

City of Krum, Texas



ANNUAL FINANCIAL REPORT

FINANCIAL STATEMENTS

**FOR THE YEAR ENDED
SEPTEMBER 30, 2016**

PB&H
PATILLO, BROWN & HILL, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS ■ BUSINESS CONSULTANTS

CITY OF KRUM, TEXAS

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FINANCIAL SECTION



PATTILLO, BROWN & HILL, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS ■ BUSINESS CONSULTANTS

INDEPENDENT AUDITORS' REPORT

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

Report on the Financial Statements

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

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Krum, Texas, as of September 30, 2016, and the respective changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison information, schedule of changes in net pension liability and related ratios, and the schedule of contributions on pages 4 through 10 and 45 through 49 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

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

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

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 2, 2017, on our consideration of the City of Krum, Texas' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering City of Krum, Texas' internal control over financial reporting and compliance.

Pattillo, Brown & Hill, L.L.P.

Hillsboro, Texas
March 2, 2017

**MANAGEMENT'S
DISCUSSION AND ANALYSIS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

The City of Krum's discussion and analysis offers readers of the City's financial statements a narrative overview and analysis of the City's financial activities for the year ended September 30, 2016. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in the accompanying basic financial statements.

FINANCIAL HIGHLIGHTS

- The assets and deferred outflows of resources for the City of Krum exceeded its liabilities and deferred inflows of resources at the close of the most recent fiscal year by \$11,059,353. Of this amount, \$3,763,383 (unrestricted net position) may be used to meet the City's ongoing obligations to citizens and creditors.
- The City of Krum's net position increased by \$388,862. This increase is due to an increase in property and sales taxes as well as decreased water and sewer and interest and other fees expenses. These changes were offset by increased general government, public safety, public works and streets expenses as well as decreased operating grants and contributions. The increase is less than the prior year increase of \$464,661.
- As of the close of the current fiscal year, the City of Krum's governmental funds reported combined ending fund balances of \$3,628,645, a decrease of \$1,851,571 in comparison with the prior year. Approximately, 15.07% of this amount, \$546,931 is available for spending at the City's discretion (unassigned fund balance).
- At the end of the current fiscal year, the unassigned fund balance for the General Fund was \$546,931 or 19.67% of total General Fund expenditures.

OVERVIEW OF THE FINANCIAL STATEMENTS

The discussion and analysis is intended to serve as an introduction to the City of Krum, Texas' basic financial statements. City of Krum'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.

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

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

The statement of activities presents information showing how the government's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in these statements 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 the statement of net position and the statement of activities are prepared utilizing the full accrual basis of accounting.

In the Statement of Net Position and the Statement of Activities, the primary government is divided into two kinds of activities:

- **Governmental activities** – Most of the City’s basic services are reported here, including administrative, police, fire, municipal court, community development, streets, parks and library. Property taxes, sales taxes, franchise fees, license and permit fees finance most of these activities.
- **Business-type activities** – The City charges a fee to customers to cover all or most of the cost of certain services it provides. The City’s water and sewer system are reported here.

The government-wide financial statements include not only the City of Krum itself (known as the primary government), but also two legally separate component units, the Krum Economic Development Corporation and the 4A Sales and Use Tax Fund. Financial information for these component units is included in the financial statements for the City as blended component units.

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. City of Krum, 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 of Krum can be divided into two categories: governmental funds and proprietary funds.

Governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as 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 of Krum maintains 8 individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General Fund, Debt Service Fund, Capital Projects Fund, Krum Economic Development Fund and 4A Sales and Use Tax Fund, which are considered to be major funds. Data from the other 3 governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these nonmajor governmental funds is provided in the form of combining statements elsewhere in this report.

The City of Krum adopts an annual appropriated budget for its General Fund, Economic Development Fund and Debt Service Fund. Budgetary comparison statements have been provided for the General Fund, Economic Development Fund and the Debt Service Fund to demonstrate compliance with the budget.

Proprietary funds. The City charges customers for the services it provides, whether to outside customers or to other units within the City. These services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Position and the Statement of Activities. There is one type of proprietary fund: Enterprise Fund. The City's Enterprise Fund is identical to the business-type activities that are reported in the government-wide statements but provide more detail and additional information, such as cash flows, for proprietary funds.

The City of Krum maintains one individual Enterprise Fund to account for its water and sewer. This fund is considered to be a major fund of the City.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found in the financial section.

Other information. The combining statements referred to earlier in connection with nonmajor governmental funds are presented immediately following the notes to the financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, over time net position may serve as a useful indicator of a government's financial position. In the case of the City of Krum, assets and deferred outflows exceeded liabilities and deferred inflows by \$11,059,353 at the close of the most recent fiscal year. One of the larger portions of the City's net position (\$5,827,428 or 52.69%) reflects its investment in capital assets (e.g. land, building, machinery, and equipment) less any related debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

	Governmental Activities		Business-Type Activities		Total	
	2016	2015	2016	2015	2016	2015
Assets						
Current and other assets	\$ 4,160,171	\$ 5,645,866	\$ 1,884,388	\$ 2,646,347	\$ 6,044,559	\$ 8,292,213
Capital and non-current assets	7,948,509	5,873,696	5,879,549	5,761,899	13,828,058	11,635,595
Total assets	<u>12,108,680</u>	<u>11,519,562</u>	<u>7,763,937</u>	<u>8,408,246</u>	<u>19,872,617</u>	<u>19,927,808</u>
Total deferred outflows of resources	<u>154,269</u>	<u>64,872</u>	<u>64,053</u>	<u>55,337</u>	<u>218,322</u>	<u>120,209</u>
Liabilities						
Current liabilities	910,032	580,381	532,529	578,970	1,442,561	1,159,351
Long-term liabilities	4,626,694	4,958,116	2,938,957	3,244,951	7,565,651	8,203,067
Total liabilities	<u>5,536,726</u>	<u>5,538,497</u>	<u>3,471,485</u>	<u>3,823,921</u>	<u>9,008,211</u>	<u>9,362,418</u>
Total deferred inflows of resources	<u>20,464</u>	<u>13,437</u>	<u>2,911</u>	<u>1,671</u>	<u>23,375</u>	<u>15,108</u>
Net position						
Net investment in fixed assets	3,199,109	2,390,036	2,628,319	2,121,350	5,827,428	4,511,386
Restricted	1,468,542	1,219,303	-	-	1,468,542	1,219,303
Unrestricted	<u>2,038,108</u>	<u>2,423,161</u>	<u>1,725,275</u>	<u>2,516,641</u>	<u>3,763,383</u>	<u>4,939,802</u>
Total net position	<u>\$ 6,705,759</u>	<u>\$ 6,032,500</u>	<u>\$ 4,353,594</u>	<u>\$ 4,637,991</u>	<u>\$ 11,059,353</u>	<u>\$ 10,670,491</u>

An additional portion of the City of Krum’s net position (\$1,468,542 or 13.28%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net position (\$3,763,383 or 34.03%) may be used to meet the government’s ongoing obligations to citizens and creditors.

At the end of the current fiscal year, the City reported a positive balance in all three categories of net position, both for the government as a whole, as well as for its separate governmental and business-type activities.

During the current fiscal year, the City’s net position increased by \$388,862. This increase represents the degree to which increases in ongoing revenues have outstripped similar increases in ongoing expenses. This increase follows a prior year increase of \$464,661 due to increases in property and sales taxes and decreased water and sewer and interest and other fees expenses offset by increased general government, public safety, public works and streets expenses as well as decreased operating grants and contributions.

Changes in the City's Net Position

	Governmental Activities		Business-Type Activities		Total	
	2016	2015	2016	2015	2016	2015
Revenues:						
Program revenues:						
Charges for services	\$ 770,894	\$ 731,600	\$ 1,793,504	\$ 1,778,159	\$ 2,564,398	\$ 2,509,759
Capital grants & contributions	261,940	242,794	-	-	261,940	242,794
Operating grants & contributions	27,951	392,492	-	-	27,951	392,492
General revenues:						
Property taxes	1,761,111	1,631,799	-	-	1,761,111	1,631,799
Sales taxes	516,755	387,801	-	-	516,755	387,801
Franchise fees	238,502	222,816	-	-	238,502	222,816
Investment earnings	34,818	26,941	638	404	35,456	27,345
Loss on sale of assets	-	-	-	-	-	-
Miscellaneous	40,549	73,023	-	32,160	40,549	105,183
Total revenues	<u>3,652,520</u>	<u>3,709,266</u>	<u>1,794,142</u>	<u>1,810,723</u>	<u>5,446,662</u>	<u>5,519,989</u>
Expenses:						
General government	475,948	457,271	-	-	475,948	457,271
Public safety	2,015,052	1,929,882	-	-	2,015,052	1,929,882
Public works	460,440	443,225	-	-	460,440	443,225
Culture and recreation	212,277	205,493	-	-	212,277	205,493
Streets	15,943	-	-	-	15,943	-
Economic development	16,814	21,478	-	-	16,814	21,478
Waster and sewer	-	-	1,581,541	1,660,062	1,581,541	1,660,062
Interest and other fees	190,884	215,762	88,901	122,155	279,785	337,917
Total expenses	<u>3,387,358</u>	<u>3,273,111</u>	<u>1,670,442</u>	<u>1,782,217</u>	<u>5,057,800</u>	<u>5,055,328</u>
Excess before transfers	265,162	436,155	123,700	28,506	388,862	464,661
Transfers	408,097	208,893	(408,097)	(208,893)	-	-
Change in net position	673,259	645,048	(284,397)	(180,387)	388,862	464,661
Net position - beginning of year	6,032,500	4,915,912	4,637,991	4,801,167	10,670,491	9,717,079
Prior period adjustment	-	471,540	-	17,211	-	488,751
Net position - end of year	<u>\$ 6,705,759</u>	<u>\$ 6,032,500</u>	<u>\$ 4,353,594</u>	<u>\$ 4,637,991</u>	<u>\$ 11,059,353</u>	<u>\$ 10,670,491</u>

City Revenues

A significant portion, 47.08% of the City’s total revenues comes from charges for services and 46.20% comes from property, sales and franchise taxes. The remaining 6.72% is comprised of interest income, other charges, donations, and grant revenues (see Figure A-3).

Governmental activities. Governmental activities net position increased by \$673,259. The increase is more than the prior year increase of \$645,048 due primarily to an increase in property and sales taxes and decreased interest and other fees expenses. These changes were offset by decreased operating grants and contributions as well as increased general government, public safety, public works and streets expenses.

Business-type activities. Business-type activities net position decreased by \$284,397. Gross revenue of the Water and Sewer Fund was \$1,794,142 for the fiscal year, which is \$16,581 less than the 2014-2015 fiscal year gross revenue of \$1,810,723. This decrease is a result of a decrease in miscellaneous revenue offset by an increase in charges for services. Direct operating expenses, excluding depreciation, were \$1,313,030 for the fiscal year. Direct operating expenses are \$66,746 less than 2014-2015 fiscal year direct operating expenses of \$1,379,776, due to decreased costs of personnel services, contractual services and repairs and maintenance.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

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

At the end of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$3,628,645. \$3,042,658 of this total is restricted to indicate constraints placed on the use of the resources either externally imposed by creditors, by laws or regulations of other governments imposed or imposed by law through constitutional provisions or enabling legislation. \$39,056 of this total is committed is for public safety. The remaining balance of \$546,931 constitutes unassigned fund balance.

Of the \$3,628,645 ending fund balance, \$54,697 is accounted for in non-major governmental funds. The General Fund balance is \$585,987 at year end – an increase of \$143,515. This increase was created primarily by a combination of increased sales taxes, franchise fees, intergovernmental and charges for services revenue offset by an increase in public safety expenditures.

The Debt Service Fund balance increased \$48,205 to \$685,866 at year end. This increase is primarily the result of increased property tax revenue offset by increased debt service expenditures. The Capital Projects Fund balance decreased \$2,243,060 to a year-end total of \$1,580,545. This decrease is caused by capital outlay expenditures related to projects including grant projects exceeding revenue. The Krum Economic Development Fund balance increased \$111,429 to a year-end total of \$435,429. This increase is primarily related to increased sales tax revenue. The 4A Sales & Use Tax Fund balance increased \$99,650 to a year-end total of \$286,121 due to an increase in sales taxes revenue offset by an increase in culture and recreation expenditures.

Proprietary funds – The City of Krum's proprietary funds provide the same type of information found in government-wide financial statements, but in more detail.

Year-end net position in the water and sewer fund amounted to \$4,353,594. This includes a current year decrease of \$284,397. See the business-type activity discussion above for more information.

General Fund budgetary highlights – Over the course of the year, the City revised its budget several times. Including these adjustments, general fund revenues were \$128,849 over budgeted revenues and expenditures were \$75,102 under budgeted expenditures. The net budget decrease for the general fund was \$60,436 for the year, which includes other financing sources and uses and transfers. There was an actual increase of \$143,515 which was \$203,951 more than the budgeted decrease.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital assets – The investment in capital assets for its governmental and business type activities as of September 30, 2016, amounts to \$13,828,058 (net of accumulated depreciation). This investment in capital assets includes land, buildings, machinery and equipment, infrastructure, construction work in progress, and water and sewer systems. Approximately 57.48% of the capital assets are governmental and 42.52% are business type activities.

	Governmental Activities		Business-Type Activities		Total	
	2016	2015	2016	2015	2016	2015
Land	\$ 869,245	\$ 869,245	\$ 166,910	\$ 166,910	\$ 1,036,155	\$ 1,036,155
Construction in progress	2,428,709	64,697	721,157	334,997	3,149,866	399,694
Park improvements	710,774	710,774	-	-	710,774	710,774
Infrastructure	3,200,914	3,200,914	8,313,647	8,313,647	11,514,561	11,514,561
Buildings and improvements	1,685,922	1,685,922	152,142	152,142	1,838,064	1,838,064
Machinery and equipment	1,878,978	1,812,980	277,774	277,774	2,156,752	2,090,754
Other	-	-	63,382	63,382	63,382	63,382
Total at historical cost	10,774,542	8,344,532	9,695,012	9,308,852	20,469,554	17,653,384
Less accumulated depreciation	(2,826,033)	(2,470,836)	(3,815,463)	(3,546,953)	(6,641,496)	(6,017,789)
Net capital assets	\$ 7,948,509	\$ 5,873,696	\$ 5,879,549	\$ 5,761,899	\$ 13,828,058	\$ 11,635,595

Long-Term Debt

At year-end, the City had \$8,120,158 in long-term debt outstanding as shown below. More detailed information about the City’s debt is presented in the notes to the financial statements.

	Governmental Activities		Business-Type Activities		Total	
	2016	2015	2016	2015	2016	2015
Notes payable	\$ 383,644	\$ 529,291	\$ -	\$ -	\$ 383,644	\$ 529,291
Capital leases	86,514	137,408	-	-	86,514	137,408
Bonds payable	4,416,704	4,673,381	3,233,296	3,621,619	7,650,000	8,295,000
Total	\$ 4,886,862	\$ 5,340,080	\$ 3,233,296	\$ 3,621,619	\$ 8,120,158	\$ 8,961,699

ECONOMIC FACTORS AND NEXT YEAR’S BUDGETS AND RATES

An appraised ad-valorem taxable value used for the 2016 budget preparation was \$294 million dollars resulting in an estimated tax levy of \$1.9 million. The City’s tax rate for 2016 is \$0.647489 per \$100 valuation. The maintenance and operation and debt service rates are \$0.467482 and \$0.180007 per \$100 valuation, respectively. This information was taken into consideration when adopting the budget for 2016. Additionally, estimated revenue from the water and sewer billing is projected to be \$2.2 million.

The tax rate of \$0.647489 together with the water and sewer revenue is expected to provide for adequate funding of expenditure in the general fund, water and sewer fund, and debt service fund to continue current operations and to appropriate funding for long-term debt and capital equipment.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

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 demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional financial information, please contact the City Finance Director.

**BASIC
FINANCIAL STATEMENTS**

CITY OF KRUM, TEXAS
STATEMENT OF NET POSITION
SEPTEMBER 30, 2016

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 3,771,551	\$ 1,519,328	\$ 5,290,879
Receivables, net	335,254	185,533	520,787
Net pension asset	14,310	2,035	16,345
Restricted cash and cash equivalents	39,056	176,800	215,856
Prepays	-	692	692
Total current assets	<u>4,160,171</u>	<u>1,884,388</u>	<u>6,044,559</u>
Capital assets:			
Non-depreciable assets	3,297,954	888,067	4,186,021
Depreciable assets, net	<u>4,650,555</u>	<u>4,991,482</u>	<u>9,642,037</u>
Total capital assets	<u>7,948,509</u>	<u>5,879,549</u>	<u>13,828,058</u>
Total assets	<u>12,108,680</u>	<u>7,763,937</u>	<u>19,872,617</u>
DEFERRED OUTFLOWS OF RESOURCES			
Deferred charge on refunding	24,005	45,527	69,532
Deferred outflow related to TMRS	<u>130,264</u>	<u>18,526</u>	<u>148,790</u>
Total deferred outflows of resources	<u>154,269</u>	<u>64,053</u>	<u>218,322</u>
LIABILITIES			
Current liabilities:			
Accounts payable	439,995	96,235	536,230
Accrued liabilities	24,997	5,371	30,368
Accrued interest	20,589	10,895	31,484
Customer deposits	-	95,320	95,320
Compensated absences	20,984	3,109	24,093
Current portion long-term debt	<u>403,467</u>	<u>321,599</u>	<u>725,066</u>
Total current liabilities	<u>910,032</u>	<u>532,529</u>	<u>1,442,561</u>
Compensated absences	62,950	9,326	72,276
Long-term debt, less current portion	<u>4,563,744</u>	<u>2,929,631</u>	<u>7,493,375</u>
Total long-term liabilities	<u>4,626,694</u>	<u>2,938,957</u>	<u>7,565,651</u>
Total liabilities	<u>5,536,726</u>	<u>3,471,485</u>	<u>9,008,211</u>
DEFERRED INFLOWS OF RESOURCES			
Deferred inflow related to TMRS	<u>20,464</u>	<u>2,911</u>	<u>23,375</u>
Total deferred inflows of resources	<u>20,464</u>	<u>2,911</u>	<u>23,375</u>
NET POSITION			
Net investment in capital assets	3,199,109	2,628,319	5,827,428
Restricted	1,468,542	-	1,468,542
Unrestricted	<u>2,038,108</u>	<u>1,725,275</u>	<u>3,763,383</u>
Total net position	<u>\$ 6,705,759</u>	<u>\$ 4,353,594</u>	<u>\$ 11,059,353</u>

The accompanying notes are an integral part of this financial statement.

CITY OF KRUM, TEXAS

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED SEPTEMBER 30, 2016

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenues</u>		
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>
Primary government				
Governmental activities:				
General governmental	\$ 475,948	\$ 214,922	\$ -	\$ -
Public safety	2,015,052	503,366	247,816	-
Public works	460,440	50,586	-	27,951
Culture and recreation	212,277	2,020	14,124	-
Streets	15,943	-	-	-
Economic development	16,814	-	-	-
Interest and other fees	190,884	-	-	-
Total governmental activities	<u>3,387,358</u>	<u>770,894</u>	<u>261,940</u>	<u>27,951</u>
Business-type activities:				
Water and sewer	1,581,541	1,793,504	-	-
Interest and other fees	88,901	-	-	-
Total business-type activities	<u>1,670,442</u>	<u>1,793,504</u>	<u>-</u>	<u>-</u>
Total primary government	<u>\$ 5,057,800</u>	<u>\$ 2,564,398</u>	<u>\$ 261,940</u>	<u>27,951</u>

General revenues:

- Taxes
 - Property taxes, levied for general purposes
 - Property taxes, levied for specific purposes
 - Sales taxes
 - Other taxes
- Franchise fees
- Investment earnings
- Miscellaneous
- Transfers
- Total general revenues and transfers
- Changes in net position
- Net position - beginning
- Net position - ending

The accompanying notes are an integral part of this financial statement.

**Net (Expense) Revenue and
Changes in Net Position**

<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
\$(261,026)	\$ -	\$(261,026)
(1,263,870)	-	(1,263,870)
(381,903)	-	(381,903)
(196,133)	-	(196,133)
(15,943)	-	(15,943)
(16,814)	-	(16,814)
(190,884)	-	(190,884)
<u>(2,326,573)</u>	<u>-</u>	<u>(2,326,573)</u>
-	211,963	211,963
<u>-</u>	<u>(88,901)</u>	<u>(88,901)</u>
<u>-</u>	<u>123,062</u>	<u>123,062</u>
<u>(2,326,573)</u>	<u>123,062</u>	<u>(2,203,511)</u>
1,187,815	-	1,187,815
573,296	-	573,296
516,755	-	516,755
2,589	-	2,589
238,502	-	238,502
34,818	638	35,456
37,960	-	37,960
<u>408,097</u>	<u>(408,097)</u>	<u>-</u>
<u>2,999,832</u>	<u>(407,459)</u>	<u>2,592,373</u>
673,259	(284,397)	388,862
<u>6,032,500</u>	<u>4,637,991</u>	<u>10,670,491</u>
<u>\$ 6,705,759</u>	<u>\$ 4,353,594</u>	<u>\$ 11,059,353</u>

CITY OF KRUM, TEXAS

BALANCE SHEET

GOVERNMENTAL FUNDS

SEPTEMBER 30, 2016

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Capital Projects Fund</u>
ASSETS			
Cash and cash equivalents	\$ 520,244	\$ 685,329	\$ 1,835,739
Receivables (net of allowances for uncollectible):			
Taxes	67,634	6,966	-
Accounts receivable	97,597	-	-
Due from other governments	-	-	115,031
Restricted cash and cash equivalents	39,056	-	-
Total assets	<u>\$ 724,531</u>	<u>\$ 692,295</u>	<u>\$ 1,950,770</u>
LIABILITIES			
Accounts payable	\$ 67,752	\$ -	\$ 370,225
Accrued liabilities	24,997	-	-
Total liabilities	<u>92,749</u>	<u>-</u>	<u>370,225</u>
DEFERRED INFLOWS OF RESOURCES			
Unavailable revenue - property taxes	18,496	6,429	-
Unavailable revenue - EMS	27,299	-	-
Total deferred inflows of resources	<u>45,795</u>	<u>6,429</u>	<u>-</u>
FUND BALANCES			
Restricted	-	685,866	1,580,545
Committed	39,056	-	-
Unassigned	546,931	-	-
Total funds balances	<u>585,987</u>	<u>685,866</u>	<u>1,580,545</u>
 Total liabilities, deferred inflows of resources and fund balances	 <u>\$ 724,531</u>	 <u>\$ 692,295</u>	 <u>\$ 1,950,770</u>

The accompanying notes are an integral part of this financial statement.

Krum Economic Development	4A Sales & Use Tax Fund	Other Governmental Funds	Total Governmental Funds
\$ 411,416	\$ 262,995	\$ 55,828	\$ 3,771,551
24,013	24,013	-	122,626
-	-	-	97,597
-	-	-	115,031
-	-	-	39,056
<u>\$ 435,429</u>	<u>\$ 287,008</u>	<u>\$ 55,828</u>	<u>\$ 4,145,861</u>
\$ -	\$ 887	\$ 1,131	\$ 439,995
-	-	-	24,997
<u>-</u>	<u>887</u>	<u>1,131</u>	<u>464,992</u>
-	-	-	24,925
-	-	-	27,299
-	-	-	52,224
435,429	286,121	54,697	3,042,658
-	-	-	39,056
-	-	-	546,931
<u>435,429</u>	<u>286,121</u>	<u>54,697</u>	<u>3,628,645</u>
<u>\$ 435,429</u>	<u>\$ 287,008</u>	<u>\$ 55,828</u>	<u>\$ 4,145,861</u>

CITY OF KRUM, TEXAS

**RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCES SHEET
TO THE STATEMENT OF NET POSITION**

SEPTEMBER 30, 2016

Total fund balance - governmental funds \$ 3,628,645

Amounts reported for governmental activities in the statement of net position are difference due to the following:

Capital assets used in governmental activities are not financial resources and therefore are not reported as assets in governmental funds. 7,948,509

Certain charges related to the issuance of debt and insurance were expended, but will be amortized over the life of the debt, and therefore are deferred in the government wide statements. 1,797

Long-term liabilities, including liabilities for compensated absences, bonds and notes payable, obligations under capital lease and net pension liability (asset) are not due and payable in the current period and therefore are not reported as liabilities in the (4,904,827)

Interest payable is not due and payable in the current period and, therefore, is not reported as a liability in the governmental funds. (20,589)

Other long-term assets are not available to pay for current period expenditures and, therefore, are reported as unavailable revenue in the funds. 52,224

Net position of governmental activities \$ 6,705,759

The accompanying notes are an integral part of this financial statement.

CITY OF KRUM, TEXAS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2016

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Capital Projects Fund</u>
REVENUES			
Property taxes	\$ 1,184,740	\$ 572,031	\$ -
Sales taxes	260,230	-	-
Franchise fees	238,502	-	-
Licenses and permits	40,535	-	-
Fines and forfeitures	122,327	-	-
Intergovernmental	293,702	-	-
Charges for services	582,412	-	-
Investment earnings	12,234	5,304	16,594
Other	<u>37,752</u>	<u>-</u>	<u>-</u>
Total revenues	<u>2,772,434</u>	<u>577,335</u>	<u>16,594</u>
EXPENDITURES			
Current:			
General government	421,585	-	-
Public safety	1,768,819	-	-
Public works	352,254	-	-
Culture and recreation	152,589	-	-
Streets	-	-	-
Economic development	-	-	-
Debt service:			
Principal	50,896	402,322	-
Interest and fiscal charges	5,612	188,538	-
Capital outlay	<u>29,075</u>	<u>-</u>	<u>2,456,110</u>
Total expenditures	<u>2,780,830</u>	<u>590,860</u>	<u>2,456,110</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(8,396)</u>	<u>(13,525)</u>	<u>(2,439,516)</u>
OTHER FINANCING SOURCES (USES)			
Transfers in	151,911	61,730	196,456
Transfers out	<u>-</u>	<u>-</u>	<u>-</u>
Total other financing sources (uses)	<u>151,911</u>	<u>61,730</u>	<u>196,456</u>
Net change in fund balances	143,515	48,205	(2,243,060)
Fund balances - beginning	<u>442,472</u>	<u>637,661</u>	<u>3,823,605</u>
Fund balances - ending	<u>\$ 585,987</u>	<u>\$ 685,866</u>	<u>\$ 1,580,545</u>

The accompanying notes are an integral part of this financial statement.

Krum Economic Development	4A Sales & Use Tax Fund	Other Governmental Funds	Total Governmental Funds
\$ -	\$ -	\$ -	\$ 1,756,771
129,557	129,557	-	519,344
-	-	-	238,502
-	-	-	40,535
-	-	6,810	129,137
-	-	-	293,702
-	-	-	582,412
686	-	-	34,818
-	208	-	37,960
<u>130,243</u>	<u>129,765</u>	<u>6,810</u>	<u>3,633,181</u>
-	-	-	421,585
-	-	2,177	1,770,996
-	-	-	352,254
-	30,115	-	182,704
-	-	15,943	15,943
16,814	-	-	16,814
-	-	-	453,218
-	-	-	194,150
-	-	-	2,485,185
<u>16,814</u>	<u>30,115</u>	<u>18,120</u>	<u>5,892,849</u>
<u>113,429</u>	<u>99,650</u>	<u>(11,310)</u>	<u>(2,259,668)</u>
-	-	-	410,097
<u>(2,000)</u>	<u>-</u>	<u>-</u>	<u>(2,000)</u>
<u>(2,000)</u>	<u>-</u>	<u>-</u>	<u>408,097</u>
111,429	99,650	(11,310)	(1,851,571)
<u>324,000</u>	<u>186,471</u>	<u>66,007</u>	<u>5,480,216</u>
<u>\$ 435,429</u>	<u>\$ 286,121</u>	<u>\$ 54,697</u>	<u>\$ 3,628,645</u>

CITY OF KRUM, TEXAS

**RECONILICATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN
FUND BALANCE OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES**

YEAR ENDED SEPTEMBER 30, 2016

Net change in fund balances - total governmental funds \$(1,851,571)

Amounts reported for governmental activities in the statement of activities are different due to the

Governmental funds report outlays for capital assets as expenditures. However, in the statement of activities, the cost of those assets is allocated over their useful lives and reported as depreciation expense. This is the amount by which capital outlays exceed depreciation expense in the current period. 2,074,813

The issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principle of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net position. Also, governmental funds report the effect of premiums, discounts and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. This amount is the net effect of these differences in the treatment of long-term debt and related items. 455,015

Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental (5,938)

Certain pension expenditures are not expended in the government-wide financials statements and recorded as deferred resource outflows. This item relates to contributions made after the measurement date. Additionally, a portion of the City's unrecognized deferred resource inflows/outflows related to the pension liability/asset were amortized. (18,399)

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds. 19,339

Changes in net position - governmental activities \$ 673,259

The accompanying notes are an integral part of this financial statement.

CITY OF KRUM, TEXAS
STATEMENT OF NET POSITION
PROPRIETARY FUND
SEPTEMBER 30, 2016

	Enterprise Fund - Water and Sewer
ASSETS	
Current assets:	
Cash and cash equivalents	\$ 1,519,328
Receivables (net of allowances for uncollectible):	
Accounts receivable	185,533
Prepaid expense	692
Restricted cash and cash equivalents	176,800
Total current assets	1,882,353
Non-current assets:	
Net pension asset	2,035
Capital assets:	
Non-depreciable assets	888,067
Depreciable assets, net	4,991,482
Total non-current assets	5,881,584
Total assets	7,763,937
DEFERRED OUTFLOWS OF RESOURCES	
Deferred charge on refunding	45,527
Deferred outflows related to TMRS	18,526
Total deferred outflows of resources	64,053
LIABILITIES	
Current liabilities:	
Accounts payable	96,235
Accrued liabilities	5,371
Accrued interest payable	10,895
Customer deposits	95,320
Compensated absences	3,109
Current portion long-term debt obligations	321,599
Total current liabilities	532,529
Compensated absences	9,326
Long-term debt obligations, less current portion	2,929,631
Total long-term liabilities	2,938,957
Total liabilities	3,471,485
DEFERRED INFLOWS OF RESOURCES	
Deferred inflows related to TMRS	2,911
Total deferred inflows of resources	2,911
NET POSITION	
Net investment in capital assets	2,628,319
Unrestricted	1,725,275
Total net position	\$ 4,353,594

The accompanying notes are an integral part of this financial statement.

CITY OF KRUM, TEXAS
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
PROPRIETARY FUND
YEAR ENDED SEPTEMBER 30, 2016

	Enterprise Fund - Water and Sewer
OPERATING REVENUES	
Charges for services	\$ 1,793,504
Total operating revenues	1,793,504
OPERATING EXPENSES	
Personnel services	227,617
Contractual services	790,440
Operations	174,219
Repairs and maintenance	66,688
Supplies and materials	54,066
Depreciation	268,511
Total operating expenses	1,581,541
Total operating income	211,963
NON-OPERATING REVENUES (EXPENSES)	
Investment earnings	638
Interest expense	(88,901)
Total non-operating expenses	(88,263)
Net income before transfers	123,700
OTHER FINANCING SOURCES	
Transfers out	(408,097)
Total other financing sources	(408,097)
Change in net position	(284,397)
Total net position - beginning of year	4,637,991
Total net position - end of year	\$ 4,353,594

The accompanying notes are an integral part of this financial statement.

CITY OF KRUM, TEXAS
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
SEPTEMBER 30, 2016

CASH FLOWS FROM OPERATING ACTIVITIES

Cash received from customers	\$ 1,865,019
Cash payments to employees for services	(226,983)
Cash payments to other suppliers for goods and services	(1,057,740)
Net cash provided by operating activities	<u>580,296</u>

CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES

Transfers to other funds	(408,097)
Net cash provided by non-capital financing activities	<u>408,097</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

Principal paid on long-term debt	(388,323)
Interest paid on long-term debt	(85,868)
Acquisition and construction of capital assets	(386,161)
Net cash used in capital and related financing activities	<u>860,352</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Interest and dividends received	<u>638</u>
Net cash provided by investing activities	<u>638</u>

Net increase in cash and cash equivalents	(687,515)
Cash and cash equivalents - beginning of year	<u>2,383,643</u>
Cash and cash equivalents - end of year	<u>1,696,128</u>

Reconciliation of operating income to net cash provided

by operating activities:

Operating income	211,963
Adjustments to reconcile operating income to net cash provided by operating activities	
Depreciation	268,511
Decrease (increase) in accounts receivable	67,705
Decrease (increase) in due from other funds	9,466
Decrease (increase) in prepaid expenses	(692)
Decrease (increase) in net pension asset	12,607
Decrease (increase) in deferred outflows related to TMRS	(13,775)
Increase (decrease) in accounts payable	18,899
Increase (decrease) in accrued liabilities	(2,049)
Increase (decrease) in deferred inflows related to TMRS	1,240
Increase (decrease) in customer deposits	3,810
Increase (decrease) in compensated absences	<u>2,611</u>
Net cash provided by operating activities	<u>\$ 580,296</u>

The accompanying notes are an integral part of this financial statement.

CITY OF KRUM, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements of the City of Krum, Texas (the City) have been prepared in conformity with generally accepted accounting principles applicable to state and local governments. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The following notes to the City's financial statements are an integral part of the City's annual financial report.

A. Reporting Entity

The City of Krum was incorporated under the laws of the State of Texas in 1955 and operates under a Mayor-Council form of government. The City's basic financial statements include all activities, organizations, and functions for which the City is considered to be financially accountable and other organizations for which the nature and significance of their relationship with the City are such that inclusion would cause the City's financial statements to be misleading or incomplete. The reporting entity is the primary government, or the City, and those component units for which the primary government is financially accountable.

Financial accountability is defined as the appointment of a voting majority of the potential component unit's board and either the ability to impose its will by the primary government or the possibility that the component unit will provide a financial benefit or impose a financial burden on the primary government. Based on these considerations, the City's financial statements include the Krum Economic Development Corporation (KEDC) and the 4A Sales and Use Tax Fund (4A) as blended component units. KEDC and 4A were created by the City under the Texas Development Corporation Act of 1979 for the purpose of promoting, assisting, and enhancing economic and development activities on behalf of the City. It is funded through voter-authorized sales tax. City Council approval is required for annual budgets and bonded debt issuance. In the event of dissolution, the net position of the KEDC and 4A shall be converted to the City. The KEDC and 4A do not issue separate financial statements.

Related organizations are excluded from the financial reporting entity because the City's accountability does not extend beyond making appointments. Audited financial statements are available from the respective organizations. Great Texoma Utility Authority (GTUA) assists local governments, including the City, in the development of water, sewer, and solid waste facilities. The City financed certain water and sewer facilities through debt issued by GTUA and the City is contractually obligated to make sufficient payments to GTUA for annual debt service requirements of that debt. The City has no significant influence over the operations of GTUA, as its scope benefits other entities beside the City.

B. Government-Wide and Fund Financial Statements

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

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 function or 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 and Enterprise Funds are reported as separate columns in the fund financial statements.

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

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue 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. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available when it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenue to be available if collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

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

The City reports the following major governmental funds:

General Fund – the primary operating fund. It accounts for all financial resources of the City except those required to be accounted for in another fund.

Capital Projects Fund – used to account for financial resources to be used for the acquisition, construction, or rehabilitation of capital assets. Such resources are derived from proceeds of general obligation bonds or other sources of revenue specifically set aside for capital projects.

Debt Service Fund – the primary long-term debt obligation fund. It is used to account for tax revenues and the payment of principal, interest, and related costs on debt for which a tax has been dedicated. Any unused sinking fund balances are transferred to the General Fund after all debt obligations have been met.

Krum Economic Development Fund – established to account for sales tax revenues collected for the purposes set forth by the Krum Economic Development Fund.

4A Sales & Use Tax Fund – established to account for sales tax revenues collected for the purposes set forth by the 4A Sales and Use Tax Fund.

The City reports the following major proprietary fund:

Water and Sewer Fund – this is the City’s primary operating fund for water and sewer distribution. It also accounts for all financial resources of the City concerning water and sewer sales. Its activity is financed with debt secured by a pledge of the net revenues and has the requirement that the cost of providing services, including capital costs, be recovered by used fees and charges.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the City’s water and wastewater function and various other functions of the government. Elimination of these charges would distort the direct costs and program revenue reported for the various functions concerned.

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

D. Assets, Liabilities and Net Position or Equity

Cash and Cash Equivalents

For purposes of the statement of cash flows, highly liquid investments are considered to be cash equivalents if they have a maturity of three months or less when purchased.

Receivables and Payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either “due to/from other funds” (i.e., the current portion of interfund loans) or “advances to/from other funds” (i.e., the noncurrent portion of interfund loans). All other outstanding balances between funds are reported as “due to/from other funds.” Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as “internal balances.”

Property taxes attach as an enforceable lien on property as of October 1. Taxes are levied each October 1 and are due and payable on or before January 31 of the following year. All unpaid taxes become delinquent February 1 of the following year. Any uncollected property taxes as of September 30, which are not expected to be collected within 60 days, are recorded as taxes receivable and unavailable revenue.

Inventories and Prepaid Items

The City records purchases of utility parts and supplies as inventories, utilizing the lower of cost or market method of accounting for inventory. Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenses.

Capital Assets

The City’s capital assets and infrastructure with useful lives of more than one year are stated at historical cost and comprehensively reported in the government-wide financial statements. The City maintains infrastructure asset records consistent with all other capital assets. Donated assets are stated at fair value on the date donated. The City generally capitalizes assets with a cost of \$5,000 or more as purchases and outlays occur. The cost of normal maintenance and repairs that do not add to the asset value or materially extend useful lives are not capitalized. Capital assets are depreciated using the straight-line method. When capital assets are disposed, the cost and applicable accumulated depreciation are removed from the respective accounts, and the resulting gain or loss is recorded in operations.

Estimated useful lives, in years, for depreciable assets are as follows:

<u>Asset Class</u>	<u>Estimated Useful Lives</u>
Park improvements	20-30 years
Infrastructure	20-30 years
Buildings and improvements	10-50 years
Equipment and vehicles	3-20 years

Compensated Absences

Compensated absences are reported as accrued in the government-wide financial statements. In the fund level financial statements, only matured compensated absences payable to currently terminated employees are reported.

Long-term Obligations

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

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

Pensions

For purposes of measuring the net pension asset, pension related deferred outflows and inflows of resources, and pension expense, City specific information about its Fiduciary Net Position in the Texas Municipal Retirement System (TMRS) and additions to/deductions from the City's Fiduciary Net Position have been determined on the same basis as they are reported by TMRS. For this purpose, plan contributions are recognized in the period that compensation is reported for the employee, which is when contributions are legally due. Benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Net Position

Net Position represents the difference between assets, deferred inflows/outflows of resources and liabilities. Net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowing used for the acquisition, construction or improvement of those assets, and adding back unspent proceeds. Net position is reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the City or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

In the government-wide financial statements, the City's restrictions on net position are for amounts that are not available for appropriation. The City's restricted net position is as follows:

Restricted for Debt Service	\$	692,295
Restricted for Economic Development		721,550
Restricted for Court Technology		7,896
Restricted for Court Security		7,565
Restricted for Public Works		<u>39,236</u>
Total	\$	<u>1,468,542</u>

Fund Balance

The governmental fund financial statements present fund balances based on classifications that comprise a hierarchy that is based primarily on the extent to which the City is bound to honor constraints on the specific purposes for which amounts in the respective governmental funds can be spent.

The classifications used in the governmental fund financial statements are as follows:

- **Nonspendable:** This classification includes amounts that cannot be spent because they are either (a) not in spendable form or (b) are legally or contractually required to be maintained intact. Nonspendable items are not expected to be converted to cash or are not expected to be converted to cash within the next year.
- **Restricted:** This classification includes amounts for which constraints have been placed on the use of the resources either (a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments, or (b) imposed by law through constitutional provisions or enabling legislation.
- **Committed:** This classification includes amounts that can be used only for specific purposes pursuant to constraints imposed by board resolution of the City Council, the City's highest level of decision making authority. These amounts cannot be used for any other purpose unless the City Council removes or changes the specified use by taking the same type of action that was employed when the funds were initially committed. This classification also includes contractual obligations to the extent that existing resources have been specifically committed for use in satisfying those contractual requirements.
- **Assigned:** This classification includes amounts that are constrained by the City's intent to be used for a specific purpose but are neither restricted nor committed. This intent can be expressed by the City Council.
- **Unassigned:** This classification includes the residual fund balance for the General Fund. The unassigned classification also includes negative residual fund balance of any other governmental fund that cannot be eliminated by offsetting of assigned fund balance amounts.

Net Position Flow Assumption

Sometimes the City will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the government-wide and proprietary fund financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the City's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

Fund Balance Flow Assumption

Sometimes the City will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements a flow assumption must be made about the order in which the resources are considered to be applied. It is the City's policy to consider restricted fund balance to have been depleted before using any of the components of unrestricted fund balance. Further, when components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

Deferred outflows/inflows of resources

In addition to assets, the statement of financial position and/or balance sheet will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. The City has the following items that qualify for reporting in this category.

- Deferred charge on refunding – A deferred charge on refunding results from the difference in the carrying value of refunded debt and its reacquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt.
- Pension contributions after measurement date – These contributions are deferred and recognized in the following fiscal year.
- Changes in actuarial assumptions related to the pension plan – This difference is deferred and recognized over the estimated average remaining lives of all members determined as of the measurement date.
- Difference in projected and actual earnings on pension assets – This difference is deferred and amortized over a closed five year period.
- Difference in expected and actual pension experience – This difference is deferred and recognized over the estimated average remaining lives of all members determined as of the measurement date.

In addition to liabilities, the statement of financial position and/or balance sheet will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The City has two types of items that qualifies for reporting in this category. The difference in expected and actual pension experience is deferred and recognized over the estimated average remaining lives of all members determined as of the measurement date.

Estimates

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 and liabilities and disclosures of contingent liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual amounts could differ from those estimates.

II. DETAILED NOTES ON ALL FUNDS

A. Deposits and Investments

The City's funds are required to be deposited and invested under the terms of a depository contract. The depository bank deposits for safekeeping and trust with the City's agent bank approved pledged securities in an amount sufficient to protect City funds on a day-to-day basis during the period of the contract. The pledge of approved securities is waived only to the extent of the depository bank's dollar amount of Federal Deposit Insurance Corporation ("FDIC") insurance.

Cash Deposits

At September 30, 2016, the total carrying amounts of the City's deposits (restricted and unrestricted cash, certificates of deposit, and interest-bearing savings accounts included in temporary investments) were \$5,506,585 and the bank balances were \$5,590,046. The City's cash deposits at September 30, 2016, were entirely covered by FDIC insurance or by pledged collateral held by the City's agent bank in the City's name.

Investments

The City is required by Government Code Chapter 2256, the Public Funds Investment Act, to adopt, implement, and publicize an investment policy. That policy must be written; primarily emphasize safety of principal and liquidity; address investment diversification, yield, and maturity and the quality and capability of investment management; and include a list of the types of authorized investments in which the investing entity's funds may be invested; and the maximum allowable stated maturity of any individual investment owned by the entity.

The Public Funds Investment Act (the "Act") requires an annual audit of investment practices. Audit procedures in this area conducted as a part of the audit of the basic financial statements disclosed that in the areas of investment practices, management reports and establishment of appropriate policies, the City adhered to the requirements of the Act. Additionally, investment practices of the City were in accordance with local practices.

The Act determines the types of investments which are allowable for the City. These include, with certain restrictions, (1) obligations of the U. S. Treasury, certain U. S. Agencies, and the State of Texas, (2) certificates of deposit, (3) certain municipal securities, (4) money market savings accounts, (5) repurchase agreements, (6) bankers acceptances, (7) mutual funds, (8) investment pools, (9) guaranteed investment contracts, and (10) common trust funds.

The City had no investments at September 30, 2016.

Analysis of Specific Deposit and Investment Risks

Professional standards require a determination as to whether the City was exposed to the following specific investment risks at year-end and, if so, the reporting of certain related disclosures:

Credit Risk. Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The ratings of securities by nationally recognized rating agencies are designed to give an indication of credit risk. At year-end, the City was not exposed to a significant amount of credit risk.

Custodial Credit Risk. Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized, collateralized with securities held by the pledging financial institution, or collateralized with securities held by the pledging financial institution's trust department or agent but not in the City's name.

Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the government, and are held by either the counterparty or the counterparty's trust department or agent but not in the City's name. At year-end, the City was not exposed to custodial credit risk.

Concentration of Credit Risk. This is the risk of loss attributed to the magnitude of a government's investment in a single issuer. At year-end, the City was not exposed to concentration of credit risk.

Interest Rate Risk. This is the risk that changes in interest rates will adversely affect the fair value of an investment. At year-end, the City was not exposed to interest rate risk.

Foreign Currency Risk. This is the risk that exchange rates will adversely affect the fair value of an investment. At year-end, the City was not exposed to foreign currency risk.

B. Receivables and Uncollectible Accounts

Sales Taxes

Sales taxes are collected and remitted to the City by the State Comptroller's Office. All sales taxes are collected within 60 days of year-end. At fiscal year-end, the receivables represent taxes collected but not yet received by the City are recorded as revenue.

Property Taxes

Property taxes are assessed and remitted to the City by the Denton County Tax Assessor's Office. Taxes, levied annually on October 1, are due by January 31. Major tax payments are received December through March. Lien dates for real property occur annually in July. Allowances for uncollectible tax receivables reported in the general fund are based upon historical experience in collecting property taxes. Uncollectible personal property taxes are periodically received and written off when deemed uncollectible; however, state statutes prohibit writing off real property taxes without specific authority from the Texas Legislature.

In the governmental fund-level financial statements, property taxes receivable are recorded in the general fund when assessed (October 1 of each fiscal year). At fiscal year-end, property tax receivables represent delinquent taxes. If delinquent taxes are not paid within 60 days of fiscal year-end, they are recorded as deferred revenue.

In the government-wide financial statements, property tax receivables and related revenues include all amounts due to the City regardless of when cash is received.

Governmental Funds Receivables

At September 30, 2016, receivables were as follows:

	Governmental Funds					Total
	General	Debt Service	Capital Projects Fund	Krum Economic Development Fund	4A Sales & Use Tax Fund	
Receivables:						
Property tax	\$ 26,142	\$ 9,288	\$ -	\$ -	\$ -	\$ 35,430
Sales tax	48,027	-	-	24,013	24,013	96,053
Accounts	469,664	-	-	-	-	469,664
Due from other governments	-	-	115,031	-	-	115,031
Gross receivables	543,833	9,288	115,031	24,013	24,013	716,178
Less: Allowance for uncollectibles	378,602	2,322	-	-	-	380,924
Net total receivables	\$ 165,231	\$ 6,966	\$ 115,031	\$ 24,013	\$ 24,013	\$ 335,254

Emergency Medical Services (EMS)

EMS revenues are collected and remitted to the City by a third-party administrator. All revenues are billed when services are performed by the City. Allowances for uncollectible EMS receivables reported in the general fund are based upon historical experience in collecting EMS revenues. Uncollectible EMS revenues are periodically review and written off when deemed uncollectible.

In the governmental fund-level financial statements, EMS revenues are recorded in the general fund when the services are performed. Any delinquent revenues not paid within 60 days of the fiscal year-end are recorded as unavailable revenue.

Utility Revenues

Receivables in the City’s proprietary fund represent amounts due from customers for water and wastewater services. These receivables are generally due within one month. Receivables are reported net of an allowance for uncollectible accounts and revenues net of what is estimated to be uncollectible. The allowance is estimated based upon accounts receivable past due by more than 90 days.

Restricted Assets

At September 30, 2016, the General Fund contained an amount designated as restricted cash and cash equivalents of \$39,056. This amount is committed for public safety.

The water and sewer fund contains an amount designated as restricted cash and cash equivalents of \$176,800. This amount is restricted for customer utility deposits and expenses related to the construction of the public works building.

Inter-Fund Balances and Activity

The City had no due to and due from other funds balances at September 30, 2016.

Transfers to and from other funds at September 30, 2016 consisted of the following:

<u>Transfer From</u>	<u>Transfer To</u>	<u>Amount</u>	<u>Reason</u>
Water and sewer	General fund	\$ 149,911	Admin transfers
Economic Development Fund	General fund	2,000	Admin transfers
Water and sewer	Capital projects fund	196,456	CIP related
Water and sewer	Debt service fund	<u>61,730</u>	Payment of debt
		<u>\$ 410,097</u>	

Capital Assets

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

	Beginning Balances	Increases	Decreases	Ending Balances
Governmental activities				
Capital assets not being depreciated:				
Land	\$ 869,245	\$ -	\$ -	\$ 869,245
Construction in progress	64,697	2,364,012	-	2,428,709
Total capital assets not being depreciated	<u>933,942</u>	<u>2,364,012</u>	<u>-</u>	<u>3,297,954</u>
Capital assets being depreciated:				
Park improvements	710,774	-	-	710,774
Infrastructure	3,200,914	-	-	3,200,914
Buildings and improvements	1,685,922	-	-	1,685,922
Equipment and vehicles	1,812,980	65,998	-	1,878,978
Total capital assets being depreciated	<u>7,410,590</u>	<u>65,998</u>	<u>-</u>	<u>7,476,588</u>
Total accumulated depreciation	(2,470,836)	(355,197)	-	(2,826,033)
Total capital assets being depreciated, net	<u>4,939,754</u>	<u>(289,199)</u>	<u>-</u>	<u>4,650,555</u>
Governmental activities capital assets, net	<u>\$ 5,873,696</u>	<u>\$ 2,074,813</u>	<u>\$ -</u>	<u>\$ 7,948,509</u>
Business-Type Activities				
Capital assets not being depreciated:				
Land	\$ 166,910	\$ -	\$ -	\$ 166,910
Construction in progress	334,997	386,160	-	721,157
Total capital assets not being depreciated	<u>501,907</u>	<u>386,160</u>	<u>-</u>	<u>888,067</u>
Capital assets being depreciated:				
Infrastructure	8,313,647	-	-	8,313,647
Buildings and improvements	152,142	-	-	152,142
Equipment and vehicles	277,774	-	-	277,774
Other	63,382	-	-	63,382
Total capital assets being depreciated	<u>8,806,945</u>	<u>-</u>	<u>-</u>	<u>8,806,945</u>
Total accumulated depreciation	(3,546,953)	(268,510)	-	(3,815,463)
Total capital assets being depreciated, net	<u>5,259,992</u>	<u>(268,510)</u>	<u>-</u>	<u>4,991,482</u>
Business-type activities capital assets, net	<u>\$ 5,761,899</u>	<u>\$ 117,650</u>	<u>\$ -</u>	<u>\$ 5,879,549</u>

Depreciation was charged to functions, but reported in the aggregate in the statement of activities for governmental activities as follows:

General government	\$ 51,891
Public safety	167,007
Public works	107,386
Culture and recreation	<u>28,913</u>
Total depreciation expense	<u>\$ 355,197</u>

Total depreciation expense for the City's business-type activities during the year-ended September 30, 2016 was \$268,510.

Long-Term Obligations

Changes in long-term obligations for the year ended September 30, 2016 are as follows:

	Beginning Balance	Increases	Decreases	Ending Balances	Amounts Due Within One Year
Governmental activities					
General obligation bonds	\$ 4,673,381	\$ -	\$ 256,677	\$ 4,416,704	\$ 258,401
Notes payable	529,289	-	145,645	383,644	102,683
Capital leases	137,410	-	50,896	86,514	42,383
Premium on bonds	84,813	-	4,464	80,349	-
Compensated absences	76,527	59,645	52,238	83,934	20,984
Total governmental activities	<u>\$ 5,501,420</u>	<u>\$ 59,645</u>	<u>\$ 509,920</u>	<u>\$ 5,051,145</u>	<u>\$ 424,451</u>
Business-type activities					
General obligation bonds	\$ 3,621,619	\$ -	\$ 388,323	\$ 3,233,296	\$ 321,599
Premium on bonds	18,930	-	996	17,934	-
Compensated absences	9,823	8,813	6,202	12,434	3,109
Total governmental activities	<u>\$ 3,650,372</u>	<u>\$ 8,813</u>	<u>\$ 395,521</u>	<u>\$ 3,263,664</u>	<u>\$ 324,708</u>

Debt service requirements on general obligation bonds at September 30, 2016 are as follows:

Years Ending September 30,	Governmental Activities		
	Principal	Interest	Total
2017	\$ 258,401	\$ 154,787	\$ 413,188
2018	270,934	148,058	418,992
2019	274,382	140,983	415,365
2020	276,106	133,834	409,940
2021	292,724	125,912	418,636
2022-2026	1,320,522	501,189	1,821,711
2027-2031	1,081,475	287,297	1,368,772
2032-2036	642,160	49,750	691,910
	<u>\$ 4,416,704</u>	<u>\$ 1,541,810</u>	<u>\$ 5,958,514</u>
Years Ending September 30,	Business-Type Activities		
	Principal	Interest	Total
2017	\$ 321,599	\$ 87,162	\$ 408,761
2018	334,066	79,858	413,924
2019	340,618	72,262	412,880
2020	348,894	64,100	412,994
2021	362,276	55,553	417,829
2022-2026	1,314,478	133,080	1,447,558
2027-2031	123,525	33,878	157,403
2032-2036	87,840	7,100	94,940
	<u>\$ 3,233,296</u>	<u>\$ 532,993</u>	<u>\$ 3,766,289</u>

The effective interest rate on outstanding bonds ranged from 3% to 4.75% at September 30, 2016.

Advance Refunding

The City issued \$3,710,000 in general obligation refunding bonds with an interest rate of 2.14%. The proceeds were used to advance refund \$3,575,000 of outstanding 2004 General Obligation Bonds and 2005 Certificates of Obligation which had interest rates ranging from 3.7% to 5.625%. The net proceeds of \$3,659,984 (after payment of \$50,016 in underwriting fees and other issuance costs) included \$3,659,984 that was deposited in an irrevocable trust with an escrow agent to provide funds for the future debt service payment on the refunded bonds. As a result, the previously noted bonds are considered defeased and the liability for those bonds has been removed from the statement of net position.

The reacquisition price exceeded the net carrying amount of the old debt by \$84,984. This amount is being netted against the new debt and amortized over the remaining life of the refunding debt. The government advance refunded the 2004 General Obligation Bonds and 2005 Certificates of Obligation to reduce its total debt service payments over 11 years by \$418,787 and to obtain an economic gain (difference between the present values of the debt service payments on the old and new debt) of \$368,536. The remaining outstanding balance of defeased debt is \$0 at September 30, 2016.

Debt service requirements on notes payable at September 30, 2016 are as follows:

Years Ending September 30,	Governmental Activities		
	Principal	Interest	Total
2017	\$ 102,683	\$ 13,360	\$ 116,043
2018	105,590	9,987	115,577
2019	109,566	6,502	116,068
2020	65,805	2,903	68,708
	<u>\$ 383,644</u>	<u>\$ 32,752</u>	<u>\$ 416,396</u>

The effective interest rate on the outstanding notes ranged from 2.69% to 4.50% at September 30, 2016.

Debt service requirements on capital leases at September 30, 2016 are as follows:

Years Ending September 30,	Governmental Activities		
	Principal	Interest	Total
2017	\$ 42,383	\$ 3,538	\$ 45,921
2018	44,131	1,805	45,936
	<u>\$ 86,514</u>	<u>\$ 5,343</u>	<u>\$ 91,857</u>

The effective interest rates on capital leases outstanding was 2.69% at September 30, 2016.

Operating Leases

Future minimum rentals on office equipment operating leases for the City at September 30, 2016 are as follows:

<u>Years Ending September 30,</u>	
2017	\$ 8,868
2018	8,868
2019	<u>5,173</u>
	<u>\$ 22,909</u>

Rental expense of \$22,530 was charges to expense during the year ended September 30, 2016.

Commitments

In 2013, the City entered into an agreement with Greater Texoma Utility Authority (GTUA), whereby GTUA to meet its water and sewer facility needs. GTUA subsequently issued \$4,910,000 in contract revenue bonds for construction of water and sewer facilities and infrastructure within the City. The City is committed to pay facility charges as well as volume rate for treatment (transportation charges).

During the year ended September 30, 2016, the City paid \$185,046 to GTUA in accordance with a contract with the Authority. Future payments under this agreement averages approximately \$281,249 per year for the next 24 years.

III. OTHER INFORMATION

A. Risk Management

The City is exposed to various risks of loss related to torts, theft, damage or destruction of assets, error and omissions, injuries to employees, and natural disasters. During fiscal year 2015, the City obtained general liability coverage at a cost that is considered to be economically justifiable by joining together with other governmental entities in the State as a member of the Texas Municipal League Intergovernmental Risk Pool (TML). TML is a self-funded pool operating as a common risk management and insurance program. The City pays an annual premium to TML for its above insurance coverage. The agreement for the formation of TML provide that TML will be self-sustaining through member premiums and will reinsure through commercial companies for claims in excess of acceptable risk levels; however, each category of coverage has its own level of reinsurance. The City continues to carry commercial insurance for other risks of loss. There were no significant reductions in commercial insurance coverage in the past fiscal year and settled claims resulting from this risk have not exceeded coverage in any of the past three fiscal years.

B. Defined Benefit Pension Policies

Plan Description

The City participates as one of 866 plans in the nontraditional, joint contributory, hybrid defined benefit pension plan administered by the Texas Municipal Retirement System (TMRS). TMRS is an agency created by the State of Texas and administered in accordance with the TMRS Act, Subtitle G, Title 8, Texas Government Code (the TMRS Act) as an agency multiple-employer retirement system for municipal employees in the State of Texas. The TMRS Act places the general administration and management of the System with a six-member Board of Trustees. Although the Governor, with the advice and consent of the Senate, appoints the Board, TMRS is not fiscally dependent on the State of Texas. TMRS's defined benefit pension plan is a tax-qualified plan under Sections 401(a) of the Internal Revenue Code. TMRS issues a publicly available comprehensive annual financial report (CAFR) that can be obtained at www.tmars.org.

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

Benefits Provided

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

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

A summary of plan provisions for the City are as follows:

Employee deposit rate	5%
Matching ratio (City to employee)	2 to 1
Years required for vesting	5
Service retirement eligibility	20 years to any age, 5 years at age 60 and above
Updated service credit	100% Repeating, Transfers
Annuity increase to retirees	70% of CPI Repeating

Employees covered by benefit terms

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

Inactive employees or beneficiaries currently receiving benefits	5
Inactive employees entitled to but not yet receiving benefits	31
Active employees	<u>27</u>
	<u><u>63</u></u>

Contributions

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

Employees for the City were required to contribute 5% of their annual gross earnings during the fiscal year. The contribution rates for the City were 3.55% and 3.69% in calendar years 2015 and 2016, respectively. The City’s contributions to TMRS for the year ended September 30, 2016, were \$50,719, and were equal to the required contributions.

Net Pension Asset

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

Actuarial assumptions

The Total Pension Liability in the December 31, 2015 actuarial valuation was determined using the following actuarial assumptions:

Inflation	2.5% per year
Overall payroll growth	3.0% per year
Investment Rate of Return	6.75%, net of pension plan investment expense, including inflation

Salary increases were based on a service-related table. Mortality rates for active members, retirees, and beneficiaries were based on the gender-distinct RP2000 Combined Healthy Mortality Tables with Blue Collar Adjustment, with male rates multiplied by 109% and female rates multiplied by 103%. The rates are projected on a fully generational basis by scale BB to account for future mortality improvements. For disabled annuitants, the gender-distinct RP2000 Combined Healthy Mortality Tables with Blue Collar Adjustment are used with males rates multiplied by 109% and female rates multiplied by 103% with a 3-year set-forward for both males and females. In addition, a 3% minimum mortality rate is applied to reflect the impairment for younger members who become disabled. The rates are projected on a fully generational basis by scale BB to account for future mortality improvements subject to the 3% floor.

Actuarial assumptions used in the December 31, 2015 valuation were based on the results of actuarial experience studies. The experience study in TMRS was for the period December 31, 2010 through December 31, 2014. Healthy post-retirement mortality rates and annuity purchase rates were updated based on a Mortality Experience Investigation Study covering the 2009 through 2011, and the dated December 31, 2013. These assumptions were first used in the December 31, 2013 valuation, along with a change to the Entry Age Normal (EAN) actuarial cost method. Assumptions are reviewed annually. No additional changes were made for the 2014 valuation. After the Asset Allocation Study analysis and experience investigation study, the Board amended the long-term expected rate of return on pension plan investments from 7% to 6.75%. Plan assets are managed on a total return basis with an emphasis on both capital appreciation as well as the production of income, in order to satisfy the short-term and long-term funding needs of TMRS.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expenses and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. In determining their best estimate of a recommended investment return assumption under the various alternative asset allocation portfolios, GRS focused on the area between (1) arithmetic mean (aggressive) without an adjustment for time (conservative) and (2) the geometric mean (conservative) with an adjustment for time (aggressive). At its meeting on July 30, 2015, the TMRS Board approved a new portfolio target allocation. The pension plan's policy in regard to the allocation of invested assets is established and may be amended by the TMRS Board of Trustees. Plan assets are managed on a total return basis with an emphasis on both capital appreciation as well as the production of income, in order to satisfy the short-term and long-term funding needs of TMRS. The target allocation and best estimates of arithmetic real rates return for each major assets class are summarized in the following table

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return (Arithmetic)
Domestic Equity	17.5%	4.55%
International Equity	17.5%	6.10%
Core Fixed Income	10.0%	1.00%
Non-Core Fixed Income	20.0%	3.65%
Real Return	10.0%	4.03%
Real Estate	10.0%	5.00%
Absolute Return	10.0%	4.00%
Private Equity	5.0%	8.00%
Total	100.0%	

Discount Rate

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

Changes in the Net Pension Asset

	Increase (Decrease)		
	Total Pension Liability	Plan Fiduciary Net Position	Net Pension Liability (Asset)
	(a)	(b)	(a) - (b)
Balance at 12/31/2014	\$ 1,053,257	\$ 1,185,645	\$(132,388)
Changes for the year:			
Service cost	116,655	-	116,655
Interest	77,390	-	77,390
Difference between expected and actual experience	(14,874)	-	(14,874)
Changes of assumptions	46,993	-	-
Contributions - employer	-	45,356	(45,356)
Contributions - employee	-	64,134	(64,134)
Net investment income	-	1,750	(1,750)
Benefit payments, including refunds of employee contributions	(12,036)	(12,036)	-
Administrative expense	-	(1,066)	1,066
Other changes	-	(53)	53
Net changes	<u>214,128</u>	<u>98,085</u>	<u>116,043</u>
Balance at 12/31/2015	<u>\$ 1,267,385</u>	<u>\$ 1,283,730</u>	<u>\$(16,345)</u>

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

	1% Decrease in Discount Rate (5.75%)	Discount Rate (6.75%)	1% Increase in Discount Rate (7.75%)
City's net pension asset	\$ 178,486	\$(16,345)	\$(174,996)

Pension Plan Fiduciary Net Position

Detailed information about the pension plan's Fiduciary Net Position is available in a separately-issued TMRS financial report. The report may be obtained on the Internet at www.tmrs.org.

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended September 30, 2016, the City recognized pension expense of \$69,950.

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

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual economic experience	\$ -	\$ 23,375
Changes in actuarial assumptions	37,499	-
Difference between projected and actual investment earnings	73,332	-
Contributions subsequent to the measurement date	<u>37,959</u>	<u>-</u>
Total	<u>\$ 148,790</u>	<u>\$ 23,375</u>

\$37,959 reported as deferred outflows of resources related to pension resulting from contributions subsequent to the measurement date will be recognized as an increase of the net pension asset for the year ending September 30, 2016. Other amounts reported as deferred outflows of resources related to pensions will be recognized in pension expenses as follows:

Year Ending December 31,	
2017	\$ 21,914
2018	21,914
2019	21,915
2020	21,713
Thereafter	-

C. Other Post Employment Benefits (OPEB)

Plan Description

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

Plan Provisions

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

Contributions

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

The City's contributions to the TMRS SDBF for the years ended 2016, 2015, and 2014, were \$1,758, \$1,497 and \$1,472, respectively, which equaled the required contributions each year.

Health Care Coverage

During the year ending September 30, 2016, employees of the City were covered by a health insurance plan (the Plan). The City paid premiums of \$202,576 to the Plan. Employees, at their option, authorized payroll withholding to pay premiums for dependents. All premiums were paid to a third-party administrator, acting on behalf of the licensed insurer. The Plan was authorized by Article 3.15-2, Texas Insurance Code and was documented by contractual agreement.

Commitments and Contingencies

Contingencies

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

Litigation

The City is subject to certain legal proceeding in the normal course of operations. In the opinion of management, the aggregate liability, if any, with respect to potential legal actions will not materially adversely affect the City's financial position, results of operations, or cash flows.

**REQUIRED SUPPLEMENTARY
INFORMATION**

CITY OF KRUM, TEXAS

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES I
FUND BALANCE - BUDGET AND ACTUAL
GENERAL FUND**

FOR THE YEAR ENDED SEPTEMBER 30, 2016

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - (Negative)
	Original	Final		
REVENUES				
Property taxes	\$ 1,188,275	\$ 1,188,275	\$ 1,184,740	\$ (3,535)
Sales taxes	301,750	223,250	260,230	36,980
Franchise fees	235,200	235,200	238,502	3,302
Licenses and permits	31,900	31,900	40,535	8,635
Fines and forfeitures	108,950	108,950	122,327	13,377
Intergovernmental	194,651	246,739	293,702	46,963
Charges for services	564,300	564,300	582,412	18,112
Investment earnings	8,500	8,500	12,234	3,734
Other	27,750	36,471	37,752	1,281
Total revenues	<u>2,661,276</u>	<u>2,643,585</u>	<u>2,772,434</u>	<u>128,849</u>
EXPENDITURES				
General government	402,648	412,648	421,585	(8,937)
Public safety	1,725,482	1,762,352	1,768,819	(6,467)
Public works	438,884	438,884	352,254	86,630
Culture and recreation	135,888	156,191	152,589	3,602
Debt service:				
Principal	56,107	50,891	50,896	(5)
Interest and fiscal charges	750	5,966	5,612	354
Capital outlay	19,500	29,000	29,075	(75)
Total expenditures	<u>2,779,259</u>	<u>2,855,932</u>	<u>2,780,830</u>	<u>75,102</u>
Excess of expenditures over appropriations	<u>(117,983)</u>	<u>(212,347)</u>	<u>(8,396)</u>	<u>203,951</u>
OTHER FINANCING SOURCES (USES)				
Transfers in	<u>151,911</u>	<u>151,911</u>	<u>151,911</u>	<u>-</u>
Total other financing sources	<u>151,911</u>	<u>151,911</u>	<u>151,911</u>	<u>-</u>
Net change in fund balance	33,928	(60,436)	143,515	203,951
Fund balance - beginning balance	<u>442,472</u>	<u>442,472</u>	<u>442,472</u>	<u>-</u>
Fund balance - end of year	<u>\$ 476,400</u>	<u>\$ 382,036</u>	<u>\$ 585,987</u>	<u>\$ 203,951</u>

CITY OF KRUM, TEXAS

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES I
FUND BALANCE - BUDGET AND ACTUAL
KRUM ECONOMIC DEVELOPMENT**

FOR THE YEAR ENDED SEPTEMBER 30, 2016

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget - (Negative)</u>
	<u>Original</u>	<u>Final</u>		
REVENUES				
Sales taxes	\$ 121,000	\$ 121,000	\$ 129,557	\$ 8,557
Investment earnings	<u>350</u>	<u>350</u>	<u>686</u>	<u>336</u>
Total revenues	<u>121,350</u>	<u>121,350</u>	<u>130,243</u>	<u>8,893</u>
EXPENDITURES				
Economic development	<u>161,831</u>	<u>161,831</u>	<u>16,814</u>	<u>-</u>
Total expenditures	<u>161,831</u>	<u>161,831</u>	<u>16,814</u>	<u>-</u>
Excess of expenditures over appropriations	<u>(40,481)</u>	<u>(40,481)</u>	<u>113,429</u>	<u>153,910</u>
OTHER FINANCING SOURCES (USES)				
Transfers out	<u>(2,000)</u>	<u>(2,000)</u>	<u>(2,000)</u>	<u>-</u>
Total other financing sources	<u>(2,000)</u>	<u>(2,000)</u>	<u>(2,000)</u>	<u>-</u>
Net change in fund balance	<u>(42,481)</u>	<u>(42,481)</u>	<u>111,429</u>	<u>153,910</u>
Fund balance - beginning balance	<u>324,000</u>	<u>324,000</u>	<u>324,000</u>	<u>-</u>
Fund balance - end of year	<u>\$ 281,519</u>	<u>\$ 281,519</u>	<u>\$ 435,429</u>	<u>\$ 153,910</u>

CITY OF KRUM, TEXAS

**SCHEDULE OF CHANGES IN NET PENSION LIABILITY
AND RELATED RATIOS**

FOR THE YEAR ENDED SEPTEMBER 30, 2016

Plan Year	<u>2014</u>	<u>2015</u>
A. Total pension liability		
Service Cost	\$ 98,877	\$ 116,655
Interest (on the Total Pension Liability)	68,383	77,390
Change of benefit terms	-	-
Difference between expected and actual experience	(18,710)	(14,874)
Change of assumptions	-	46,993
Benefit payments, including refunds of employee contributions	(45,518)	(12,036)
Net change in total pension liability	103,032	214,128
Total pension liability - beginning	<u>950,225</u>	<u>1,053,257</u>
Total pension liability - ending (a)	<u>\$ 1,053,257</u>	<u>\$ 1,267,385</u>
B. Plan fiduciary net position		
Contributions - employer	\$ 25,423	\$ 45,356
Contributions - employee	56,498	64,134
Net investment income	62,245	1,750
Benefit payments, including refunds of employee contributions	(45,518)	(12,036)
Administrative expenses	(650)	(1,066)
Other	<u>(53)</u>	<u>(53)</u>
Net change in plan fiduciary net position	97,945	98,085
Plan fiduciary net position - beginning	<u>1,087,700</u>	<u>1,185,645</u>
Plan fiduciary net position - ending (b)	<u>\$ 1,185,645</u>	<u>\$ 1,283,730</u>
C. Net pension liability - ending (a) - (b)	<u>\$(132,388)</u>	<u>\$(16,345)</u>
D. Plan fiduciary net position as a percentage of total pension liability	112.57%	101.29%
E. Covered employee payroll	\$ 1,129,969	\$ 1,270,747
F. Net position liability as a percentage of covered employee payroll	-11.72%	-1.29%

Note: 10 years of information is required to be provided in this schedule, but information prior to 2014 is not available.

CITY OF KRUM, TEXAS
SCHEDULE OF CONTRIBUTIONS
FOR THE YEAR ENDED SEPTEMBER 30, 2016

Fiscal Year	<u>2014</u>	<u>2015</u>	<u>2016</u>
Actuarial determined contribution	\$ 25,735	\$ 39,124	\$ 50,719
Contributions in relation to the actuarially determined contribution	<u>25,735</u>	<u>39,124</u>	<u>50,719</u>
Contribution deficiency (excess)	-	-	-
Covered employee payroll	1,159,615	1,220,678	1,387,741
Contributions as a percentage of covered employee payroll	2.22%	3.21%	3.65%

NOTES TO SCHEDULE OF CONTRIBUTIONS

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

Methods and Assumptions Used to Determine Contribution Rates:

Actuarial Cost Method	Entry Age Normal
Amortization Method	Level Percentage of Payroll, Closed
Remaining Amortization Period	30 years
Asset Valuation Method	10 Year smoothed market; 15% soft corridor
Inflation	2.50%
Salary Increases	3.50% to 10.50% including inflation
Investment Rate of Return	6.75%
Retirement Age	Experience-based table of rates that are specific to the City's plan of benefits. Last updated for the 2015 valuation pursuant to an experience study of the period 2010-2014.
Mortality	RP2000 Combined Mortality Table with Blue Collar Adjustment with male rates multiplied by 109% and female rates multiplied by 103% and projected on a fully generational basis of with BB.

Other Information There were no benefit changes during the year.

Note: 10 years of information is required to be provided in this schedule, but information prior to 2014 is not available.

CITY OF KRUM

NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION

SEPTEMBER 30, 2016

A. GENREAL FUND BUDGETARY ANALYSIS

Budgetary Information

The City Council adopts an annual budget prepared on a non-GAAP cash basis. City management may transfer part of all of any unencumbered appropriation balance within specific categories (i.e., personnel, operations, supplies, or capital outlay) within programs; however, any revisions that alter the total expenditures of the categories must be approved by the City Council. The City, for management purposes, adopts budgets for all funds. Legal budgets are also adopted for all funds, and the legal level of control is the fund level.

All unused appropriations, except appropriations for capital expenditures, lapse at the close of the fiscal year to the extent they have not been expended or encumbered. An appropriation for capital expenditures shall continue in force until the purpose for which it was made is accomplished or abandoned. No supplemental budgetary appropriations occurred in the debt service fund, the general fund or in the KEDC fund. Revised budgets, if any, are used to budget versus actual comparisons. The 4A Sales and Use Tax fund was introduced during the 2016 fiscal year and had no legally adopted budget.

B. BUDGET VERSUS ACTUAL RESULTS

In the General Fund, the City's expenditures exceeded appropriations in general government, public safety, debt service – principal and capital outlay. These excesses were covered by other expenditure functions and available fund balance. The City's expenditures did not exceed appropriations in the Economic Development or Debt Service Fund.

**OTHER SUPPLEMENTARY
INFORMATION**

CITY OF KRUM, TEXAS

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES I
FUND BALANCE - BUDGET AND ACTUAL
DEBT SERVICE FUND**

FOR THE YEAR ENDED SEPTEMBER 30, 2016

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget - (Negative)</u>
	<u>Original</u>	<u>Final</u>		
REVENUES				
Property taxes	\$ 573,647	\$ 573,647	\$ 572,031	\$ (1,616)
Investment earnings	<u>2,000</u>	<u>2,000</u>	<u>5,304</u>	<u>3,304</u>
Total revenues	<u>575,647</u>	<u>575,647</u>	<u>577,335</u>	<u>1,688</u>
EXPENDITURES				
Debt service:				
Principal	385,136	436,708	402,322	34,386
Interest and fiscal charges	<u>190,511</u>	<u>200,668</u>	<u>188,538</u>	<u>12,130</u>
Total expenditures	<u>575,647</u>	<u>637,376</u>	<u>590,860</u>	<u>46,516</u>
Excess of expenditures over appropriations	<u>-</u>	<u>(61,729)</u>	<u>(13,525)</u>	<u>48,204</u>
OTHER FINANCING SOURCES (USES)				
Transfers in	<u>-</u>	<u>-</u>	<u>61,730</u>	<u>61,730</u>
Total other financing sources	<u>-</u>	<u>-</u>	<u>61,730</u>	<u>61,730</u>
Net change in fund balance	-	(61,729)	48,205	109,934
Fund balance - beginning balance	<u>637,661</u>	<u>637,661</u>	<u>637,661</u>	<u>-</u>
Fund balance - end of year	<u>\$ 637,661</u>	<u>\$ 575,932</u>	<u>\$ 685,866</u>	<u>\$ 109,934</u>

CITY OF KRUM, TEXAS

**NONMAJOR GOVERNMENTAL FUNDS
COMBINING BALANCE SHEET**

SEPTEMBER 30, 2016

	<u>Street Sales Tax</u>	<u>Court Technology</u>	<u>Court Security</u>	<u>Total Other Governmental Funds</u>
ASSETS				
Cash and cash equivalents	\$ 40,367	\$ 7,896	\$ 7,565	\$ 55,828
Total assets	<u>\$ 40,367</u>	<u>\$ 7,896</u>	<u>\$ 7,565</u>	<u>\$ 55,828</u>
LIABILITIES				
Accounts payable	\$ 1,131	\$ -	\$ -	\$ 1,131
Total liabilities	<u>1,131</u>	<u>-</u>	<u>-</u>	<u>1,131</u>
FUND BALANCES				
Restricted	<u>39,236</u>	<u>7,896</u>	<u>7,565</u>	<u>54,697</u>
Total funds balances	<u>39,236</u>	<u>7,896</u>	<u>7,565</u>	<u>54,697</u>
Total liabilities, deferred inflows of resources and fund balances	<u>\$ 40,367</u>	<u>\$ 7,896</u>	<u>\$ 7,565</u>	<u>\$ 55,828</u>

CITY OF KRUM, TEXAS
COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES - NONMAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2016

	Street Sales Tax	Court Technology	Court Security	Total Other Governmental Funds
REVENUES				
Fines and forfeitures	\$ -	\$ 3,891	\$ 2,919	\$ 6,810
Total revenues	-	3,891	2,919	6,810
EXPENDITURES				
Current:				
Public safety	-	1,500	677	2,177
Streets	15,943	-	-	15,943
Total expenditures	15,943	1,500	677	18,120
Excess (deficiency) of revenues over (under) expenditures	(15,943)	2,391	2,242	(11,310)
Net change in fund balances	(15,943)	2,391	2,242	(11,310)
Fund balances - beginning of year	55,179	5,505	5,323	66,007
Fund balances - end of year	\$ 39,236	\$ 7,896	\$ 7,565	\$ 54,697



PATILLO, BROWN & HILL, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS ■ BUSINESS CONSULTANTS

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

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

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Krum, Texas, as of and for the year ended September 30, 2016, and the related notes to the financial statements, which collectively comprise City of Krum, Texas's basic financial statements, and have issued our report thereon dated March 2, 2017.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

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

Purpose of this Report

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

Pattillo, Brown & Hill, L.L.P.

Hillsboro, Texas
March 2, 2017