

**ANNUAL
FINANCIAL REPORT**

CITY OF GROVES, TEXAS

**For the fiscal year ended
September 30, 2012**



CITY OF GROVES, TEXAS
ANNUAL FINANCIAL REPORT
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Introductory Section

CITY OF GROVES, TEXAS
PRINCIPAL CITY OFFICIALS

CITY COUNCIL

Brad P. Bailey Mayor

Joseph P. Arisco Council Member, Ward 1

Karen Theis Council Member, Ward 2

Sidney Badon Council Member, Ward 3

Kyle Hollier Council Member, Ward 4

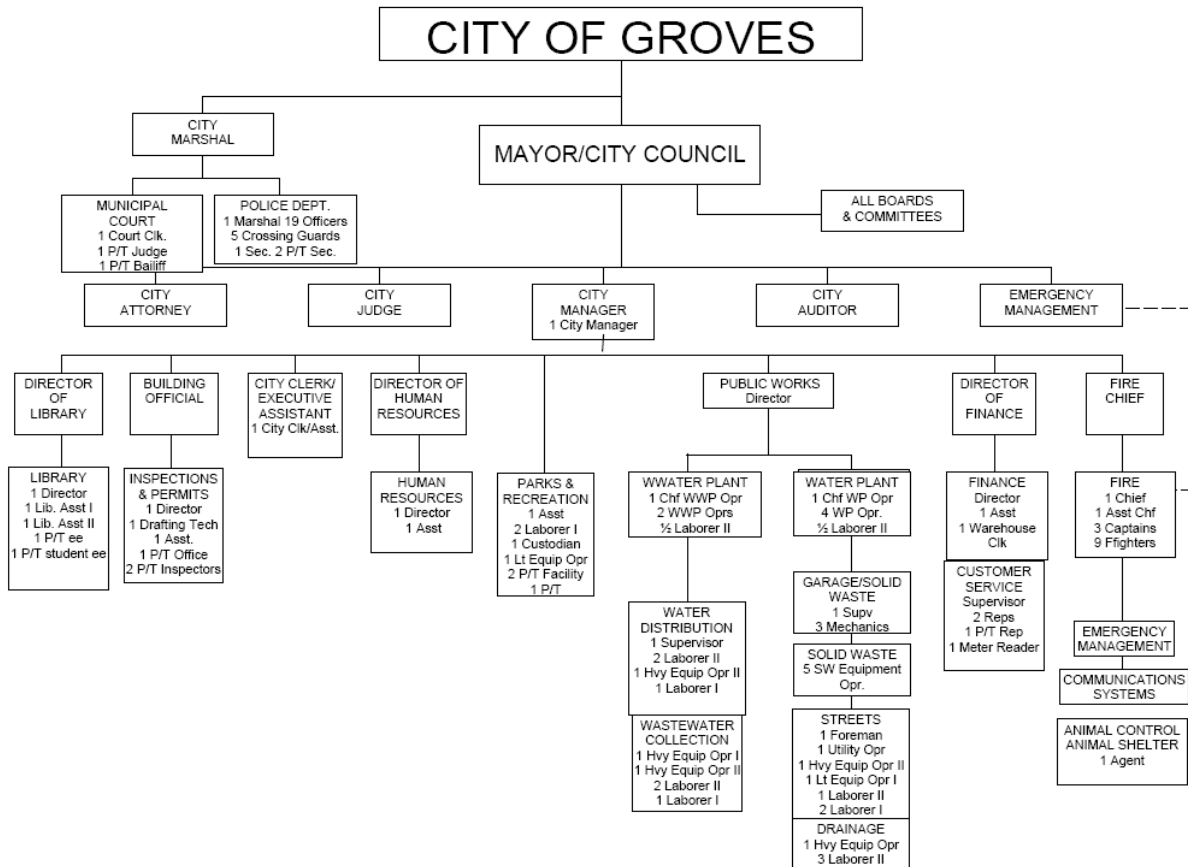
CITY MANAGER

D.E. Sosa

CITY ATTORNEY

James Black

CITY OF GROVES, TEXAS
ORGANIZATIONAL CHART



Report of Independent Auditors

To the Honorable Mayor and
Members of the City Council
City of Groves, 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 City of Groves, Texas (the City), as of and for the year ended September 30, 2012, 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's management. 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. 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 as of September 30, 2012, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison and schedule of funding progress on Pages 3 through 12 and Pages 46 through 48 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

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

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Groves, Texas's financial statements. The introductory section and combining and individual nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the financial statements. The combining and individual nonmajor fund financial statements are the 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 introductory section has 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 them

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

April 22, 2013

CITY OF GROVES, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Groves (the "City"), we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended September 30, 2012.

Overview of the Financial Statements

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

Government-wide Financial Statements

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

The statement of net assets presents information on all of the City's assets and liabilities, with the difference between the two 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 is improving or deteriorating.

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

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City include general government, public safety, public works, culture and recreation and administration and general. The business-type activities of the City include water and sewer operating system and a solid waste system.

The government-wide financial statements can be found on Pages 15 through 17 of this report.

Fund Financial Statements

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

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

Governmental Funds

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

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

The City maintains six individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures and changes in fund balances for the General and Debt Service Funds which are considered to be major funds. Data from the other governmental funds are combined into a single, aggregated presentation.

The City adopts an annual appropriated budget for its General and Debt Service Funds. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

The basic governmental fund financial statements can be found on Pages 18 through 21 of this report.

Proprietary Funds

The City maintains one type of proprietary fund. Enterprise Funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses an Enterprise Fund to account for its Water and Sewer Fund and Solid Waste Fund.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The basic proprietary fund financial statements, which begin on Page 22 of this report, provide separate information for the Water and Sewer and Solid Waste Enterprise Funds since they are considered to be major funds of the City.

The basic proprietary fund financial statements can be found on Pages 22 through 24 of this report.

Notes to the Basic Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on Pages 25 through 44 of this report.

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

Other Information

In addition to the basic financial statements and accompanying notes, this report also presents other required supplementary information as well as combining and individual fund statements and schedules that further support the information in the financial statements. This information is presented immediately following the notes to the financial statements beginning on Page 46 of this report.

Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. The assets of the City exceeded its liabilities at the close of the most recent fiscal year by \$30.2 million (net assets). 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 government as a whole, as well as for its separate governmental and business-type activities.

By far, the largest portion of the City's net assets (\$26.5 million) reflects its investment in capital assets (e.g., land, buildings, infrastructure, machinery and equipment); less any related debt used to acquire those assets that is still outstanding. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

CONDENSED SCHEDULE OF NET ASSETS

September 30, 2012 and 2011

Amounts in (000's)

	Governmental Activities		Business-type Activities		Total	
	2012	2011	2012	2011	2012	2011
Current and other assets	\$ 4,272	\$ 5,842	\$ 1,821	\$ 1,337	\$ 6,093	\$ 7,179
Internal balances	2,265	2,250	(2,265)	(2,250)		
Capital assets	8,258	8,528	30,110	31,051	38,368	39,579
Total Assets	14,795	16,620	29,666	30,138	44,461	46,758
Other liabilities	386	303	740	666	1,126	969
Long-term liabilities	11,572	12,677	1,523	1,786	13,095	14,463
Total Liabilities	11,958	12,980	2,263	2,452	14,221	15,432
Net assets:						
Invested in capital assets, net of related debt	(2,143)	(4,180)	28,634	29,310	26,491	25,130
Restricted	539	680			539	680
Unrestricted	4,441	7,140	(1,231)	(1,624)	3,210	5,516
Total Net Assets	\$ 2,837	\$ 3,640	\$ 27,403	\$ 27,686	\$ 30,240	\$ 31,326

An additional portion of the City's net assets (2%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets, \$3.2 million, may be used to meet the government's ongoing obligations to citizens and creditors.

The City's net assets decreased by \$1.1 million during the current fiscal year, primarily due to unexpected wastewater plant repairs and higher depreciation expenses due to construction projects that became active in the current year for both the business and governmental activities.

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

Government-wide Financial Analysis (continued)

The following table summarizes the changes in net assets for the City for the year ended September 30, 2012.

CONDENSED SCHEDULE OF CHANGES IN NET ASSETS

For the Fiscal Years Ended September 30, 2012 and 2011

Amounts in (000's)

	Governmental Activities		Business-type Activities		Total	
	2012	2011	2012	2011	2012	2011
Revenues						
Program revenue:						
Charges for services	\$ 340	\$ 355	\$ 5,821	\$ 5,850	\$ 6,161	\$ 6,205
Operating grants and contributions	189	381			189	381
Capital grants and contributions		1,015				1,015
Property taxes	4,805	4,756			4,805	4,756
Sales and use taxes	1,815	1,746			1,815	1,746
Franchise taxes	1,013	1,076			1,013	1,076
Unrestricted investment earnings	1	4			1	4
Miscellaneous	156	793	20		175	793
Total Revenues	8,319	10,126	5,841	5,850	14,159	15,976
General government	1,336	1,290			1,336	1,290
Public safety	4,397	4,207			4,397	4,207
Public works	2,498	2,205			2,498	2,205
Culture and recreation	673	949			673	949
Economic development	115	364			115	364
Interest on long-term debt	451	471			451	471
Water and sewer			4,724	4,988	4,724	4,988
Solid Waste			1,052	1,164	1,052	1,164
Total Expenses	9,470	9,486	5,776	6,152	15,246	15,638
Decrease in net assets before transfers	(1,151)	640	65	(303)	(1,086)	337
Transfers	348	416	(348)	(416)		
Change in net assets	(803)	1,056	(283)	(719)	(1,086)	337
Net Assets - Beginning Restated	3,640	2,584	27,686	28,405	31,326	30,989
Net Assets - Ending	\$ 2,837	\$ 3,640	\$ 27,403	\$ 27,686	\$ 30,240	\$ 31,326

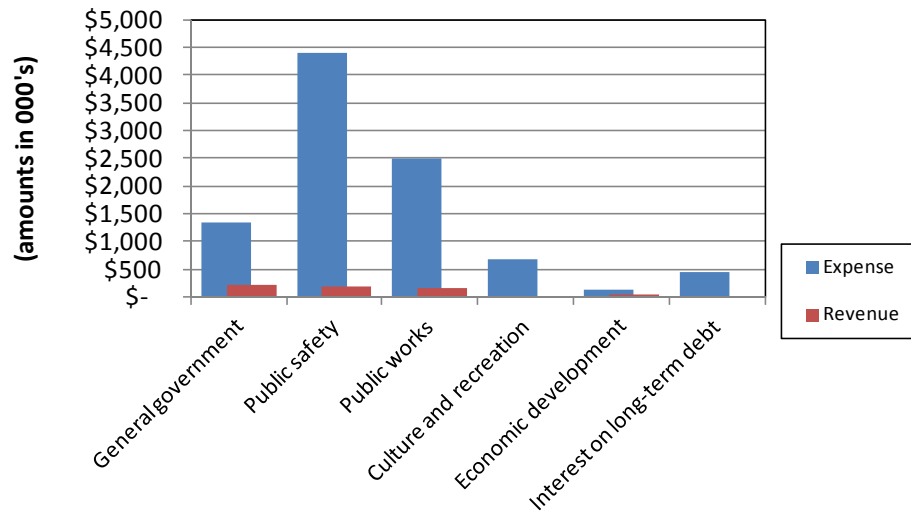
CITY OF GROVES, TEXAS
MANAGEMENT’S DISCUSSION AND ANALYSIS (continued)

Governmental Activities

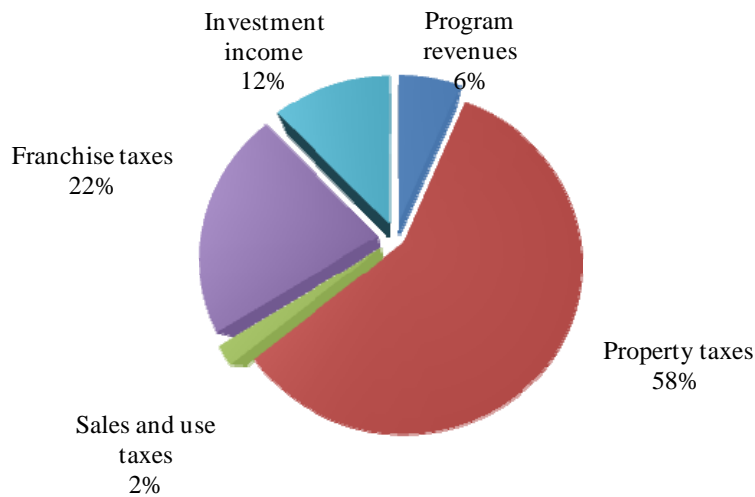
Governmental activities decreased the City’s net assets by approximately \$0.8 million. The key element of this decrease is the following:

- Decrease in capital grants and operating grants and contributions of 1.2 million.
- Decrease in the amount transferred out of Business type activities into Governmental activities.

A comparison of program expenses to program revenues follows:



Revenue sources for governmental activities were distributed as follows:

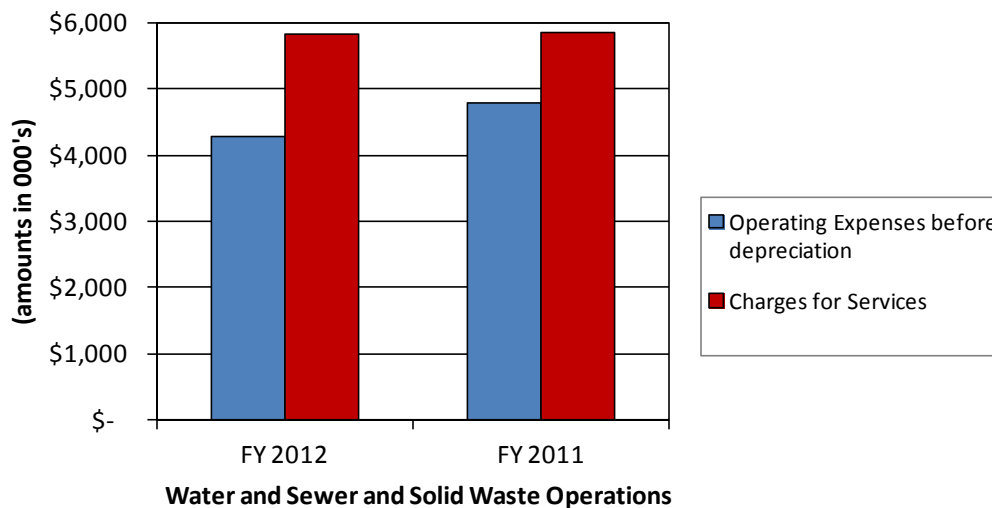


CITY OF GROVES, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Business-type Activities

Business-type activities decreased the City's net assets by \$ 283,000. The majority of this decrease was due to net transfers of \$348,000 to governmental funds. Operating activity included the following:

- Charges for services of \$5.8 million, a decrease of approximately \$29 thousand from prior year due to decreased usage from fiscal year 2011 to 2012.
- Water and sewer and solid waste expenses of \$4.7 million and \$1.1 million respectively. This resulted in a decrease in expenses of \$264 thousand from prior year for water and sewer expenses and a decrease of expenses of \$112 thousand for solid waste expenses.



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

Financial Analysis of the Government's Funds

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

Governmental Funds

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

As of the close of the current fiscal year, the City's governmental funds reported a combined ending fund balance of \$5.6 million, a decrease of approximately \$1.6 million from the prior year. The key elements of this decrease are as follows:

- A decrease of \$1,477,288 in the general fund, due primarily to reduction in intergovernmental revenue of \$1.2 million.
- A decrease of \$226,760 in the economic development fund primarily due to transfers to the debt service fund of \$700,000 for payment of debt.

The General Fund is the chief operating fund of the City. At the end of the current fiscal year, unassigned fund balance of the general fund was 24% or \$1.1 million. The unassigned fund balance decreased by \$1,873,957 from fiscal year 2011. The key element of this decrease was decrease in intergovernmental revenues.

The General Fund has assigned fund balance amounts of \$490,526 and \$572,573 for long-term compensated absences and equipment replacement respectively as of September 30, 2012.

At the close of the current fiscal year, the City's debt service fund reported a fund balance of \$201,788, an increase of \$90,067 from the prior year. Debt service expenditures for the year ending September 30, 2012, totaled \$1,578,066.

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

Proprietary Funds

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

The deficit in unrestricted net assets at the end of the year amounted to \$1.7 million for the Water and Sewer Fund. Total net assets of the Water and Sewer Fund decreased by \$568,641. Unrestricted net assets at the end of the year amounted to \$563,002 for the Solid Waste Fund. Net assets of the Solid Waste Fund increased by \$285,220. Other factors concerning the finances of these funds have already been addressed in the discussion of the City's business-type activities.

General Fund Budgetary Highlights

Actual revenues differed from budgeted revenues by \$156,000 , primarily due to sales and use taxes actual revenue being \$291,482 less than budgeted for, and \$161,613 unbudgeted intergovernmental revenue. During the budgeting process, the city factored in still maintaining a fund balance amount sufficient to cover over a three-month operating reserve.

Actual expenditures exceeded budgeted appropriations by \$535,527, the key elements of which are as follows:

- Culture and recreation with a positive variance of \$154,266 due to lower costs than anticipated.
- Capital outlay with a negative variance of \$696,024 due to greater construction and maintenance activity, which were unbudgeted expenditures expected to be partially reimbursed by state and federal proceeds.

Capital Asset and Debt Administration

The City's investment in capital assets for its governmental and business-type activities as of September 30, 2012, amounted to \$38.4 million (net of accumulated depreciation). This investment in capital assets includes land, buildings, roads, park facilities, water and sewer plants and service lines, machinery and equipment, and construction in progress. Capital asset balances decreased by approximately \$31 thousand from the prior year due to depreciation expenses being greater than the capital outlay expended during the year.

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

The following table shows the balances at September 30, 2012 and 2011 (in 000's):

	<u>2011</u>	<u>2012</u>
Governmental Activities		
Capital Assets not being depreciated:		
Land	\$	74
Construction in progress	176	195
Capital Assets, net of depreciation:		
Infrastructure	4,833	4,332
Buildings	760	920
Machinery and Equipment	1,957	2,019
Improvements other than buildings	801	717
Total capital assets - Governmental Activities	<u>\$ 8,528</u>	<u>\$ 8,258</u>
Business-Type Activities		
Capital Assets not being depreciated:		
Land	\$ 678	\$ 678
Construction in progress	4,313	18
Capital Assets, net of depreciation:		
Buildings & System	20,022	23,622
Machinery and Equipment	6,038	5,792
Total capital assets - Business-Type Activities	<u>\$ 31,051</u>	<u>\$ 30,110</u>

Additional information on the City's capital assets can be found in Note 5 to the basic financial statements of this report.

Long-term Liabilities

At the end of the current fiscal year, the City had total long-term debt outstanding of \$14.2 million. This is a decrease from the prior year of \$1.1 million, due to scheduled principal debt payments. The entire amount of bonded debt is backed by the full faith and credit of the City. In addition, the debt agreements allow for the obligations to be paid from certain sales and use tax receipts and water/wastewater revenues. A schedule of long-term debt at September 30, 2011 and 2012 follows (in \$000's):

	<u>2011</u>	<u>2012</u>
Governmental Activities		
General obligation bonds	\$ 11,785	\$ 10,700
Tax notes	254	214
Compensated absences	638	658
	<u>\$ 12,677</u>	<u>\$ 11,572</u>
Business Activities		
Tax notes	\$ 526	\$ 425
Capital leases	1,215	1,050
	<u>\$ 1,741</u>	<u>\$ 1,476</u>

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

Capital Asset and Debt Administration (continued)

The City and its Water and Sewer Enterprise Fund both maintain a rating of A1 from Moody's Investor Services.

The City has no legal debt limit provision in its charter. Additional information on the City's long-term debt can be found in Note 6 to the basic financial statements of this report.

Economic Factors and Next Year's Budget and Rates

The anticipated economic conditions discussed in the previous financial reports continued and the steps the City has taken proved beneficial. The City did realize its anticipated recovery in its sales tax receipts with an 11.6% increase. The City does not anticipate any significant variance for the upcoming year and maintained the same budgeted amount of revenue. The City's aggressive economic development activities continue to attract and retain diverse businesses which are reflected in the sales tax improvements.

The City's demolition program continues to address the dangerous structures and has resulted in continued renovation and new construction including plans for two new subdivisions within the City. The City's efforts to replace older, decaying structures with new and more valuable buildings will continue.

The City has continued to utilize reductions in its workforce through retirements and attrition with each new vacancy being evaluated and some had their duties reassigned to existing personnel and the positions were eliminated.

Interest rates continue to remain at historic lows and the City budgeted accordingly. The City does not anticipate any sharp rises in interest rate for the upcoming year, but does expect rates to slightly rise over the upcoming year, with accelerating inflationary pressures in the subsequent years. During FYE 2013 the City anticipates refinancing some of its debt to capitalize on the low rates.

The City's 2013 budget is very similar to the 2012 budget with the exception of a major construction project. The City was awarded a two million dollar federal grant to construct a new emergency operations center that will house the police department and municipal court. This new structure will require the issuance of additional debt by the City to afford the matching requirements of the grant. The City will utilize the additional offering to refinance a portion of its higher interest rate debt.

Requests for Information

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to show accountability for the funding it receives. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the City of Groves, Finance Department, 3947 Lincoln, Groves, Texas, 77619.

Basic Financial Statements

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CITY OF GROVES, TEXAS

STATEMENT OF NET ASSETS

September 30, 2012

	Primary Government		
	Governmental Activities	Business-type Activities	Total
Assets			
Cash and cash equivalents	\$ 3,169,422	\$ 725,633	\$ 3,895,055
Accounts receivable	764,742	524,542	1,289,284
Due from other governments	332,737		332,737
Internal balances	2,265,487	(2,265,487)	
Inventories	4,585	79,974	84,559
Prepaid items	660		660
Restricted cash and cash equivalents		491,247	491,247
Capital assets, not subject to depreciation:			
Land	73,668	677,865	751,533
Construction in progress	195,660	17,900	213,560
Capital assets, net of depreciation:			
Infrastructure	5,049,311		5,049,311
Buildings and improvements	920,106	23,621,985	24,542,091
Machinery and equipment	2,019,024	5,791,842	7,810,866
Total Capital Assets	<u>8,257,769</u>	<u>30,109,592</u>	<u>38,367,361</u>
Total Assets	<u>14,795,402</u>	<u>29,665,501</u>	<u>44,460,903</u>
Liabilities			
Accounts payable and accrued expenses	352,665	730,948	1,083,613
Accrued interest	33,068	8,191	41,259
Long-term liabilities:			
Due within one year	1,323,537	289,409	1,471,883
Due in more than one year	10,248,913	1,233,957	11,623,933
Total Liabilities	<u>11,958,183</u>	<u>2,262,505</u>	<u>14,220,688</u>
Net Assets			
Invested in capital assets, net of related debt	(2,143,254)	28,633,858	26,490,604
Restricted for:			
Debt service	209,658		209,658
Economic development	233,227		233,227
Public safety	96,241		96,241
Unrestricted	4,441,347	(1,230,862)	3,210,485
Total Net Assets	<u>\$ 2,837,219</u>	<u>\$ 27,402,996</u>	<u>\$ 30,240,215</u>

See Notes To Basic Financial Statements.

CITY OF GROVES, TEXAS
STATEMENT OF ACTIVITIES
For the Year Ended September 30, 2012

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenue</u>	
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>
Primary government			
Governmental Activities:			
General government	\$ 1,335,942	\$ 77,852	\$ 128,504
Public safety	4,396,692	163,536	15,768
Public works	2,498,335	98,870	41,659
Culture and recreation	673,011		
Economic development	114,977		3,450
Interest on long-term debt	450,860		
Total governmental activities	<u>9,469,817</u>	<u>340,258</u>	<u>189,381</u>
Business-type activities:			
Water and sewer	4,724,117	4,487,819	
Solid Waste	1,051,907	1,332,825	
Total business-type activities	<u>5,776,024</u>	<u>5,820,644</u>	
Total primary government	<u>\$ 15,245,841</u>	<u>\$ 6,160,902</u>	<u>\$ 189,381</u>

General revenues:

Taxes:

Property taxes

Sales and use taxes

Franchise taxes

Unrestricted investment earnings

Miscellaneous

Transfers

Total general revenues

Change in net assets

Net Assets - Beginning, Restated

Net Assets - Ending

See Notes to Basic Financial Statements.

Net (Expense) Revenue and Changes in Net Assets

Primary Government

Governmental Activities	Business-type Activities	Total
\$ (1,129,586)	\$	\$ (1,129,586)
(4,217,388)		(4,217,388)
(2,357,806)		(2,357,806)
(673,011)		(673,011)
(111,527)		(111,527)
(450,860)		(450,860)
<u>(8,940,178)</u>		<u>(8,940,178)</u>
	(236,298)	(236,298)
	280,918	280,918
	44,620	44,620
<u>(8,940,178)</u>	<u>44,620</u>	<u>(8,895,558)</u>
4,805,198		4,805,198
1,815,259		1,815,259
1,012,554		1,012,554
973		973
155,516	19,703	175,219
347,744	(347,744)	
<u>8,137,244</u>	<u>(328,041)</u>	<u>7,809,203</u>
(802,934)	(283,421)	(1,086,355)
3,640,153	27,686,417	31,326,570
<u>\$ 2,837,219</u>	<u>\$ 27,402,996</u>	<u>\$ 30,240,215</u>

CITY OF GROVES, TEXAS

BALANCE SHEET

GOVERNMENTAL FUNDS

September 30, 2012

	<u>General Fund</u>	<u>Debt Service</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets				
Cash and cash equivalents	\$ 2,307,934	\$ 201,787	\$ 659,728	\$ 3,169,449
Taxes receivable, net	397,173	40,939		438,112
Other receivables	326,631			326,631
Due from other funds	2,265,487		183,508	2,448,995
Receivable from other governments	332,737			332,737
Inventories	4,585			4,585
Prepaid expenses	660			660
Total Assets	<u>\$ 5,635,207</u>	<u>\$ 242,726</u>	<u>\$ 843,236</u>	<u>\$ 6,721,169</u>
 Liabilities and Fund Balances				
Liabilities:				
Accounts payable	\$ 28,620	\$	\$ 27	\$ 28,647
Due to other funds	183,508			183,508
Deferred revenue	582,219	40,938		623,157
Other accrued expenses	324,045			324,045
Total Liabilities	<u>1,118,392</u>	<u>40,938</u>	<u>27</u>	<u>1,159,357</u>
 Fund balances:				
Nonspendable				
Inventories	4,585			4,585
Prepaid expenses	660			660
Restricted				
Debt service		201,788		201,788
Capital projects			513,741	513,741
Public safety			96,241	96,241
Economic development			233,227	233,227
Grants and memorials	117,770			117,770
Assigned				
Long-term compensated absences	490,526			490,526
Equipment replacement	572,573			572,573
Long-term interfund receivables	2,265,487			2,265,487
Unassigned	1,065,214			1,065,214
Total Fund Balances	<u>4,516,815</u>	<u>201,788</u>	<u>843,209</u>	<u>5,561,812</u>
Total Liabilities and Fund Balances	<u>\$ 5,635,207</u>	<u>\$ 242,726</u>	<u>\$ 843,236</u>	<u>\$ 6,721,169</u>

See Notes to Basic Financial Statements.

CITY OF GROVES, TEXAS

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET

TO THE STATEMENT OF NET ASSETS

September 30, 2012

Total fund balance, governmental funds \$ 5,561,812

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

Capital assets used in governmental activities are not current financial resources and therefore are not reported in this fund financial statement, but are reported in the governmental activities of the Statement of Net Assets. 8,257,769

Certain other long-term assets are not available to pay current period expenditures and therefore are not reported in this fund financial statement, but are reported in the governmental activities of the Statement of Net Assets. 623,157

Some liabilities are not due and payable in the current period and are not included in the fund financial statement, but are included in the governmental activities of the Statement of Net Assets.

Bonds and capital leases	(10,914,764)
Accrued long-term interest	(33,068)
Accrued compensated absences	(657,687)

Net Assets of Governmental Activities in the Statement of Net Assets \$ 2,837,219

See Notes to Basic Financial Statements.

CITY OF GROVES, TEXAS
STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
For the Year Ended September 30, 2012

	<u>General Fund</u>	<u>Debt Service</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenues				
Taxes:				
Property taxes	\$ 4,415,739	\$ 420,362	\$	\$ 4,836,101
Sales and use taxes	1,172,518		584,737	1,757,255
Franchise taxes	1,009,511			1,009,511
Hotel taxes	61,047			61,047
Fines and forfeitures	157,407			157,407
Licenses and permits	154,031			154,031
Intergovernmental	161,613		15,768	177,381
Charges for services	26,125		3,450	29,575
Investment earnings	904	27	43	974
Other	78,014		1,668	79,682
Total Revenues	<u>7,236,909</u>	<u>420,389</u>	<u>605,666</u>	<u>8,262,964</u>
Expenditures				
Current:				
General government	1,139,188			1,139,188
Public safety	4,103,754			4,103,754
Public works	2,015,819			2,015,819
Culture and recreation	593,142			593,142
Economic development			114,977	114,977
Capital Outlay	742,524		11,144	753,668
Debt Service:				
Principal		1,124,200		1,124,200
Interest and other charges		453,866		453,866
Total Expenditures	<u>8,594,427</u>	<u>1,578,066</u>	<u>126,121</u>	<u>10,298,614</u>
Revenues over (under) expenditures	<u>(1,357,518)</u>	<u>(1,157,677)</u>	<u>479,545</u>	<u>(2,035,650)</u>
Other Financing Sources (Uses)				
Capital Contributions	72,230			72,230
Transfers in	8,000	1,365,000		1,373,000
Transfers out	(200,000)	(117,256)	(708,000)	(1,025,256)
Total other financing sources (uses)	<u>(119,770)</u>	<u>1,247,744</u>	<u>(708,000)</u>	<u>419,974</u>
Net Changes in Fund Balances	(1,477,288)	90,067	(228,455)	(1,615,676)
Fund Balances - Beginning of Year Restated	<u>5,994,103</u>	<u>111,721</u>	<u>1,071,664</u>	<u>7,177,488</u>
Fund Balances - End of Year	<u>\$ 4,516,815</u>	<u>\$ 201,788</u>	<u>\$ 843,209</u>	<u>\$ 5,561,812</u>

See Notes to Basic Financial Statements.

CITY OF GROVES, TEXAS
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE
STATEMENT OF ACTIVITIES
For the Year Ended September 30, 2012

Net change in fund balances - total governmental funds: \$ (1,615,676)

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

Governmental funds report outlays for capital assets as expenditures because such outlays use current financial resources. In contrast, the Statement of Activities reports only a portion of the outlay as expense. The capital asset expenditures are allocated over the assets' estimated useful lives as depreciation expense for the period.

This is the amount by which depreciation of \$999,433 is less than capital outlay of \$729,375 in the current period. (270,058)

Governmental funds do not present revenues that are not available to pay current obligations. In contrast, such revenues are reported in the Statement of Activities when earned. (24,785)

Governmental funds report repayment of bond principal and capital leases as an expenditure. In contrast, the Statement of Activities treats such repayments as a reduction in long-term liabilities. This is the amount of payments made on long-term debt. 1,124,200

Some expenses reported in the statement of activities do not require the use of current financial resources and these are not reported as expenditures in governmental funds:

Accrued interest not reflected in Governmental funds 3,006
 Compensated absences (19,621)

Change in net assets of governmental activities \$ (802,934)

See Notes to Basic Financial Statements.

CITY OF GROVES, TEXAS

STATEMENT OF NET ASSETS

PROPRIETARY FUNDS

September 30, 2012

	Business-type Activities		
	Water and Sewer	Solid Waste	Total
Assets			
Current assets:			
Cash and cash equivalents	\$ 277,342	\$ 448,291	\$ 725,633
Accounts receivable, net	524,542		524,542
Due from other funds		185,270	185,270
Restricted cash and cash equivalents	491,247		491,247
Inventories	79,974		79,974
Total Current Assets	1,373,105	633,561	2,006,666
Non-current assets:			
Capital assets not being depreciated:			
Land and improvements	677,865		677,865
Construction in progress	17,900		17,900
Other capital assets, net of depreciation:			
Infrastructure	6,006,906		6,006,906
Buildings	17,615,079		17,615,079
Equipment and furniture	5,236,799	555,043	5,791,842
Total Non-Current Assets	29,554,549	555,043	30,109,592
Total Assets	30,927,654	1,188,604	32,116,258
Liabilities			
Current liabilities:			
Accounts payable and accrued expenses	125,608	57,315	182,923
Due to other funds	2,450,757		2,450,757
Deposits	491,247		491,247
Accrued interest payable	8,191		8,191
Salaries payable	48,345	8,433	56,778
Total Current Liabilities	3,124,148	65,748	3,189,896
Non-current liabilities:			
Compensated absences	42,821	4,811	47,632
Capital lease obligation	1,050,498		1,050,498
Bonds, notes and loans payable	425,236		425,236
Total Non-Current Liabilities	1,518,555	4,811	1,523,366
Total Liabilities	4,642,703	70,559	4,713,262
Net Assets			
Invested in capital assets	28,078,815	555,043	28,633,858
Unrestricted	(1,793,864)	563,002	(1,230,862)
Total Net Assets	\$ 26,284,951	\$ 1,118,045	\$ 27,402,996

See Notes to Basic Financial Statements.

CITY OF GROVES, TEXAS
STATEMENT OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
For the Year Ended September 30, 2012

	Business-type Activities		
	Water and Sewer	Solid Waste	Total
Operating Revenues			
Charges for services	\$ 4,487,819	\$ 1,332,825	\$ 5,820,644
Total Operating Revenues	<u>4,487,819</u>	<u>1,332,825</u>	<u>5,820,644</u>
Operating Expenses			
Personnel services	1,739,513	332,578	2,072,091
Supplies	744,761	134,774	879,535
Contracted services	222,790	410,014	632,804
Utilities	234,726	1,919	236,645
Repairs and maintenance	343,298	44,049	387,347
Depreciation	1,370,756	128,573	1,499,329
Total Operating Expenses	<u>4,655,844</u>	<u>1,051,907</u>	<u>5,707,751</u>
Operating income (loss)	<u>(168,025)</u>	<u>280,918</u>	<u>112,893</u>
Non-Operating Revenues (Expenses)			
Interest expense	(68,273)		(68,273)
Gain on sale of equipment	15,401	4,302	19,703
Total Non-Operating Expenses	<u>(52,872)</u>	<u>4,302</u>	<u>(48,570)</u>
Income (loss) before Transfers	<u>(220,897)</u>	<u>285,220</u>	<u>64,323</u>
Transfers in	117,256		117,256
Transfers out	(465,000)	-	(465,000)
Change in Net Assets	(568,641)	285,220	(283,421)
Total Net Assets - Beginning of Year	<u>26,853,592</u>	<u>832,825</u>	<u>27,686,417</u>
Total Net Assets - End of Year	<u>\$ 26,284,951</u>	<u>\$ 1,118,045</u>	<u>\$ 27,402,996</u>

See Notes to Basic Financial Statements.

CITY OF GROVES, TEXAS
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
For the Year Ended September 30, 2012

	Business-type Activities - Enterprise Funds		
	Water and Sewer	Solid Waste	Totals
Cash Flows From Operating Activities			
Receipts from customers and users	\$ 4,436,961	\$ 1,332,825	\$ 5,769,786
Disbursed for personnel services	(1,738,453)	(332,515)	(2,070,968)
Disbursed for goods and services	(1,473,876)	(586,852)	(2,060,728)
Net cash provided by operating activities	1,224,632	413,458	1,638,090
Cash Flows From Noncapital Financing Activities			
Transfers from other funds	117,256		117,256
Transfers to other funds	(465,000)		(465,000)
Loans from other funds	40,244	(24,984)	15,260
Net cash used by noncapital financing activities	(307,500)	(24,984)	(332,484)
Cash Flows From Capital and Related Financing Activities			
Principal payments on debt	(267,121)		(267,121)
Cash receipts from sale of assets			
Acquisition and construction of capital assets	(332,105)	(206,656)	(538,761)
Cash used by capital and related financing activities	(597,103)	(206,656)	(803,759)
Cash Flows From Investing Activities			
Interest paid	(69,527)	-	(69,527)
Net cash used by investing activities	(69,527)	-	(69,527)
Net increase in cash and cash equivalents	250,502	181,818	432,320
Cash and cash equivalents - beginning of year	518,087	266,473	784,560
Cash and cash equivalents - end of year	\$ 768,589	\$ 448,291	\$ 1,216,880
Unrestricted cash and cash equivalents	\$ 277,342	\$ 448,291	\$ 725,633
Restricted cash and cash equivalents	491,247	-	491,247
	\$ 768,589	\$ 448,291	\$ 1,216,880
Reconciliation of operating income to net cash provided by operating activities			
Operating Income (loss)	\$ (168,025)	\$ 280,918	\$ 112,893
Adjustments to reconcile operating income to net cash provided by operating activities:			
Depreciation	1,370,756	128,573	1,499,329
Increase in accounts receivable	(59,968)	-	(59,968)
Increase in compensated absences	2,817	-	2,817
Increase (decrease) in accounts payable	61,382	3,904	65,286
Decrease in salaries payable	1,060	63	1,123
Increase in customer deposits	9,110	-	9,110
Net cash provided by operating activities	\$ 1,224,632	\$ 413,458	\$ 1,638,090

See Notes to Basic Financial Statements.

CITY OF GROVES, TEXAS
NOTES TO THE BASIC FINANCIAL STATEMENTS

Note 1 - Organization

The City of Groves, Texas, was incorporated in December 1952. The City operates under a Council-Manager form of government.

Pursuant to its provisions and subject only to its limitations imposed by the State Constitution and by the City's charter, all powers of the City shall be vested in an elective Council composed of four Council Members and a Mayor, collectively known as the City Council. The City Council enacts local legislation, adopts budgets, determines policies, and appoints the City Manager, who in turn is responsible to the City Council for the execution of laws and the administration of the government of the City. The City Marshal is elected at-large by the citizens in Groves to manage the municipal court and police department. Departments and agencies of the City submit budget requirements to the Mayor. The Mayor is the presiding officer of the City Council.

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

Note 2 - Summary of Significant Accounting Policies

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

A. Reporting Entity

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

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

In conformity with generally accepted accounting principles, the financial statements of the Groves Economic Development Corporation (GEDC) are presented as a blended component unit. The GEDC board of directors includes a majority of the City Council, and this majority constitutes a voting majority on the GEDC board of directors. GEDC's revenues (from sales tax) are required to be used to pay debt for the City's debt obligations authorized by the GEDC board. The GEDC is reported as a governmental fund. Separately-issued financial statements are not available for this entity.

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 2 - Summary of Significant Accounting Policies (continued)

B. Government-wide and Fund Financial Statements

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

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

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

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

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

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

General property taxes are recorded as receivables when levied and as revenue in the period for which they were levied and become available. Property taxes receivable have been recorded as deferred revenues at year-end.

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 2 - Summary of Significant Accounting Policies (continued)

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

Property taxes collected within 60 days subsequent to September 30, 2012, have not been recorded as revenue as the amount is not considered material. Franchise taxes and sales taxes relating to underlying transactions that occurred prior to September 30, 2012, have been recorded as receivables and revenue. Licenses and permits and fines are not susceptible to accrual since they are not measurable until received. Revenue on federal and state cost-reimbursement grants is accrued when the related expenditures are incurred. Interest is recorded when earned.

The City has the following major governmental funds:

- **General Fund** - The General Fund is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in other funds.
- **Debt Service Fund** - The Debt Service Fund accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

The City reports the following major proprietary funds:

- **Water and Sewer Fund** - The Water and Sewer Fund accounts for the provision of water and sewer services to residents and commercial businesses in the City.
- **Solid Waste Fund** - The Solid Waste Fund accounts for solid waste disposal services for residents and commercial businesses in the City.

These funds are financed and operated in a manner similar to private business enterprises -- where the intent of the City is that the cost (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges. The acquisition, maintenance and improvement of the physical plant facilities required to provide these goods and services are financed from existing cash resources, the issuance of bonds (revenue or general obligation), impact fees and other City funds.

Private-sector standards for accounting and financial reporting issued prior to December 1, 1999, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Government Accounting Standards Board. The City has elected not to follow private sector guidance issued subsequent to that date.

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 2 - Summary of Significant Accounting Policies (continued)

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

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

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

Net assets are categorized into three components -- invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are as follows:

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

D. Cash and Cash Equivalents

The City reports cash and cash equivalents in the District's statement of cash flows for Proprietary Fund Types and in all other financial statements of financial position. The City considers cash and cash equivalents to be cash on hand, demand deposits, certificates of deposit, balances in public funds investment pools and short-term investments with original maturities of three months or less from the date of acquisition.

E. Receivables

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

F. Due to and from Other Funds

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

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 2 - Summary of Significant Accounting Policies (continued)

G. Inventories and Prepaid Items

The costs of governmental fund-type inventories are recorded as expenditures when consumed rather than when purchased. Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items.

H. Capital Assets

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

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

<u>Asset</u>	<u>Estimated Useful Lives</u>
Building	40
Building Improvements	15-40
System Improvements	15-40
Vehicles	5-10
Office Equipment	5-10
Computer Equipment	3-5

I. Compensated Absences

Employees earn vacation based on years of service with the City. In accordance with GAAP, the liability for accumulated vacation at September 30, 2012, has been recorded as a liability in the Government-Wide Statement of Net Assets.

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 2 - Summary of Significant Accounting Policies (continued)

I. Compensated Absences (continued)

Full-time, permanent employees are granted vacation benefits in varying amounts to specified maximums depending on tenure with the City. Sick leave accrues to full-time, permanent employees to specified maximums. Although employees are encouraged to take vacations in the year earned, payment of accrued vacation time is eligible to employees who separated from the City in good standing. Accumulated sick leave is not compensated upon resignation or dismissal. Fifty percent of accumulated sick leave is compensated in the event of the death or retirement of an employee.

Employees continuously employed with the City in good-standing prior to 1984 can have their accrued sick hours up to 960 paid to them upon no longer being employed with the City.

J. General Property Taxes

Property taxes are levied by October 1 in conformity with Subtitle E, Texas Property Tax Code. Taxes are due upon receipt and all taxes not paid prior to February 1 are deemed delinquent and are subject to such penalty and interest set forth by the Property Tax Code. On January 1 of each year, a tax lien attaches to property to secure the payment of all taxes, penalties and interest ultimately imposed. Appraised values are established by the Jefferson County Appraisal District (the "Appraisal District"). Taxes are levied by the City Council based on the appraised values received from the Appraisal District.

K. Debt Service

The ad valorem tax rate is allocated each year between the General Fund and the Debt Service Fund. The full amount estimated to be required for debt service on the general obligation debt is provided by the debt service tax together with interest earned in the Debt Service Fund.

L. Use of Estimate

The preparation of financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual amounts may differ from these estimates.

M. Bond Discounts/Issuance Costs

In governmental fund types, bond discounts and issuance costs are recognized in the current period and are deferred and amortized in the Government-wide Statement of Activities. Bond discounts and issuance costs for proprietary fund types are deferred and amortized over the term of the bonds using the bonds-outstanding method, which approximates the effective interest method. Bond discounts and issuance costs are recorded as deferred charges.

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 2 - Summary of Significant Accounting Policies (continued)

N. Fund Equity

Governmental fund equity is classified according to the relative strength of the spending constraints as follows:

Non-spendable fund balance – amounts that are not in spendable form or are legally or contractually required to be maintained intact.

Restricted fund balance – amounts that are subject to external restrictions from creditors, grantors, contributors, or laws of other governments.

Committed fund balance – amounts constrained for specific purposes as determined by the City itself, using its highest level of decision-making authority (i.e. City Council). To be reported as committed, amounts cannot be used for any other purposes unless the City takes the same highest level of action to remove or change the constraint. The City establishes (and modifies or rescinds) fund balance commitments by passage of a resolution. City Council will approve obligations of funds, such as multiyear contracts, prior to the end of the fiscal year.

Assigned fund balance – amounts the City intends to use for a specific purpose that is neither restricted or committed and includes the remaining positive fund balance of all governmental funds except for the General Fund. Balances for encumbrances, other than those committed by City Council, fall into this category. Intent can be established by City Council or delegated to the City Manager.

Unassigned fund balance – amounts that are available for any purpose. Positive amounts are reported only in the General Fund.

The City will typically use restricted fund balances first, followed by committed resources, and then assigned resources, as appropriate opportunities arise, but reserves the right to selectively spend unassigned resources first to defer the use of these other classified funds.

The City has no formal minimum fund balance policy in place at this time.

Unrestricted net assets for proprietary funds represent the net assets available for future operations or distribution. Restricted net assets for proprietary funds represent the net assets that have been legally identified for specific purposes.

O. Revenues and Expenditures/Expenses

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

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

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 2 - Summary of Significant Accounting Policies (continued)

P. Post-employment Healthcare Benefits

The City does not provide post-employment healthcare benefits except those mandated by the Consolidated Omnibus Budget Reconciliation Act (COBRA). The requirements established by COBRA are fully funded by employees who elect coverage under the Act, and the City incurs no direct costs.

Note 3 - Deposits (Cash) and Investments

Authorization for Deposits and Investments

The Texas Public Funds Investment Act (PFIA), as prescribed in Chapter 2256 of the Texas Government Code, regulates deposits and investment transactions of the City.

In accordance with applicable statutes, the City has a depository contract with an area bank (depository) providing for interest rates to be earned on deposited funds and for banking charges the City incurs for banking services received. The City may place funds with the depository in interest and non-interest bearing accounts. State law provides that collateral pledged as security for bank deposits must have a market value of not less than the amount of the deposits and must consist of: (1) obligations of the United States or its agencies and instrumentalities; (2) direct obligations of the State of Texas or its agencies; (3) other obligations, the principal and interest on which are unconditionally guaranteed or insured by the State of Texas; and/or (4) obligations of states, agencies, counties, cities, and other political subdivisions of any state having been rated as to investment quality by a nationally recognized investment rating firm and having received a rating of not less than A or its equivalent. City policy requires the collateralization level to be at least 102% of market value of principal and accrued interest.

The Council has adopted a written investment policy regarding the investment of City funds as required by the Public Funds Investment Act (Chapter 2256, Texas Government Code). The investments of the City are in compliance with the City's investment policy. The City's investment policy is more restrictive than the PFIA requires. It is the City's policy to restrict its direct investments to obligations of the U.S. Government or U.S. Government Agencies, fully collateralized certificates of deposit, money market mutual funds and local government investment pools. The maximum maturity allowed is ten years from date of purchase. The City's investment policy does not allow investments in certain collateralized mortgage obligations.

The City measures interest rate risk using the weighted average maturity method for the portfolio. The City's investment policy specifies a maximum weighted average maturity of 365 days based on the stated maturity date for each investment in the portfolio. To the extent possible, the City attempts to match investments with anticipated cash flow requirements. The City does not directly invest in securities with a stated maturity date more than 10 years from date of purchase. The settlement date is considered the date of purchase.

CITY OF GROVES, TEXAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 3 - Deposits (Cash) and Investments (continued)

Authorization for Deposits and Investments (continued)

The City's investment policy allows investments by type based on the following diversification requirements:

U.S. Treasury Securities	100%
Certificates of Deposit	100%
Agencies and Instrumentalities	75%
Authorized Pools	50%
Other Obligations Described in V. B-C	50%
Repurchase Agreements	5%
Money Market Mutual Funds	5%
Collateralized Accounts	100%

Deposits

The City's cash and investments consist of cash on hand, deposits with financial institutions, and non-negotiable certificates of deposit. The restricted cash and investments are assets restricted for specific use.

The following schedule shows the City's deposits at year-end:

	<u>Fair Value</u>
Primary Government	
Cash Deposits	\$ 4,286,302
Certificates of Deposit	<u>100,000</u>
Total	<u>\$ 4,386,302</u>

Custodial Risk

At September 30, 2012, the entire amount of the city's deposits was covered by federal depository insurance or by collateral held by the City's agent in the City's name.

CITY OF GROVES, TEXAS**NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)****Note 4 - Receivables**

Amounts recorded as receivables as of September 30, 2012, for the government's individual major and non-major funds, including the applicable allowance for uncollectible accounts, are as follows:

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Water and Sewer</u>	<u>Total</u>
Receivables:				
Fines and Forfeitures	\$ 185,046			\$ 185,046
Property taxes	422,525	\$ 43,552		466,077
Customer accounts	141,585		\$ 1,057,411	1,198,996
Due from state (Sales Tax)	<u>332,737</u>			<u>332,737</u>
Gross Receivables	1,081,893	43,552	1,057,411	2,182,856
Less: allowance for uncollectibles	<u>(25,352)</u>	<u>(2,613)</u>	<u>(532,869)</u>	<u>(560,834)</u>
Net Total Receivables	<u>\$ 1,056,541</u>	<u>\$ 40,939</u>	<u>\$ 524,542</u>	<u>\$ 1,622,022</u>

Revenue from delinquent property taxes and outstanding warrants receivable of at September 30, 2012, has been deferred in the fund financial statements until collected. Delinquent tax collections during the first sixty days subsequent to September 30, 2012, have not been recorded as revenue as of September 30, 2012, as the amount is not considered material.

CITY OF GROVES, TEXAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 5 - Capital Assets

A summary of activity for capital assets capitalized by the City for the year ended September 30, 2012, follows:

Governmental Activities:

	Beginning Balance	Additions	Deletions	Ending Balance
Capital Assets not being depreciated:				
Land	\$ -	\$ 73,668	\$ -	\$ 73,668
Construction in Progress	176,240	217,140	(197,720)	195,660
Total	<u>176,240</u>	<u>290,808</u>	<u>(197,720)</u>	<u>269,328</u>
Capital Assets being depreciated:				
Buildings	3,660,747	215,855	-	3,876,602
Improvements other than Buildings	2,142,872	-	-	2,142,872
Machinery & Equipment	3,474,022	420,430	(46,029)	3,848,423
Public domain infrastructure	15,230,068	-	-	15,230,068
Total Capital Assets being depreciated	<u>24,507,709</u>	<u>636,285</u>	<u>(46,029)</u>	<u>25,097,965</u>
Less Accumulated Depreciation for:				
Buildings	2,900,437	56,059	-	2,956,496
Improvements other than Buildings	1,341,479	84,050	-	1,425,529
Machinery & Equipment	1,517,130	358,298	(46,029)	1,829,399
Public domain infrastructure	10,397,076	501,024	-	10,898,100
Total	<u>16,156,122</u>	<u>999,431</u>	<u>(46,029)</u>	<u>17,109,524</u>
Total Capital Assets being depreciated, Net	<u>8,351,587</u>	<u>(363,146)</u>	<u>-</u>	<u>7,988,441</u>
Total Government Activities Capital Assets, Net	<u>\$ 8,527,827</u>	<u>\$ (72,338)</u>	<u>\$ (197,720)</u>	<u>\$ 8,257,769</u>

Business-Type Activities:

	Beginning Balance	Additions	Deletions	Ending Balance
Capital Assets not being depreciated:				
Land	\$ 677,865	\$ -	\$ -	\$ 677,865
Construction in Progress	4,312,925	178,355	(4,473,380)	17,900
Total	<u>4,990,790</u>	<u>178,355</u>	<u>(4,473,380)</u>	<u>695,765</u>
Capital Assets being depreciated:				
Buildings & System	28,904,325	4,473,379	-	33,377,704
Machinery & Equipment	14,539,697	379,418	-	14,919,115
Total Capital Assets being depreciated	<u>43,444,022</u>	<u>4,852,797</u>	<u>-</u>	<u>48,296,819</u>
Less Accumulated Depreciation for:				
Buildings & System	8,881,847	873,872	-	9,755,719
Machinery & Equipment	8,501,816	625,457	-	9,127,273
Total	<u>17,383,663</u>	<u>1,499,329</u>	<u>-</u>	<u>18,882,992</u>
Total Capital Assets being depreciated, Net	<u>26,060,359</u>	<u>3,353,468</u>	<u>-</u>	<u>29,413,827</u>
Total Business Type Activities Capital Assets, Net	<u>\$ 31,051,149</u>	<u>\$ 3,531,823</u>	<u>\$ (4,473,380)</u>	<u>\$ 30,109,592</u>

CITY OF GROVES, TEXAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 5 - Capital Assets (continued)

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

Governmental Activities	
General	\$ 13,012
Public safety	286,395
Public works	607,903
Culture and recreation	92,121
	<u>\$ 999,431</u>
Business-type Activities	
Water and sewer	\$ 1,370,756
Solid waste	128,573
	<u>\$ 1,499,329</u>

Note 6 - Long-Term Debt

The City issues a variety of long-term debt instruments in order to acquire and/or construct major capital facilities and equipment for general government and enterprise fund activities. These instruments include general obligation bonds. Future ad valorem tax revenues secure these debt obligations.

During the year ended September 30, 2012, the following changes occurred in long-term liabilities:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Governmental Activities:					
General obligation bonds	\$ 11,785,000	\$	\$ (1,085,000)	\$ 10,700,000	\$ 1,150,000
Tax notes	253,964		(39,200)	214,764	42,000
Capital leases					
Compensated absences	638,065	19,621		657,686	131,537
Governmental Activities Long-term Liabilities	<u>\$ 12,677,029</u>	<u>\$ 39,242</u>	<u>\$ (1,124,200)</u>	<u>\$ 11,572,450</u>	<u>\$ 1,323,537</u>
Business Activities:					
Capital leases	\$ 1,214,696	\$	\$ (164,198)	\$ 1,050,498	\$ 171,883
Tax notes	526,036		(100,800)	425,236	108,000
Compensated absences	45,509	2,123		47,632	9,526
Business-type Activities Long-term Liabilities	<u>\$ 1,786,241</u>	<u>\$ 2,123</u>	<u>\$ (264,998)</u>	<u>\$ 1,523,366</u>	<u>\$ 289,409</u>

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 6 - Long-Term Debt (continued)

The following is a summary of the terms of obligations of general obligation bonds outstanding as of September 30, 2012:

Governmental Activities:				Maturity	Debt
Series	Interest Rate	Original Issue	Date	Outstanding	
General Obligation Bonds					
Series 2004	1.85%-4.25%	\$ 715,000	2026	\$ 555,000	
Series 2005	3.25%-4.00%	10,855,000	2018	6,080,000	
Series 2006	3.65%	5,000,000	2027	4,065,000	
Total General Obligation Bonds				<u>10,700,000</u>	
Tax Notes					
Series 2010	1.70%-4.00%	\$ 284,764	2016	\$ 214,764	
Total Tax Notes				<u>214,764</u>	
Total Governmental Activities				<u>\$ 10,914,764</u>	

Business Activities:				Debt
Series	Interest Rate	Original Issue		Outstanding
Tax Notes				
Series 2010	1.70%-4.00%	\$ 605,236	2016	\$ 425,236
Total Business Activities				<u>\$ 425,236</u>

Annual debt service requirements to retire outstanding general obligation bonds and tax notes are as follows:

Year Ending	Governmental Activities			
	General Obligation Bonds		Tax Notes	
	Principal	Interest	Principal	Interest
<u>9/30</u>				
2013	\$ 1,150,000	\$ 406,804	\$ 42,000	\$ 5,401
2014	1,195,000	365,119	55,255	4,173
2015	1,250,000	320,344	58,055	2,713
2016	1,300,000	272,016	59,454	952
2017	1,350,000	222,883		
2018	1,405,000	170,240		
2019	300,000	115,288		
2020	310,000	104,448		
2021	315,000	93,073		
2022	330,000	81,495		
2023	345,000	69,195		
2024	355,000	56,145		
2025	370,000	42,520		
2026	380,000	28,285		
2027	345,000	13,455		
	<u>\$ 10,700,000</u>	<u>\$ 2,361,310</u>	<u>\$ 214,764</u>	<u>\$ 13,238</u>

CITY OF GROVES, TEXAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 6 - Long-Term Debt (continued)

Year Ending	Business Activities	
	Tax Notes	
9/30	Principal	Interest
2013	\$ 108,000	\$ 13,887
2014	99,745	10,729
2015	106,945	6,975
2016	110,546	2,448
	<u>\$ 425,236</u>	<u>\$ 34,039</u>

Capital Leases

The City entered into a lease agreement to finance the acquisition of equipment for use in the Water and Sewer Enterprise Fund. This lease bears an interest rate 4.6 percent. The total purchase price of the equipment is approximately \$1.7 million. The agreement matures in 2018.

Amortization of leased vehicles under capital assets is included with depreciation expense. Annual debt service requirements to retire the capital lease is as follows:

Year Ending	Business Activities	
	Capital Leases	
9/30	Principal	Interest
2013	\$ 171,883	\$ 45,386
2014	179,927	37,342
2015	188,348	28,922
2016	197,130	20,139
2017	206,389	10,880
2018	106,821	1,228
	<u>\$ 1,050,498</u>	<u>\$ 143,897</u>

Legal Compliance

A number of limitations and restrictions are contained in the various bond ordinances. The City has complied with all significant limitations and restrictions.

CITY OF GROVES, TEXAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 7 - Interfund Transactions

The composition of interfund balances as of September 30, 2012, is as follows:

<u>Interfund Receivable</u>	<u>Interfund Payable</u>	<u>Amounts</u>	<u>Purpose</u>
General Fund	Water and Sewer Fund	\$ 2,265,487	Claim on cash due to pooled cash
Solid Waste	Water and Sewer Fund	185,270	Accounts Receivable due to Solid Waste fund
Nonmajor Governmental Fund	General Fund	<u>183,508</u>	Sales tax receivable due to EDC
		<u>\$ 2,634,265</u>	

The Water and Sewer Fund has an amount due to the General Fund for \$2.2 million. This amount is considered a long-term receivable as it will be paid from future cash flows from water and sewer activity. Amounts recorded as interfund receivables and payables are considered to be temporary loans and will be repaid during the following fiscal year.

A summary of interfund transfers, the purpose of which is to cover operational expenses/expenditures, for the year ended September 30, 2012, is as follows:

<u>Transfers Out</u>	<u>Transfers In</u>	<u>Amounts</u>	<u>Purpose</u>
Debt Service	Water and Sewer	117,256	Reclass series 2010 tax notes payments
Economic Development	Debt Service	700,000	Budgeted payment for EDC debt service
Police Forfeiture	General	8,000	Purchase of undercover narcotics vehicle
Water and Sewer	Debt Service	465,000	Budgeted payment for water and sewer debt service
General	Debt Service	<u>200,000</u>	Transfer cash to pay debt service payment
		<u>\$ 1,490,256</u>	

CITY OF GROVES, TEXAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 8 - Employee Retirement System

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 that have been adopted by the City are within the options available in the governing statutes of TMRS.

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

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 at least 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 (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 of the City, within the options available in the state statutes governing TMRS and within the actuarial constraints also in the statutes. Plan provisions for the City are as follows:

Employee deposit rate:	6%
Matching ratio (city to employee):	2 to 1
Years required for vesting	10
Updated service credit	100% repeating transfers

Members can retire at age 60 and above with five or more years of service or with 20 years of service regardless of age.

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 8 - Employee Retirement System (continued)

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 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 (i.e. December 31, 2010, valuation is effective for rates beginning in January 2012).

The City's total payroll in fiscal year 2012 was \$5.6 million and the City's contributions were based on a payroll of \$6.0 million. Contributions made by employees totaled \$334 thousand, and the City made contributions of \$644 thousand during the fiscal year ended September 30, 2012.

Annual Pension Cost

The City's annual pension cost was equal to the City's required and actual contributions. Three-year trend information for the City's TMRS plan follows:

<u>Fiscal Year</u>	<u>Annual Pension Cost (APC)</u>	<u>Percent Contributed</u>
2010	\$ 869,684	100%
2011	\$ 830,353	100%
2012	\$ 644,508	100%

Funding Policy

Cities are required to contribute at an actuarially determined rate; these rates are provided to the City on an annual basis, following the completion of actuarial valuation. As explained above, there is a time delay in the valuation and when the rate becomes effective. For example, the January 1, 2012, contribution rate is based on the December 31, 2010, valuation results. If a change in plan provisions is elected by the City, this rate can change. The actuary determines contribution rates on a calendar-year basis; the City discloses the annual pension costs (which equal the required contributions) based on the calculated rate(s) for the City's fiscal year.

CITY OF GROVES, TEXAS
NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 8 - Employee Retirement System (continued)

Funding Policy (continued)

The required contribution rates for fiscal year 2012 were determined as part of the December 31, 2009 and 2010, valuations. Additional information as of the latest actuarial valuation, December 31, 2011, also follows:

Valuation date	December 31, 2009	December 31, 2010	December 31, 2011
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	28 years; closed period	26.1 years; closed period	24.6 years; closed period
Amortization period for new gains/losses	30 years	30 years	30 years
Asset valuation method	Amortized cost	Amortized cost	Amortized cost
Actuarial Assumptions:			
Investment return *	7.5%	7.0%	7.0%
Projected salary increases *	varies by age and service	varies by age and service	varies by age and service
* Includes inflation at	3.0%	3.0%	3.0%
Cost-of-living adjustments	0.0%	0.0%	0.0%

The funded status of the plan as of December 31, 2011, the most recent actuarial valuation date, is as follows:

	December 31, 2011
Actuarial valuation date	
Actuarial value of plan assets (a)	29,038,587
Actuarial accrued liability (AAL) (b)	29,911,098
Unfunded/(Overfunded) actuarial accrued liability (UAAL or OAAL) (b-a)	\$872,511
Funded Ratio (a/b)	97.1%
Projected Annual Covered Payroll (c)	6,034,863
UAAL or OAAL as % of covered payroll ((b-a)/c)	14.5%

The schedule of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, presents multiyear trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Note 9 - Employee Section 457 Plan

The City offers its employees a deferred compensation plan through the International City Management Association (ICMA), created in accordance with Internal Revenue Code Section 457. The plan, available to all City employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency.

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 9 - Employee Section 457 Plan (continued)

Prior to the passage of a City ordinance on December 16, 1996, all amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to those amounts or rights were (until paid or made available to the employee or other beneficiary) solely the property and rights of the City (without being restricted to the provision of benefits under the plan). As a result of these terms, the City considered itself as an agent of the plan acting in a fiduciary capacity and reflected this status in previous years' financial statements.

However, as mentioned above, the City of Groves, Texas passed an ordinance on December 16, 1996, whereby the City amended and restated the deferred compensation plan (the "Plan") in the form of the ICMA Retirement Corporation Deferred Compensation Plan and Trust. The assets of the Plan shall be held in trust for the exclusive benefit of the Plan participants and their beneficiaries, and the assets shall not be diverted to any other purpose. The beneficial ownership of Plan assets held in the ICMA Retirement Trust shall be held for the participants and their beneficiaries, and not subject to the claims of the City's general creditors.

Note 10 - Employee Section 401 Plans

The City offers its employees options under two separate qualified defined contribution retirement plans which meet the requirements of Section 401(a) of the Internal Revenue Code. The City has selected ICMA Retirement Corporation, an agent multiple-employer public employee retirement program, as the administrator for the employee 401(a) retirement programs.

- (1) Section 401 Money Purchase Plan - Each participant has a plan account to which they may contribute up to 8% of qualified earnings on a pretax basis with the City matching 4%. Employee contributions, employer contributions, and earnings are not taxed until they are withdrawn. Participants may choose from a variety of mutual funds available in which to invest. Participants are always fully vested in their own contributions and the earnings on those contributions. Participant vesting in employer contributions are based on years of service.
- (2) Section 401 Profit Sharing Plan - Each participant has a plan account to which he/she may contribute up to 8% of qualified earnings on an after-tax basis, with the City matching one-half up to 4% of employee earnings. Earnings on plan contributions are not taxed until withdrawn.

	<u>Current Year</u>
401 Money Purchase Plan	
Employee Contributions	\$ 104,234
Employer Contributions	<u>52,117</u>
Total	\$ 156,351
401 Profit Sharing	
Employee Contributions	\$ 136,794
Employer Contributions	<u>68,397</u>
Total	\$ 205,191

CITY OF GROVES, TEXAS

NOTES TO THE BASIC FINANCIAL STATEMENTS (continued)

Note 11 - Commitments and Contingencies

Litigation and Other Contingencies

From time to time, the City is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, it is the opinion of City Management and legal counsel that any ultimate uninsured liability to the City from these lawsuits will not be material.

Note 12 - Risk Management

The City is exposed to various risks of losses related to torts, theft of, damage to and destruction of fixed assets; errors and omissions; injuries to employees; and natural disasters. The City has obtained commercial insurance coverage for these risks and provided various employee education and prevention programs.

There have been no significant reductions in insurance from the prior year. The liabilities for claims have not changed since last year. There have been no settlements in excess of coverage in the past three years. Claims liabilities are based on estimates of the ultimate cost of reported claims (including future claim adjustment expenses) and an estimate for claims incurred but not reported based on historical experience. Claims liabilities include specific, incremental claim adjustment expenses, allocated loss adjustment expenses, and are reduced for estimated recoveries on unsettled claims such as salvage or subrogation.

Required Supplementary Information

CITY OF GROVES, TEXAS

GENERAL FUND

SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE

BUDGET AND ACTUAL UNAUDITED

For the Year Ended September 30, 2012

	2012			
	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Variance Positive (Negative)</u>
Revenues				
Taxes:				
Property taxes	\$ 4,280,680	\$ 4,280,680	\$ 4,415,739	\$ 135,059
Sales and use taxes	1,464,000	1,464,000	1,172,518	(291,482)
Franchise taxes	1,025,000	1,025,000	1,009,511	(15,489)
Hotel taxes	85,000	85,000	61,047	(23,953)
Fines and forfeitures	208,500	208,500	157,407	(51,093)
Licenses and permits	163,750	163,750	154,031	(9,719)
Intergovernmental			161,613	161,613
Charges for services	87,970	87,970	26,125	(61,845)
Investment earnings	25,000	25,000	904	(24,096)
Miscellaneous	53,000	53,000	78,014	25,014
Total Revenues	<u>7,392,900</u>	<u>7,392,900</u>	<u>7,236,909</u>	<u>(155,991)</u>
Expenditures				
Current:				
General government	1,104,898	1,104,898	1,139,188	(34,290)
Public Safety	4,118,201	4,118,201	4,103,754	14,447
Public Works	2,041,893	2,041,893	2,015,819	26,074
Culture and recreation	747,408	747,408	593,142	154,266
Capital Outlay	46,500	46,500	742,524	(696,024)
Total Expenditures	<u>8,058,900</u>	<u>8,058,900</u>	<u>8,594,427</u>	<u>(535,527)</u>
Revenues under expenditures	(666,000)	(666,000)	(1,357,518)	(691,518)
Other Financing Sources (Uses)				
Proceeds from sale of assets			72,230	72,230
Transfers in	600,000	600,000	8,000	(592,000)
Transfers out	(200,000)	(200,000)	(200,000)	
Total other financing sources (uses)	<u>400,000</u>	<u>400,000</u>	<u>(119,770)</u>	<u>(592,000)</u>
Changes in fund balance	(266,000)	(266,000)	(1,477,288)	(1,283,518)
Fund Balances - Beginning of Year, as restated	<u>5,994,103</u>	<u>5,994,103</u>	<u>5,994,103</u>	
Fund Balances - End of Year	<u>\$ 5,728,103</u>	<u>\$ 5,728,103</u>	<u>\$ 4,516,815</u>	<u>\$ (1,211,288)</u>

CITY OF GROVES, TEXAS

NOTES TO REQUIRED SUPPLEMENTARY BUDGET INFORMATION

Year ended September 30, 2012

General Budget Policies

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for the following governmental funds: the General Fund, Groves Economic Development Fund, and Debt Service Fund. All other governmental funds are unbudgeted. All annual appropriations lapse at fiscal year-end. Budget amounts and comparisons presented in the financial statements are unaudited.

The City follows these procedures in establishing the budgetary data reflected in the financial statements.

1. On or before the first day of August each year, the Mayor or the City Manager shall submit to the City Council a budget estimate of the revenues of the City and the expenditures or expenses of conducting the affairs thereof for the ensuing year.
2. On receipt of the estimate, the City Council shall at once prepare an appropriation ordinance, using the estimate as a basis. Provisions shall be made for public hearings upon the appropriation ordinance before a committee of the City Council, or before the entire City Council sitting as a committee as a whole.
3. Following the public hearing, and before the second reading and final passage, the appropriation ordinance shall be published in the official newspaper of the City.
4. The City Council shall not pass the appropriation ordinance until at least ten days after its publication, but shall pass the appropriation ordinance no later than September 30 of each year.
5. The legal level of control is by fund level where the City Council's approval is required. The City Council may transfer unencumbered appropriations for the use of a department, division or purpose or any other department, division or purpose without public notice and public hearing except when such transfer shall be made of revenue or earnings of any non-tax supported public utility to any other purpose. No amendment is necessary if department expenditures exceed budget, as long as fund expenditures do not exceed the fund budget.
6. All budgets are adopted on a basis consistent with generally accepted accounting principles.

The City has not complied with budgetary spending rules for the year ended September 30, 2012, as expenditures exceeded appropriations at the fund level for the General Fund and GEDC.

CITY OF GROVES, TEXAS

REQUIRED PENSION SYSTEM SUPPLEMENTARY INFORMATION

September 30, 2012

TEXAS MUNICIPAL RETIREMENT SYSTEM (UNAUDITED)

Schedule of Funding Progress

Actuarial Valuation Date December 31,	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	(UAAL) as a Percentage of Covered Payroll ((b-a)/c)
2009	17,244,164	21,987,964	4,743,800	78.4%	6,158,168	77.0%
2010	27,386,285	29,117,087	1,730,802	94.1%	6,032,138	28.7%
2011	29,038,587	29,911,098	872,511	97.1%	6,034,863	14.5%

**Combining and Individual Fund
Statements and Schedules**

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Non-Major Governmental Funds

Special Revenue Funds

To account for the proceeds and specific revenue sources that are legally restricted to expenditures for specific purposes.

GEDC

This special revenue fund is used to account for the Groves Economic Development Corporation.

Police Special Fund

This special revenue fund is used to account for the receipt of state and federal narcotics seizure revenue and the expenditures of such funds for law enforcement drug-related areas.

Grant Fund

This special revenue fund is used to account for the activity relating to federal and state programs.

Capital Projects Fund

This special revenue fund is used to account for the activity relating to capital projects.

CITY OF GROVES, TEXAS
COMBINING BALANCE SHEET
NON-MAJOR GOVERNMENTAL FUNDS
September 30, 2012

	<u>GEDC</u>	<u>Police Forfeiture Fund</u>	<u>Grant Fund</u>	<u>Capital Projects Fund</u>	<u>Totals</u>
Assets					
Cash and cash equivalents	\$ 49,746	\$ 60,631	\$ 35,610	\$ 513,741	\$ 659,728
Due from other funds	183,508				183,508
Total Assets	<u>\$ 233,254</u>	<u>\$ 60,631</u>	<u>\$ 35,610</u>	<u>\$ 513,741</u>	<u>\$ 843,236</u>
Liabilities and Fund Balances					
Liabilities:					
Accounts payable	\$ 27	\$	\$	\$	\$ 27
Total Liabilities	<u>27</u>				<u>27</u>
Fund balances:					
Restricted for:					
Capital projects				513,741	513,741
Public safety		60,631	35,610		96,241
Economic development	233,227				233,227
Total Fund Balances	<u>233,227</u>	<u>60,631</u>	<u>35,610</u>	<u>513,741</u>	<u>843,209</u>
Total Liabilities and Fund Balances	<u>\$ 233,254</u>	<u>\$ 60,631</u>	<u>\$ 35,610</u>	<u>\$ 513,741</u>	<u>\$ 843,236</u>

CITY OF GROVES, TEXAS
COMBINING STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCE
NON-MAJOR GOVERNMENTAL FUNDS
For the Year Ended September 30, 2012

	<u>GEDC</u>	<u>Police Forfeiture Fund</u>	<u>Grant Fund</u>	<u>Capital Projects Fund</u>	<u>Totals</u>
Revenues					
Taxes:					
Sales taxes	\$ 584,737	\$	\$	\$	\$ 584,737
Intergovernmental			15,768		15,768
Charges for services	3,450				3,450
Investment earnings	30	13			43
Miscellaneous				1,668	1,668
Total Revenues	<u>588,217</u>	<u>13</u>	<u>15,768</u>	<u>1,668</u>	<u>605,666</u>
Expenditures					
Current:					
Public safety					
Economic development	114,977				114,977
Capital Outlay		11,144			11,144
Debt Service					
Principal					
Interest and other charges					
Total Expenditures	<u>114,977</u>	<u>11,144</u>			<u>126,121</u>
Revenues over expenditures	<u>473,240</u>	<u>(11,131)</u>	<u>15,768</u>	<u>1,668</u>	<u>479,545</u>
Other Financing Sources (Uses)					
Transfers out	(700,000)	(8,000)			(708,000)
Total other financing sources (uses)	<u>(700,000)</u>	<u>(8,000)</u>			<u>(708,000)</u>
Changes in Fund Balance	(226,760)	(19,131)	15,768	1,668	(228,455)
Fund Balances - Beginning of Year	<u>459,987</u>	<u>79,762</u>	<u>19,842</u>	<u>512,073</u>	<u>1,071,664</u>
Fund Balances - End of Year	<u>\$ 233,227</u>	<u>\$ 60,631</u>	<u>\$ 35,610</u>	<u>\$ 513,741</u>	<u>\$ 843,209</u>

CITY OF GROVES, TEXAS**DEBT SERVICE FUND****SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE -****BUDGET AND ACTUAL***For the Year Ended September 30, 2012*

	2012		
	Final Budget	Actual	Variance Positive (Negative)
Revenues			
Taxes:			
Property taxes	\$ 409,143	\$ 420,362	\$ 11,219
Investment earnings		27	27
Total Revenues	<u>409,143</u>	<u>420,389</u>	<u>11,246</u>
Expenditures			
Current:			
Debt Service:			
Principal	1,225,000	1,124,200	100,800
Interest and other charges	470,321	453,866	16,455
Total Expenditures	<u>1,695,321</u>	<u>1,578,066</u>	<u>117,255</u>
Revenues over (under) expenditures	(1,286,178)	(1,157,677)	128,501
Other Financing Sources			
Transfers in	1,365,000	1,365,000	
Transfers out		(117,256)	117,256
Total other financing sources (uses)	<u>1,365,000</u>	<u>1,247,744</u>	<u>(117,256)</u>
Revenues and other financing sources over expenditures	78,822	90,067	11,245
Fund Balances - Beginning of Year	<u>111,721</u>	<u>111,721</u>	
Fund Balances - End of Year	<u>\$ 190,543</u>	<u>\$ 201,788</u>	<u>\$ 11,245</u>

CITY OF GROVES, TEXAS**GROVES ECONOMIC DEVELOPMENT CORPORATION FUND****SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE -****BUDGET AND ACTUAL UNAUDITED***For the Year Ended September 30, 2012*

	2012		
	Final Budget	Actual	Variance Positive (Negative)
Revenues			
Taxes:			
Sales and use taxes	\$ 600,000	\$ 584,737	\$ (15,263)
Charges for services		3,450	3,450
Investment earnings	5,831	30	(5,801)
Total Revenues	<u>605,831</u>	<u>588,217</u>	<u>(17,614)</u>
Expenditures			
Current:			
Economic development	70,000	114,977	(44,977)
Total Expenditures	<u>70,000</u>	<u>114,977</u>	<u>(44,977)</u>
Revenues over (under) expenditures	535,831	473,240	(62,591)
Other Financing Uses			
Transfers out	<u>(775,000)</u>	<u>(700,000)</u>	<u>75,000</u>
Revenues and other financing sources over under expenditures	(239,169)	(226,760)	12,409
Fund Balances - Beginning of Year	<u>459,987</u>	<u>459,987</u>	
Fund Balances - End of Year	<u>\$ 220,818</u>	<u>\$ 233,227</u>	<u>\$ 12,409</u>