

CITY OF HEMPHILL, TEXAS
ANNUAL FINANCIAL REPORT
FOR THE YEAR ENDED JUNE 30, 2011

CITY OF HEMPHILL, TEXAS
Annual Financial Report
For the Year Ended June 30, 2011

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Annual Financial Report
For the Year Ended June 30, 2011**

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FINANCIAL SECTION



Certified Public Accountants

Goff & Herrington, P.C.

A.J. Goff, CPA
Ronnie Herrington, CPA

P.O. Box 153320 • Lufkin, TX. 75915-3320 • (936) 875-3317 • Fax:(936) 622-6823

Independent Auditor's Report

Honorable Mayor and Members of the City Council
City of Hemphill, Texas

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 Hemphill, Texas as of and for the year ended June 30, 2011, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our 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 Hemphill, Texas as of June 30, 2011, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated November 4, 2011, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Independent Auditor's Report

Honorable Mayor and Members of City Council
City of Hemphill, Texas
Page 2

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 10 and page 37 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by Governmental Accounting Standards Board, who considers it to be an essential part of the 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 the 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's financial statements as a whole. The other schedules and statistical tables are presented for purposes of additional analysis and are not a required part of the financial statements. The other schedules are responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Goff & Herrington, P.C.

GOFF & HERRINGTON, P. C.
Certified Public Accountants

November 4, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the City of Hemphill, Texas annual financial report presents our narrative discussion and analysis of the City's financial activities for the year ended June 30, 2011. Please read it in conjunction with the City's financial statements, which immediately follow this section.

Financial Highlights

- ▶ The City's total net assets were \$5,744,785 as of June 30, 2011. Of this amount, \$1,479,829 (unrestricted net assets) may be used to meet the City's continuing obligations to citizens, customers and creditors.
- ▶ During the year ended June 30, 2011, the City's net assets **increased** by \$636,753.
- ▶ Total long-term debt of the City decreased by \$437,433 to \$615,000 during the current fiscal year.
- ▶ At the end of the current fiscal year, unreserved fund balance for the general fund was \$78,181 or 8.2 percent of total general fund current expenditures.

Overview of the Financial Statements

This annual financial report consists of three parts - **management's discussion and analysis** (this section), the **basic financial statements**, and **required supplementary information**. The basic financial statements include: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. The required supplementary information further explains and supports the information in the financial statements.

Government-wide Financial Statements

The City's annual financial report includes two government-wide financial statements. These statements provide both long-term and short-term information about the City's finances. Financial reporting at this level uses a perspective similar to that found in the private sector.

The first of these government-wide financial statements is the **Statement of Net Assets**. This is the City wide statement of financial position presenting information that includes all of the City's assets and liabilities, with the difference reported as **net assets**. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City as a whole is improving or deteriorating. Evaluation of the overall health of the City would extend to other non financial factors such as changes to the City's tax base.

The second government-wide financial statement is the **Statement of Activities**, which reports how the City's net assets changed during the current year. All current revenues and expenses are included regardless of when the cash is received or paid.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Both of the government-wide financial statements distinguish governmental activities of the City that are principally supported by taxes and intergovernmental revenues, from business-type activities that are intended to recover all or a significant portion of their costs through user fees and charges. Governmental activities include general government, public safety, streets, parks and recreation, health and welfare, and sanitation collection. Business-type activities include water and sewer operations, natural gas utilities, and electric services.

Fund Financial Statements

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

Governmental funds - Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term cash inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating the City'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 City's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and change in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The City maintains one individual governmental fund, the general fund, which is considered a major fund. The City adopts an annual budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

Proprietary funds - Proprietary funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses an enterprise fund (a type of proprietary fund) to account for its water and sewer operations, natural gas utilities, and electric services.

Notes to the financial statements - The accompanying notes to the financial statements provide essential information to a full understanding of the government-wide and fund financial statements.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Other information - In addition to the basic financial statements and accompanying notes, this report also presents other supplementary information which includes detail expenditures by fund and department. Supplementary information follows the notes to the financial statements.

Government-wide Financial Analysis

Net Assets. As noted earlier, net assets may serve over time as a useful indicator of the City's financial position. The City's assets exceed liabilities by \$5,744,785 at the close of the fiscal year.

By far the largest portion of the City's net assets (72.7 percent) reflects its investment in capital assets (land, buildings, utility systems, machinery and equipment), less any related debt used to acquire those assets that is still outstanding. The City uses these assets to provide services to the citizens, consequently, these assets are not available for future spending. Although the City 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.

The City's Net Assets

	Governmental Activities		Business-type activities		Total	
	2011	2010	2011	2010	2011	2010
Current and Other Assets	107,661	137,285	1,995,926	1,643,006	2,103,587	1,780,291
Capital and Non-Current Assets	753,144	635,936	4,015,432	4,172,312	4,768,576	4,808,248
Total Assets	860,805	773,221	6,011,358	5,815,318	6,872,163	6,588,539
Other Liabilities	46,154	45,622	466,224	382,453	512,378	428,075
Long Term Liabilities	-	-	615,000	1,052,433	615,000	1,052,433
Total Liabilities	46,154	45,622	1,081,224	1,434,886	1,127,378	1,480,508
Net Assets:						
Investment in Capital Assets,						
Net of Related Debt	753,144	635,936	3,426,861	3,119,879	4,180,005	3,755,815
Restricted	3,650	2833	81,301	79,634	84,951	82,467
Unrestricted	57,857	88,830	1,421,972	1,180,920	1,479,829	1,269,750
Total Net Assets	814,651	727,599	4,930,134	4,380,433	5,744,785	5,108,032

A portion of the City's net assets (1.5 percent) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets in the amount of \$1,479,829 may be used to meet the City's ongoing obligations to citizens and creditors.

MANAGEMENT'S DISCUSSION AND ANALYSIS

At the end of the current fiscal year, the City is able to report positive balances in all three categories of net assets, both for the City as a whole, as well as for its separate governmental and business-type activities.

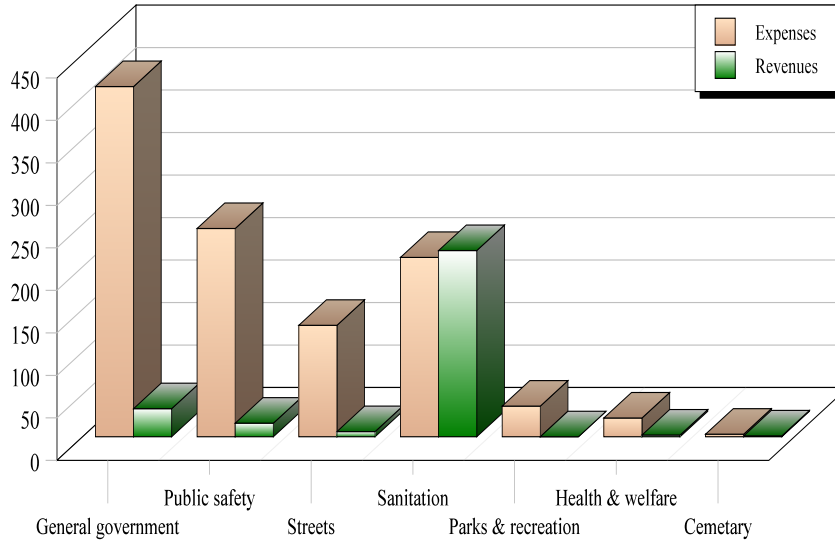
Changes in the City's Net Assets

	Governmental Activities		Business-type activities		Total	
	2011	2010	2011	2010	2011	2010
Revenues:						
Program Revenues:						
Charges for services	237,416	232,915	4,367,402	4,282,317	4,604,818	4,515,232
Operating grants	34,267	34,030	-	-	34,267	34,030
Capital grants	198,867	69,189	-	-	198,867	69,189
General Revenues:						
Sales taxes	407,814	371,321	-	-	407,814	371,321
Other taxes	11,718	11,959	-	-	11,718	11,959
Other	17,446	62,242	392,100	33,728	409,546	95,970
Total revenues	907,528	781,656	4,759,502	4,316,045	5,667,030	5,097,701
Expenses:						
General government	411,957	405,128	-	-	411,957	405,128
Public safety	245,531	295,820	-	-	245,531	295,820
Streets	130,780	124,553	-	-	130,780	124,553
Sanitation	211,503	218,827	-	-	211,503	218,827
Parks and recreation	36,044	42,912	-	-	36,044	42,912
Health and welfare	22,299	21,458	-	-	22,299	21,458
Cemetery	3,460	5,750	-	-	3,460	5,750
Debt service	-	-	-	-	-	-
Electric	-	-	1,836,529	1,721,737	1,836,529	1,721,737
Natural gas	-	-	280,666	249,141	280,666	249,141
Water	-	-	1,458,174	1,352,981	1,458,174	1,352,981
Sewer	-	-	393,334	421,361	393,334	421,361
Total expenses	1,061,574	1,114,448	3,968,703	3,745,220	5,030,277	4,859,668
Transfers	241,098	368,088	(241,098)	(368,088)	-	-
Increase in net assets	87,052	35,296	549,701	202,737	636,753	238,033
Beginning net assets	727,599	692,303	4,380,433	4,177,696	5,108,032	4,869,999
Ending net assets	<u>814,651</u>	<u>727,599</u>	<u>4,930,134</u>	<u>4,380,433</u>	<u>5,744,785</u>	<u>5,108,032</u>

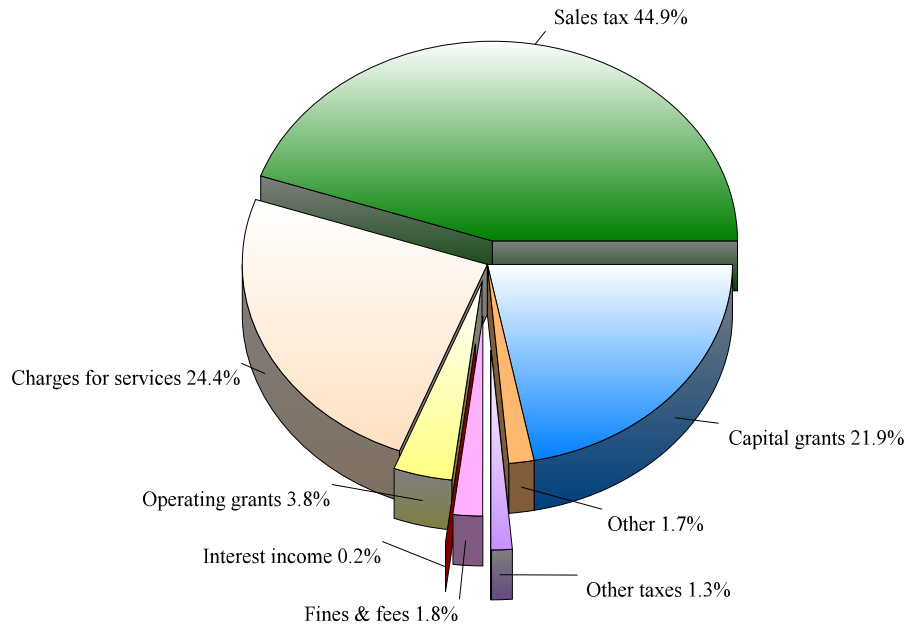
MANAGEMENT'S DISCUSSION AND ANALYSIS

Governmental Activities. Governmental activities increased the City's net assets by \$87,052 contributing to the overall increase in the City's total net assets.

Expenses and Program Revenues - Governmental Activities



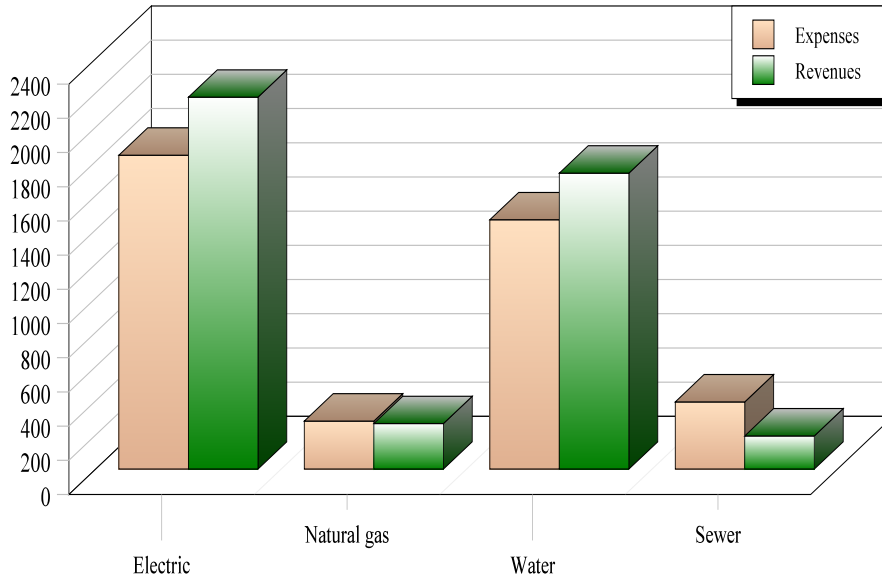
Revenues by Source - Governmental Activities



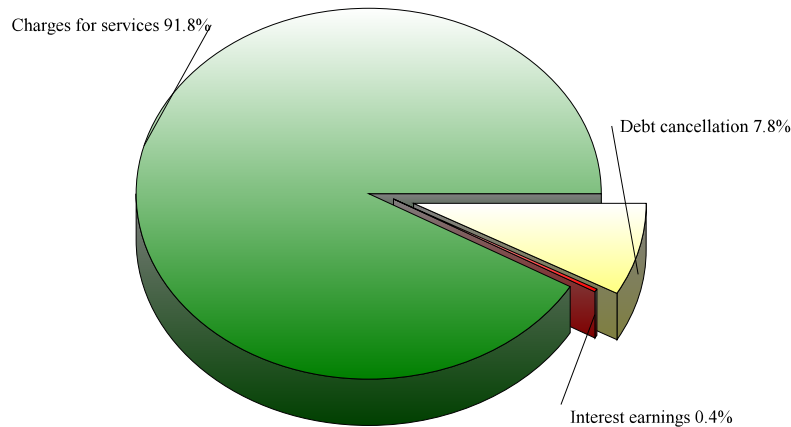
MANAGEMENT'S DISCUSSION AND ANALYSIS

Business-type Activities. Business-type activities increased the City's net assets by \$549,701, contributing to the overall increase in the City's total net assets.

Expenses and Program Revenues - Business-Type Activities



Revenues by Source - Business-Type Activities



Financial Analysis of the City's Funds

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

MANAGEMENT DISCUSSION AND ANALYSIS

As of the end of the current fiscal year, the City’s governmental funds reported an ending fund balance of \$81,831, a decrease of \$9,832 compared with the prior year. This balance is unreserved, which is available for current expenditures.

Proprietary funds. The City’s proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail. Unrestricted net assets of the proprietary fund at the end of the year amounted to \$1,421,972.

General Fund Budgetary Highlights

During the year, the City Council approved an increase in appropriations between the original and final amended budget. The following are components of amounts amended:

- ▶ \$10,673 increase in personnel costs across all functions.

This increase was needed to fund increased health care benefit costs..

Capital Asset and Debt Administration

Capital Assets. At the end of the current fiscal year, the City’s investment in capital assets for the governmental and business type activities amounted to \$4,768,576 (net of accumulated depreciation). This investment in capital assets included land, buildings, utility system improvements, machinery, equipment, and park facilities.

	City’s Capital Assets (net of depreciation)					
	Governmental		Business-type activities		Total	
	2011	2010	2011	2010	2011	2010
Land	92,641	92,641	79,523	79,523	172,164	172,164
Buildings & improvements	531,246	374,008	-	-	531,246	374,008
Utility systems	-	-	3,636,909	3,987,481	3,636,909	3,987,481
Property - capital lease	-	-	-	-	-	-
Vehicles and equipment	129,257	169,287	253,000	195,308	382,257	364,595
Construction in progress	-	-	46,000	-	46,000	-
Net capital assets	<u>753,144</u>	<u>635,936</u>	<u>4,015,432</u>	<u>4,262,312</u>	<u>4,768,576</u>	<u>4,898,248</u>

More detailed information about the City’s capital assets is presented in the notes to the financial statements.

MANAGEMENT DISCUSSION AND ANALYSIS

Long-term debt. At the end of the current fiscal year, the City had total long term debt of \$615,000.

	City's Outstanding Debt					
	Governmental Activities		Business-type activities		Total	
	2011	2010	2011	2010	2011	2010
Revenue bonds	-	-	615,000	656,000	615,000	656,000
Capital lease	-	-	-	170,090	-	170,090
Promissory notes	-	-	-	226,343	-	226,343
Bank loans	-	-	-	-	-	-
Net capital assets	-	-	615,000	1,052,433	615,000	1,052,433

The City's total long term debt decreased by \$437,433 during the current fiscal year. The City's revenue bonds are owned by the Texas Water Development Board and the U. S. Department of Agriculture and are not rated.

More detailed information about the City's long term debt is presented in the notes to the financial statements.

Economic Factors and Next Year's Budgets and Rates

The City considered many factors when setting the fiscal year 2011-2012 budget, including estimated sales tax receipts and fees that will be charged for business-type activities. The City estimates revenues and operating transfers in the General Fund will provide resources to fund the necessary operating expenses of the General Fund.. The other ongoing general fund revenue items (charges for services, etc.) should generate similar revenues as the prior year. The City's business-type activities budget reflect a one percent increase in utility rates. Major capital expenditures estimated at \$529,800 are expected at the water treatment plant to comply with Texas Commission on Environmental Quality mandates.

Additionally, the City anticipates spending \$171,825 in capital improvements during fiscal year 2011-2012. These include purchasing a police vehicle, utility truck, facility improvements, technology equipment purchases, cemetery, park, and street improvements.

If these estimates are realized, the City's budgetary general fund balance and utility reserves are expected to increase by the close of 2012.

Request for Information

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the City of Hemphill's finances and to demonstrate accountability for the money it receives. If you have any questions about this report or need additional financial information contact the City Secretary, P. O. Box 788, Hemphill, Texas, 75948.

Government-Wide Financial Statements

**CITY OF HEMPHILL, TEXAS
STATEMENT OF NET ASSETS
JUNE 30, 2011**

	Primary Government		
	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and cash equivalents	69,305	1,438,134	1,507,439
Sales tax receivable	34,706	-	34,706
Accounts receivable	-	437,765	437,765
Inventories	-	12,297	12,297
Deferred charges	-	26,429	26,429
Restricted assets:			
Cash and cash equivalents	3,650	81,301	84,951
Capital Assets (net of accumulated depreciation):			
Land	92,641	79,523	172,164
Other capital assets, net of depreciation	660,503	3,935,909	4,596,412
Total assets	860,805	6,011,358	6,872,163
LIABILITIES			
Accounts payable	23,627	318,971	342,598
Accrued expenses	22,527	33,510	56,037
Accrued interest payable	-	8,499	8,499
Customer meter deposits	-	105,244	105,244
Long Term Liabilities:			
Due within one year	-	41,000	41,000
Due after one year	-	574,000	574,000
Total liabilities	46,154	1,081,224	1,127,378
NET ASSETS			
Invested in capital assets, net of related debt	753,144	3,426,861	4,180,005
Restricted for other purposes	3,650	81,301	84,951
Unrestricted net assets	57,857	1,421,972	1,479,829
Total net assets	814,651	4,930,134	5,744,785

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2011**

Functions/Programs	Program Revenues		
	Expenses	Charges for Services	Operating Grants and Contributions
Governmental activities:			
General government	411,957	508	32,660
Public safety	245,531	15,889	857
Streets	130,780	601	-
Sanitation	211,503	219,148	-
Parks and recreation	36,044	-	-
Health and welfare	22,299	220	-
Cemetery	3,460	1,050	750
Interest on long term debt	-	-	-
Total governmental activities	1,061,574	237,416	34,267
Business-type activities:			
Electric	1,836,529	2,175,843	-
Natural gas	280,666	266,390	-
Water	1,458,174	1,730,777	-
Sewer	393,334	194,392	-
Total business-type activities	3,968,703	4,367,402	-
	5,030,277	4,604,818	34,267

General revenues:
 Sales taxes
 Franchise taxes
 Miscellaneous
 Cancellation of debt
 Net grants not restricted to specific programs
 Investment earnings
 Transfers

Total general revenues and transfers
 Change in net assets
 Net assets, beginning

Net assets, ending

See accompanying notes to the financial statements

Program Revenues	Net (Expense) Revenues and Changes in Net Assets		
Capital Grants and Contributions	Governmental Activities	Business Activities	Total
-	(378,789)	-	(378,789)
-	(228,785)	-	(228,785)
198,867	68,688	-	68,688
-	7,645	-	7,645
-	(36,044)	-	(36,044)
-	(22,079)	-	(22,079)
-	(1,660)	-	(1,660)
-	-	-	-
198,867	(591,024)	-	(591,024)
-	-	339,314	339,314
-	-	(14,276)	(14,276)
-	-	272,603	272,603
-	-	(198,942)	(198,942)
-	-	398,699	398,699
198,867	(591,024)	398,699	(192,325)
	407,814	-	407,814
	11,718	-	11,718
	15,753	-	15,753
	-	374,051	374,051
	-	-	-
	1,693	18,049	19,742
	241,098	(241,098)	-
	678,076	151,002	829,078
	87,052	549,701	636,753
	727,599	4,380,433	5,108,032
	-	-	-
	814,651	4,930,134	5,744,785

See accompanying notes to the financial statements

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Fund Financial Statements

**CITY OF HEMPHILL, TEXAS
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2011**

	General Fund	Other Governmental Funds	Total Governmental Funds
ASSETS			
Cash and cash equivalents	69,305	-	69,305
Sales tax receivable	34,706	-	34,706
Cash and cash equivalents - restricted	3,650	-	3,650
Total assets	<u>107,661</u>	-	<u>107,661</u>
LIABILITIES AND FUND BALANCES			
Liabilities:			
Accounts payable	23,627	-	23,627
Accrued liabilities	2,203	-	2,203
Total liabilities	<u>25,830</u>	-	<u>25,830</u>
Fund balances:			
Restricted fund balance	3,650		3,650
Unassigned fund balance	78,181	-	78,181
Total fund balances	<u>81,831</u>	-	<u>81,831</u>
Total liabilities and fund balances	<u>107,661</u>	-	<u>107,661</u>

See accompanying notes to the financial statements

CITY OF HEMPHILL, TEXAS
RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS
JUNE 30, 2011

Total fund balances - governmental funds	81,831
Capital assets used in governmental activities are not financial resources and therefore are not reported in governmental funds. At the beginning of the year, the cost of these assets was \$1,188,654 and the accumulated depreciation was \$552,718. The effect of including beginning balances for capital assets (net of depreciation) in the governmental activities is to increase (decrease) net assets.	635,936
Capital outlays are expenditures in the fund financial statements, but they should be shown as increases in capital assets in the government-wide financial statements. The net effect of including the current year capital outlays, less current year depreciation is to increase net assets.	117,208
Long term liabilities are not due and payable in the current period and therefore are not reported in the funds.	<u>(20,324)</u>
Net assets of governmental activities	<u><u>814,651</u></u>

See accompanying notes to the financial statements

CITY OF HEMPHILL, TEXAS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2011

	General Fund	Other Governmental Funds	Total Governmental Funds
REVENUES			
Taxes:			
Sales taxes	407,814	-	407,814
Franchise taxes	4,243	-	4,243
Permits, fees and assessments	7,665	-	7,665
Fines	13,808	-	13,808
Charges for services	218,454	-	218,454
Interest income	1,693	-	1,693
Intergovernmental	231,526	-	231,526
Contributions and donations	1,800	-	1,800
Other	20,525	-	20,525
Total revenues	907,528	-	907,528
EXPENDITURES			
Current:			
General government:			
Finance and administration	364,477	-	364,477
Municipal court	28,309	-	28,309
Public safety:			
Fire	22,027	-	22,027
Police	181,240	-	181,240
Streets	100,379	-	100,379
Sanitation	205,948	-	205,948
Parks and recreation	25,604	-	25,604
Health and welfare	21,249	-	21,249
Cemetery	3,460	-	3,460
Debt service	-	-	-
Capital outlay	205,765	-	205,765
Total expenditures	1,158,458	-	1,158,458
Excess (deficiency) of revenues over expenditures	(250,930)	-	(250,930)
OTHER FINANCING SOURCES (USES)			
Transfers in	241,098	-	241,098
Total other financing sources and uses	241,098	-	241,098
Net change in fund balance	(9,832)	-	(9,832)
Fund balance - beginning	91,663	-	91,663
Fund balance - ending	81,831	-	81,831

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2011**

Net change in fund balances - governmental funds	(9,832)
Current year capital outlays are expenditures in the governmental fund financial statements but they should be shown as increases in capital assets in the government-wide financial statements. The effect of removing the current year capital outlays is to increase net assets.	204,615
Depreciation is not recognized as an expense in governmental fund financial statements since it does not require the use of current financial resources. The net effect of the current year depreciation and retiring assets not fully depreciated is to decrease net assets.	(87,407)
Some expenses reported in the statement of activities do not require the use of current financial resources; therefore, they are not reported as expenditures in governmental funds. This amount reflects the change in the accrued liability for compensated absences.	<u>(20,324)</u>
Change in net assets of governmental activities	<u><u>87,052</u></u>

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
STATEMENT OF NET ASSETS
PROPRIETARY FUND
JUNE 30, 2011**

ASSETS

Current assets:	
Cash and cash equivalents	1,438,134
Accounts receivable	437,765
Inventories	12,297
Total current assets	1,888,196
Noncurrent assets:	
Restricted cash and cash equivalents	81,301
Deferred charges	26,429
Capital assets:	
Land	79,523
Other capital assets, net of depreciation	3,935,909
Total noncurrent assets	4,123,162
 Total assets	 6,011,358

LIABILITIES

Current liabilities:	
Accounts payable	318,971
Accrued expenses	33,510
Accrued interest payable	8,499
Current portion of:	
Capital leases	-
Promissory note	-
Revenue bonds payable	41,000
Total current liabilities	401,980
Noncurrent liabilities:	
Capital leases	-
Promissory note	-
Revenue bonds payable	574,000
Customer deposits	105,244
Total noncurrent liabilities	679,244
 Total liabilities	 1,081,224

NET ASSETS

Invested in capital assets, net of related debt	3,426,861
Restricted for debt service	81,301
Unrestricted	1,421,972
Total net assets	4,930,134
 Total liabilities and net assets	 6,011,358

See accompanying notes to the financial statements

CITY OF HEMPHILL, TEXAS
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUND
FOR THE YEAR ENDED JUNE 30, 2011

Operating revenues:	
Water sales	1,713,192
Sewer charges	192,394
Electric sales	2,153,730
Gas sales	263,681
Other services	44,405
	<hr/>
Total operating revenues	4,367,402
Operating expenses:	
Personnel	659,539
Supplies and materials	359,659
Maintenance and repairs	46,266
Contractual services	89,536
Cost of services	2,354,946
Depreciation	350,315
Other operating	55,387
	<hr/>
Total operating expenses	3,915,648
Operating income	451,754
Nonoperating revenues (expenses):	
Interest income	18,049
Cancellation of debt	374,051
Interest expense	(53,055)
	<hr/>
Total nonoperating revenue (expenses)	339,045
Income before transfers	790,799
Transfers to other funds	(241,098)
	<hr/>
Change in net assets	549,701
Total net assets - beginning	4,380,433
	<hr/>
Total net assets - ending	4,930,134
	<hr/> <hr/>

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
STATEMENT OF CASH FLOWS
PROPRIETARY FUND
FOR THE YEAR ENDED JUNE 30, 2011**

Cash flows from operating activities:	
Receipts from customers	4,365,909
Payments to suppliers and contractors	(2,834,618)
Payments to employees	(652,161)
Net cash provided by (used for) operating activities	<u>879,130</u>
Cash flows from noncapital financing activities:	
Operating transfers	(241,098)
Net cash provided by (used for) noncapital activities	<u>(241,098)</u>
Cash flows from capital and related financing activities:	
Capital grant received	-
Purchases of capital assets	(193,435)
Principal paid on capital debt	(63,381)
Interest paid on capital debt	(52,500)
Net cash provided by (used for) capital activities	<u>(309,316)</u>
Cash flows from investing activities:	
Interest received	18,049
Net cash provided by (used for) investing activities	<u>18,049</u>
 Net increase (decrease) in cash and cash equivalents	 346,765
 Cash and cash equivalents, beginning	 <u>1,172,670</u>
 Cash and cash equivalents, ending	 <u><u>1,519,435</u></u>
 Reconciliation of operating income to net cash used by operating activities:	
Operating income	451,754
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	350,315
Changes in assets and liabilities:	
(Increase) decrease in accounts receivable	(7,157)
(Increase) decrease in supply inventory	(326)
Increase (decrease) in accounts payable	71,503
Increase (decrease) in accrued liabilities	7,229
Increase (decrease) in customer meter deposits	5,812
Net cash provided by operating activities	<u><u>879,130</u></u>

See accompanying notes to the financial statements

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CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity - The City of Hemphill, Texas, (City) operates under Section 4, Article XI of the Texas constitution as a general law city. The City is governed by a Mayor and five council members. The accompanying financial statements present the City's primary government which includes all functions which the City's mayor and council exercise significant influence and are financially accountable. Significant influence or accountability is based on any budget adoption, rate setting, taxing authority, outstanding debt secured by the City to finance any deficits that may occur, and receipt of significant subsidies from the City.

Budget adoption, rate setting, taxing authority, outstanding debt secured by the City to finance any deficits that may occur, and receipt of significant subsidies from the City.

Government-wide and Fund Financial Statements - The government-wide financial statements include the statement of net assets and the statement of activities. These statements report financial information for the City as a whole. Individual funds are not displayed in the government-wide financial statements. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which are normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

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

Separate fund financial statements are provided for governmental funds and proprietary funds.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation - The accounting policies of the City conform to accounting principles generally accepted in the United States of America as applicable to governments. The City's reporting entity applies all relevant Governmental Accounting Standards Board (GASB) pronouncements. The proprietary fund applies Financial Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which GASB prevails.

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

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. Grants and similar items are recognized as revenue as soon as all eligibility requirements are met.

Governmental fund financial statements are reported using the current financial resources measurement focus and 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 with 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, are recorded only when payment is due.

Sales tax, franchise taxes and interest associated with the current fiscal year are all considered to susceptible to accrual and so have been recognized as revenues of the current fiscal year. All other revenue items are considered to be measurable and available only when cash is received by the City.

The City reports the following major governmental funds:

General Fund - The General Fund is the general operating fund of the City. It is used to account for all financial resources except for those required to be accounted for in another fund.

The City reports the following major proprietary funds:

Utility Fund - accounts for the activities of the City's electric distribution operations, water and sewer services, and natural gas utilities.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the City's utility functions and various other functions of the City. Elimination of these charges would distort the direct cost and program revenues reported for the various functions concerned.

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

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

The proprietary fund distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the proprietary fund's principal operations. The principal operating revenues of the Utility Fund are charges to customers for sale and services. The Utility Fund also recognizes as operating revenues tap fees intended to recover the cost of connecting new customers to the system. Operating expenses for the Utility Fund include 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, then unrestricted resources as they are needed.

Budget - Annual appropriated budgets are adopted for the general fund and utility fund. All annual appropriation lapse at fiscal year end. The budget presented includes all approved amendments.

Deposits and Investments - The City's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. The City only invests in short term certificates of deposit. Investments are stated at cost, which approximates market.

Short-term Interfund Receivables/Payables - During the course of operations, transactions occur between individual funds for advances or for goods provided or services rendered. These receivables and payables are classified as due from other funds or due to other funds on the balance sheet.

Inventory of Supplies - Inventory of supplies consist primarily of supplies held for consumption stated at cost, which approximates market. Inventory is expended at the time the individual items are used or consumed.

Restricted Assets - Certain resources set aside for repayment of utility fund revenue bonds and tax anticipation notes are classified as restricted assets on the balance sheet, since use is limited by bond covenants or City Council authorization.

Capital assets - Capital assets, which include property, utility systems, buildings, vehicles and equipment, are reported in the applicable governmental or business-types activities column in the government-wide financial statements. Capital assets are defined by the City as assets with an initial, individual cost of more than \$2,000 and an estimated useful life in excess of five years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

not capitalized.

Depreciation is provided on all capital assets used by the general and utility funds over the following estimated useful lives using the straight-line method. The estimated useful lives are:

<u>Assets</u>	<u>Years</u>
Buildings and improvements	10-30
Utility distribution systems	30
Vehicles and equipment	3-10
Furniture and equipment	5-10

Net Assets and Fund Balance - Net assets in the statement of net assets include components that are restricted for debt service and other specific uses. Unreserved fund balance in the governmental fund financial statements represents that portion of fund balance that is available for budgeting in future periods.

Fund Balance Policy - The City reports fund balances for governmental funds in classifications based primarily on the extent to which the City is bound to honor constraints on the specific purposes for which amounts in those funds can be spent. The nonspendable classification represents assets that will be consumed or “must be maintained intact” and therefore will never convert to cash, such as inventories of supplies and endowments. Provisions of laws, contracts, and grants specify how fund resources can be used in the restricted classification. The nature of these two classifications precludes a need for a policy from the City Council. However, the City Council has adopted fund balance policies for the three unrestricted classifications—committed, assigned, and unassigned.

The City’s restricted fund balances represents amounts for cemetery expenses and amounts to be spent on technology and security.

Compensated Absences - The City allows employees to accumulate sick leave and vacation time. Upon termination, the City pays any accumulated vacation that is earned, but not used. Accumulated sick leave is not paid upon termination. Accumulated vacation is accrued, when incurred in the government-wide and proprietary fund financial statements. A liability for the estimated amount to be paid from current resources is reported in the governmental funds.

Long-Term Obligations - In the government-wide financial statements, and proprietary fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities or proprietary fund financial statements. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

Interfund Transactions - Transactions that constitute reimbursements to a fund for expenditures initially made from it that are properly applicable to another fund, are recorded as expenditures in the reimbursing fund and as reductions of expenditures in the fund that is reimbursed. All other interfund transactions are reported as operating transfers.

Use of Estimates - The preparation of financial statements in conformity with generally accepted accounting principles includes the use of estimates that affect the financial statements. Accordingly, actual results could differ from those estimates.

Statement of Cash Flows - For the purposes of cash flows, the City considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

DEPOSITS AND INVESTMENTS

Legal and Contractual Provisions Governing Deposits and Investments. The Public Funds Investment Act (Government Code Chapter 2256) contains specific provisions in the areas of investment practices, management reports, and establishment of appropriate policies. Among other things, it requires the City to adopt, implement, and publicize an investment policy. That policy must address the following areas: (1) safety of principal and liquidity, (2) portfolio diversification, (3) allowable investments, (4) acceptable risk levels, (5) expected rates of return, (6) maximum allowable stated maturity of portfolio investments, (7) maximum average dollar-weighted maturity allowed based on stated maturity date for the portfolio, (8) investment staff quality and capabilities, (9) and bid solicitation preferences for certificates of deposit. Statutes authorize the City to invest in (1) obligations of the U.S. Treasury, certain U.S. agencies, and the State of Texas; (2) certificates of deposit, (3) certain municipal securities, (4) money market saving accounts, (5) repurchase agreements, (6) bankers acceptances, (7) Mutual Funds, (8) Investment pools, (9) guaranteed investment contracts, and (10) common trust funds. The Act also requires the City to have independent auditors perform test procedures related to investment practices as provided by the Act. The City is in substantial compliance with the requirements of the Act and with local policies.

In compliance with the Public Funds Investment Act, the City has adopted a deposit and investment policy. The policy addresses the following risks:

Deposits

Custodial Credit Risk - Deposits. In the case of deposits, this is the risk that in the event of a bank failure, the City's deposits may not be returned to it. The City's policy regarding types of deposits allowed and collateral requirements is that the funds of the City must be deposited under the terms

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

of a contract, contents of which are set out in the Depository Contract Law. The depository bank places approved pledged securities for safekeeping and trust with the City's agent bank in an amount sufficient to protect City funds on a day-to-day basis during the period of the contract. The pledge of approved securities is waived only to the extent of the depository bank's dollar amount of Federal Deposit Insurance Corporation ("FDIC") insurance. The City's cash deposits at June 30, 2011 were entirely covered by FDIC insurance or by pledged collateral held by the City's agent bank in the City's name.

As of June 30, 2011, the bank balances of the City's deposits (demand and certificates) were \$1,607,803. The City is not exposed to custodial credit risk for its deposits as all are covered by depository insurance or by pledged collateral as of June 30, 2011 as follows:

FDIC Insurance	500,000
Market value of securities pledged	<u>2,401,432</u>
Total coverage	<u><u>2,901,432</u></u>

Investments

Credit Risk. - This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The ratings of securities by nationally recognized rating agencies are designed to give an indication of credit risk. The City was not exposed to credit risk at June 30, 2011.

Custodial Credit Risk - Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the government, and are held by either the counterparty or the counterparty's trust department or agent but not in the name of the City. The City was not exposed to custodial credit risk at June 30, 2011.

Interest Rate Risk. - This is the risk that changes in interest rates will adversely affect the fair value of an investment. The City was not exposed to interest rate risk at June 30, 2011.

Concentration of Credit Risk.- This is the risk of loss attributed to the magnitude of the government's investment in a single issuer. The City was not exposed to concentration of credit risk at June 30, 2011.

Foreign Currency Risk. - This is the risk that exchange rates will adversely affect the fair value of an investment. The City was not exposed to foreign currency risk at June 30, 2011.

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

The City's investments , which are reported as cash ad cash equivalents, as of June 30, 2011 are with the depository bank in certificates of deposit in the amount of \$976,724.

Restricted deposits - Resources set aside for repayment of revenue bonds are classified as restricted assets in the statement of net assets since their use is limited by bond covenants. At June 30, 2011, the City's business type activities restricted assets consisted of \$81,301 for debt service. The governmental activities restricted assets consisted of \$2,987 for cemetery operations and \$663 for other purposes.

PROPERTY TAXES

The City did not levy property taxes in October, 2010. An allowance in the amount of \$2,224 is established for the entire balance of delinquent property taxes due to the City.

DUE FROM OTHER GOVERNMENTS

Amount due from other governments as of June 30, 2011 is \$34,706 for sales tax due from the State of Texas.

CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2011 was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements/ Adjustments</u>	<u>Ending Balance</u>
Governmental activities:				
Capital assets, not being depreciated:				
Land	92,641	-	-	92,641
Capital assets, being depreciated:				
Buildings and improvements	556,699	204,615	-	761,314
Vehicles and equipment	539,314	-	(4,052)	535,262
Total capital assets being depreciated	1,096,013	204,615	(4,052)	1,296,576
Less accumulated depreciation for:				
Buildings and improvements	182,691	47,376	-	230,067
Vehicles and equipment	370,027	40,031	(4,052)	406,006
Total accumulated depreciation	552,718	87,407	(4,052)	636,073

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements/ Adjustments</u>	<u>Ending Balance</u>
Total capital assets, being depreciated, net	543,295	117,208	-	660,503
Governmental activities capital assets, net	<u>635,936</u>	<u>117,208</u>	<u>-</u>	<u>753,144</u>
Business-type activities:				
Capital assets, not being depreciated:				
Land	79,523	-	-	79,523
Construction in progress	-	46,000	-	46,000
Capital assets, being depreciated:				
Buildings and improvements	32,500	-	(3,650)	28,850
Utility systems	8,360,654	392,030	(523,238)	8,229,446
Vehicles and equipment	801,524	117,942	(115,128)	804,338
Property under capital lease	350,000	-	(350,000)	0
Totals at cost	<u>9,544,678</u>	<u>509,972</u>	<u>(992,016)</u>	<u>9,062,634</u>
Less accumulated depreciation:				
Buildings and improvements	32,500	-	(3,650)	28,850
Utility system	4,463,172	302,466	(173,286)	4,592,352
Vehicles and equipment	606,216	47,849	(102,542)	551,523
Property under capital lease	350,000	-	(350,000)	0
Total accumulated depreciation	<u>5,451,888</u>	<u>350,315</u>	<u>(629,478)</u>	<u>5,172,725</u>
Total capital assets, being depreciated, net	<u>4,092,790</u>	<u>159,657</u>	<u>(362,538)</u>	<u>3,889,909</u>
Business-type activities capital assets, net	<u>4,172,313</u>	<u>205,657</u>	<u>(362,538)</u>	<u>4,015,432</u>

Depreciation expense was charged to functions of the City as follows:

Governmental activities:	
General government	7,345
Public safety	36,370
Streets	27,557

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

Sanitation	5,555
Health and welfare	440
Parks and recreation	<u>10,140</u>
Total depreciation expense - governmental activities	<u>87,407</u>
Business-type activities:	
Overhead	47,849
Water	20,956
Sewer	105,032
Natural Gas	25,246
Electric	22,671
Water Plant	<u>128,561</u>
Total depreciation expense - business-type activities	<u>350,315</u>

CAPITAL LEASE

In previous years, the City entered into a lease agreement with the Sabine River Authority (Authority) to lease water treatment and transmission facilities that were constructed by the Authority. The lease agreement has been accounted for as capital lease in the accompanying financial statements. In June 2011, the Authority terminated this agreement, thereby forgiving the remaining debt in the amount of \$157,172 and conveying the property and improvements to the City debt free.

The City paid \$7,479 in interest expense for the scheduled debt service during the year ended June 30, 2011 under this capital lease.

LONG-TERM DEBT

Revenue Bonds

In April 1995, the City Council authorized the issuance of Waterworks and Sewer System Revenue Bonds in the amount of \$495,000. The proceeds were used to make improvements and extensions to the Water and Sewer system, including water supply and treatment facilities. The revenue bonds are scheduled to mature April 1, 2015, with interest rates ranging from 6.65% to 8.25%. The revenue bonds are payable solely from the net revenues derived from the operations of the City's water and sewer system.

The revenue bond ordinance contains significant requirements for annual debt service and reserve

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

funds, in addition to various other requirements. The City is in compliance with all significant requirements of the bond ordinance. As of June 30, 2011, the City had 693 water connections and 589 sewer connections.

The City's compliance with the balances required as of June 30, 2011 in each account is as follows:

	<u>Balance Required</u>	<u>Balance Available</u>	<u>Excess (Deficiency)</u>
Series 1995 Revenue Bonds:			
Interest & Sinking Fund	12,242	13,867	1,625
Reserve Fund	50,560	50,560	-

In March 2005, the City Council authorized the issuance of Waterworks and Sewer System Revenue Bonds in the amount of \$477,000. The proceeds were used for construction of a waste water treatment plant. The revenue bonds are scheduled to mature May 1, 2044, with an interest rate of 4.50%. The revenue bonds are payable solely from the net revenues derived from the operations of the City's water and sewer system. The City is in compliance with all significant requirements of this bond ordinance.

The City's compliance with the balances required as of June 30, 2011 in each account is as follows:

	<u>Balance Required</u>	<u>Balance Available</u>	<u>Excess (Deficiency)</u>
Series 2005 Revenue Bonds:			
Interest & Sinking Fund	6,506	6,784	278
Reserve Fund	10,000	10,090	90

Promissory Note

In previous years, the City entered into a promissory note with the Sabin River Authority (Authority) in the amount of \$288,062 to fund renovations and improvements to the water plant. In June 2011, the Authority forgave the balance due in the amount of \$216,879.

The City paid \$7,922 in interest expense for the scheduled debt service during the year ended June 30, 2011 under this promissory note.

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

The annual debt service requirements to maturity, including principal and interest, for the City's business type activities long term debt as of June 30, 2011, is as follows:

Year ending June 30,	
2012	74,995
2013	76,873
2014	79,322
2015	80,295
2016	26,855
2017-2021	131,740
2022-2026	130,300
2027-2031	131,565
2032-2036	127,365
2037-2041	122,870
2042-2044	89,000
Total principal and interest	1,071,180
Less interest	456,180
Total debt at June 30, 2011	615,000

Change in Long-Term Liabilities

Long term liability activity for the year ended June 30, 2011 was as follows:

	Beginning Balance	Issued	Retired	Ending Balance	Due in One Year
Business-type activities:					
Capital lease	181,972	-	181,972	-	-
Promissory Notes	235,503	-	235,503	-	-
Revenue bonds	656,000	-	41,000	615,000	41,000
Business-type activity, long-term liabilities	1,073,475	-	458,475	615,000	41,000

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

AGREEMENT TO PURCHASE WATER

On July 1, 1996, the City entered into a long term water supply agreement with the Sabine River Authority of Texas (Authority). The agreement requires the City to take and pay for a minimum monthly quantity of treated water of 18,000,000 gallons. The City will pay the Authority a monthly fee based on the unit cost for treated water. The unit cost is recalculated each year based on the total estimated annual cost for the next full contract year. Along with the forgiveness of debt by the Authority, this water supply agreement was terminated in June 2011. For the year ended June 30, 2011, the City's cost for treated water under this agreement was \$792,640.

On July 1, 2011, the City entered into a long term water supply contract with the Authority to purchase raw untreated water. The agreement initially requires the City to take and pay for a minimum of 500,000 gallons per day of untreated raw water.

WATER TREATMENT AND TRANSMISSION FACILITIES OPERATING AGREEMENT

On July 1, 1996, the City entered into a long term operating agreement with the Sabine River Authority of Texas (Authority). The agreement stipulates that the City will operate and maintain the treatment and transmission facilities as an independent contractor and shall be paid a monthly fee by the Authority based on the actual quantity of water purchased times the unit cost for treated water. Along with the forgiveness of debt by the Authority, this water treatment and operating agreement was terminated in June 2011. For the year ended June 30, 2011, the City earned \$810,796 under the operating agreement.

RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City maintains workers' compensation and other risks of loss coverage through the Texas Municipal League Intergovernmental Risk Pool, which is a public entity risk pool. The pool is to be self-sustaining through member premiums and obtains reinsurance through commercial insurance companies for claims in excess of dollar amount. City management believes such coverage is sufficient to preclude any significant uninsured losses to the City. Settled claims did not exceed the commercial coverage during the current fiscal year.

COMMITMENTS AND CONTINGENCIES

Grants

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

Intergovernmental grants received by the City are subject to audit and adjustment by the funding agency or its representatives. If grant revenues are received for expenditures which are subsequently disallowed, the City may be required to repay the revenues to the funding agency. In the opinion of City management, liabilities resulting from such disallowed expenditures, if any, will not be material to the accompanying financial statements as of June 30, 2011.

RETIREMENT PLAN

Plan Description

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

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

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

	Plan Year 2010	Plan year 2011
Employee deposit rate	5.0%	5.0%
Matching ratio (city to employee)	1 to 1	1 to 1
Years required for vesting	5	5
Service retirement eligibility (expresses as age/years of service)	60/5,0/25	60/5,0/25
Updates Service Credit	100% Repeating	100% Repeating
Annuity Increase (to retirees)	0% of CPI	0% of CPI

Contributions

Under the state law governing TMRS, the contribution rate for each city is determined annually by the actuary, using the Projected Unit Credit actuarial cost method. This rate consists of the normal

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

cost contribution rate and the prior service cost contribution rate, which is calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the portion of an active member's projected benefit allocated annually; the prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the applicable period for that city. Both the normal cost and prior service contribution rates include recognition of the projected impact of annually repeating benefits, such as Updated Service Credits and Annuity Increases.

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

Annual Required Contribution (ARC)	31,963
Interest on Net Pension Obligation	0
Adjustment to the ARC	0
Annual Pension Cost (APC)	31,963
Contributions Made	31,963
Increase (decrease) in net pension obligation	0
Net Pension Obligation/(Asset) beginning of year	0
Net Pension Obligation/(Asset), end of year	0

Three-year Trend Information

Accounting Year End	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
6/30/10	30,395	100%	---
6/30/09	29,935	100%	---
6/30/08	27,619	100%	---

The required contribution rates for fiscal year 2011 were determined as part of the December 31, 2008 and 2009 actuarial valuations. Additional information as of the latest actuarial valuation, December 31, 2010, also follows:

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

Valuation Date	12/31/08	12/31/09	12/31/10
Actuarial Cost Method	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit
Amortization Method	Level Percent of Payroll	Level Percent of Payroll	Level Percent of Payroll
GASB 25 Equivalent Single Amortization Period	24 years; closed period	24 years; closed period	25 years; closed period
Amortization Period for new Gains/Losses	25 years	22.4 years	25 years
Asset Valuation Method	Amortized Cost	10 Year Smoothed Market	10 Year Smoothed Market
Actuarial Assumptions			
Investment Rate of Return*	7.50%	7.50%	7.50%
Projected Salary Increases*	Varies by age and service	Varies by age and service	Varies by age and service
*Includes Inflation at	3.00%	3.00%	3.00%
Cost-of-Living Adjustment	0.00%	0.00%	0.00%

Funded Status and Funding Progress - In June 2011, SB350 was enacted by the Texas Legislature, resulting in a restructure of the TMRS funds. This legislation provided for the actuarial valuation to be completed, as if restructuring had occurred on December 31, 2010. In addition, the actuarial assumptions were updated for the new fund structure, based on an actuarial experience study that was adopted by the TMRS Board at their May, 2011 meeting. For a complete description of the combined impact of the legislation and new actuarial assumptions, including the effects on TMRS City rates and funding ratios, please see the December 31, 2010 TMRS Comprehensive Annual Financial Report.

The funded status as of December 31, 2010, is presented as follows:

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2011

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Funded Ratio	Unfunded AAL (UAAL)	Covered Payroll	UAAL as a Percentage of Covered Payroll
12/31/10 (1)	\$1,244,810	\$1,216,419	102.3%	\$(28,391)	\$871,799	(3.3%)
12/31/10 (2)	\$1,506,566	\$1,294,391	116.4%	\$(212,175)	\$871,799	(24.3%)

(1) Actuarial valuation performed under the original fund structure.

(2) Actuarial valuation performed under the new fund structure.

Schedule of Funding Progress:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Funded Ratio	Unfunded AAL (UAAL)	Covered Payroll	UAAL as a Percentage of Covered Payroll
12/31/08	\$1,154,757	\$1,130,755	102.1%	\$(24,002)	\$850,235	-2.8%
12/31/09	\$1,122,589	\$1,106,120	101.5%	\$(16,469)	\$878,589	-1.9%
12/31/10	\$1,506,566	\$1,294,391	116.4%	\$(212,175)	\$871,799	-24.3%

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

The death benefit for active employees provides a lump-sum payment approximately equal to the employee’s annual salary (calculated based on the employee’s actual earnings, for the 12-month period preceding the month of death); retired employees are insured for \$7,500; this coverage is an “other post employment 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 one-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 upcoming year; the intent is not to pre-fund retiree life insurance during employees’ entire careers. The City’s contribution to the TMRS SDBF for the fiscal years ended 2011, 2010, and 2009 were \$2,381, \$2,366, and \$2,521, respectively, which equaled the required contributions each year.

Budgetary Comparison Reporting

CITY OF HEMPHILL, TEXAS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE - BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2011

	Budgeted Amounts		Actual Amounts	Variance With Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Taxes:				
Sales taxes	402,885	402,885	407,814	4,929
Franchise taxes	6,333	6,333	4,243	(2,090)
Permits, fees & assessments	26,108	26,108	7,665	(18,443)
Fines	7,386	7,386	13,808	6,422
Charges for services	216,122	216,122	218,454	2,332
Interest income	3,329	3,329	1,693	(1,636)
Intergovernmental	68,015	68,015	231,526	163,511
Contributions and donations	1,100	1,100	1,800	700
Other	14,466	21,966	20,525	(1,441)
Total revenues	745,744	753,244	907,528	154,284
EXPENDITURES				
Current:				
General government:				
Finance and administration	359,462	364,257	364,477	(220)
Municipal court	22,034	22,450	28,309	(5,859)
Public safety:				
Fire	24,234	24,234	22,027	2,207
Police	193,215	196,185	181,240	14,945
Streets	111,952	113,824	100,379	13,445
Sanitation	193,987	194,063	205,948	(11,885)
Parks and recreation	43,222	43,354	25,604	17,750
Health and welfare	22,247	22,659	21,249	1,410
Cemetary	6,900	6,900	3,460	3,440
Debt service	-	-	-	-
Capital outlay	-	-	205,765	(205,765)
Total expenditures	977,253	987,926	1,158,458	(170,532)
Excess (deficiency) of revenues over expenditures	(231,509)	(234,682)	(250,930)	(16,248)
OTHER FINANCING SOURCES (USES)				
Transfers in	241,098	241,098	241,098	-
Total other financing sources (uses)	241,098	241,098	241,098	-
Net change in fund balance	9,589	6,416	(9,832)	(16,248)
Fund balance - beginning	91,663	91,663	91,663	-
Fund balance - ending	101,252	98,079	81,831	(16,248)

See accompanying notes to the financial statements

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Other Schedules

**CITY OF HEMPHILL, TEXAS
GENERAL FUND
SCHEDULE OF CURRENT EXPENDITURES BY DEPARTMENT
BUDGET AND ACTUAL FOR THE YEAR ENDED JUNE 30, 2011**

General Government	Budget	Actual	Variance favorable (unfavorable)
Administration:			
Personnel	258,818	279,116	(20,298)
Supplies and materials	10,788	16,293	(5,505)
Maintenance and repairs	18,316	20,931	(2,615)
Contractual services	41,243	38,156	3,087
Miscellaneous	52,331	38,290	14,041
Total administration	381,496	392,786	(11,290)
Public Safety			
Fire Department:			
Personnel	2,265	600	1,665
Supplies and materials	9,512	7,749	1,763
Maintenance and repairs	5,552	8,186	(2,634)
Contractual services	4,534	4,347	187
Miscellaneous	2,371	1,145	1,226
Total fire department	24,234	22,027	2,207
Police department:			
Personnel	165,650	158,866	6,784
Supplies and materials	14,428	15,442	(1,014)
Maintenance and repairs	4,237	2,739	1,498
Contractual services	5,385	2,980	2,405
Miscellaneous	3,515	1,213	2,302
Total police department	193,215	181,240	11,975
Total public safety	217,449	203,267	14,182
Sanitation			
Personnel	5,750	4,042	1,708
Supplies and materials	1,560	5,885	(4,325)
Maintenance and repairs	600	598	2
Contractual services	185,827	189,458	(3,631)
Miscellaneous	250	5,965	(5,715)
Total sanitation	193,987	205,948	(11,961)

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
GENERAL FUND
SCHEDULE OF CURRENT EXPENDITURES BY DEPARTMENT
BUDGET AND ACTUAL FOR THE YEAR ENDED JUNE 30, 2011**

	Budget	Actual	Variance favorable (unfavorable)
Streets			
Personnel	82,532	82,713	(181)
Supplies and materials	24,181	10,735	13,446
Maintenance and repairs	2,915	811	2,104
Contractual services	2,324	6,120	(3,796)
Miscellaneous	-	-	-
Total streets	111,952	100,379	11,573
Parks and recreation			
Personnel	16,368	10,692	5,676
Supplies and materials	16,466	2,967	13,499
Maintenance and repairs	3,955	7,503	(3,548)
Contractual services	4,878	4,442	436
Miscellaneous	1,555	-	1,555
Total parks and recreation	43,222	25,604	17,618
Health and welfare			
Personnel	19,546	20,307	(761)
Supplies and materials	1,781	829	952
Maintenance and repairs	550	-	550
Contractual services	270	113	157
Miscellaneous	100	-	100
Total health and welfare	22,247	21,249	998
Cemetery			
Supplies and materials	100	-	100
Maintenance and repairs	6,300	3,460	2,840
Contractual services	500	-	500
Miscellaneous	-	-	-
Total cemetery	6,900	3,460	3,440
Total current expenditures	977,253	952,693	24,560

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
UTILITY FUND
SCHEDULE OF EXPENDITURES BY DEPARTMENT
BUDGET AND ACTUAL FOR THE YEAR ENDED JUNE 30, 2011**

	Budget	Actual	Variance favorable (unfavorable)
Electric Department			
Personnel	146,887	172,622	(25,735)
Supplies and materials	109,482	88,460	21,022
Maintenance and repairs	2,767	5,699	(2,932)
Contractual services	1,500	8,547	(7,047)
Cost of services	1,347,868	1,398,922	(51,054)
Depreciation	35,348	46,103	(10,755)
Other operating expenses	2,750	339	2,411
Total electric department	1,646,602	1,720,692	(74,090)
Gas department			
Supplies and materials	16,979	10,057	6,922
Maintenance and repairs	100	-	100
Contractual services	3,839	2,703	1,136
Cost of services	123,350	125,078	(1,728)
Depreciation	25,927	25,246	681
Other operating expenses	1,694	1,744	(50)
Total gas department	171,889	164,828	7,061
Water department			
Supplies and materials	38,127	34,627	3,500
Maintenance and repairs	2,112	164	1,948
Contractual services	951	336	615
Depreciation	22,258	20,956	1,302
Other operating expenses	2,097	3,631	(1,534)
Total water department	65,545	59,714	5,831

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
UTILITY FUND
SCHEDULE OF EXPENDITURES BY DEPARTMENT
BUDGET AND ACTUAL FOR THE YEAR ENDED JUNE 30, 2011**

	Budget	Actual	Variance favorable (unfavorable)
Sewer department			
Personnel	43,205	47,487	(4,282)
Supplies and materials	71,051	64,123	6,928
Maintenance and repairs	10,573	15,927	(5,354)
Contractual services	12,387	17,941	(5,554)
Depreciation	100,913	105,032	(4,119)
Other operating expenses	7,780	6,068	1,712
Total sewer department	245,909	256,578	(10,669)
Warehouse			
Personnel	329,981	310,520	19,461
Supplies and materials	41,901	44,172	(2,271)
Maintenance and repairs	5,201	15,345	(10,144)
Contractual services	18,555	35,179	(16,624)
Depreciation	21,052	24,417	(3,365)
Miscellaneous	22,392	33,719	(11,327)
Total warehouse	439,082	463,352	(24,270)
Water plant			
Personnel	150,657	128,910	21,747
Supplies and materials	119,922	118,221	1,701
Maintenance and repairs	23,017	9,130	13,887
Contractual services	22,512	22,768	(256)
Cost of services	813,859	830,946	(17,087)
Depreciation	110,626	128,561	(17,935)
Other operating expenses	13,033	11,949	1,084
Total water plant	1,253,626	1,250,485	3,141
Total expenditures	3,822,653	3,915,649	(92,996)

See accompanying notes to the financial statements

Statistical Tables

CITY OF HEMPHILL, TEXAS

SCHEDULE OF INSURANCE POLICIES IN FORCE

JUNE 30, 2011

Insurer	Amount of Coverage	Risk Covered	Expiration Date
Texas Municipal League Intergovernmental Risk Pool	\$2,000,000	Comprehensive General liability	10-01-11
	\$2,000,000	Sudden events - Pollution	10-01-11
	\$2,000,000	Automobile liability	10-01-11
	\$2,000,000	Law enforcement liability	10-01-11
	\$2,000,000	Errors and omissions	10-01-11
	\$3,410,900	Real and personal property	10-01-11
	\$500,000	Boiler and machinery accident	10-01-11
	As scheduled	Automobile physical damage	10-01-11
	\$268,684	Mobile equipment	10-01-11
	Statutory	Workers compensation	10-01-11
Texas Water Conservation Association Risk Management	\$1,455,755	Water treatment plant facilities and equipment	06-30-10

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FEDERAL AWARDS SECTION



Certified Public Accountants

Goff & Herrington, P.C.

A.J. Goff, CPA
Ronnie Herrington, CPA

P.O. Box 153320 • Lufkin, TX. 75915-3320 • (936) 875-3317 • Fax:(936) 622-6823

**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 AUDIT STANDARDS**

Honorable Mayor and Members of the City Council
City of Hemphill, Texas

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Hemphill, Texas (City) as of and for the year ended June 30, 2011, which collectively comprise the City's basic financial statements and have issued our report thereon dated November 4, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

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 AUDIT STANDARDS

Honorable Mayor and Members of the City Council
City of Hemphill, Texas
Page 2

Compliance and Other Matters

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

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

Goff & Herrington, P.C.

GOFF & HERRINGTON
Certified Public Accountants

November 4, 2011

**CITY OF HEMPHILL, TEXAS
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2011**

No findings reported.

**CITY OF HEMPHILL, TEXAS
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2011**

No prior audit findings reported.

**CITY OF HEMPHILL, TEXAS
CORRECTIVE ACTION PLAN
FOR THE YEAR ENDED JUNE 30, 2011**

None required.

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