

CITY OF HEMPHILL, TEXAS
ANNUAL FINANCIAL REPORT
FOR THE YEAR ENDED JUNE 30, 2008

CITY OF HEMPHILL, TEXAS
Annual Financial Report
For the Year Ended June 30, 2008

Table of Contents

	Page
FINANCIAL SECTION	
Independent Auditor's Report	1-2
Management's Discussion and Analysis	3-10
Basic Financial Statements:	
Government-wide Financial Statements:	
Statement of Net Assets	11
Statement of Activities	12-13
Fund Financial Statements:	
Balance Sheet - Governmental Funds	14
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets	15
Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds	16
Reconciliation of the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances to the Statement of Activities	17
Statement of Net Assets - Proprietary Fund	18
Statement of Revenues, Expenses, and Changes in Fund Net Assets - Proprietary Fund	19
Statement of Cash Flows - Proprietary Fund	20
Notes to the Financial Statements	21-35
Budgetary Comparison Reporting:	
Statement of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual - General Fund	36
Other Schedules:	
Schedule of General Fund Current Expenditures by Department - Budget and Actual	37-38
Schedule of Utility Fund Expenditures by Department - Budget and Actual	39-40
Statistical Tables:	
Schedule of Insurance Policies in Force	41

CITY OF HEMPHILL, TEXAS
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For the Year Ended June 30, 2008

Table of Contents

	Page
FEDERAL AWARDS SECTION	
Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <u>Government Auditing Standards</u>	42-43
Schedule of Findings	44
Schedule of Prior Audit Findings	45
Corrective Action Plan	46

FINANCIAL SECTION



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Certified Public Accountants

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, 2008, 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, 2008, 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 3, 2008, 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 important for assessing the results of our audit.

Independent Auditor's Report

Honorable Mayor and Members of City Council

City of Hemphill, Texas

Page 2

Management's discussion and analysis on pages 3 through 10 and the budgetary comparison schedule on page 36 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The other schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements. The other schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Pipes & Associates

PIPES & ASSOCIATES

Certified Public Accountants

November 3, 2008

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, 2008. 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 \$4,868,532 as of June 30, 2008. Of this amount, \$1,008,364 (unrestricted net assets) may be used to meet the City's continuing obligations to citizens, customers and creditors.
- ▶ During the year ended June 30, 2008, the City's net assets **increased** by \$17,844.
- ▶ Total long-term debt of the City decreased by \$72,109 to \$1,163,137 during the current fiscal year.
- ▶ At the end of the current fiscal year, unreserved fund balance for the general fund was \$93,660 or 10.4 percent of total general fund 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 governmental-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.

Other information - In addition to the basic financial statements and accompanying notes, this

MANAGEMENT'S DISCUSSION AND ANALYSIS

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 \$4,868,532 at the close of the fiscal year.

By far the largest portion of the City's net assets (77.9 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	
	2008	2007	2008	2007	2008	2007
Current and Other Assets	130,111	161,139	1,326,255	1,683,986	1,456,366	1,845,125
Capital and Non-Current	566,115	490,960	4,391,798	4,312,306	4,957,913	4,803,266
Total Assets	696,226	652,099	5,718,053	5,996,292	6,414,279	6,648,391
Other Liabilities	36,451	52,831	346,159	509,626	382,610	562,457
Long Term Liabilities	-	6,629	1,163,137	1,228,617	1,163,137	1,235,246
Total Liabilities	36,451	59,460	1,509,296	1,738,243	1,545,747	1,797,703
Net Assets:						
Investment in Capital Assets,						
Net of Related Debt	566,115	484,331	3,228,661	3,083,689	3,794,776	3,568,020
Restricted	-	-	78,369	64,487	78,369	64,487
Unrestricted	93,660	108,308	901,727	1,109,873	995,387	1,218,181
Total Net Assets	659,775	592,639	4,208,757	4,258,049	4,868,532	4,850,688

A portion of the City's net assets (1.3 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 \$995,387 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.

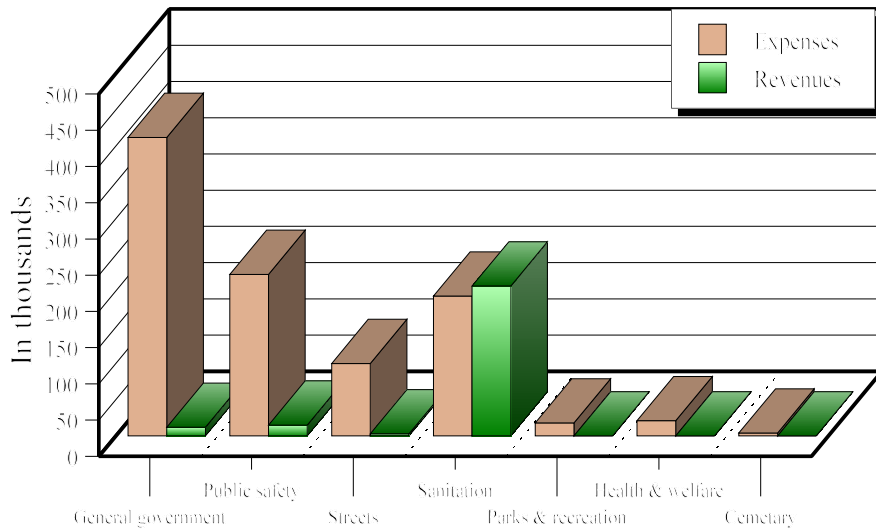
Changes in the City's Net Assets

	Governmental Activities		Business-type activities		Total	
	2008	2007	2008	2007	2008	2007
Revenues:						
Program Revenues:						
Charges for services	225,977	200,053	3,430,858	3,370,983	3,656,835	3,571,036
Operating grants	1,063	2,862	-	-	1,063	2,862
Capital grants	11,753	76,053	184,400	524,550	196,153	600,603
General Revenues:						
Sales taxes	358,912	479,023	-	-	358,912	479,023
Other taxes	7,278	7,558	-	-	7,278	7,558
Other	66,605	73,840	36,180	39,716	102,785	113,556
Total revenues	671,588	839,389	3,651,438	3,935,249	4,323,026	4,774,638
Expenses:						
General government	411,505	376,225	-	-	411,505	376,225
Public safety	222,634	218,884	-	-	222,634	218,884
Streets	100,265	102,422	-	-	100,265	102,422
Sanitation	193,077	168,430	-	-	193,077	168,430
Parks and recreation	18,135	12,877	-	-	18,135	12,877
Health and welfare	20,913	20,413	-	-	20,913	20,413
Cemetary	4,490	4,675	-	-	4,490	4,675
Debt service	201	641	-	-	201	641
Electric	-	-	1,680,885	1,486,453	1,680,885	1,486,453
Natural gas	-	-	330,557	271,068	330,557	271,068
Water	-	-	997,264	967,392	997,264	967,392
Sewer	-	-	325,256	233,467	325,256	233,467
Total expenses	971,220	904,567	3,333,962	2,958,380	4,305,182	3,862,947
Transfers	366,768	110,000	(366,768)	(110,000)	-	-
Increase in net assets	67,136	44,822	(49,292)	866,869	17,844	911,691
Beginning net assets	592,639	547,817	4,258,049	3,391,180	4,850,688	3,938,997
Ending net assets	659,775	592,639	4,208,757	4,258,049	4,868,532	4,850,688

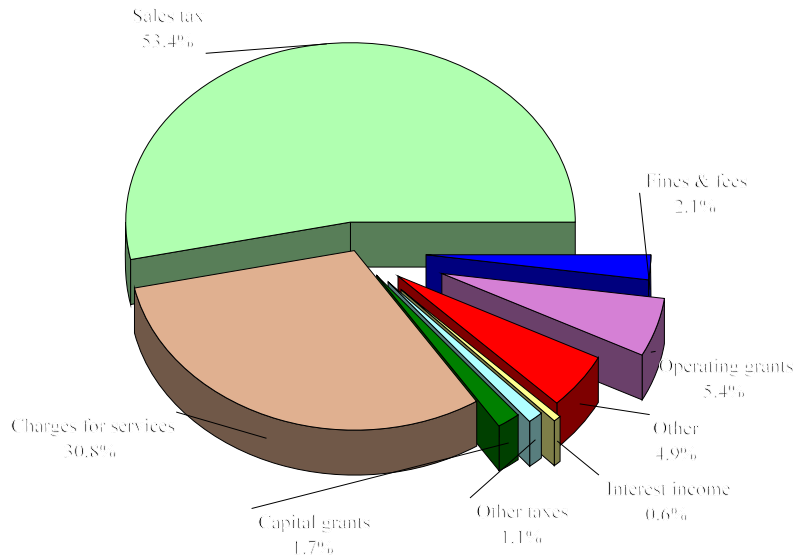
MANAGEMENT'S DISCUSSION AND ANALYSIS

Governmental Activities. Governmental activities increased the City's net assets by \$67,136 contributing to the overall increase in the City's total net assets.

Expenses and Program Revenues - Governmental Activities



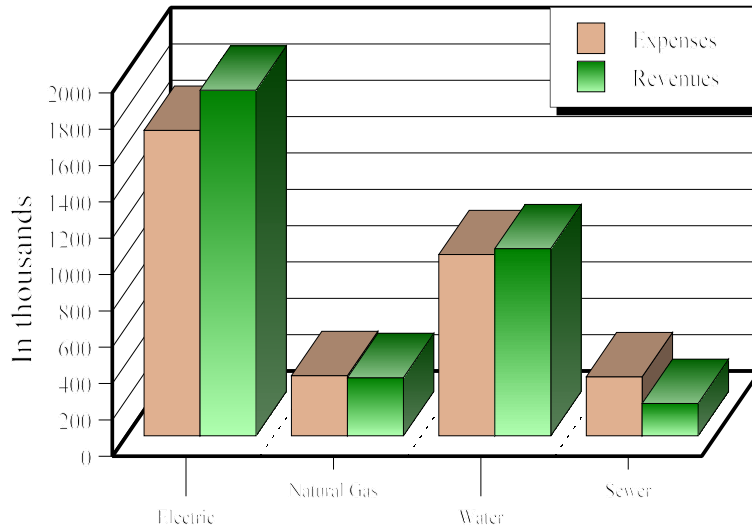
Revenues by Source - Governmental Activities



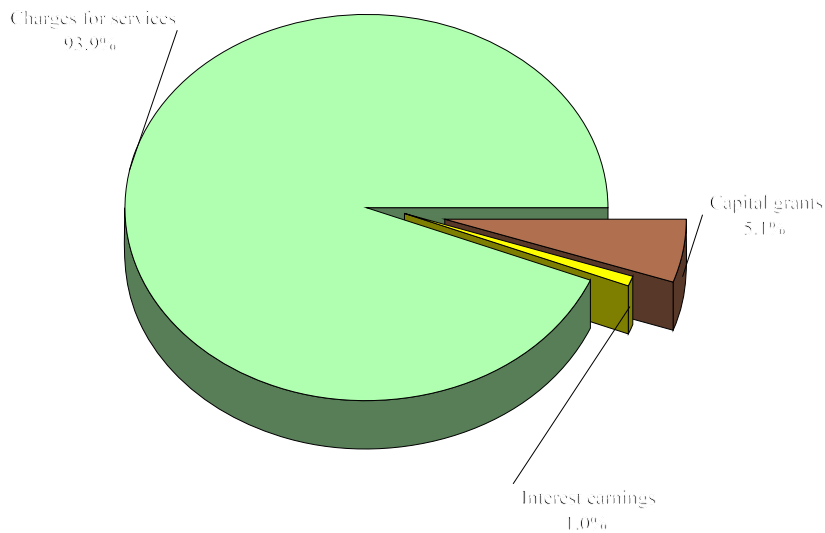
MANAGEMENT'S DISCUSSION AND ANALYSIS

Business-type Activities. Business-type activities decreased the City's net assets by \$49,292, partially offsetting the increase generated by the governmental activities.

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 \$93,660, a decrease of \$14,648 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 \$901,727.

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:

- ▶ \$55,000 increase in the Street department capital outlay.
- ▶ \$10,000 increase in the Fire department capital outlay.
- ▶ \$12,500 increase in the Park department capital outlay.
- ▶ \$2,500 increase in the General Government department capital outlay.

These capital outlay budget increases were to provide for street paving, equipment purchases, and land clearing

Capital Asset and Debt Administration

Capital Assets. At the end of the current fiscal year, the City's investment in capital assets for its governmental and business type activities amounts to \$4,957,913 (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	
	2008	2007	2008	2007	2008	2007
Land	88,290	53,653	79,523	79,523	167,813	133,176
Buildings & improvements	269,386	182,238	-	-	269,386	182,238
Utility systems	-	-	3,950,690	4,062,474	3,950,690	4,062,474
Property - capital lease	-	-	12,367	30,917	12,367	30,917
Vehicles and equipment	208,439	255,069	115,336	125,292	323,775	380,361
Construction in progress	-	-	233,882	14,100	233,882	14,100
Net capital assets	<u>566,115</u>	<u>490,960</u>	<u>4,391,798</u>	<u>4,312,306</u>	<u>4,957,913</u>	<u>4,803,266</u>

MANAGEMENT DISCUSSION AND ANALYSIS

More detailed information about the City's capital assets is presented in the notes to the financial statements. Construction in progress at year end is related to a low water intake structure at the water treatment plant.

Long-term debt. At the end of the current fiscal year, the City had total long term debt of \$1,128,137.

	City's Outstanding Debt					
	Governmental Activities		Business-type activities		Total	
	2008	2007	2008	2007	2008	2007
Revenue bonds	-	-	692,000	727,000	692,000	727,000
Capital lease	-	-	193,093	203,949	193,093	203,949
Promissory notes	-	-	243,044	248,809	243,044	248,809
Bank loans	-	6,629	-	18,859	0	25,488
Net capital assets	-	6,629	1,128,137	1,198,617	1,128,137	1,205,246

The City's total long term debt decreased by \$77,109 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.

Economic Factors and Next Year's Budgets and Rates

The City considered many factors when setting the fiscal year 2008-2009 budget, including estimated sales tax receipts and fees that will be charged for business-type activities. The City estimates a net increase in general fund revenues due to an increase in sales tax revenue. The other ongoing general fund revenue items (charges for services, etc.) should generate similar revenues as the prior year. The City has budgeted funds for an additional police officer in the General Fund budget. The City's business-type activities budget reflects increased utility rates of 6% to offset increases in energy, fuel, and other supplier costs.

The City anticipates spending \$187,400 in capital improvements during fiscal year 2008-2009. These include technology equipment purchases, vehicles, and completion of low water intake structure at the water treatment plant, utility system improvements, and park improvements.

If these estimates realized, the City's budgetary general fund balance and utility reserves are expected to increase modestly by the close of 2009.

Request for Information

This financial report is designed to provide our citizens, taxpayers, customers, and 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, 2008**

	Primary Government		
	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and cash equivalents	70,956	829,376	900,332
Sales tax receivable	25,486	-	25,486
Accounts receivable	-	359,982	359,982
Inventories	-	6,840	6,840
Deferred charges	-	30,419	30,419
Restricted assets:			
Cash and cash equivalents	33,669	99,638	133,307
Capital Assets (net of accumulated depreciation):			
Land	88,290	79,523	167,813
Other capital assets, net of depreciation	477,825	4,312,275	4,790,100
Total assets	696,226	5,718,053	6,414,279
LIABILITIES			
Accounts payable	18,116	208,181	226,297
Accrued expenses	18,335	24,570	42,905
Accrued interest payable	-	10,603	10,603
Customer meter deposits	-	102,805	102,805
Long Term Liabilities:			
Due within one year	-	53,229	53,229
Due after one year	-	1,109,908	1,109,908
Total liabilities	36,451	1,509,296	1,545,747
NET ASSETS			
Invested in capital assets, net of related debt	566,115	3,228,661	3,794,776
Restricted for other purposes	-	78,369	78,369
Unrestricted net assets	93,660	901,727	995,387
Total net assets	659,775	4,208,757	4,868,532

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2008**

Functions/Programs	Program Revenues		
	Expenses	Charges for Services	Operating Grants and Contributions
Governmental activities:			
General government	411,505	318	-
Public safety	222,634	13,883	813
Streets	100,265	2,624	-
Sanitation	193,077	206,717	-
Parks and recreation	18,135	-	-
Health and welfare	20,913	285	-
Cemetery	4,490	2,150	250
Interest on long term debt	201	-	-
Total governmental activities	971,220	225,977	1,063
Business-type activities:			
Electric	1,680,885	1,902,128	-
Natural gas	330,557	320,469	-
Water	997,264	1,030,026	-
Sewer	325,256	178,235	-
Total business-type activities	3,333,962	3,430,858	-
	4,305,182	3,656,835	1,063

General revenues:
 Sales taxes
 Franchise taxes
 Miscellaneous
 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
11,753	(399,434)	-	(399,434)
-	(207,938)	-	(207,938)
-	(97,641)	-	(97,641)
-	13,640	-	13,640
-	(18,135)	-	(18,135)
-	(20,628)	-	(20,628)
-	(2,090)	-	(2,090)
-	(201)	-	(201)
11,753	(732,427)	-	(732,427)
-	-	221,243	221,243
-	-	(10,088)	(10,088)
171,400	-	204,162	204,162
13,000	-	(134,021)	(134,021)
184,400	-	281,296	281,296
196,153	(732,427)	281,296	(451,131)
	358,912	-	358,912
	7,278	-	7,278
	27,535	-	27,535
	35,033	-	35,033
	4,037	36,180	40,217
	366,768	(366,768)	-
	799,563	(330,588)	468,975
	67,136	(49,292)	17,844
	592,639	4,258,049	4,850,688
	-	-	-
	659,775	4,208,757	4,868,532

See accompanying notes to the financial statements

Fund Financial Statements

**CITY OF HEMPHILL, TEXAS
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2008**

	General Fund	Other Governmental Funds	Total Governmental Funds
ASSETS			
Cash and cash equivalents	70,956	-	70,956
Sales tax receivable	25,486	-	25,486
Cash and cash equivalents - restricted	33,669	-	33,669
Total assets	130,111	-	130,111
LIABILITIES AND FUND BALANCES			
Liabilities:			
Accounts payable	18,116	-	18,116
Accrued liabilities	18,335	-	18,335
Total liabilities	36,451	-	36,451
Fund balances:			
Unreserved and undesignated	93,660	-	93,660
Total fund balances	93,660	-	93,660
Total liabilities and fund balances	130,111	-	130,111

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, 2008

Total fund balances - governmental funds	93,660
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 \$825,866 and the accumulated depreciation was \$334,906. The effect of including beginning balances for capital assets (net of depreciation) in the governmental activities is to increase (decrease) net assets.	490,960
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.	75,155
Long term liabilities are not due and payable in the current period and therefore are not reported in the funds.	<u>-</u>
Net assets of governmental activities	<u><u>659,775</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, 2008

	General Fund	Other Governmental Funds	Total Governmental Funds
REVENUES			
Taxes:			
Sales taxes	358,912	-	358,912
Franchise taxes	7,278	-	7,278
License and permits	135	-	135
Fines	14,086	-	14,086
Charges for services	206,717	-	206,717
Interest income	4,037	-	4,037
Intergovernmental	47,601	-	47,601
Contributions and donations	2,400	-	2,400
Other	30,421	-	30,421
Total revenues	671,587	-	671,587
EXPENDITURES			
Current:			
General government:			
Finance and administration	371,780	-	371,780
Municipal court	26,432	-	26,432
Public safety:			
Fire	17,146	-	17,146
Police	156,623	-	156,623
Streets	99,825	-	99,825
Sanitation	193,077	-	193,077
Parks and recreation	11,083	-	11,083
Health and welfare	19,858	-	19,858
Cemetery	4,490	-	4,490
Debt service	6,828	-	6,828
Capital outlay	145,861	-	145,861
Total expenditures	1,053,003	-	1,053,003
Excess (deficiency) of revenues over expenditures	(381,416)	-	(381,416)
OTHER FINANCING SOURCES (USES)			
Transfers in	366,768	-	366,768
Total other financing sources and uses	366,768	-	366,768
Net change in fund balance	(14,648)	-	(14,648)
Fund balance - beginning	108,308	-	108,308
Fund balance - ending	93,660	-	93,660

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, 2008**

Net change in fund balances - governmental funds	(14,648)
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.	145,861
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.	(70,705)
The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of the governmental funds. The net effect of removing principal payments is to increase net assets.	<u>6,628</u>
Change in net assets of governmental activities	<u><u>67,136</u></u>

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
STATEMENT OF NET ASSETS
PROPRIETARY FUND
JUNE 30, 2008**

ASSETS

Current assets:	
Cash and cash equivalents	829,376
Accounts receivable	359,982
Inventories	6,840
Total current assets	1,196,198
Noncurrent assets:	
Restricted cash and cash equivalents	99,638
Deferred charges	30,419
Capital assets:	
Land	79,523
Other capital assets, net of depreciation	4,312,275
Total noncurrent assets	4,521,855
Total assets	5,718,053

LIABILITIES

Current liabilities:	
Accounts payable	208,181
Accrued expenses	24,570
Accrued interest payable	10,603
Current portion of:	
Capital leases	11,120
Promissory note	7,109
Revenue bonds payable	35,000
Total current liabilities	296,583
Noncurrent liabilities:	
Capital leases	181,973
Promissory note	235,935
Revenue bonds payable	692,000
Customer deposits	102,805
Total noncurrent liabilities	1,212,713
Total liabilities	1,509,296

NET ASSETS

Invested in capital assets, net of related debt	3,228,661
Restricted for debt service	78,369
Unrestricted	901,727
Total net assets	4,208,757
Total liabilities and net assets	5,718,053

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, 2008

Operating revenues:	
Water sales	1,021,041
Sewer charges	176,648
Electric sales	1,885,535
Gas sales	317,684
Other services	<u>29,950</u>
Total operating revenues	<u>3,430,858</u>
 Operating expenses:	
Personnel	540,886
Supplies and materials	383,708
Maintenance and repairs	39,143
Contractual services	53,046
Cost of services	1,879,894
Depreciation	311,220
Other operating	<u>54,008</u>
Total operating expenses	<u>3,261,905</u>
Operating income	168,953
 Nonoperating revenues (expenses):	
Interest income	36,180
Capital grant	184,400
Interest expense	<u>(72,057)</u>
Total nonoperating revenue (expenses)	148,523
Income before transfers	317,476
Transfers to other funds	<u>(366,768)</u>
Change in net assets	(49,292)
Total net assets - beginning	<u>4,258,049</u>
Total net assets - ending	<u><u>4,208,757</u></u>

See accompanying notes to the financial statements

**CITY OF HEMPHILL, TEXAS
STATEMENT OF CASH FLOWS
PROPRIETARY FUND
FOR THE YEAR ENDED JUNE 30, 2008**

Cash flows from operating activities:	
Receipts from customers	3,355,861
Payments to suppliers and contractors	(2,393,887)
Payments to employees	(544,082)
Net cash provided by (used for) operating activities	417,892
Cash flows from noncapital financing activities:	
Operating transfers	(366,768)
Net cash provided by (used for) noncapital activities	(366,768)
Cash flows from capital and related financing activities:	
Capital grant received	198,600
Purchases of capital assets	(569,794)
Principal paid on capital debt	(65,480)
Interest paid on capital debt	(71,277)
Net cash provided by (used for) capital activities	(507,951)
Cash flows from investing activities:	
Interest received	36,180
Net cash provided by (used for) investing activities	36,180
Net increase (decrease) in cash and cash equivalents	(420,647)
Cash and cash equivalents, beginning	1,349,661
Cash and cash equivalents, ending	929,014
Reconciliation of operating income to net cash used by operating activities:	
Operating income	168,953
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	311,220
Changes in assets and liabilities:	
(Increase) decrease in accounts receivable	(78,011)
(Increase) decrease in supply inventory	(436)
Increase (decrease) in accounts payable	15,756
Increase (decrease) in accrued liabilities	(739)
Increase (decrease) in customer meter deposits	1,149
Net cash provided by operating activities	417,892

See accompanying notes to the financial statements

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

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.

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.

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

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

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.

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

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

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 \$5,000 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 not capitalized.

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

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. Unreserved fund balance in the governmental fund financial statements represents that portion of fund balance that is available for budgeting in future periods.

Compensated Absences - The City allows employees to accumulate sick leave and vacation time. Upon termination, the City pays any accumulated vacation that was not used. Accumulated sick leave is not paid upon termination. The liability for accrued vacation is recorded in the applicable funds. The amount expected to be paid from current resources is not significant.

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.

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.

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

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 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, 2008 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, 2008, the bank balances of the City's deposits (demand and certificates) were \$1,136,018. 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, 2008 as follows:

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

FDIC Insurance	300,000
Market value of securities pledged	<u>1,825,394</u>
Total coverage	<u>2,125,394</u>

Investments

Custodial Credit Risk - Investments. For an investment, this is the risk that, in the event of the failure of the counterparty, the City will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The City's investments in money market accounts and certificates of deposits were not exposed to custodial risk.

Interest Rate Risk. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Investments held for longer periods are subject to increased risk of adverse interest rate changes. The City's policy provides that to the extent practicable, investments are matched with anticipated cash flows. Certificates of deposit may not be purchased with maturities greater than one year from date of purchase.

Concentration of Credit Risk. The City places no limit on the amount the City may invest in any one issuer. Investments are governed by the objectives of preservation and safety of principal, liquidity, and yield. More than 5% of the City's investments are at First State Bank (100.0%).

The City's investments as of June 30, 2008 are with the depository bank in certificates of deposit in the amount of \$894,291.

Restricted deposits - Resources set aside for repayment of revenue bonds and for construction of utility system improvements are classified as restricted assets in the statement of net assets since their use is limited by bond covenants or Council authorization. At June 30, 2008, the City's business type activities restricted assets consisted of \$78,369 for debt service and \$21,269 for construction. The governmental activities restricted assets consisted of \$767 for training of volunteer fire department personnel, \$7,799 for cemetery operations, \$2,005 for police department functions, and \$23,098 for disaster recovery.

PROPERTY TAXES

The City did not levy property taxes in October, 2007. An allowance in the amount of \$2,224 is established for the entire balance of property taxes due to the City.

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

DUE FROM OTHER GOVERNMENTS

Amount due from other governments as of June 30, 2008 is \$25,486 for sales tax due from the State of Texas.

CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2008 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	53,653	34,637	-	88,290
Capital assets, being depreciated:				
Buildings and improvements	297,446	102,554	-	400,000
Vehicles and equipment	474,767	8,669	-	483,436
Total capital assets being depreciated	<u>772,213</u>	<u>111,223</u>	<u>0</u>	<u>883,436</u>
Less accumulated depreciation for:				
Buildings and improvements	115,208	15,406	-	130,614
Vehicles and equipment	219,698	55,299	-	274,997
Total accumulated depreciation	<u>334,906</u>	<u>70,705</u>	<u>0</u>	<u>405,611</u>
Total capital assets, being depreciated, net	<u>437,307</u>	<u>40,518</u>	<u>-</u>	<u>477,825</u>
Governmental activities capital assets, net	<u><u>490,960</u></u>	<u><u>75,155</u></u>	<u><u>-</u></u>	<u><u>566,115</u></u>

Business-type activities:

Capital assets, not being depreciated:

Land	79,523		-	79,523
Construction in progress	14,100		219,782	233,882
Total capital assets, not being depreciated	<u>93,623</u>	<u>-</u>	<u>219,782</u>	<u>313,405</u>

Capital assets, being depreciated:

Buildings and improvements	32,500	-	-	32,500
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CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements/ Adjustments</u>	<u>Ending Balance</u>
Utility systems	7,725,628	148,869	-	7,874,497
Vehicles and equipment	629,610	22,061	-	651,671
Property under capital lease	350,000	-	-	350,000
Totals at cost	<u>8,737,738</u>	<u>170,930</u>	<u>0</u>	<u>8,908,668</u>
Less accumulated depreciation:				
Buildings and improvements	32,500	-	-	32,500
Utility system	3,663,336	260,471	-	3,923,807
Vehicles and equipment	504,136	32,199	-	536,335
Property under capital lease	319,083	18,550	-	337,633
Total accumulated depreciation	<u>4,519,055</u>	<u>311,220</u>	<u>0</u>	<u>4,830,275</u>
Total capital assets, being depreciated, net	<u>4,218,683</u>	<u>(140,290)</u>	<u>0</u>	<u>4,078,393</u>
Business-type activities capital assets, net	<u>4,312,306</u>	<u>(140,290)</u>	<u>219,782</u>	<u>4,391,798</u>

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

Governmental activities:

General government	13,293
Public safety	48,865
Streets	440
Health and welfare	1,055
Parks and recreation	<u>7,052</u>
Total depreciation expense - governmental activities	<u>70,705</u>

Business-type activities:

Overhead	26,297
Water	22,572
Sewer	95,840
Natural Gas	25,801
Electric	32,147
Water Plant	<u>108,563</u>
Total depreciation expense - business-type activities	<u>311,220</u>

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

CAPITAL LEASE

The City has 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.

The lease agreement was entered into in September, 1980 and went into effect in 1981. This contract was entered into to provide for the additional sale of water to a major purchaser. The lease is for a period of 40 years, with minimum payments ranging from \$1,683 to \$1,833 per month. The facilities are owned by the Authority, with the City having the exclusive use of the entire project throughout its useful life. Amortization is computed using the straight-line method and is included in depreciation expense. Interest expense for this lease was \$9,919 for the year ended June 30, 2008.

The following is a schedule of the future minimum lease payments under the capitalized lease together with the present value of the net minimum lease payments as of June 30, 2008:

Years ending June 30,	
2009	22,183
2010	20,725
2011	21,133
2012	20,658
2013	20,842
2014-2018	107,025
2019-2023	46,659
Total minimum lease payments	259,225
Less: Amount representing interest	66,132
Present value of future minimum lease payments	<u>193,093</u>

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

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

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 funds, in addition to various other requirements. The City is in compliance with all significant requirements of the bond ordinance. As of June 30, 2008, the City had 682 water connections and 598 sewer connections.

The City's compliance with the balances required as of June 30, 2008 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	12,905	14,723	1,818
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, 2008 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	6,448	10,564	4,116
Reserve Fund	2,500	2,522	22

Promissory Note

In May 1998, the City entered into a promissory note in the amount of \$288,062 to fund repairs and improvements to the water plant. The note is payable in monthly installments to the Sabine River Authority of Texas with an annual adjustable interest rate, maturing May 2028. The City's water and sewer system will service the debt from net revenues of the system. In April, 2006, the interest rate was adjusted to 7.0%.

The annual debt service requirements to maturity, including principal and interest, for the City's

CITY OF HEMPHILL, TEXAS
NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

business type activities long term debt is as of June 30, 2008 is as follows:

	Year ending June 30,
2009	119,293
2010	116,210
2011	118,933
2012	115,353
2013	117,414
2014-2018	444,625
2019-2023	276,936
2024-2028	226,385
2029-2033	131,490
2034-2038	124,300
2039-2043	120,410
2044-2045	42,700
Total principal and interest	1,954,049
Less interest	790,912
Total debt at June 30, 2008	1,163,137

Change in Long-Term Liabilities

Long term liability activity for the year ended June 30, 2008 was as follows:

	Beginning Balance	Issued	Retired	Ending Balance	Due in One Year
Governmental Activities:					
Bank loans	6,629	-	6,629	-	-
Governmental Activities, long-term liabilities	6,629	-	6,629	-	-
Business-type activities:					
Capital lease	203,948	-	10,856	193,092	11,120
Promissory Notes	248,810	-	5,765	243,045	7,109

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

	Beginning Balance	Issued	Retired	Ending Balance	Due in One Year
Bank loans	18,859	-	18,859	-	-
Revenue bonds	757,000	-	30,000	727,000	35,000
Business-type activity, long-term liabilities	1,228,617	-	65,480	1,163,137	53,229

WATER SUPPLY AGREEMENT

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. The agreement expires in 2020, and the City must make minimum monthly payments whether or not it is able to take delivery of the water. For the year ended June 30, 2008, the City's cost for treated water under this agreement was \$417,757.

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. The unit cost for treated water is developed from an annual budget. The agreement expires in 2020. For the year ended June 30, 2008, the City earned \$403,111 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.

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

COMMITMENTS AND CONTINGENCIES

Grants

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, 2008.

RETIREMENT PLAN

Plan Description

The City provides pension benefits for all of its full-time employees through a non-traditional, joint contributory, hybrid defined benefit plan in the state-wide Texas Municipal Retirement System (TMRS), one of 827 administered by TMRS, an agent multiple-employer public employee retirement system.

Benefits

Benefits depend upon the sum of the employee's contributions to the plan, with interest, and the City-financed monetary credits, with interest. At the date the plan began, the City granted monetary credits for service rendered before the plan began of a theoretical amount equal to two times what would have been contributed by the employee, with interest, prior to establishment of the plan. Monetary credits for service since the plan began are a percent (100%, 150%, or 200%) of the employee's accumulated contributions. In addition, the City can grant, as often as annually, another type of monetary credit referred to as an updated service credit which is a theoretical amount which, when added to the employee's accumulated contributions and the monetary credits for service since the plan began, would be the total monetary credits and employee contributions accumulated with interest if the current employee contribution rate and City matching percent had always been in existence and if the employee's salary had always been the average of his salary in the last three years that are one year before the effective date. At retirement, the benefit is calculated as if the sum of the employee's accumulated contributions with interest and the employer-financed monetary credits with interest were used to purchase an annuity.

The plan provisions are adopted by the City Council, within the options available in the state statutes governing TMRS. Members can retire at ages 60 and above with 5 or more years of service or with 25 years of service regardless of age. A member is vested after 5 years. The contribution rate for the employees is 5% and the City matching ratio (City to Employee) is 1 to 1.

CITY OF HEMPHILL, TEXAS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

Contributions

Under the state law governing TMRS, the actuary annually determines the City contribution rate. This rate consists of the normal cost contribution rate and the prior service contribution rate, both of which are calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the currently accruing monetary credits due to the City matching percent, which are the obligation of the City as of an employee's retirement date, not at the time the employee's contributions are made. The normal cost contribution rate is the actuarially determined percent of payroll necessary to satisfy the obligation of the City to each employee at the time his/her retirement becomes effective. The prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the remainder of the plan's 25-year amortization period. The unit credit actuarial cost method is used for determining the City contribution rate. Both the employees and the City make contributions monthly. Since the City needs to know its contribution rate in advance to budget for it, there is a one-year delay between the actuarial valuation that is the basis for the rate and the calendar year when the rate goes into effect (i.e. December 31, 2007 valuation is effective for rates beginning January 2008).

Actuarial Valuation Information

The City of Hemphill is one of 827 municipalities having the benefit plan administered by TMRS. Each of the 827 municipalities have an individual actuarial valuation performed. All assumptions for the December 31, 2007 valuations are contained in the 2007 TMRS Comprehensive Annual Financial Report, a copy of which may be obtained in writing to P.O. Box 149153, Austin, Texas 78714-9153.

Trend Information

Accounting Year End	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
6/30/07	25,234	100%	---
6/30/06	24,280	100%	---
6/30/05	20,184	100%	---

CITY OF HEMPHILL, TEXAS
NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2008

Schedule of Funding Progress

	Actuarial Valuation Date		
	12/31/05	12/31/06	12/31/07
a. Actuarial value of assets	835,607	934,267	1,038,581
b. Actuarial accrued liability (AAL)	859,736	948,048	1,002,772
Unfunded (Overfunded) AAL	24,129	13,781	(35,809)
Funded ratio	97.20%	98.55%	103.60%
c. Annual covered payroll	692,018	701,967	695,127
UAAL as percentage of covered payroll	3.50%	1.96%	(5.20)%

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, 2008

	Budgeted Amounts		Actual Amounts	Variance With Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Taxes:				
Sales taxes	446,826	446,826	358,912	(87,914)
Franchise taxes	8,012	8,012	7,278	(734)
Licenses and permits	3,200	3,200	135	(3,065)
Fines	14,396	14,396	14,086	(310)
Charges for services	184,136	184,136	206,717	22,581
Interest income	3,278	3,278	4,037	759
Intergovernmental	5,513	5,513	47,601	42,088
Contributions and donations	-	-	2,400	2,400
Other	10,527	10,527	30,421	19,894
Total revenues	675,888	675,888	671,587	(4,301)
EXPENDITURES				
Current:				
General government:				
Finance and administration	340,848	310,848	371,780	(60,932)
Municipal court	27,956	27,956	26,432	1,524
Public safety:				
Fire	24,914	24,914	17,146	7,768
Police	170,021	170,021	156,623	13,398
Streets	105,341	105,341	99,825	5,516
Sanitation	181,089	181,089	193,077	(11,988)
Parks and recreation	20,959	20,959	11,083	9,876
Health and welfare	20,795	20,795	19,858	937
Cemetery	-	-	4,490	(4,490)
Debt service	300	300	6,828	(6,528)
Capital outlay	74,150	154,150	145,861	8,289
Total expenditures	966,373	1,016,373	1,053,003	(36,630)
Excess (deficiency) of revenues over expenditures	(290,485)	(340,485)	(381,416)	(40,931)
OTHER FINANCING SOURCES (USES)				
Transfers in	290,768	290,768	366,768	76,000
Total other financing sources (uses)	290,768	290,768	366,768	76,000
Net change in fund balance	283	(49,717)	(14,648)	35,069
Fund balance - beginning	108,308	108,308	108,308	-
Fund balance - ending	108,591	58,591	93,660	35,069

See accompanying notes to the financial statements

Other Schedules

**CITY OF HEMPHILL, TEXAS
GENERAL FUND
SCHEDULE OF CURRENT EXPENDITURES BY DEPARTMENT
BUDGET AND ACTUAL FOR THE YEAR ENDED JUNE 30, 2008**

General Government	Budget	Actual	Variance favorable (unfavorable)
Administration:			
Personnel	228,376	249,501	(21,125)
Supplies and materials	8,600	6,171	2,429
Maintenance and repairs	16,667	19,394	(2,727)
Contractual services	46,296	35,801	10,495
Miscellaneous	68,865	87,345	(18,480)
Total administration	368,804	398,212	(29,408)
Public Safety			
Fire Department:			
Personnel	2,486	600	1,886
Supplies and materials	8,957	6,587	2,370
Maintenance and repairs	6,440	5,381	1,059
Contractual services	4,525	3,576	949
Miscellaneous	2,506	1,002	1,504
Total fire department	24,914	17,146	7,768
Police department:			
Personnel	149,387	133,878	15,509
Supplies and materials	11,499	16,185	(4,686)
Maintenance and repairs	2,985	2,205	780
Contractual services	2,864	2,312	552
Miscellaneous	3,286	2,043	1,243
Total police department	170,021	156,623	13,398
Total public safety	194,935	173,769	21,166
Sanitation			
Supplies and materials	5,115	6,450	(1,335)
Contractual services	175,974	186,449	(10,475)
Miscellaneous	-	178	(178)
Total sanitation	181,089	193,077	(11,988)

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, 2008**

	Budget	Actual	Variance favorable (unfavorable)
Streets			
Personnel	73,567	74,998	(1,431)
Supplies and materials	26,226	18,205	8,021
Maintenance and repairs	3,436	2,153	1,283
Contractual services	2,062	4,457	(2,395)
Miscellaneous	50	12	38
Total streets	105,341	99,825	5,516
Parks and recreation			
Supplies and materials	1,615	1,319	296
Maintenance and repairs	6,274	3,498	2,776
Contractual services	12,820	6,266	6,554
Miscellaneous	250	-	250
Total parks and recreation	20,959	11,083	9,876
Health and welfare			
Personnel	18,203	18,221	(18)
Supplies and materials	967	1,201	(234)
Maintenance and repairs	775	-	775
Contractual services	400	436	(36)
Miscellaneous	450	-	450
Total health and welfare	20,795	19,858	937
Cemetery			
Maintenance and repairs	-	4,490	(4,490)
Total cemetery	-	4,490	(4,490)
Total current expenditures	891,923	900,314	(8,391)

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, 2008**

	Budget	Actual	Variance favorable (unfavorable)
Electric Department			
Personnel	88,929	104,944	(16,015)
Supplies and materials	76,939	145,381	(68,442)
Maintenance and repairs	22,745	17,112	5,633
Contractual services	4,500	12,549	(8,049)
Cost of services	1,344,466	1,262,751	81,715
Depreciation	29,856	36,618	(6,762)
Other operating expenses	3,137	4,896	(1,759)
Total electric department	1,570,572	1,584,251	(13,679)
Gas department			
Supplies and materials	5,900	28,773	(22,873)
Maintenance and repairs	345	22	323
Contractual services	1,841	3,242	(1,401)
Cost of services	170,034	172,230	(2,196)
Depreciation	25,116	25,800	(684)
Other operating expenses	3,970	4,314	(344)
Total gas department	207,206	234,381	(27,175)
Water department			
Supplies and materials	37,834	36,919	915
Maintenance and repairs	1,250	1,400	(150)
Contractual services	865	845	20
Depreciation	26,016	22,572	3,444
Other operating expenses	1,950	205	1,745
Total water department	67,915	61,941	5,974

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, 2008**

	Budget	Actual	Variance favorable (unfavorable)
Sewer department			
Personnel	28,061	24,784	3,277
Supplies and materials	42,019	60,273	(18,254)
Maintenance and repairs	5,170	9,772	(4,602)
Contractual services	3,467	7,814	(4,347)
Depreciation	42,500	95,841	(53,341)
Other operating expenses	3,120	8,947	(5,827)
Total sewer department	124,337	207,431	(83,094)
Warehouse			
Personnel	312,538	273,709	38,829
Supplies and materials	35,188	40,883	(5,695)
Maintenance and repairs	8,768	6,658	2,110
Contractual services	13,832	16,139	(2,307)
Depreciation	18,444	21,826	(3,382)
Miscellaneous	30,115	25,374	4,741
Total warehouse	418,885	384,589	34,296
Water plant			
Personnel	137,098	137,449	(351)
Supplies and materials	97,395	71,479	25,916
Maintenance and repairs	17,738	4,179	13,559
Contractual services	17,006	12,457	4,549
Cost of services	548,739	444,913	103,826
Depreciation	103,980	108,563	(4,583)
Other operating expenses	11,926	10,272	1,654
Total water plant	933,882	789,312	144,570
Total expenditures	3,322,797	3,261,905	60,892

See accompanying notes to the financial statements

Statistical Tables

CITY OF HEMPHILL, TEXAS

SCHEDULE OF INSURANCE POLICIES IN FORCE

JUNE 30, 2008

Insurer	Amount of Coverage	Risk Covered	Expiration Date
Texas Municipal League Intergovernmental Risk Pool	\$2,000,000	Comprehensive General liability	10-01-08
	\$2,000,000	Sudden events - Pollution	10-01-08
	\$2,000,000	Automobile liability	10-01-08
	\$2,000,000	Law enforcement liability	10-01-08
	\$2,000,000	Errors and omissions	10-01-08
	\$3,261,100	Real and personal property	10-01-08
	\$500,000	Boiler and machinery accident	10-01-08
	As scheduled	Automobile physical damage	10-01-08
	\$161,684	Mobile equipment	10-01-08
	Statutory	Workers compensation	10-01-08
Texas Water Conservation Association Risk Management	\$1,355,588	Water treatment plant facilities and equipment	06-30-08

FEDERAL AWARDS SECTION



**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, 2008, which collectively comprise the City's basic financial statements and have issued our report thereon dated November 3, 2008. 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 control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the City's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

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

We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

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.

Pipes & Associates

PIPES & ASSOCIATES
Certified Public Accountants

November 3, 2008

**CITY OF HEMPHILL, TEXAS
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2008**

No findings reported.

**CITY OF HEMPHILL, TEXAS
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2008**

No prior audit findings reported.

**CITY OF HEMPHILL, TEXAS
CORRECTIVE ACTION PLAN
FOR THE YEAR ENDED JUNE 30, 2008**

None required.