The City's annual OPEB cost for the fiscal year ended September 30, 2016 is as follows:

	<u>09-30-16</u>	<u>09-30-15</u>
Annual required contribution	\$ 47,977	\$ 32,952
Interest on net OPEB obligation	-0-	-0-
Adjustment to annual required contribution	<u>-0-</u>	<u>-0-</u>
Annual OPEB cost	47,977	32,952
Net estimated employer contributions	<u>(9,000)</u>	<u>(2,250)</u>
Increase in net OPEB obligation	38,977	30,702
Net OPEB obligation – beginning of year	<u>30,702</u>	<u>-0-</u>
Net OPEB obligation – end of year	<u>\$ 69,679</u>	<u>\$ 30,702</u>

The City's annual OPEB cost, the amount contributed by the employer, the percentage of annual OPEB costs contributed to the plan, and the net OPEB obligation for the fiscal year ended September 30, 2016 and the preceding year were as follows:

<u>Fiscal Year Ended</u>	<u>Annual OPEB Cost</u>	<u>Employer Amount Contributed</u>	<u>Percentage Contributed</u>	<u>Net OPEB Obligation</u>
September 30, 2015	\$ 32,952	\$ 2,250	6.8%	\$ 30,702
September 30, 2016	47,977	9,000	22.6%	69,679

CITY OF FREEPORT
Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 10 - POST-EMPLOYMENT HEALTH CARE PLAN - Continued

Funding Status – The funded status of the City’s retiree health care plan, under GASB Statement No. 45 as of December 31, 2015 is as follows:

Actuarial Valuation	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (d)	Ratio UAAL to Annual Covered (b-a)/d
Payroll Date as of						
September 30, 2015	\$ -0-	\$ 340,161	\$ 340,161	0%	\$4,976,675	0.068%
September 30, 2016	-0-	379,138	379,138	0%	5,501,315	0.069%

Under the reporting parameters, the City’s retiree health care plan is 0.0% funded with the actuarial accrued liability exceeding the actuarial assets by \$ 379,138 at December 31, 2015. As of the most recent valuation, the ratio of the unfunded actuarial liability to annual covered payroll is 0.069%.

Actuarial Methods and Assumptions – The Individual Entry Age Cost Method is used to calculate the GASB ARC for the City’s retiree health care plan. Using the plan benefits, the present health premiums and a set of actuarial assumptions, the anticipated future payments are projected. The actuarial cost method then provides for a systematic funding for these anticipated payments. The yearly ARC is computed to cover the cost of benefits being earned by covered members as well as to amortize a portion of the unfunded accrued liability.

Projections of health benefits are based on the plan as understood by the City and include the types of benefits in force at the valuation date and the pattern of sharing benefit costs between the City and the City’s employees to that point. Actuarial calculations reflect a long-term prospective and employ methods and assumptions that are designed to reduce short term volatility in actuarial accrued liabilities and the actuarial value of assets. Significant methods and assumptions were as follows:

Actuarial Methods and Assumptions

Inflation rate	2.50% per annum
Investment rate of return	4.25% per annum, net of expenses
Actuarial cost method	Individual Entry Age Normal Cost Method
Amortization method	Level as a percentage of employee payroll
Amortization period	30-year open amortization
Payroll growth	3.00% per annum
Medical Trend	The explicit subsidy provided by the City is Not assumed to increase in the future.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events in the future. Amounts determined regarding the funded status and the annual required contributions of the City’s retiree health care plan are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The required schedule of funding progress presented as required supplementary information provides multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 11 - INDUSTRIAL DISTRICT CONTRACTS

The City of Freeport in conjunction with the cities of Lake Jackson and Clute entered into an industrial contract with the Dow Chemical Company, BASF Corporation and LNG Corporation. A formula using Dow Chemical Company's, BASF Corporation's and LNG Corporation's assets determine how much the City of Freeport will receive each year. The amount received under this contract and various other industrial district contracts during the year ended September 30, 2016 was \$ 6,370,196 and is reported in the General Fund.

NOTE 12 - WATER SUPPLY CONTRACT

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

NOTE 13 - JOINT VENTURE

The City is party to an agreement with the City of Oyster Creek to share costs associated with the operation of a sewer treatment plant. The plant went on-line during the fiscal year ended September 30, 1989. The percentage for sharing the operating expenses is determined based upon meter flow calibrations. For the year ended September 30, 2016, the City of Freeport's portion of these expenses was not recognized, as the City of Oyster Creek has not determined the amount and currently that information is unavailable. Prior amounts have not been significant and its omission will not impair the financial statements. The City of Oyster Creek maintains both budgetary and accounting responsibility over these operations.

During the year ended September 30, 2003, the City began a joint venture with the City of Clute, City of Lake Jackson, and the SPCA for an animal shelter. The shelter is located in Lake Jackson and provides programs for the claiming and adoption of lost or abandoned animals for the three cities. The term of the agreement is from March 1, 2003 through February 28, 2023. The City and Clute contributed \$ 150,000 each and the SPCA contributed \$ 250,000 for a total of \$ 550,000 to Lake Jackson for the design, construction, and furnishing of the \$ 1,100,000 facility. The City pays each year for administrative operating costs. For the year ended September 30, 2016, the City paid \$ 110,218 for their portion of the operating costs.

NOTE 14 - LONG-TERM DEBT

General Obligation Bonded Debt

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

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 14 - LONG-TERM DEBT - Continued

General Obligation Bonded Debt - Continued

The general obligation bonds payable at September 30, 2016 are summarized as follows:

Purpose	Interest Rate (%)	Series Dates			Bonds Outstanding 09-30-16
		Issued	Maturity	Callable	
Certificate Obligation					
Bonds Series 2008	3.79%	2008	2023		\$ 1,795,000
Bonds Series 2003	4.84%	2003	2018	2014	781,000
Refunding Bonds					
Series 2003	4.84%	2003	2018	2014	<u>569,000</u>
					<u>\$ 3,145,000</u>

General obligation bond transactions for the year ended September 30, 2016 were as follows:

	<u>2016</u>
Bonds outstanding, October 1, 2015	\$ 3,774,000
Maturities	<u>(629,000)</u>
Bonds outstanding, September 30, 2016	<u>\$ 3,145,000</u>

Aggregate maturities of certificate of obligation bonds subsequent to September 30, 2016 are as follows:

<u>Year Ended September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 659,000	\$ 118,630	\$ 777,630
2018	689,000	88,476	777,476
2019	717,000	56,997	773,997
2020	255,000	36,100	291,100
2021	265,000	26,246	291,246
2022	275,000	16,013	291,013
2023	<u>285,000</u>	<u>5,400</u>	<u>290,400</u>
Total	<u>\$ 3,145,000</u>	<u>\$ 347,862</u>	<u>\$ 3,492,862</u>

Notes Payable

On November 21, 2014, the Freeport Economic Development Corporation (Corporation) refinanced the remaining First State Bank of Louise note balance of \$ 1,356,747 with the First State Bank of Clute. The loan is secured by the Corporation's sales tax remittance guaranty and subordination agreement. The note calls for an interest rate of 3.50% and one hundred and twenty-one (121) monthly payments of \$ 13,234 and one (1) payment on February 1, 2025 of \$ 4,491.41. Current requirements for principal and interest accounted for in the Debt Service Fund were \$ 118,414 and \$ 41,056, respectively.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 14 - LONG-TERM DEBT - Continued

Notes Payable – Continued

On September 4, 2015, the Freeport Economic Development Corporation (Corporation) financed the purchase of land from Western Seafood Company with a note payable of \$ 2,450,000. On the same date, the Corporation made an \$ 875,000 principal payment, bring the note balance to \$ 1,575,000. The loan is secured by the land. The remaining note calls for an interest rate of 3.00% and three (3) annual payments of \$ 525,000, with final payment on September 4, 2018. Current requirements for principal and interest accounted for in the Debt Service Fund were \$ 525,000 and \$ 47,250, respectively.

The notes payable at September 30, 2016 is summarized as follows:

Purpose	Interest Rate (%)	Series Dates			Bonds Outstanding 09-30-16
		Issued	Maturity	Callable	
Note Payable	3.50%	2014	2025		\$ 1,140,344
Note Payable	3.00%	2015	2018		<u>1,050,000</u>
					<u>\$ 2,190,344</u>

Note transactions for the year ended September 30, 2016 were as follows:

	2016
Notes outstanding, October 1, 2015	\$ 2,833,758
Maturities	<u>(643,414)</u>
Notes outstanding, September 30, 2016	<u>\$ 2,190,344</u>

Aggregate maturities of notes payable subsequent to September 30, 2016 are as follows:

Year Ended September 30,	Principal	Interest	Total
2017	\$ 643,547	\$ 71,761	\$ 715,308
2018	648,016	51,542	699,558
2019	127,653	31,155	158,808
2020	132,465	26,343	158,808
2021	137,458	21,350	158,808
2022	142,640	16,168	158,808
2023	148,017	10,791	158,808
2024	153,596	5,212	158,808
2025	<u>56,952</u>	<u>475</u>	<u>57,427</u>
Total	<u>\$ 2,190,344</u>	<u>\$ 234,797</u>	<u>\$ 2,425,141</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 14 - LONG-TERM DEBT - Continued

Changes in Long-Term Debt

Transactions for the year ended September 30, 2016 are summarized as follows:

	Balance 10-01-15	Issues or Additions	Payments or Expenditures	Balance 09-30-16	Due Within One Year
Governmental Type Activities:					
General obligation bonds	\$ 3,774,000	\$	\$ 629,000	\$ 3,145,000	\$ 659,000
Notes payable	2,833,758		643,414	2,190,344	643,547
Capital lease		387,548	82,090	305,458	73,045
Compensated absences	760,247	415,978	277,591	898,634	400,000
Net OPEB obligation	26,103	40,790	7,652	59,241	
TMRS net pension obligation	3,168,968	3,412,323	1,985,452	4,595,839	
TESRS net pension obligation		20,906	6,029	14,877	
Component of Long-Term Debt:					
Accrued interest payable	75,166	73,543	75,166	73,543	73,543
Total governmental activities	10,638,242	4,351,088	3,706,394	11,282,936	1,849,135
Business Type Activities:					
Capital leases	116,185	34,785	108,446	42,524	11,798
Compensated absences	89,089	100,502	54,809	134,782	47,000
Net OPEB obligation	4,599	7,187	1,348	10,438	
TMRS net pension obligation	558,400	601,231	349,824	809,807	
Component of Long-Term Debt:					
Accrued interest payable	203	28	203	28	28
Total business type activities	768,476	743,733	514,630	997,579	58,826
Total government (net)	\$ 11,406,718	\$ 5,094,821	\$ 4,221,024	\$ 12,280,515	\$ 1,907,961

Advance Refunding Debt Issuances and Defeased Debt

General Long-Term Debt:

During the year ended September 30, 2004, the City issued \$ 2,185,000 in Certificate of Obligation Refunding Bonds, Series 2003 for refunding of previously issued and outstanding \$ 2,135,000 Economic Development Corporation Certificate of Obligation Bonds – Series 2001. The City placed \$ 2,142,889 from the proceeds of the refunding in an escrow fund. The escrow fund is irrevocably pledged to the payment of principal and interest on the issue being refunded. The difference between the cash flow required to service the old debt and that required to service the new debt and complete the refunding was a decrease of \$ 216,580. The economic gain resulting from the transaction was \$ 252,180. The outstanding balance of these defeased bonds at September 30, 2016 was \$ 860,000 and the balance held in escrow was \$ 852,434.

CITY OF FREEPORT
Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 15 - LEASES

Operating leases

Lessor (Governmental)

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

Aggregate maturities of operating lease receivables subsequent to September 30, 2016 are as follows:

<u>Year Ended</u> <u>September 30,</u>	<u>Total</u>
2017	\$ <u>6,843</u>
Minimum payments under operating leases	\$ <u>6,843</u>

Operating lease and rental income for the year ended September 30, 2016 was as follows:

Office lease income	\$ 68,136
Other rental income	<u>79,012</u>
Total	\$ <u>147,148</u>

Lessee (Governmental)

During the year ended September 30, 2014, the City entered into an operating lease for a postage machine through June 30, 2019, which called for twenty quarterly payments of \$ 492.00.

During the year ended September 30, 2013 and 2015, the City entered into an operating lease agreements for copy machines, meters, and maintenance through October 31, 2019, which calls for monthly payments of \$ 96, \$ 388 and \$ 333 per month.

Aggregate maturities of operating lease obligations subsequent to September 30, 2016 are as follows:

<u>Year Ended</u> <u>September 30,</u>	<u>Total</u>
2017	\$ 11,773
2018	11,101
2019	10,129
2020	<u>721</u>
Minimum payments under operating leases	\$ <u>33,723</u>

Lease expense for the year ended September 30, 2016 was \$ 11,835.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 15 - LEASES - Continued

Lessee (Proprietary)

On December 21, 2014, the City's Golf Course Fund (enterprise fund) entered into an operating lease for a John Deere Top Dresser (greens machine) from December 1, 2014 through November 30, 2018, which calls for forty-eight (48) monthly payments of \$ 319.54

Aggregate maturities of operating lease obligations for the five years subsequent to September 30, 2015 are as follows:

<u>Year Ended</u> <u>September 30,</u>	<u>Total</u>
2016	\$ 3,835
2017	3,834
2018	3,835
2020	<u>639</u>
Minimum payments under operating leases	<u>\$ 12,143</u>

Lease expense for the year ended September 30, 2016 was \$ 3,834.

Capital Leases (Governmental)

During the year ended September 30, 2016, the City purchased a Case 621 F Wheel Loader for use in the Streets and Drainage Department under capital lease, with a cost of \$ 143,004 and an effective interest rate of 2.94%. Current requirements for principal and interest expenditures accounted for in the Streets and Drainage Department of the General Fund were \$ 30,291 and \$ 3,060, respectively.

During the year ended September 30, 2016, the City purchased a Gradall D152 2x4 for use in the Streets and Drainage Department under capital lease, with a cost of \$ 244,544 and an effective interest rate of 2.94%. Current requirements for principal and interest expenditures accounted for in the Streets and Drainage Department of the General Fund were \$ 51,800 and \$ 4,797, respectively.

The leased assets and related obligations are accounted for in the business-type activities column of the government wide financial statements as capital assets and noncurrent liabilities. Current year depreciation on leased assets totaled \$ 58,824 and has been included in depreciation expense.

The capital assets acquired through capital leases are as follows:

Asset:	
Machinery and equipment	\$ 387,548
Less accumulated depreciation	<u>58,824</u>
Total	<u>\$ 328,724</u>

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 15 - LEASES - Continued

Capital Leases (Governmental) - Continued

The following is a schedule of future minimum lease payments under capital leases, together with the net present value of the minimum lease payments, as of September 30, 2016:

<u>Year Ended</u> <u>September 30,</u>	<u>Amount</u>
2017	\$ 82,091
2018	82,091
2019	82,091
2020	<u>82,091</u>
	328,364
Less amount representing interest	<u>22,906</u>
Net present value of minimum lease payments	<u>\$ 305,458</u>

Capital Leases (Proprietary)

During the year ended September 30, 2012, the City purchased a John Deere precision cut fairway mower for \$ 39,678, under capital lease, with an effective interest rate of 4.67%. Current requirements for principal and interest expense accounted for in the Golf Course fund (Enterprise fund) were \$ 2,904 and \$ 11, respectively. This lease was paid in full on October 28, 2015.

During the year ended September 30, 2015, the City purchased a John Deere Top Dresser for \$ 14,200, under capital lease, with an effective interest rate of 4.00%. Current requirements for principal and interest expense accounted for in the Golf Course fund (Enterprise fund) were \$ 3,427 and \$ 408, respectively.

During the year ended September 30, 2013, the City purchased forty-five (45) Toyota golf cars for \$ 170,378, under capital lease, with an effective interest rate of 4.792%. This lease called for thirty-six monthly payments of \$ 3,330 with a \$ 67,500 balloon payment on March 15, 2016. Current requirements for principal and interest expense accounted for in the Golf Course fund (Enterprise fund) were \$ 12,125 and \$ 1,037, respectively. On March 15, 2016, the City exchanged the golf carts for the payoff balance of \$ 67,232 (\$ 67,500 less interest of \$ 268).

During the year ended September 30, 2013, the City purchased ten (10) Toyota golf cars for \$ 37,489, under capital lease, with an effective interest rate of 4.792%. This lease calls for thirty-six monthly payments of \$ 600 with a \$ 20,000 balloon payment on March 15, 2016. Current requirements for principal and interest expense accounted for in the Golf Course fund (Enterprise fund) were \$ 2,061 and \$ 295, respectively. On March 15, 2016, the City exchanged the golf carts for the payoff balance of \$ 19,920 (\$ 20,000 less interest of \$ 80).

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 15 - LEASES - Continued

Capital Leases (Proprietary) - Continued

During the year ended September 30, 2016, the City purchased a Toro GreensMaster (greens mower) 3150-Q w/attachments for \$ 34,785, under capital lease, with an effective interest rate of 3.59%. Current requirements for principal accounted for in the Golf Course fund (Enterprise fund) was \$ 777.

The leased assets and related obligations are accounted for in the business-type activities column of the government wide financial statements as capital assets and noncurrent liabilities. Current year depreciation on leased assets totaled \$ 31,724 and has been included in depreciation expense.

The capital assets acquired through capital leases are as follows:

Asset:

Machinery and equipment	\$ 48,985
Less accumulated depreciation	<u>2,029</u>
Total	<u>\$ 46,956</u>

The following is a schedule of future minimum lease payments under capital leases, together with the net present value of the minimum lease payments, as of September 30, 2016:

<u>Year Ended September 30,</u>	<u>Amount</u>
2017	\$ 13,155
2018	13,156
2019	10,600
2020	<u>8,544</u>
	45,455
Less amount representing interest	<u>2,931</u>
Net present value of minimum lease payments	<u>\$ 42,524</u>

NOTE 16 - RISK POOL PARTICIPATION

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

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 17 - GRANTS, ENTITLEMENTS AND SHARED REVENUES

During the year ended September 30, 2016, the City applied for and received federal grants related to various activities. The operations of these grants are reported in the General fund, the Streets, Drainage and Sidewalk (special revenue fund), and the Water and Sewer (enterprise fund). For the most part, these grants are reimbursement type grants, therefore, revenues equal expenditures. Grant revenues are classified as intergovernmental revenues and capital contributions. The federal grants are covered by the requirements of the Single Audit Act and Uniform Guidance. The state grants are covered by the State of Texas Single Audit Circular. Since the total federal state revenues exceed \$ 750,000, a Single Audit was required.

NOTE 18 - DEFICIT NET POSITION

The following funds reported a net position deficit as of September 30, 2016:

Golf Course (enterprise fund)	\$	343,640
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Deficit balances will either be offset by future revenues or reimbursed by the General Fund.

NOTE 19 - EXPENDITURES IN EXCESS OF APPROPRIATIONS

Expenditures exceeded appropriations for the year ended September 30, 2015 for the following funds:

Special Revenue Funds:		
Hotel/Motel	\$	250
Economic Development		130,671
Beach Maintenance		12,931
Debt Service Funds:		
Series 2003B		222
Series 2008		4,169
EDC Note		690

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

NOTE 20 - EVALUATION OF SUBSEQUENT EVENTS

The City has evaluated subsequent events through February 24, 2017, the date which the financial statements were available to be issued.

NOTE 21 - LITIGATION AND CONTINGENCIES

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. During fiscal year 2016, the City obtained insurance to cover general liabilities. There were no significant reductions in coverage in the past fiscal year, and there were no settlements exceeding insurance coverage for each of the past three fiscal years.

CITY OF FREEPORT

Freeport, Texas

NOTES TO THE FINANCIAL STATEMENTS

For The Year Ended September 30, 2016

NOTE 21 - LITIGATION AND CONTINGENCIES - Continued

The City participates in numerous state and Federal grant programs, which are governed by various rules and regulations of the grantor agencies. Costs charged to the respective grant programs are subject to audit and adjustment by the grantor agencies; therefore, to the extent that the City has not complied with the rules and regulations governing the grants, if any, refunds of any money received may be required and the collectability of any related receivable at September 30, 2016 may be impaired. In the opinion of the City, there are no significant contingent liabilities relating to compliance with the rules and regulations governing the respective grants; therefore, no provision has been recorded in the accompanying combined financial statements for such contingencies.

NOTE 22 - ECONOMIC DEVELOPMENT AGREEMENTS

On June 2, 2014 the City entered into an Economic Development Agreement with Headway Estate, LTD, Sunlake Limited and Skymark Development Company, collectively (the Developer) in accordance with Chapter 380 of the Texas Local Government Code. Under terms of the agreement, the Developer, who owns 343.254 acres of land located within the corporate City limits, will construct water, sewer, drainage and road improvements on the property which will be developed within a five-year period from the date of receiving applicable governmental and Union Pacific approvals. As certain sections of the development are completed the Developer will convey at no cost to the City the improvements which include the water, sewer, drainage and street improvements. The City is expected to make a payment to the Developer from new development created tax revenue once received each year in reimbursement of funds spent by the Developer. The development payments made by the city shall not exceed \$ 7.5 Million for rail improvements, \$ 1.6 million for street improvements, and \$ 900 thousand for fire water supply plant and fire loop. Both the City and the Developer have agreed to various covenants, warranties, obligations and duties as a part of this agreement. No funds have been expended by the City in regards to this agreement for the year ended September 30, 2016.

On June 19, 2014, the City entered into an Economic Development Agreement with BrazTex Development, LLC (the Developer) in accordance with Chapter 380 of the Texas Local Government Code. Under terms of the agreement, the Developer owns 1.6 acres of land within the City limits and will construct 16 single family homes on the property. The City agrees to provide the Developer with a rebate of City ad valorem taxes not to exceed \$ 215,675. The rebate will be paid in annual installments equal in amount to the ad valorem taxes collected each year by the City from the previously described property improvements.

During the year ended September 30, 2016, the City satisfied \$ 93,157 of its liability under the agreement (\$ 21,000 for 1.425 acres of land, \$ 21,270 for water and sewer improvements, \$ 8,887 in property tax collections, and \$ 42,000 for 0.741 acres of land). Therefore, the remaining amount to be provided to the Developer at September 30, 2016 was \$ 122,518.

REQUIRED SUPPLEMENTARY INFORMATION

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CITY OF FREEPORT

Freeport, Texas

Exhibit E-1

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES - BUDGET AND ACTUAL
GENERAL FUND**

For the Year Ended September 30, 2016

	General Fund			
	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Property taxes	\$ 2,041,326	\$ 2,041,326	\$ 2,096,452	\$ 55,126
Other taxes	2,578,176	2,578,176	2,821,956	243,780
Industrial district	6,714,870	6,714,870	6,370,196	(344,674)
Intergovernmental	52,000	446,264	345,812	(100,452)
Revenue producing facilities	1,057,103	1,057,103	1,075,084	17,981
Fines, licenses and fees	409,926	409,926	615,826	205,900
Investment income	3,500	3,500	30,089	26,589
Miscellaneous	229,221	322,133	129,035	(193,098)
Total revenues	<u>13,086,122</u>	<u>13,573,298</u>	<u>13,484,450</u>	<u>(88,848)</u>
Expenditures:				
Current:				
General government and administration	1,557,799	1,837,799	2,146,337	(308,538)
Public safety	5,537,098	6,095,143	5,940,988	154,155
Streets and drainage	3,799,424	3,908,092	2,008,648	1,899,444
Sanitation	847,500	847,500	914,275	(66,775)
Service center	210,919	210,919	171,530	39,389
Library	43,192	43,192	18,933	24,259
Parks and recreation	1,868,835	2,074,977	1,977,510	97,467
Debt Service:				
Principal	84,159	84,159	82,090	2,069
Interest and fees	2,569	2,569		2,569
Total expenditures	<u>13,951,495</u>	<u>15,104,350</u>	<u>13,260,311</u>	<u>1,844,039</u>
Excess of revenues over (under) expenditures	<u>(865,373)</u>	<u>(1,531,052)</u>	<u>224,139</u>	<u>1,755,191</u>
Other Financing Sources (Uses):				
Sale of capital assets	5,000	51,022	42,000	(9,022)
Proceeds from issuance of capital leases			387,548	
Transfers out	<u>(1,050,659)</u>	<u>(1,050,659)</u>	<u>(1,068,659)</u>	<u>(18,000)</u>
Total other financing sources (uses)	<u>(1,045,659)</u>	<u>(999,637)</u>	<u>(639,111)</u>	<u>(27,022)</u>
Net change in fund balance	<u>(1,911,032)</u>	<u>(2,530,689)</u>	<u>(414,972)</u>	<u>1,728,169</u>
Fund balance - beginning	<u>9,744,776</u>	<u>9,744,776</u>	<u>9,744,776</u>	<u>-0-</u>
Fund balance - ending	<u>\$ 7,833,744</u>	<u>\$ 7,214,087</u>	<u>\$ 9,329,804</u>	<u>\$ 1,728,169</u>

**SCHEDULE OF TMRS CONTRIBUTIONS
FOR THE LAST TEN YEARS (1)
September 30, 2016 with Measurement Date of December 31, 2015**

	<u>2016</u>	<u>2015</u>
Actuarially determined contribution	\$ 699,079	\$ 677,622
Contributions in relation to the actuarially determined contribution	<u>699,079</u>	<u>677,622</u>
Contribution deficiency (excess)	<u>\$ -0-</u>	<u>\$ -0-</u>
Covered-employee payroll	<u>\$ 5,501,315</u>	<u>\$ 4,976,675</u>
Contributions as a percentage of covered-employee payroll	12.71%	13.62%

Notes to Schedule of TMRS Contributions

Valuation date

Notes Actuarially determined contribution rates are calculated as of December 31 and become effective in January, 13 months later.

Methods and Assumptions Used to Determine Contribution Rates:

Actuarial cost method	Entry age normal
Amortization method	Level Percentage of Payroll, Closed
Remaining Amortization period	30 years
Asset valuation method	10 Year smoothed market; 15% soft corridor
Inflation	2.5%
Salary increases	3.50% to 10.50% including inflation
Investment rate of return	6.75%
Retirement Age	Experience-based table of rates that are specific to the City's plan of benefits. Last updated for the 2015 valuation pursuant to an experience study of the period 2010 – 2014.
Mortality	RP2000 Combined Mortality Table with Blue Collar Adjustment with male rates multiplied by 109% and female rates multiplied by 103% and projected on a fully generated basis with scale BB

Other Information

Notes There were no benefit changes during the year.

(1) The first TMRS actuarial report was completed for the year ended December 31, 2014 (measurement date), therefore, only two years of required supplemental information are available.

CITY OF FREEPORT

Freeport, Texas

Exhibit E-3

**SCHEDULE OF TMRS CHANGES IN NET PENSION LIABILITY AND RELATED RATIOS
FOR THE LAST TEN YEARS (1)**

September 30, 2016 with Measurement Date of December 31, 2015

	<u>2016</u>	<u>2015</u>
Service cost	\$ 867,502	\$ 749,370
Interest (on the Total Pension Liability)	1,511,254	1,424,774
Changes in benefit terms		
Difference between expected and actual experience	276,833	(132,087)
Changes in assumptions	116,881	
Benefit payments, including refunds of employee contributions	<u>(874,894)</u>	<u>(856,501)</u>
Net Change in Total Pension Liability	1,897,576	1,185,556
Total Pension Liability – Beginning (2)	<u>21,593,032</u>	<u>20,407,476</u>
Total Pension Liability – Ending (a)	<u>\$ 23,490,608</u>	<u>\$ 21,593,032</u>
Contributions - employer	\$ 699,079	\$ 600,889
Contributions - employees	385,600	348,367
Net Investment Income	26,362	962,281
Benefit payments, including refunds of employee contributions	(874,894)	(856,501)
Administrative expense	(16,057)	(10,047)
Other	<u>(792)</u>	<u>(826)</u>
Net Change in Plan Fiduciary Net Position	219,298	1,044,163
Plan Fiduciary Net Position – Beginning	<u>17,865,664</u>	<u>16,821,501</u>
Plan Fiduciary Net Position – Ending (b)	<u>\$ 18,084,962</u>	<u>\$ 17,865,664</u>
Net Pension Liability (a-b)	<u>\$ 5,405,646</u>	<u>\$ 3,727,368</u>
Plan Fiduciary Net Position as a Percentage of Total Pension Liability	<u>76.99%</u>	<u>82.74%</u>
Covered Employee Payroll	<u>\$ 5,501,315</u>	<u>\$ 4,976,675</u>
Net Pension Liability as a Percentage of Covered Employee Payroll	<u>98.26%</u>	<u>74.90%</u>

Notes to Schedule:

- (1) This schedule is presented to illustrate the requirement to show information for ten years. However, until a full ten-year trend is compiled, only available information is shown.
- (2) Determined from the end of year total pension liability using the roll back procedure allowed for the initial year of implementing GASB 67.

CITY OF FREEPORT

Freeport, Texas

Exhibit E-4

**SCHEDULE OF TESRS CHANGES IN NET PENSION LIABILITY AND RELATED RATIOS
FOR THE LAST TEN YEARS (1)**

September 30, 2016 with Measurement Date of August 31, 2015

	<u>2016</u>	<u>2015</u>
Service cost	\$ 1,058	\$ 961
Interest (on the Total Pension Liability)	5,291	4,233
Benefit payments, including refunds of employee contributions	<u>(2,810)</u>	<u>(2,192)</u>
Net Change in Total Pension Liability	3,539	3,002
Total Pension Liability – Beginning (2)	<u>57,759</u>	<u>54,757</u>
Total Pension Liability – Ending (a)	<u>\$ 61,298</u>	<u>\$ 57,759</u>
Contributions - employer	\$ 2,196	\$ 2,196
Contributions - state	1,023	805
Net Investment Income	(2,057)	6,261
Benefit payments	(2,810)	(2,192)
Administrative expense	(135)	(87)
Other	<u>(1)</u>	<u> </u>
Net Change in Plan Fiduciary Net Position	(1,784)	6,983
Plan Fiduciary Net Position – Beginning	<u>48,205</u>	<u>41,222</u>
Plan Fiduciary Net Position – Ending (b)	<u>\$ 46,421</u>	<u>\$ 48,205</u>
Net Pension Liability (a-b)	<u>\$ 14,877</u>	<u>\$ 9,554</u>
Plan Fiduciary Net Position as a Percentage of Total Pension Liability	<u>75.73%</u>	<u>83.46%</u>
Number of Active Members (3)	<u>5</u>	<u>5</u>
City's Net Pension Liability per Active Member	<u>\$ 2,975</u>	<u>\$ 1,910</u>

Notes to Schedule:

- (1) This schedule is presented to illustrate the requirement to show information for ten years. However, until a full ten-year trend is compiled, only available information is shown.
- (2) Determined from the end of year total pension liability using the roll back procedure allowed for the initial year of implementing GASB 67.
- (3) There is no compensation for active members, so number of active members is used instead.

CITY OF FREEPORT

Freeport, Texas

Exhibit E-5

**SCHEDULE OF TESRS INVESTMENT RETURNS
FOR THE LAST TEN YEARS (1)**

September 30, 2016 with Measurement Date of August 31, 2015

<u>Fiscal Year Ending</u>	<u>Annual Money-Weighted Net Real Rate of Return (2)</u>
August 31, 2013	13.84%
August 31, 2014	14.92%
August 31, 2015	(3.58%)

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Notes to Schedule:

- (1) This schedule is presented to illustrate the requirement to show information for ten years. However, until a full ten-year trend is compiled, only available information is shown.
- (2) The money-weighted rate of return expresses investment performance, net of investment expenses, reflecting changing amounts actually invested during the year.

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OTHER SCHEDULES

CITY OF FREEPORT

Freeport, Texas

COMBINING BALANCE SHEET- NONMAJOR GOVERNMENTAL FUNDS

September 30, 2016

	Special Revenue Funds			
	Hotel/ Motel Tax	Economic Development Corporation	Beach Maintenance	Total
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES				
Assets:				
Cash and temporary investments	\$ 13,354	\$ 129,296	\$ 888	\$ 143,538
Receivables (Net of Allowance for Uncollectable):				
Property taxes				-0-
Sales taxes		177,371		177,371
Accounts	3,560			3,560
Due from other governments				-0-
Due from other funds				-0-
Total assets	16,914	306,667	888	324,469
Deferred Outflows of Resources:				
Total deferred outflows of resources				-0-
Total assets and deferred outflows of resources	\$ 16,914	\$ 306,667	\$ 888	\$ 324,469
LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCE				
Liabilities:				
Accounts payable	\$	\$ 41,432	\$ 16	\$ 41,448
Accrued wages and benefits		2,442	120	2,562
Due to other funds		13,871		13,871
Total liabilities	-0-	57,745	136	57,881
Deferred Inflows of Resources:				
Deferred inflows of resources – property taxes				-0-
Total deferred inflows of resources	-0-	-0-	-0-	-0-
Fund Balances:				
Restricted:				
Economic development	16,914	248,922		265,836
Debt Service				-0-
Construction				-0-
Assigned:				
Beach maintenance			752	752
Total fund balances	16,914	248,922	752	266,588
Total liabilities, deferred inflows of resources and fund balances	\$ 16,914	\$ 306,667	\$ 888	\$ 324,469

Debt Service Funds					Capital Projects Fund	Total Nonmajor Governmental Funds
Debt Service Series 2003A	Debt Service Series 2003B	Debt Service Series 2008	Debt Service EDC Note	Total	2008 Bond Construction	
\$ 10,551	\$ 19,747	\$ 10,511	\$	\$ 40,809	\$ 1,706	\$ 186,053
	10,239	10,404		20,643		20,643
				-0-		177,371
				-0-		3,560
	303	322		625		625
<u>13,871</u>	<u>7,754</u>	<u>42,247</u>		<u>63,872</u>	<u>52,323</u>	<u>116,195</u>
24,422	38,043	63,484	-0-	125,949	54,029	504,447
				-0-		-0-
<u>\$ 24,422</u>	<u>\$ 38,043</u>	<u>\$ 63,484</u>	<u>\$ -0-</u>	<u>\$ 125,949</u>	<u>\$ 54,029</u>	<u>\$ 504,447</u>
\$	\$	\$	\$	\$	\$ -0-	\$ 41,448
					-0-	2,562
<u>300</u>				<u>300</u>		<u>14,171</u>
<u>300</u>	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>	<u>300</u>		<u>58,181</u>
	<u>9,236</u>	<u>9,356</u>		<u>18,592</u>		<u>18,592</u>
<u>-0-</u>	<u>9,236</u>	<u>9,356</u>	<u>-0-</u>	<u>18,592</u>	<u>-0-</u>	<u>18,592</u>
				-0-		265,836
24,122	28,807	54,128		107,057		107,057
				-0-	54,029	54,029
				-0-		752
<u>24,122</u>	<u>28,807</u>	<u>54,128</u>	<u>-0-</u>	<u>107,057</u>	<u>54,029</u>	<u>427,674</u>
<u>\$ 24,422</u>	<u>\$ 38,043</u>	<u>\$ 63,484</u>	<u>\$ -0-</u>	<u>\$ 125,949</u>	<u>\$ 54,029</u>	<u>\$ 504,447</u>

CITY OF FREEPORT

Freeport, Texas

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

For the Year Ended September 30, 2016

	Special Revenue Funds			
	Hotel/ Motel Tax	Economic Development Corporation	Beach Maintenance	Total
Revenues:				
Property taxes	\$	\$	\$	\$ -0-
Sales taxes		1,058,441		1,058,441
Hotel-motel tax	16,510			16,510
Interest income	13	615		628
Miscellaneous		2,077		2,077
Total revenues	<u>16,523</u>	<u>1,061,133</u>	<u>-0-</u>	<u>1,077,656</u>
Expenditures:				
Current:				
Economic development	11,500	287,166		298,666
Parks and recreation			15,731	15,731
Capital outlay		2,810		2,810
Debt Service:				
Principal		525,000		525,000
Interest		47,250		47,250
Total expenditures	<u>11,500</u>	<u>862,226</u>	<u>15,731</u>	<u>889,457</u>
Excess of revenues over (under) expenditures	<u>5,023</u>	<u>198,907</u>	<u>(15,731)</u>	<u>188,199</u>
Other Financing Sources (Uses):				
Transfers in				-0-
Transfers out		(377,071)		(377,071)
Total other financing sources (uses)	<u>-0-</u>	<u>(377,071)</u>	<u>-0-</u>	<u>(377,071)</u>
Net changes in fund balance	5,023	(178,164)	(15,731)	(188,872)
Fund balance - beginning	11,891	427,086	16,483	455,460
Fund balance - ending	<u>\$ 16,914</u>	<u>\$ 248,922</u>	<u>\$ 752</u>	<u>\$ 266,588</u>

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Debt Service Funds					Capital Projects Fund	Total Nonmajor Governmental Funds
Debt Service Series 2003A	Debt Service Series 2003B	Debt Service Series 2008	Debt Service EDC Note	Total	2008 Bond Construction	
\$	\$ 304,175	\$ 315,578	\$	\$ 619,753	\$	\$ 619,753
				-0-		1,058,441
				-0-		16,510
29	6	33		68		696
				-0-		2,077
<u>29</u>	<u>304,181</u>	<u>315,611</u>	<u>-0-</u>	<u>619,821</u>	<u>-0-</u>	<u>1,697,477</u>
				-0-		298,666
				-0-		15,731
				-0-		2,810
172,000	237,000	220,000	118,414	747,414		1,272,414
<u>31,730</u>	<u>44,058</u>	<u>76,668</u>	<u>41,056</u>	<u>193,512</u>		<u>240,762</u>
<u>203,730</u>	<u>281,058</u>	<u>296,668</u>	<u>159,470</u>	<u>940,926</u>	<u>-0-</u>	<u>1,830,383</u>
<u>(203,701)</u>	<u>23,123</u>	<u>18,943</u>	<u>(159,470)</u>	<u>(321,105)</u>	<u>-0-</u>	<u>(132,906)</u>
217,601	18,000		159,470	395,071		395,071
				-0-		(377,071)
<u>217,601</u>	<u>18,000</u>	<u>-0-</u>	<u>159,470</u>	<u>395,071</u>	<u>-0-</u>	<u>18,000</u>
13,900	41,123	18,943	-0-	73,966	-0-	(114,906)
<u>10,222</u>	<u>(12,316)</u>	<u>35,185</u>		<u>33,091</u>	<u>54,029</u>	<u>542,580</u>
<u>\$ 24,122</u>	<u>\$ 28,807</u>	<u>\$ 54,128</u>	<u>\$ -0-</u>	<u>\$ 107,057</u>	<u>\$ 54,029</u>	<u>\$ 427,674</u>

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CITY OF FREEPORT

Freeport, Texas

Exhibit F-3

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

For the Year Ended September 30, 2016

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Hotel-motel taxes	\$ 14,500	\$ 14,500	\$ 16,510	\$ 2,010
Investment income			13	13
Total revenues	<u>14,500</u>	<u>14,500</u>	<u>16,523</u>	<u>2,023</u>
Expenditures:				
Current:				
Economic development	<u>11,250</u>	<u>11,250</u>	<u>11,500</u>	<u>(250)</u>
Total expenditures	<u>11,250</u>	<u>11,250</u>	<u>11,500</u>	<u>(250)</u>
Excess of revenues over expenditures	<u>3,250</u>	<u>3,250</u>	<u>5,023</u>	<u>1,773</u>
Other Financing Sources (Uses):				
Total other financing sources (uses)				<u>-0-</u>
Net change in fund balance	3,250	3,250	5,023	1,773
Fund balance - beginning	<u>11,891</u>	<u>11,891</u>	<u>11,891</u>	<u>-0-</u>
Fund balance - ending	<u>\$ 15,141</u>	<u>\$ 15,141</u>	<u>\$ 16,914</u>	<u>\$ 1,773</u>

CITY OF FREEPORT

Freeport, Texas

Exhibit F-4

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES - BUDGET AND ACTUAL
ECONOMIC DEVELOPMENT SPECIAL REVENUE FUND**

For the Year Ended September 30, 2016

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Sales taxes	\$	\$ 1,020,000	\$ 1,058,441	\$ 38,441
Investment income		150	615	465
Miscellaneous		200	2,077	1,877
Total revenues	-0-	1,020,350	1,061,133	40,783
Expenditures:				
Current:				
Economic development		131,555	287,166	(155,611)
Capital outlay			2,810	(2,810)
Debt Service:				
Principal		525,000	525,000	-0-
Interest and fees		75,000	47,250	27,750
Total expenditures	-0-	731,555	862,226	(130,671)
Excess of revenues over (under) expenditures	-0-	288,795	198,907	(89,888)
Other Financing Sources (Uses):				
Transfers out		(362,510)	(377,071)	(14,561)
Total other financing sources (uses)	-0-	(362,510)	(377,071)	(14,561)
Net change in fund balance	-0-	(73,715)	(178,164)	(104,449)
Fund balance - beginning	427,086	427,086	427,086	-0-
Fund balance - ending	\$ 427,086	\$ 353,371	\$ 248,922	\$(104,449)

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CITY OF FREEPORT

Freeport, Texas

Exhibit F-5

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

For the Year Ended September 30, 2016

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Revenue producing facilities	\$ 15,000	\$ 15,000	\$ -	\$(15,000)
Total revenues	<u>15,000</u>	<u>15,000</u>	<u>-0-</u>	<u>(15,000)</u>
Expenditures:				
Parks and recreation	<u>2,800</u>	<u>2,800</u>	<u>15,731</u>	<u>(12,931)</u>
Total expenditures	<u>2,800</u>	<u>2,800</u>	<u>15,731</u>	<u>(12,931)</u>
Excess of revenues over expenditures	<u>12,200</u>	<u>12,200</u>	<u>(15,731)</u>	<u>(27,931)</u>
Other Financing Sources (Uses):				
Total other financing sources (uses)				<u>-0-</u>
Net change in fund balance	<u>12,200</u>	<u>12,200</u>	<u>(15,731)</u>	<u>(27,931)</u>
Fund balance - beginning	<u>16,483</u>	<u>16,483</u>	<u>16,483</u>	<u>-0-</u>
Fund balance - ending	<u>\$ 28,683</u>	<u>\$ 28,683</u>	<u>\$ 752</u>	<u>\$(27,931)</u>

CITY OF FREEPORT

Freeport, Texas

Exhibit F-6

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

For the Year Ended September 30, 2016

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Investment income	\$	\$	29	29
Total revenues	-0-	-0-	29	29
Expenditures:				
Debt Service:				
Principal		172,000	172,000	-0-
Interest		31,730	31,730	-0-
Total expenditures	-0-	203,730	203,730	-0-
Excess of revenues over (under) expenditures	-0-	(203,730)	(203,701)	29
Other Financing Sources (Uses):				
Transfers in		203,730	217,601	13,871
Total other financing sources (uses)	-0-	203,730	217,601	13,871
Net change in fund balance	-0-	-0-	13,900	13,900
Fund balance - beginning	10,222	10,222	10,222	-0-
Fund balance - ending	\$ 10,222	\$ 10,222	\$ 24,122	\$ 13,900

CITY OF FREEPORT

Freeport, Texas

Exhibit F-7

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

For the Year Ended September 30, 2016

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Property taxes	\$ 280,836	\$ 280,836	\$ 304,175	\$ 23,339
Investment income			6	6
Total revenues	<u>280,836</u>	<u>280,836</u>	<u>304,181</u>	<u>23,345</u>
Expenditures:				
Debt Service:				
Principal	237,000	237,000	237,000	-0-
Interest	43,836	43,836	44,058	(222)
Total expenditures	<u>280,836</u>	<u>280,836</u>	<u>281,058</u>	<u>(222)</u>
Excess of revenues over (under) expenditures	<u>-0-</u>	<u>-0-</u>	<u>23,123</u>	<u>23,123</u>
Other Financing Sources (Uses):				
Transfer in			18,000	18,000
Total other financing sources (uses)	<u>-0-</u>	<u>-0-</u>	<u>18,000</u>	<u>18,000</u>
Net change in fund balance	<u>-0-</u>	<u>-0-</u>	<u>41,123</u>	<u>41,123</u>
Fund balance - beginning	<u>(12,316)</u>	<u>(12,316)</u>	<u>(12,316)</u>	<u>-0-</u>
Fund balance - ending	<u><u>\$(12,316)</u></u>	<u><u>\$(12,316)</u></u>	<u><u>\$28,807</u></u>	<u><u>\$41,123</u></u>

CITY OF FREEPORT

Freeport, Texas

Exhibit F-8

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

For the Year Ended September 30, 2016

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues:				
Taxes	\$ 292,499	\$ 292,499	\$ 315,578	\$ 23,079
Investment income			33	33
Total revenues	<u>292,499</u>	<u>292,499</u>	<u>315,611</u>	<u>23,112</u>
Expenditures:				
Debt Service:				
Principal	220,000	220,000	220,000	-0-
Interest	<u>72,499</u>	<u>72,499</u>	<u>76,668</u>	<u>(4,169)</u>
Total expenditures	<u>292,499</u>	<u>292,499</u>	<u>296,668</u>	<u>(4,169)</u>
Excess of revenues over (under) expenditures	<u>-0-</u>	<u>-0-</u>	<u>18,943</u>	<u>18,943</u>
Other Financing Sources (Uses):				
Total other financing sources (uses)				<u>-0-</u>
Net change in fund balance	-0-	-0-	18,943	18,943
Fund balance - beginning	<u>35,185</u>	<u>35,185</u>	<u>35,185</u>	<u>-0-</u>
Fund balance - ending	<u>\$ 35,185</u>	<u>\$ 35,185</u>	<u>\$ 54,128</u>	<u>\$ 18,943</u>

CITY OF FREEPORT

Freeport, Texas

Exhibit F-9

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

For the Year Ended September 30, 2016

	<u>Budgeted Amounts</u>		<u>Actual</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Revenues:				
Total revenues	\$ -0-	\$ -0-	\$ -0-	\$ -0-
Expenditures:				
Debt Service:				
Principal		115,511	118,414	(2,903)
Interest		43,269	41,056	2,213
Total expenditures	-0-	158,780	159,470	(690)
Excess of revenues over (under) expenditures	-0-	(158,780)	(159,470)	(690)
Other Financing Sources (Uses):				
Transfers in		158,780	159,470	690
Total other financing sources (uses)	-0-	158,780	159,470	690
Net change in fund balance	-0-	-0-	-0-	-0-
Fund balance - beginning				-0-
Fund balance - ending	\$ -0-	\$ -0-	\$ -0-	\$ -0-

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FINAL

CITY OF FREEPORT

Freeport, Texas

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

For the Year Ended September 30, 2016

	Budgeted Amounts		Actual GAAP Basis	Adjustments to Budgetary Basis
	Original	Final		
Operating Revenues:				
Water service	\$ 2,772,766	\$ 2,772,766	\$ 3,032,832	\$
Sewer service	1,687,058	1,687,058	1,793,976	
Charges for other services	84,900	84,900	283,940	
Miscellaneous	24,300	57,653		
Total operating revenues	4,569,024	4,602,377	5,110,748	-0-
Operating Expenses:				
Personnel services	85,778	85,778	80,194	
Employee benefits	33,406	33,406	38,486	
Contract and professional services	2,388,585	2,727,487	2,827,153	
Other operating costs	58,498	58,498	52,827	
Supplies	26,300	26,300	35,432	
Cost of sales	1,949,900	1,919,900	2,199,757	
Operating expenses before depreciation	4,512,467	4,851,369	5,233,849	-0-
Depreciation			315,381	(315,381)
Total operating expenses	4,512,467	4,851,369	5,549,230	(315,381)
Net operating income (loss)	56,557	(248,992)	(438,482)	315,381
Non-Operating Revenues (Expenses):				
Interest revenue			1,342	
Capital outlay	(677,450)	(677,450)		(463,800)
Total non-operating revenues (expenses)	(677,450)	(677,450)	1,342	(463,800)
Net income (loss) before contributions and operating transfers	(620,893)	(926,442)	(437,140)	(148,419)
Contributions (capital)			1,184,220	(1,184,220)
Transfers in	620,893	620,893	620,893	-0-
Change in net position	\$ -0-	\$ (305,549)	\$ 1,367,973	\$ (1,332,639)

Actual Budgetary Basis	Variance on Final Budget - Positive (Negative)
\$ 3,032,832	\$ 260,066
1,793,976	106,918
283,940	199,040
<u> </u>	<u>(57,653)</u>
<u>5,110,748</u>	<u>508,371</u>
80,194	5,584
38,486	(5,080)
2,827,153	(99,666)
52,827	5,671
35,432	(9,132)
<u>2,199,757</u>	<u>(279,857)</u>
5,233,849	(382,480)
<u> </u>	<u>-0-</u>
<u>5,233,849</u>	<u>(382,480)</u>
<u>(123,101)</u>	<u>125,891</u>
1,342	1,342
<u>(463,800)</u>	<u>213,650</u>
<u>(462,458)</u>	<u>214,992</u>
(585,559)	340,883
<u>620,893</u>	<u>-0-</u>
<u>\$ 35,334</u>	<u>\$ 340,883</u>

FINAL

CITY OF FREEPORT

Freeport, Texas

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

For the Year Ended September 30, 2016

	Budgeted Amounts		Actual GAAP Basis	Adjustments to Budgetary Basis
	Original	Final		
Operating Revenues:				
Golf course fees and charges	\$ 585,000	\$ 585,000	\$ 344,278	\$
Intergovernmental charges			6,412	
Total operating revenues	<u>585,000</u>	<u>585,000</u>	<u>350,690</u>	<u>-0-</u>
Operating Expenses:				
Personnel services	393,824	393,824	386,868	
Employee benefits	148,320	148,320	182,018	
Contract and professional services	81,950	81,950	95,706	
Supplies	53,750	53,750	78,751	
Cost of sales and services	129,660	129,660	134,710	
Operating expenses before depreciation	<u>807,504</u>	<u>807,504</u>	<u>878,053</u>	<u>-0-</u>
Depreciation			93,195	(93,195)
Total operating expenses	<u>807,504</u>	<u>807,504</u>	<u>971,248</u>	<u>(93,195)</u>
Net operating income (loss)	<u>(222,504)</u>	<u>(222,504)</u>	<u>(620,558)</u>	<u>93,195</u>
Non-Operating Revenues (Expenses):				
Interest revenue			507	
Loss on sale of capital assets			(16,782)	16,782
Capital outlay	(114,350)	(114,350)		(110,181)
Lease principal	(13,962)	(13,962)		(61,719)
Interest expense and agent fees			(2,146)	
Total non-operating revenues (expenses)	<u>(128,312)</u>	<u>(128,312)</u>	<u>(18,421)</u>	<u>(155,118)</u>
Net income (loss) before operating transfers	<u>(350,816)</u>	<u>(350,816)</u>	<u>(638,979)</u>	<u>(61,923)</u>
Transfers in (out)	<u>350,816</u>	<u>350,816</u>	<u>350,816</u>	
Change in net position	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$(288,163)</u>	<u>\$(61,923)</u>

Actual Budgetary Basis	Variance on Final Budget - Positive (Negative)
\$ 344,278	\$(240,722)
6,412	6,412
350,690	(234,310)
386,868	6,956
182,018	(33,698)
95,706	(13,756)
78,751	(25,001)
134,710	(5,050)
878,053	(70,549)
878,053	-0-
(527,363)	(304,859)
507	507
(110,181)	4,169
(61,719)	(47,757)
(2,146)	2,146
(173,539)	(40,935)
(700,902)	(345,794)
350,816	-0-
\$(350,086)	\$(345,794)

FINAL

CITY OF FREEPORT

Freeport, Texas

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

For the Year Ended September 30, 2016

	Budgeted Amounts		Actual GAAP Basis	Adjustments to Budgetary Basis
	Original	Final		
Operating Revenues:				
Charges for other services	\$ 647,000	\$ 647,000	\$ 475,183	\$
Miscellaneous	87,808	87,808	1,448	
Total operating revenues	<u>734,808</u>	<u>734,808</u>	<u>476,631</u>	<u>-0-</u>
Operating Expenses:				
Personnel services	452,537	452,537	490,000	
Employee benefits	169,221	169,221	157,770	
Other operating	75,000	75,000	24,937	
Supplies	50,500	50,500	45,324	
Operating expenses before depreciation	<u>747,258</u>	<u>747,258</u>	<u>718,031</u>	<u>-0-</u>
Depreciation			90,020	(90,020)
Total operating expenses	<u>747,258</u>	<u>747,258</u>	<u>808,051</u>	<u>(90,020)</u>
Net operating income (loss)	<u>(12,450)</u>	<u>(12,450)</u>	<u>(331,420)</u>	<u>90,020</u>
Non-Operating Revenues (Expenses):				
Interest revenue			88	
Loss on sale of capital assets			(2,637)	2,637
Capital outlay	(66,500)	(66,500)		(59,164)
Total non-operating revenues (expenses)	<u>(66,500)</u>	<u>(66,500)</u>	<u>(2,549)</u>	<u>(56,527)</u>
Net income (loss) before operating transfers	(78,950)	(78,950)	(333,969)	33,493
Transfers in	<u>78,950</u>	<u>78,950</u>	<u>78,950</u>	
Change in net position	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$(255,019)</u>	<u>\$ 33,493</u>

Actual Budgetary Basis	Variance on Final Budget - Positive (Negative)
\$ 475,183	\$(171,817)
<u>1,448</u>	<u>(86,360)</u>
<u>476,631</u>	<u>(258,177)</u>
490,000	(37,463)
157,770	11,451
24,937	50,063
<u>45,324</u>	<u>5,176</u>
718,031	29,227
<u>718,031</u>	<u>-0-</u>
<u>(241,400)</u>	<u>(228,950)</u>
88	88
<u>(59,164)</u>	<u>7,336</u>
<u>(59,076)</u>	<u>7,424</u>
(300,476)	(221,526)
<u>78,950</u>	<u>-0-</u>
<u>\$(221,526)</u>	<u>\$(221,526)</u>

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CITY OF FREEPORT

Freeport, Texas

Exhibit H-1

SCHEDULE OF AD VALOREM TAX LEVY AND COLLECTIONS

September 30, 2016

Levy Year	Balance 10-01-15	Current Year Levy	Collections	Adjustments	Balance 09-30-16
2006 & Prior	\$ 37,087	\$	\$ 3,936	\$(6,340)	\$ 26,811
2007	8,424		66	(161)	8,197
2008	7,229		180	(15)	7,034
2009	7,437		300	(101)	7,036
2010	8,237		395	(16)	7,826
2011	85,878		80,571	(17)	5,290
2012	97,459		90,855	(16)	6,588
2013	18,736		5,425	(3,836)	9,475
2014	50,141		21,363	(8,323)	20,455
2015		2,349,446	2,409,939	108,277	47,784
	<u>\$ 320,628</u>	<u>\$ 2,349,446</u>	<u>\$ 2,613,030</u>	<u>\$ 89,452</u>	146,496
Less reserve for uncollectible taxes					<u>50,229</u>
Net delinquent ad valorem taxes receivable					<u>\$ 96,267</u>

FEDERAL AWARDS SECTION

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Kennemer, Masters & Lunsford

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Independent Auditor's Report

On Internal Control Over Financial Reporting and On Compliance and
Other Matters Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards*

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

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Freeport (the "City"), Texas, as of and for the year ended September 30, 2016, and the related notes to the financial statements, which collectively comprise the City's basic financial statements and have issued our report thereon dated February 24, 2017.

Internal Control over Financial Reporting

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

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be material weaknesses. See finding reference numbers 2016-001 and 2016-002.

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

Compliance and Other Matters

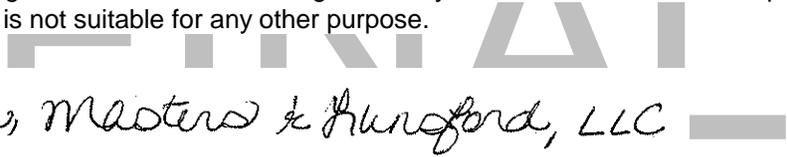
As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect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

City of Freeport, Texas's Response to Findings

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

Purpose of this Report

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



Kennemer, Masters & Hunford, LLC

Certified Public Accountants
Lake Jackson, Texas
February 24, 2017

Kennemer, Masters & Lunsford

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Independent Auditor's Report

On Compliance for Each Major Program and on Internal Control Over
Compliance Required by the Uniform Guidance

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

Report on Compliance for Each Major Federal Program

We have audited the City of Freeport (the "City"), Texas's compliance with the types of compliance requirements described in the *OMB 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, 2016. The City's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance)* 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 District'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, 2016.

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

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Report on Internal Control over Compliance - Continued

auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

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

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 2016-001 and 2016-002 to be material weaknesses.

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

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

Kennemer, Masters & Hunzford, LLC

Certified Public Accountants
Lake Jackson, Texas 77566
February 24, 2017

I. Summary of Auditor's Results

1. Type of auditor's report issued on the financial statements: Unmodified.
2. Two (2) internal control deficiencies, which were considered a material weakness that is required to be reported in this schedule, were disclosed in the audit of the financial statements.
3. Noncompliance, which is material to the financial statements: None.
4. Two (2) internal control deficiencies that are required to be reported in this schedule were disclosed in the audit of major programs.
5. Type of auditor's report on compliance for major programs: Unmodified.
6. Did the audit disclose findings, which are required to be reported under 2 CFR Sec. 200.516 (a): No.
7. Major Programs Include:
Federal:
 - Community Development Block Grant – CFDA #14.228
8. Dollar threshold used to distinguish between Type A and Type B programs: \$ 750,000.
9. Low Risk Auditee: No.

II. Findings related to the financial statements

1. Schedule reference number 2016-001; Balance Sheet Year-end Accruals - Numerous year-end accruals were not accurately recorded requiring recommended audit adjustments (accepted by the City) to ensure the financial statements were fairly presented for the year ended September 30, 2016.

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

Condition: During our audit procedures we performed tests of the year-end accruals as of September 30, 2016 and determined that audit adjustments were required to present fairly stated financial statements.

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

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

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

II. Findings related to the financial statements - Continued

1. Schedule reference number 2016-001; Balance Sheet Year-end Accruals - Continued

Questioned Cost/Basis: None.

2. Schedule reference number 2016-002; Grant Accounting for Revenues and Expenditures/Expenses at Gross – Grant revenue and expenditure/expense accounts were netted and failed to accurately report the grant revenue and expenditures/expenses.

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

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

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

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

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

Questioned Cost/Basis: None.

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

1. Schedule reference number 2016-001; (Community Development Block Grant, CFDA #14.228) Balance sheet year-end accruals.

See Finding in Section II above.

2. Schedule reference number 2016-002, (Community Development Block Grant, CFDA #14.228) Grant accounting for revenues and expenditures/expenses at gross.

See Finding in Section II above.

CITY OF FREEPORT

*SCHEDULE OF STATUS OF PRIOR FINDINGS
FOR THE YEAR ENDED SEPTEMBER 30, 2016*

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1. Schedule reference number 2015-001; Balance Sheet Year-end Accruals - Numerous year-end accruals were not accurately recorded requiring recommended audit adjustments (accepted by the City) to ensure the financial statements were fairly presented for the year ended September 30, 2015. This finding continues with the 2016-001 finding for the year ended September 30, 2016.

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CITY OF FREEPORT
SCHEDULE OF CORRECTIVE ACTION PLAN
FOR THE YEAR ENDED SEPTEMBER 30, 2016

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1. Schedule reference number 2016-001; balance sheet year-end accruals.

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

2. Schedule reference number 2016-002; Grant accounting for revenues and expenditures/expenses at gross.

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

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CITY OF FREEPORT

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED SEPTEMBER 30, 2016**

Exhibit I-1

Federal Grantor/ Pass-Through Grantor/ Program Title	Federal CFDA Number	Pass-Through Grantor's Number	Pass-Through Disbursements and Expenditures
U.S. Department of Justice:			
Direct:			
Bullet Proof Vest Partnership	16.607	--	\$ <u>2,587</u>
TOTAL U.S. DEPARTMENT OF JUSTICE			\$ <u>2,587</u>
U.S. Department of Housing and Urban Development:			
Passed Through Texas General Land Office:			
Community Development Block Grant – Disaster Recovery Program – Program (1)	14.228	13-151-000-7243	\$ 1,163,562
Passed Through Brazoria County, Texas:			
Community Development Block Grant – Freeport Lift Station Improvements	14.218	B-15-UC-48-0005	<u>20,658</u>
TOTAL U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT			\$ <u>1,184,220</u>
U.S. Department of Homeland Security:			
Passed Through Port Freeport, Texas:			
Port Security Grant – Freeport Police Department Surveillance	97.056	EMW-2014PU-00637	\$ <u>260,820</u>
TOTAL U.S. DEPARTMENT OF HOMELAND SECURITY			\$ <u>260,820</u>
TOTAL FEDERAL ASSISTANCE			\$ <u>1,447,627</u>
TOTAL MAJOR PROGRAMS			\$ <u>1,163,562</u>
TYPE A PROGRAM			\$ <u>750,000</u>

(1) – Major Program

CITY OF FREEPORT

NOTES ON ACCOUNTING POLICIES FOR FEDERAL AWARDS

Year Ended September 30, 2016

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

Governmental Fund Types:

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

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

Proprietary Fund Types:

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

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

CITY OF FREEPORT

NOTES ON ACCOUNTING POLICIES FOR FEDERAL AWARDS - *Continued* Year Ended September 30, 2016

2. Continued

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

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

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

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

3. The accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal grant activity of the City under programs of the federal government for the year ended September 30, 2016. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*. Because the schedule presents only a selected portion of the operations of the City, it is not intended to and does not present the financial position, changes in net position or cash flows of the City.

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