

ANNUAL FINANCIAL REPORT

of the

CITY OF NASSAU BAY, TEXAS

For the Year Ended
September 30, 2011

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CITY OF NASSAU BAY, TEXAS

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CITY OF NASSAU BAY, TEXAS

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INTRODUCTORY SECTION

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CITY OF NASSAU BAY, TEXAS

PRINCIPAL OFFICIALS

September 30, 2011

City Officials	Elective Position	Term Expires
Donald C. Matter	Mayor	05/2012
David Braun	Council Member	05/2013
Sandra Mossman	Council Member	05/2012
Ron Swofford	Council Member	05/2013
Brad Bailey	Council Member	05/2012
Jonathan Amdur	Council Member	05/2013
Bob Warters	Council Member	05/2012

Key Staff	Position
Chris Reed	City Manager
Csilla Stiles	Director of Finance
Pat Jones, T.R.M.C.	City Secretary

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FINANCIAL SECTION

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INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and
City Council Members of the
City of Nassau Bay, Texas:

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Nassau Bay, Texas (the "City"), as of and for the year ended September 30, 2011, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City as of September 30, 2011, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with generally accepted accounting principles in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 13, 2012 on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis, the budgetary comparison information, and the schedule of funding progress are not a required part of the basic financial statements but are supplementary information required by generally accepted accounting principles in the United States of America. 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.

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

BELT HARRIS PECHACEK, LLLP

Belt Harris Pechacek, LLLP
Certified Public Accountants
Houston, Texas
March 13, 2012

***MANAGEMENT'S DISCUSSION
AND ANALYSIS***

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CITY OF NASSAU BAY, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
For the Year Ended September 30, 2011

The Statement of Net Assets presents information on all of the City's assets and liabilities. The difference between the two is reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating. Other nonfinancial factors, such as the City's property tax base and the condition of the City's infrastructure, need to be considered in order to assess the overall health of the City.

The Statement of Activities presents information showing how the City's net assets changed during the most recent year. All changes in the net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows using the accrual method rather than modified accrual that is used in the fund level statements.

The Statement of Net Assets and the Statement of Activities divide the City into three classes of activities:

1. Governmental Activities – Most of the City's basic services are reported here including general government, public safety, public works, public services, economic development, and tourism. Interest payments on the City's debt are also reported here. Sales tax, property tax, franchise taxes, municipal court fines, and permit fees finance most of these activities.
2. Business-type Activities – Services involving a fee for those services are reported here. These services include the City's water distribution and wastewater collection/treatment.
3. Component Units – The City of Nassau Bay itself is the primary government. The Nassau Bay Economic Development Corporation (the "Corporation") and the NASA Management District ("the District") are established as separate legal entities. The City maintains financial accountability; thus, the Corporation and the District are reported as *component units*, separate from the financial transactions of the City. In addition, the City also maintains two blended component units, the Tax Increment Reinvestment Zone #1 ("TIRZ") and the Nassau Bay Redevelopment Authority (the "Authority").

The government-wide financial statements can be found after the MD&A.

FUND FINANCIAL STATEMENTS

Funds may be considered as operating companies of the parent corporation, which is the City. They are usually segregated for specific activities or objectives. The City uses fund accounting to ensure and demonstrate compliance with finance related legal reporting requirements. The two categories of City funds are governmental and proprietary.

Governmental Funds

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

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance

CITY OF NASSAU BAY, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
For the Year Ended September 30, 2011

sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The City maintains eight 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, and the special revenue and grants fund, which are considered to be major funds. Data from the other five governmental funds are combined into a single, aggregated presentation.

The City adopts an annual appropriated budget for its general, debt service, special revenue and grants, tourism, and streets funds. Budgetary comparison schedules have been provided for these funds to demonstrate compliance with this budget.

Proprietary Funds

The City maintains one type of proprietary fund, an enterprise fund. The enterprise fund is used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses the enterprise fund to account for its water distribution and wastewater collection/treatment. The proprietary fund financial statements provide separate information for the water distribution and wastewater collection/treatment. The basic proprietary fund financial statements can be found in the basic financial statements of this report.

Notes to Financial Statements

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes are the last section of the basic financial statements.

Other Information

In addition to basic financial statements, MD&A, and accompanying notes, this report also presents certain RSI that GASB Statement No. 34 requires including a budgetary comparison schedule for the general fund and special revenue and grants fund, as well as a schedule of funding progress for the Texas Municipal Retirement System. The RSI can be found after the basic financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of the City's financial position. For the City, assets exceed liabilities by \$13,825,652 as of year end in the primary government.

As required by GASB Statement No. 34, a comparative analysis of government-wide data has been presented as a component of the MD&A.

The largest portion of the City's net assets, 72 percent, reflects its investments in capital assets (e.g., land, City hall, fleet equipment, streets, and drainage systems) less any 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 assets themselves cannot be used to liquidate these liabilities.

CITY OF NASSAU BAY, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
For the Year Ended September 30, 2011

Statement of Net Assets:

The following table reflects the condensed Statement of Net Assets:

CONDENSED STATEMENT OF NET ASSETS

	Governmental Activities		Business-type Activities		Total Primary Government	
	2011	2010	2011	2010	2011	2010
Current and other assets	\$ 3,539,980	\$ 2,857,163	\$ 3,465,678	\$ 404,667	\$ 7,005,658	\$ 3,261,830
Capital assets, net	9,564,541	9,413,217	3,162,461	3,209,669	12,727,002	12,622,886
Total Assets	13,104,521	12,270,380	6,628,139	3,614,336	19,732,660	15,884,716
Long-term liabilities	2,783,452	3,245,283	2,471,741	25,072	5,255,193	3,270,355
Other liabilities	515,974	310,175	135,841	136,038	651,815	446,213
Total Liabilities	3,299,426	3,555,458	2,607,582	161,110	5,907,008	3,716,568
Net Assets:						
Invested in capital assets, net of related debt	6,985,480	6,350,194	2,934,570	3,209,669	9,920,050	9,559,863
Restricted	1,256,636	1,145,364	-	-	1,256,636	1,145,364
Unrestricted	1,562,979	1,219,364	1,085,987	243,557	2,648,966	1,462,921
Total Net Assets	\$ 9,805,095	\$ 8,714,922	\$ 4,020,557	\$ 3,453,226	\$ 13,825,652	\$ 12,168,148

A portion of the primary government's net assets, \$1,256,636 or 9 percent, represents resources that are subject to restrictions on how they may be used. The remaining balance of unrestricted net assets, \$2,648,966, may be used to meet the City's ongoing obligation to citizens and creditors. The overall condition of the City improved this year as total net assets increased by \$1,657,504.

CITY OF NASSAU BAY, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
For the Year Ended September 30, 2011

Statement of Activities:

The following table provides a summary of the City's changes in net assets:

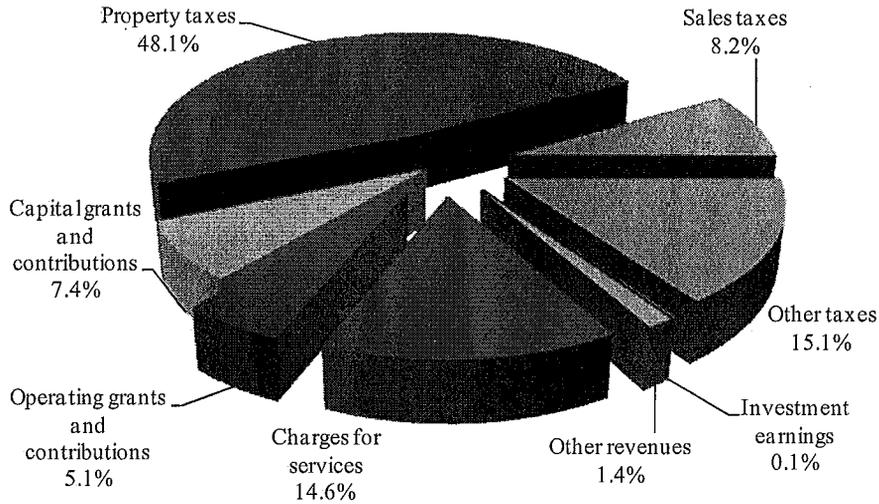
CONDENSED STATEMENT OF ACTIVITIES

	Governmental Activities		Business-type Activities		Total Primary Government	
	2011	2010	2011	2010	2011	2010
Revenues						
Program revenues:						
Charges for services	\$ 902,190	\$ 757,357	\$ 2,278,665	\$ 1,604,649	\$ 3,180,855	\$ 2,362,006
Operating grants and contributions	319,109	215,725	-	-	319,109	215,725
Capital grants and contributions	457,920	1,378,569	-	-	457,920	1,378,569
General revenues:						
Property taxes	2,977,296	2,744,903	-	-	2,977,296	2,744,903
Sales taxes	510,714	475,983	-	-	510,714	475,983
Other taxes	940,787	908,959	-	-	940,787	908,959
Investment earnings	5,852	4,592	717	252	6,569	4,844
Other revenues	84,277	91,226	-	-	84,277	91,226
Total Revenues	<u>6,198,145</u>	<u>6,577,314</u>	<u>2,279,382</u>	<u>1,604,901</u>	<u>8,477,527</u>	<u>8,182,215</u>
Expenses						
General government	984,489	848,567	-	-	984,489	848,567
Public safety	2,063,988	2,191,543	-	-	2,063,988	2,191,543
Public works	1,281,108	1,468,257	-	-	1,281,108	1,468,257
Public services	349,625	324,004	-	-	349,625	324,004
Economic development/tourism	622,197	674,001	-	-	622,197	674,001
Interest on long-term debt	101,875	105,936	-	-	101,875	105,936
Water and sewer	-	-	1,656,566	1,937,922	1,656,566	1,937,922
Total Expenses	<u>5,403,282</u>	<u>5,612,308</u>	<u>1,656,566</u>	<u>1,937,922</u>	<u>7,059,848</u>	<u>7,550,230</u>
Increase (Decrease) in Net Assets						
Before Transfers	794,863	965,006	622,816	(333,021)	1,417,679	631,985
Gain on sale of capital assets	62,325	-	-	-	62,325	-
Contributions	-	-	177,500	-	177,500	-
Transfers	232,985	-	(232,985)	-	-	-
Change in Net Assets	1,090,173	965,006	567,331	(333,021)	1,657,504	631,985
Beginning net assets	8,714,922	7,749,916	3,453,226	3,786,247	12,168,148	11,536,163
Ending Net Assets	<u>\$ 9,805,095</u>	<u>\$ 8,714,922</u>	<u>\$ 4,020,557</u>	<u>\$ 3,453,226</u>	<u>\$ 13,825,652</u>	<u>\$ 12,168,148</u>

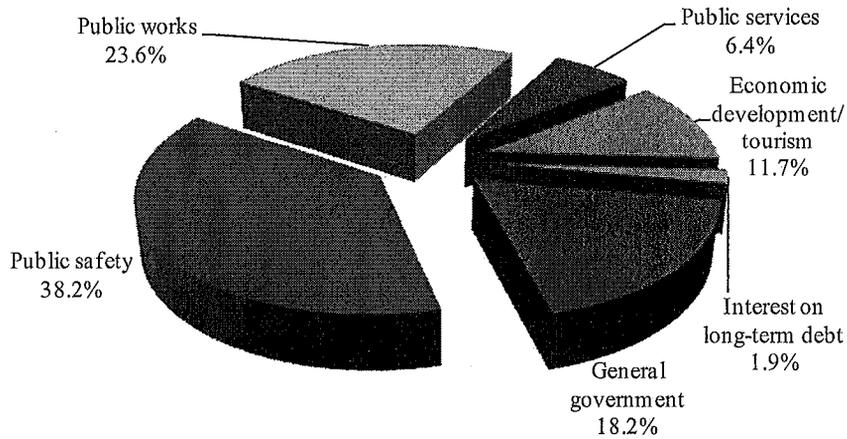
CITY OF NASSAU BAY, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
 For the Year Ended September 30, 2011

Graphic presentations of selected data from the summary tables follow to assist in the analysis of the City's activities.

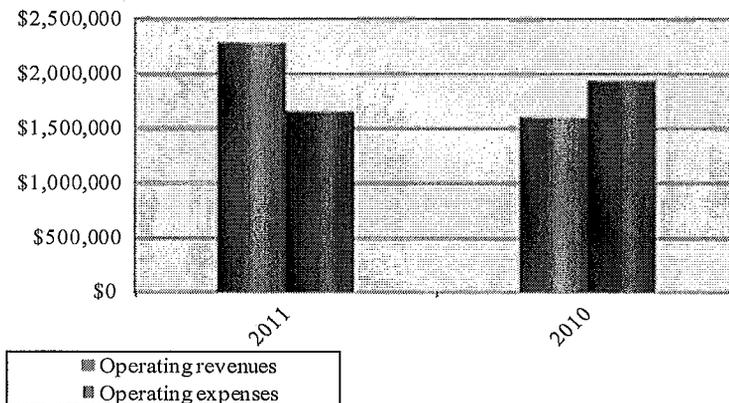
GOVERNMENTAL REVENUES



GOVERNMENTAL EXPENSES



BUSINESS-TYPE ACTIVITIES



CITY OF NASSAU BAY, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
For the Year Ended September 30, 2011

For the year ended, revenues from governmental activities totaled \$6,260,470. Revenues decreased by five percent during the year mainly due to a large decrease in capital grants and contributions. This decrease was caused by a larger amount of the capital projects related to the Economic Adjustment Assistance grant being completed in the prior year.

For the year ended, expenses for governmental activities totaled \$5,403,282. The total expenses decreased four percent from the prior year, which can be attributed primarily to a decrease in Economic Adjustment Assistance grant related expenses as larger grant related projects were completed in the prior year.

Business-type activities net assets increased by \$567,331, which is due to an increase of 42 percent in charges for services revenue in comparison to the prior year and a 15 percent decrease in water and sewer expenses compared to the prior year. The increase in revenue is due to the severe drought conditions and increases in water sales due to high irrigation and pool related water sales.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

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

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

The City's governmental funds reflect a combined fund balance of \$2,818,736. Of this, \$193,966 is restricted for debt service, \$252,467 is restricted for enabling legislation, \$827,462 is restricted for projects, and \$1,544,841 is unassigned.

The general fund had a positive change in fund balance of \$381,188 for the year due mainly to an increase in property tax revenue compared to the prior year.

The debt service fund decreased fund balance by \$1,986 as a result of an excess of principal and interest charges over total revenues.

The special revenue and grants fund had an increase in fund balance of \$144,438. Expenditures and revenues for the fund were \$560,872 and \$705,310, respectively, as a result of fewer projects related to the economic development grant.

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

GENERAL FUND BUDGETARY HIGHLIGHTS

Actual revenues exceeded original and final budgeted revenues by \$193,989 during the year due to higher than expected revenues for sales taxes, other taxes, licenses and permits, fines and forfeitures, and other revenues. These were offset by lower than expected revenues for property taxes and charges for services. General fund expenditures were under the final budget by \$216,362.

CITY OF NASSAU BAY, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)
For the Year Ended September 30, 2011

CAPITAL ASSETS

At the end of the year, the City's governmental activities funds had invested \$9,564,541 in a variety of capital assets. This represents a net increase of \$151,324. Depreciation is included with the governmental capital assets as required by GASB Statement No. 34.

Major capital asset events during the current year include the following:

- Purchase of 10 bulletproof vests for \$7,188
- Construction in progress related to the Saturn and Space Park improvement project of \$525,551.
- Purchase of a Dodge Charger for \$23,000

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

LONG-TERM DEBT

At the end of the current year, the City had total certificates of obligation, tax notes, and capital leases of \$5,024,061. Of this amount, \$4,395,015 represents certificates of obligation, \$135,000 represents tax notes, and \$494,046 represents capital leases.

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

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The Nassau Bay City Council approved a \$9.4 million budget for the 2011-2012 fiscal year. This is a 15 percent increase from the prior year. The tax rate adopted for the FY12 budget will remain unchanged at 0.692120. The budgeted taxable assessed valuations decreased by .26 percent to \$406 million. Budgeted property tax receipts comprise 29.8 percent of all City-wide revenue sources and 63 percent of the general fund revenue.

The economic growth and vitality of the City are supported by several mechanisms including the Nassau Bay Economic Development Corporation, the NASA Area Management District, the Nassau Bay Tax Increment Reinvestment Zone #1 and the Nassau Bay Redevelopment Authority. Through these entities and a Federal Economic Development Authority Recovery Grant, the City has been able to support the redevelopment of a 27-acre commercial area and actively pursue retail and commercial expansion in this area.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of the City of Nassau Bay's finances. Questions concerning this report or requests for additional financial information should be directed to Csilla Stiles at 281.333.4211, or by email at finance.office@nassaubay.com.

BASIC FINANCIAL STATEMENTS

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CITY OF NASSAU BAY, TEXAS

STATEMENT OF NET ASSETS

September 30, 2011

	Primary Government			Component Units	
	Governmental Activities	Business-Type Activities	Total	Nassau Bay Economic Dev. Corp.	NASA Area Management District
Assets					
Cash and cash equivalents	\$ 2,551,658	\$ 808,093	\$ 3,359,751	\$ 78,003	\$ 51,315
Receivables, net	925,374	388,959	1,314,333	38,720	13,200
Due from component units	17,211	-	17,211	-	-
Deferred charges	45,737	51,517	97,254	-	-
Restricted assets:					
Temporarily restricted cash and cash equivalents	-	407,321	407,321	-	-
Temporarily restricted investments	-	1,809,788	1,809,788	-	-
Capital assets:					
Non-depreciable	3,474,748	43,459	3,518,207	-	-
Net depreciable	6,089,793	3,119,002	9,208,795	-	-
Total Assets	13,104,521	6,628,139	19,732,660	116,723	64,515
Liabilities					
Accounts payable and accrued liabilities	493,916	82,060	575,976	-	-
Customer deposits	-	53,781	53,781	-	-
Accrued interest payable	22,058	-	22,058	-	-
Due to primary government	-	-	-	17,159	-
Noncurrent liabilities:					
Long-term liabilities due within one year	672,130	109,067	781,197	-	-
Long-term liabilities due in more than one year	2,111,322	2,362,674	4,473,996	-	-
Total Liabilities	3,299,426	2,607,582	5,907,008	17,159	-
Net Assets					
Invested in capital assets, net of related debt	6,985,480	2,934,570	9,920,050	-	-
Restricted for:					
Debt service	176,707	-	176,707	-	-
Enabling legislation	252,467	-	252,467	-	-
Special projects	821,956	-	821,956	-	-
Capital projects	5,506	-	5,506	-	-
Nassau Bay Economic Development	-	-	-	99,564	-
NASA Area Management District	-	-	-	-	64,515
Unrestricted	1,562,979	1,085,987	2,648,966	-	-
Total Net Assets	\$ 9,805,095	\$ 4,020,557	\$ 13,825,652	\$ 99,564	\$ 64,515

See Notes to Financial Statements.

CITY OF NASSAU BAY, TEXAS

STATEMENT OF ACTIVITIES

For the Year Ended September 30, 2011

Functions/Programs	Expenses	Program Revenues		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary Government				
Governmental Activities				
General government	\$ 984,489	\$ 528,299	\$ -	\$ -
Public safety	2,063,988	147,815	-	-
Public works	1,281,108	226,076	319,109	-
Public services	349,625	-	-	-
Economic development/tourism	622,197	-	-	457,920
Interest and fiscal agent fees on long-term debt	101,875	-	-	-
Total Governmental Activities	<u>5,403,282</u>	<u>902,190</u>	<u>319,109</u>	<u>457,920</u>
Business-Type Activities				
Water and sewer	1,656,566	2,278,665	-	-
Total Business-Type Activities	<u>1,656,566</u>	<u>2,278,665</u>	<u>-</u>	<u>-</u>
Total Primary Government	<u>\$ 7,059,848</u>	<u>\$ 3,180,855</u>	<u>\$ 319,109</u>	<u>\$ 457,920</u>
Component Units				
Nassau Bay Economic Development Corp.	\$ 281,468	\$ -	\$ -	\$ -
NASA Area Management District	50,967	-	-	-
Total Component Units	<u>\$ 332,435</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

General Revenues:

Taxes
 Property taxes
 Sales taxes
 Other taxes
 Investment earnings
 Other revenues
 Gain on sale of capital assets
 Contributions
 Transfers

Total General Revenues and Transfers

Change in Net Assets

Beginning net assets

Ending Net Assets

See Notes to Financial Statements.

Net (Expense) Revenue and Changes in Net Assets			Component Units	
Primary Government			Nassau Bay	NASA Area
Governmental	Business-Type	Total	Economic	Management
Activities	Activities		Dev. Corp	District
\$ (456,190)	\$ -	\$ (456,190)	\$ -	\$ -
(1,916,173)	-	(1,916,173)	-	-
(735,923)	-	(735,923)	-	-
(349,625)	-	(349,625)	-	-
(164,277)	-	(164,277)	-	-
(101,875)	-	(101,875)	-	-
(3,724,063)	-	(3,724,063)	-	-
-	622,099	622,099	-	-
-	622,099	622,099	-	-
(3,724,063)	622,099	(3,101,964)	-	-
-	-	-	(281,468)	-
-	-	-	-	(50,967)
-	-	-	(281,468)	(50,967)
2,977,296	-	2,977,296	-	-
510,714	-	510,714	202,864	73,799
940,787	-	940,787	-	-
5,852	717	6,569	214	4
84,277	-	84,277	-	-
62,325	-	62,325	-	-
-	177,500	177,500	-	-
232,985	(232,985)	-	-	-
4,814,236	(54,768)	4,759,468	203,078	73,803
1,090,173	567,331	1,657,504	(78,390)	22,836
8,714,922	3,453,226	12,168,148	177,954	41,679
\$ 9,805,095	\$ 4,020,557	\$ 13,825,652	\$ 99,564	\$ 64,515

CITY OF NASSAU BAY, TEXAS

BALANCE SHEET

GOVERNMENTAL FUNDS

September 30, 2011

	General	Debt Service	Special Revenue and Grants	Nonmajor Governmental Funds
Assets				
Cash and cash equivalents	\$ 1,567,801	\$ 193,966	\$ 146,910	\$ 642,981
Receivables, net	375,159	4,799	400,670	144,746
Due from component units	17,211	-	-	-
Total Assets	\$ 1,960,171	\$ 198,765	\$ 547,580	\$ 787,727
Liabilities				
Accounts payable and accrued liabilities	\$ 238,538	\$ -	\$ 243,677	\$ 11,701
Deferred revenue	176,792	4,799	-	-
Total Liabilities	415,330	4,799	243,677	11,701
Fund Balances				
Restricted for:				
Debt service	-	193,966	-	-
Enabling legislation	-	-	-	252,467
Capital projects	-	-	-	5,506
Special projects	-	-	303,903	518,053
Unassigned	1,544,841	-	-	-
Total Fund Balances	1,544,841	193,966	303,903	776,026
Total Liabilities and Fund Balances	\$ 1,960,171	\$ 198,765	\$ 547,580	\$ 787,727

Adjustments for the Statement of Net Assets:

Capital assets used in governmental activities are not current financial resources and, therefore, not reported in the governmental funds.

Capital assets - non-depreciable	3,474,748
Capital assets - net depreciable	6,089,793

Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.

Some liabilities, including bonds payable, are not reported as liabilities in the governmental funds.

Accrued interest payable	(22,058)
Non-current liabilities due in one year	(672,130)
Non-current liabilities due in more than one year	(2,111,322)
Deferred charges for issuance costs	45,737

Net Assets of Governmental Activities

See Notes to Financial Statements.

**Total
Governmental
Funds**

\$ 2,551,658
925,374
17,211
\$ 3,494,243

\$ 493,916
181,591
675,507

193,966
252,467
5,506
821,956
1,544,841
2,818,736

9,564,541

181,591

(2,759,773)
\$ 9,805,095

CITY OF NASSAU BAY, TEXAS

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE

GOVERNMENTAL FUNDS

For the Year Ended September 30, 2011

	General	Debt Service	Special Revenue and Grants	Nonmajor Governmental Funds
Revenues				
Property taxes	\$ 2,618,415	\$ 166,347	\$ -	\$ 227,888
Sales taxes	409,282	-	-	101,432
Other taxes	466,675	-	-	474,112
Licenses and permits	226,076	-	-	-
Fines and forfeitures	147,815	-	-	-
Charges for services	495,002	-	-	-
Intergovernmental	-	71,919	705,110	-
Investment earnings	3,756	358	200	1,538
Other revenues	84,277	-	-	-
Total Revenues	4,451,298	238,624	705,310	804,970
Expenditures				
Current:				
General government	886,194	-	-	92,782
Public safety	1,806,145	-	560,872	-
Public works	1,095,995	-	-	34,309
Public services	346,376	-	-	-
Economic development/tourism	-	-	-	540,588
Capital outlay	-	-	-	166,800
Debt Service:				
Principal	-	386,776	-	-
Interest and fiscal charges	-	86,819	-	-
Total Expenditures	4,134,710	473,595	560,872	834,479
Excess (Deficiency) of Revenues Over (Under) Expenditures	316,588	(234,971)	144,438	(29,509)
Other Financing Sources (Uses)				
Transfers in	-	232,985	-	227,888
Transfers (out)	-	-	-	(227,888)
Sale of capital assets	64,600	-	-	-
Total Other Financing Sources (Uses)	64,600	232,985	-	-
Net Change in Fund Balances	381,188	(1,986)	144,438	(29,509)
Beginning fund balances	1,163,653	195,952	159,465	805,535
Ending Fund Balances	\$ 1,544,841	\$ 193,966	\$ 303,903	\$ 776,026

See Notes to Financial Statements.

**Total
Governmental
Funds**

\$ 3,012,650
510,714
940,787
226,076
147,815
495,002
777,029
5,852
84,277
6,200,202

978,976
2,367,017
1,130,304
346,376
540,588
166,800

386,776
86,819
6,003,656

196,546

460,873
(227,888)
64,600

297,585

494,131

2,324,605

\$ 2,818,736

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CITY OF NASSAU BAY, TEXAS

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

For the Year Ended September 30, 2011

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

Net changes in fund balances - total governmental funds	\$	494,131
---	----	---------

Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

Capital outlay	604,544
Capital disposals, net	(2,275)
Depreciation expense	(450,945)

Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds.	(2,057)
--	---------

The issuance of long-term debt (e.g., bonds, leases, certificates of obligation) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when they are first issued, whereas these amounts are deferred and amortized in the Statement of Activities.

Principal expenditures	483,962
Amortization of issuance costs	(8,586)

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 funds.

Accrued interest	(6,470)
Compensated absences	(22,131)

Change in Net Assets of Governmental Activities	\$	<u>1,090,173</u>
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See Notes to Financial Statements.

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CITY OF NASSAU BAY, TEXAS

STATEMENT OF NET ASSETS

PROPRIETARY FUND

September 30, 2011

	<u>Business-Type Activities</u>
	<u>Enterprise Fund</u>
<u>Assets</u>	
<u>Current Assets</u>	
Cash and cash equivalents	\$ 808,093
Receivables, net	388,959
<u>Current Restricted Assets</u>	
Cash and cash equivalents	407,321
Investments	1,809,788
Total Current Assets	<u>3,414,161</u>
Deferred charges	51,517
Capital assets:	
Land	43,459
Water and sewer system	6,198,470
Water rights, SEWPP	2,114,318
Machinery and equipment	279,265
Less: accumulated depreciation	<u>(5,473,051)</u>
Total Capital Assets, Net of Accumulated Depreciation	<u>3,162,461</u>
Total Noncurrent Assets	<u>3,213,978</u>
Total Assets	<u>6,628,139</u>
<u>Liabilities</u>	
<u>Current Liabilities</u>	
Accounts payable and accrued liabilities	82,060
Customer deposits	53,781
Bond payable, due within one year	85,000
Compensated absences due in one year	24,067
Total Current Liabilities	<u>244,908</u>
<u>Noncurrent Liabilities</u>	
Bond payable, due in more than one year	2,360,000
Compensated absences in more than one year	2,674
Total Noncurrent Liabilities	<u>2,362,674</u>
Total Liabilities	<u>2,607,582</u>
<u>Net Assets</u>	
Invested in capital assets, net of related debt	2,934,570
Unrestricted	1,085,987
Total Net Assets	<u>\$ 4,020,557</u>

See Notes to Financial Statements.

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CITY OF NASSAU BAY, TEXAS
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUND

For the Year Ended September 30, 2011

	Business-Type Activities Enterprise Fund
<u>Operating Revenues</u>	
Water charges	\$ 1,127,816
Sewer charges	1,093,374
Penalties and reconnect fees	17,993
Other revenues	39,482
Total Operating Revenues	2,278,665
<u>Operating Expenses</u>	
General and administrative	887,084
Water expenses	294,550
Sewer expenses	195,704
Depreciation	224,706
Total Operating Expenses	1,602,044
Operating Income	676,621
<u>Nonoperating Revenues (Expenses)</u>	
Investment earnings	717
Interest expense	(54,522)
Total Nonoperating Revenues (Expenses)	(53,805)
Income Before Transfers	622,816
Capital contribution	177,500
Transfers (out)	(232,985)
Change in Net Assets	567,331
Beginning net assets	3,453,226
Ending Net Assets	\$ 4,020,557

See Notes to Financial Statements.

CITY OF NASSAU BAY, TEXAS

STATEMENT OF CASH FLOWS PROPRIETARY FUND (Page 1 of 2) For the Year Ended September 30, 2011

	<u>Business-Type Activities</u> <u>Enterprise Fund</u>
<u>Cash Flows from Operating Activities</u>	
Receipts from customers	\$ 2,307,337
Payments to suppliers	(504,539)
Payments to employees	(885,415)
Net Cash Provided by Operating Activities	<u>917,383</u>
<u>Cash Flows from Noncapital Financing Activities</u>	
Transfers (out) to other funds	(232,985)
Net Cash (Used) by Noncapital Financing Activities	<u>(232,985)</u>
<u>Cash Flows from Capital and Related Financing Activities</u>	
Proceeds from issuance of bonds	2,445,000
Bond issuance costs	(51,517)
Interest paid on debt	(54,522)
Net Cash Provided by Capital and Related Financing Activities	<u>2,338,961</u>
<u>Cash Flows from Investing Activities</u>	
Purchase of investments	(1,809,788)
Interest on investments	717
Net Cash (Used) by Investing Activities	<u>(1,809,071)</u>
Net Increase in Cash and Cash Equivalents	1,214,288
Beginning cash and cash equivalents	<u>1,126</u>
Ending Cash and Cash Equivalents	<u>\$ 1,215,414</u>
Ending Cash and Cash Equivalents:	
Unrestricted cash and cash equivalents	\$ 808,093
Restricted cash and cash equivalents	<u>407,321</u>
	<u>\$ 1,215,414</u>

CITY OF NASSAU BAY, TEXAS

STATEMENT OF CASH FLOWS PROPRIETARY FUND (Page 2 of 2) For the Year Ended September 30, 2011

	<u>Business-Type Activities</u> <u>Enterprise Fund</u>
<u>Reconciliation of Operating Income</u>	
<u>to Net Cash Provided by Operating Activities</u>	
Operating Income	\$ 676,621
Adjustments to Reconcile Operating income to Net Cash Provided by Operating Activities:	
Depreciation	224,706
Changes in Operating Assets and Liabilities:	
(Increase) Decrease in:	
Accounts receivable	14,582
Increase (Decrease) in:	
Accounts payable and accrued liabilities	(14,285)
Compensated absences	1,669
Customer deposits	14,090
Net Cash Provided by Operating Activities	<u>\$ 917,383</u>
 Noncash Investing, Capital, and Financing Activities:	
Contributions of capital assets from government	<u>\$ 177,500</u>

See Notes to Financial Statements.

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CITY OF NASSAU BAY, TEXAS

NOTES TO FINANCIAL STATEMENTS

For the Year Ended September 30, 2011

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The City of Nassau Bay, Texas (the "City") was incorporated in June 1970 and adopted a "Home Rule Charter" in April 1973. The City operates under a Council – Manager form of government. The Mayor and six Council Members are elected from the City at large serving two-year terms. Currently, the City charter provides for a term limitation of four terms. The City Council is the principal legislative body of the City. The City Manager is appointed by a majority vote of the City Council and is responsible for the administration of all affairs of the City. The City Manager is responsible for law enforcement, appointment and removal of department directors and employees, supervision and control of all City departments, and preparation of the annual budget. The Mayor presides at meetings of the City Council and can vote.

The City provides the following services: public safety, public works, public services, economic development, tourism, water and sewer services, and general administration.

The City is an independent political subdivision of the State and is considered a primary government. As required by generally accepted accounting principles, these basic financial statements have been prepared based on considerations regarding the potential for inclusion of other entities, organizations, or functions as part of the City's financial reporting entity. The component units, as listed below, although legally separate, are considered part of the reporting entity. No other entities have been included in the City's reporting entity. Additionally, as the City is considered a primary government for financial reporting purposes, its activities are not considered a part of any other governmental or other type of reporting entity.

Considerations regarding the potential for inclusion of other entities, organizations, or functions in the City's financial reporting entity are based on criteria prescribed by generally accepted accounting principles. These same criteria are evaluated in considering whether the City is a part of any other governmental or other type of reporting entity. The overriding elements associated with prescribed criteria considered in determining that the City's financial reporting entity status is that of a primary government are that it has a separately elected governing body, it is a legally separate entity and it is fiscally independent of other state and local governments. Additionally, prescribed criteria under generally accepted accounting principles include considerations pertaining to organizations for which the primary government is financially accountable, and considerations pertaining to organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

Discretely Presented Component Units

Nassau Bay Economic Development Corporation

Nassau Bay Economic Development Corporation (the "Corporation") has been included in the reporting entity as a discretely presented component unit. The citizens of Nassau Bay approved an additional one-half of one percent sales and use tax on November 4, 1997. The Corporation was created to encourage the retention of business enterprises and the promotion and development of new and expanded business enterprises within the City. The Board of Directors is appointed by the City Council and includes the Mayor, three City Council members, and three residents not affiliated with the City government. City Council approval is required for annual budgets. In the event of

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

dissolution, net assets of the Corporation shall be conveyed to the City. The operations of the Corporation are presented as a governmental fund type. Separate financial statements of the Corporation may be obtained from the Finance Department of the City.

NASA Area Management District

NASA Area Management District (the "District") has been included in the reporting entity as a discretely presented component unit. The District was created to develop, encourage, and maintain employment, commerce, transportation, housing, tourism, recreation, the arts, entertainment, economic development, safety, and the public welfare in the District territory. The Board of Directors is appointed by the City Council. The District began collecting a sales tax in March 2008 to finance these activities.

Blended Component Units

Tax Increment Reinvestment Zone # 1

During fiscal year 2008, the City passed an ordinance creating a Tax Increment Reinvestment Zone # 1 ("TIRZ") in accordance with Section 311.005 of the Texas Tax Code, for the purpose of tax increment financing, in order to facilitate the development of a mixed use commercial development, which may include a hotel, office buildings, residential units, and retail developments. The TIRZ includes participation by a developer and another governmental entity, the NASA Area Management District. Under this arrangement, increases in property taxes will be utilized to pay for certain infrastructure costs. Such taxes are controlled by a Board of Directors appointed by the City managing the TIRZ and accounted for as a special revenue fund with the City's financial oversight.

Nassau Bay Redevelopment Authority

Nassau Bay Redevelopment Authority (the "Authority") has been included in the reporting entity as a blended component unit. The Authority has been created to assist and act on behalf of the City in the performance of the City's governmental and proprietary functions with respect to the common good and general welfare of the area included in the TIRZ. During fiscal year 2010, the City passed a formal agreement (the "Agreement") between the City, the Authority, and the TIRZ in which the Authority will facilitate the implementation of the TIRZ plan and assist the City with reimbursement to the Developer participating in the TIRZ. Reimbursement to the Developer will be made through the issuance of bonds and with certain other monies available to the Authority but only after consent of the City Council. Efforts of the Authority will be financed using tax increments from the TIRZ as outlined in the Agreement. Such taxes are controlled by a Board of Directors appointed by the City managing the Authority and accounted for as a special revenue fund with the City's financial oversight.

B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the Statement of Net Assets and the Statement of Activities) report information about the City as a whole. These statements include all 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.

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

The Statement of Activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Program revenues include charges paid by the recipients of goods or services offered by the programs and grants that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, such as taxes and investment earnings, are presented as general revenues.

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds and major individual proprietary funds are reported as separate columns in the fund financial statements. In the fund financial statements, the accounts of the City are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures or expenses, as appropriate. Following is a description of the various funds:

Governmental Funds

Governmental funds are those funds through which most governmental functions are typically financed.

General Fund

The general fund is used to account for all financial transactions not properly includable in other funds. The principal sources of revenues include local property taxes, sales and franchise taxes, licenses and permits, fines and forfeitures, and charges for services. Expenditures include general government, public safety, public works, and public services. The general fund is always considered a major fund for reporting purposes.

Special Revenue Funds

The special revenue funds are used to account for proceeds of specific revenue sources that are legally restricted to expenditures for specified purposes. The special revenue funds include tourism, streets, tax increment reinvestment zone # 1 (TIRZ), Nassau Bay redevelopment authority (RDA), and special revenue and grants. The special revenue and grants fund is considered a major fund for reporting purposes while the tourism, streets, TIRZ, and RDA are considered nonmajor funds.

Debt Service Fund

The debt service fund is used to account for the payment of interest and principal on all general obligation bonds and other long-term debt of the City. The primary source of revenue for debt service is local property taxes. The debt service fund is considered a major fund for reporting purposes.

Capital Projects Fund

The capital projects fund is used to account for the expenditures of resources accumulated from certificates of obligation and tax notes as well as related interest earnings for capital

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

improvement projects. The capital projects fund is considered a nonmajor fund for reporting purposes.

Proprietary Fund Types

Proprietary funds are used to account for activities that are similar to those often found in the private sector. All assets, liabilities, equities, revenues, expenses, and transfers relating to the government's business activities are accounted for through proprietary funds. The measurement focus is on determination of net income, financial position, and cash flows. Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues include charges for services. Operating expenses include costs of materials, contracts, personnel, and depreciation. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. Proprietary fund types follow GAAP prescribed by the Governmental Accounting Standards Board (GASB) and all Financial Accounting Standards Board's standards issued prior to November 30, 1989. Subsequent to this date, the City accounts for its enterprise funds as presented by GASB.

The proprietary fund types used by the City include the following:

Enterprise Fund

The enterprise fund is used to account for the operations that provide water and wastewater collection and wastewater treatment operations. The services are financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the costs (expenses including depreciation) of providing goods or services to the general public on a continuing basis will be financed or recovered primarily through user charges. The enterprise fund is considered a major fund for reporting purposes.

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

The government-wide Statements of Net Assets and Statements of Activities and all proprietary funds are accounted for on a flow of economic resources measurement focus, accrual basis of accounting. With this measurement focus, all assets and all liabilities associated with the operations of these activities are included on the balance sheet. Government-wide and proprietary fund equity consists of net assets. Operating statements of these funds present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds and blended component units are accounted for using a current financial resources measurement focus, modified accrual basis of accounting. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

Under the modified accrual basis of accounting, revenues are recognized in the accounting period when they are susceptible to accrual (i.e., when they are measurable and available). "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues available if they are collected within 60 days of the end of the current period.

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

Property taxes, sales taxes, franchise taxes, and interest associated with the current period are all considered to be susceptible to accrual and so have been recognized as revenues of the current period. Other receipts and other taxes become measurable and available when cash is received by the government and are recognized as revenue at that time.

Under modified accrual accounting, expenditures are recognized in the accounting period in which the liability is incurred, if measurable, except for interest on general long-term debt, which is recognized when due.

Under the accrual basis of accounting, revenues are recognized in the accounting period in which they are earned, and expenses in the accounting period in which they are incurred.

D. Assets, Liabilities, and Net Assets or Fund Equity

1. Deposits and Investments

The City's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition. For the purpose of the statement of cash flows, the proprietary fund types consider temporary investments with maturity of three months or less when purchased to be cash equivalents.

The City maintains a pooled cash and investments account for all funds of the City. Each fund's positive equity in the pooled cash account is presented as cash and cash equivalents or investments. Interest income is allocated to each respective individual fund monthly based on their representative fund balances.

In accordance with GASB Statement No. 31, *Accounting and Reporting for Certain Investments and External Investment Pools*, the City reports all investments at fair value, except for "money market investments" and "2a7-like pools." Money market investments, which are short-term highly liquid debt instruments that may include U.S. Treasury and agency obligations, are reported at amortized costs. Investment positions in external investment pools that are operated in a manner consistent with the SEC's Rule 2a7 of the Investment Company Act of 1940, such as TexPool are reported using the pools' share price.

The City has adopted a written investment policy regarding the investment of its funds as defined in the Public Funds Investment Act, Chapter 2256, Texas Government Code. In summary, the City is authorized to invest in the following:

- Obligations of the U.S. Treasury
- Fully collateralized certificates of deposit and money market accounts with local depository banks
- Local government investment pools
- Repurchase agreements

2. Receivables

Transactions between funds that are representative of lending/borrowing arrangements outstanding at the end of the year are referred to as either "interfund receivables/payables" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds" in

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

the fund financial statements. If the transactions are between the primary government and its component units, these receivables and payables are classified as “due to/from component units/primary government.” Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as “internal balances.”

Advances between funds are offset by a fund balance reserve account in an applicable governmental fund to indicate they are not available for appropriation and are not expendable available financial resources.

All trade receivables are shown net of an allowance for uncollectibles.

Property taxes

Property taxes are levied on October 1 of each year, are due upon receipt of the City’s tax bill, and become delinquent on February 1 of the following year. The City’s tax lien exists from January 1 (the assessment date) each year until the taxes are paid.

3. Inventories and Prepaid Items

The costs of governmental fund type inventories are recorded as expenditures when the related liability is incurred (i.e., the purchase method). Certain payments to vendors reflect costs applicable to future accounting periods (prepaid expenditures) are recognized as expenditures when utilized.

4. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. In accordance with GASB Statement No. 34, infrastructure has been capitalized retroactively. Capital assets are defined by the government as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Interest costs incurred in connection with construction of enterprise fund capital assets are capitalized when the effects of capitalization materially impact the financial statements.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets’ lives are not capitalized.

Property, plant, and equipment of the primary government are depreciated using the straight-line method over the following estimated useful years.

<u>Asset Description</u>	<u>Estimated Useful Life</u>
Machinery and equipment	2 to 10 years
Buildings and improvements	10 to 50 years
Water and sewer system	10 to 45 years

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

5. Compensated Employee Absences

It is the City's policy to permit employees to accumulate earned but unused vacation up to a maximum of forty (40) days. Compensatory time not used can also be accumulated. Vacation and compensatory time amounts accumulated may be paid to employees upon termination of employment or at retirement. The City also allows employees to accumulate unused sick leave up to a maximum of 100 days. Upon severance, any full-time employee will receive a percentage of the accumulated sick leave paid at the employee's current rate of compensation based on years of service with the City. The estimated amount of compensation for services provided that is expected to be liquidated with expendable, available financial resources are reported as expenditures and a fund liability of the governmental fund that will pay it when it becomes due. Amounts of vested or accumulated vacation leave that are not expected to be liquidated with expendable, available financial resources are maintained separately and represent a reconciling item between the fund and government-wide presentations.

6. Long-Term Obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities or business-type activities column on the Statement of Net Assets. The long-term debt consists primarily of certificates of obligation payable and accrued compensated absences.

Long-term debt for governmental funds is not reported as a liability in the fund financial statements until due. The debt proceeds are reported as other financing sources, net of the applicable premium or discount and payments of principal and interest are reported as expenditures. In the governmental fund types, issuance costs, even if withheld from the actual net proceeds received, are reported as debt service expenditures. However, claims and judgments paid from governmental funds are reported as a liability in the fund financial statements only for the portion expected to be financed from expendable, available financial resources.

Long-term debt and other obligations, financed by proprietary funds, are reported as liabilities in the appropriate funds. For proprietary fund types, bond premiums, discounts and issuance costs are deferred and amortized over the life of the bonds using the effective interest method, if material. Bonds payable are reported net of the applicable bond premium or discount. Issuance costs are reported as deferred charges.

The property tax rate is allocated each year between the general and debt service funds. The full amount estimated to be required for debt service on general obligation debt is provided by the tax along with interest earned in the debt service fund. Though a portion of the general obligation debt was directly related to the purchase of water and sewer infrastructure, the debt service expenditures are included in the governmental fund financial statements as they are expected to be paid from debt service tax revenues instead of water system revenues.

Assets acquired under the terms of capital leases are recorded as liabilities and capitalized in the government-wide financial statements at the present value of net minimum lease payments at inception of the lease. In the year of acquisition, capital lease transactions are recorded as other financing sources and as capital outlay expenditures in the general fund. Lease payments representing both principal and interest are recorded as expenditures in the general fund upon

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

payment, with an appropriate reduction of principal recorded in the government-wide financial statements.

7. Fund Equity

Fund balances of governmental funds are classified as follows:

Nonspendable fund balance – represents amounts that cannot be spent because they are either in nonspendable form (such as inventory or prepaid insurance) or are legally required to remain intact (such as notes receivable or principal of a permanent fund).

Restricted fund balance – represents amounts that are constrained by external parties, constitutional provisions, or by enabling legislation.

Committed fund balance – represents amounts constrained to specific purposes by the City itself, using its highest level of decision-making authority (i.e., City Council). To be reported as committed, amounts cannot be used for any other purpose unless the City takes the same highest level action to remove or change the constraint. The commitment must be made prior to year end.

Assigned fund balance – represents amounts the City intends to use for a specific purpose. Intent can be expressed by the City Council or by an official or body to which the City Council delegates the authority. In governmental funds other than the general fund, assigned fund balance represents the amount that is not restricted or committed. This indicates that resources in other governmental funds are, at a minimum, intended to be used for the purpose of that fund. Assignments can be made at any time.

Unassigned fund balance – represents amounts that are available for any purpose. Positive amounts are reported only in the general fund. Other governmental funds might report a negative balance in this classification because of overspending for specific purposes for which amounts had been restricted, committed, or assigned.

When an expenditure is incurred for which committed, assigned, or unassigned fund balances are available, the City considers amounts to have been spent first out of committed, then assigned funds, and finally unassigned funds.

The City Council is the government's highest level of decision-making authority and the formal action that is required to be taken to establish, modify, or rescind a fund balance commitment is a ordinance approved by the Council. The ordinance must either be approved or rescinded, as applicable, prior to the last day of the fiscal year for which the commitment is made. The amount subject to the constraint may be determined in the subsequent period.

The City Council has the authority to assign fund balance to a specific purpose as approved by the City's fund balance policy.

The City strives to maintain an unassigned fund balance of not less than 90 days of expenditures. The purpose of the unassigned balance is to alleviate significant unanticipated budget shortfalls and to ensure the orderly provisions of services to citizens. Should unassigned fund balance fall below the goal or has a deficiency, the City will seek to reduce expenditures prior to increasing revenues to replenish fund balance within a reasonable timeframe.

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

8. 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 disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

II. STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Annual budgets are adopted on a basis consistent with generally accepted accounting principles (GAAP). The original budget is adopted by the City Council prior to the beginning of the year. The legal level of control as defined by the charter in the approved budget is the department level. The City Manager may transfer appropriations within a department without seeking the approval of City Council. Appropriations lapse at the end of the year. Encumbrance accounting is not utilized.

III. DETAILED NOTES ON ALL FUNDS

A. Deposits and Investments

As of year end, the City had the following investments:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Weighted Average Maturity (Years)</u>
U.S. agencies	\$ 1,745,000	0.36
External investment pools	128,366	0.00
Total fair value	<u>\$ 1,873,366</u>	
Portfolio weighted average maturity		0.34

Interest rate risk. In accordance with the City investment policy, the City manages its exposure to declines in fair values by structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations.

Credit risk. The City's investment policy limits investments in money market mutual funds rated as to investment quality not less than AAA by at least one nationally recognized rating service. As of September 30, 2011, the City's investment in TexPool was rated AAAM by Standard & Poor's. The City's investment policy also requires repurchase agreements to be fully collateralized as described in the PFIA. The purchased securities shall have a minimum market value, including accrued interest, of 102 percent of the dollar value of the transaction. The City's investment in U.S. agency securities, held as of September 30, 2011, were rated not less than AAA by Standard & Poor's.

Custodial credit risk – deposits. In the case of deposits, this is the risk that in the event of a bank failure, the City's deposits may not be returned to it. As of September 30, 2011, the bank balances were \$3,312,585, \$994,050 of which was insured by FDIC. The market values of pledged securities were \$3,079,455.

Custodial credit risk – investments. For an investment, this is the risk that, in the event of the failure of the counterparty, the City will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The City's investment policy requires that it

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

will seek to safekeeping securities at financial institutions, avoiding physical possession. Further, all trades, where applicable, are executed by delivery versus payment to ensure that securities are deposited in the City's safekeeping account prior to the release of funds. As of September 30, 2011, market values of pledged securities related to the City's repurchase agreement were \$3,410,869 and the bank balances were \$159,511.

TexPool

TexPool was established as a trust company with the Treasurer of the State of Texas as trustee, segregated from all other trustees, investments, and activities of the trust company. The State Comptroller of Public Accounts exercises oversight responsibility over TexPool. Oversight includes the ability to significantly influence operations, designation of management, and accountability for fiscal matters. Additionally, the State Comptroller has established an advisory board composed of both participants in TexPool and other persons who do not have a business relationship with TexPool. The advisory board members review the investment policy and management fee structure. Finally, Standard & Poor's rate TexPool AAAM. As a requirement to maintain the rating, weekly portfolio information must be submitted to Standard & Poor's, as well as to the office of the Comptroller of Public Accounts for review.

B. Receivables

The following comprise receivable balances at year end:

Governmental and Proprietary Funds

	<u>Governmental Funds</u>					<u>Proprietary Fund</u>
	<u>Special</u>					<u>Enterprise</u>
	<u>General</u>	<u>Debt Service</u>	<u>Revenue and Grants</u>	<u>Tourism</u>	<u>Streets</u>	
Accounts	\$ 2,526	\$ -	\$ 3,815	\$ -	\$ -	\$ 435,686
Property taxes	175,757	11,122	-	-	-	-
Sales taxes	77,439	-	-	-	19,360	-
Other taxes	52,856	-	-	125,386	-	-
Grants	-	-	396,855	-	-	-
Ambulance billing	1,804,548	-	-	-	-	-
Commercial trash	65,546	-	-	-	-	-
Less allowance	(1,803,513)	(6,323)	-	-	-	(46,727)
	<u>\$ 375,159</u>	<u>\$ 4,799</u>	<u>\$ 400,670</u>	<u>\$ 125,386</u>	<u>\$ 19,360</u>	<u>\$ 388,959</u>

Component Units

	<u>Nassau Bay Economic Dev. Corp.</u>	<u>NASA Area Management District</u>
Sales taxes	<u>\$ 38,720</u>	<u>\$ 13,200</u>

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

C. Capital Assets

A summary of changes in capital assets for governmental activities for the year end is as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Governmental Activities:				
Capital assets not being depreciated:				
Land	\$ 963,332	\$ -	\$ (2,275)	\$ 961,057
Construction in progress	1,939,335	574,356	-	2,513,691
	2,902,667	574,356	(2,275)	3,474,748
Other capital assets:				
Buildings	1,146,064	-	-	1,146,064
Improvements other than buildings	6,700,524	-	-	6,700,524
Machinery and equipment	2,644,658	30,188	-	2,674,846
Total other capital assets	10,491,246	30,188	-	10,521,434
Total capital assets	13,393,913	604,544	(2,275)	13,996,182
Less accumulated depreciation for:				
Buildings	(195,115)	(23,724)	-	(218,839)
Improvements other than buildings	(2,145,551)	(236,617)	-	(2,382,168)
Machinery and equipment	(1,640,030)	(190,604)	-	(1,830,634)
Total accumulated depreciation	(3,980,696)	(450,945)	-	(4,431,641)
Other capital assets, net	6,510,550	(420,757)	-	6,089,793
Totals	\$ 9,413,217	\$ 153,599	\$ (2,275)	9,564,541
				Less associated debt (2,579,061)
				Invested in capital assets, net of related debt \$ 6,985,480

All capital assets constructed or paid for with funds of the component units are titled in the City's name. Accordingly, component units' capital assets and construction in progress are recorded in the governmental activities totals.

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

Depreciation was charged to governmental functions as follows:

General government	\$	13,654
Public safety		207,162
Public works		146,820
Public services		1,700
Economic development		81,609
Total Governmental Activities Depreciation Expense	\$	<u>450,945</u>

The City has active governmental activities construction projects as of September 30, 2011. The projects include:

Project Description	Authorized Contract	Contract Expenditures	Remaining Commitment
EDA Phase 3 - Hardscape	\$ 430,185	\$ 412,615	\$ 17,570
Hazard Mitigation Grant - Generators	303,769	150,869	152,900
Total	<u>\$ 733,954</u>	<u>\$ 563,484</u>	<u>\$ 170,470</u>

The following is a summary of changes in capital assets for business-type activities for the year ended September 30, 2011:

	Beginning Balance	Increases	(Decreases)	Ending Balance
Business-Type Activities:				
Capital assets not being depreciated:				
Land	\$ 43,459	\$ -	\$ -	\$ 43,459
	<u>43,459</u>	<u>-</u>	<u>-</u>	<u>43,459</u>
Other capital assets:				
Water and sewer system	6,033,470	165,000	-	6,198,470
Water rights, SEWPP	2,114,318	-	-	2,114,318
Machinery and equipment	266,764	12,501	-	279,265
Total other capital assets	<u>8,414,552</u>	<u>177,501</u>	<u>-</u>	<u>8,592,053</u>
Less accumulated depreciation for:				
Water and sewer system	(4,217,333)	(169,625)	-	(4,386,958)
Water rights, SEWPP	(778,067)	(50,606)	-	(828,673)
Machinery and equipment	(252,942)	(4,478)	-	(257,420)
Total accumulated depreciation	<u>(5,248,342)</u>	<u>(224,709)</u>	<u>-</u>	<u>(5,473,051)</u>
Total capital assets, being depreciated, net	<u>3,166,210</u>	<u>(47,208)</u>	<u>-</u>	<u>3,119,002</u>
Business-Type Activities Capital Assets, Net	<u>\$ 3,209,669</u>	<u>\$ (47,208)</u>	<u>\$ -</u>	<u>\$ 3,162,461</u>

Less associated debt	\$ (2,445,000)
Plus unspent bond proceeds	<u>2,217,109</u>

Invested in capital assets, net of related debt	<u>\$ 2,934,570</u>
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CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

Depreciation was charged to business-type functions as follows:

Water and sewer \$ 224,709

D. Long-Term Debt

The following is a summary of changes in the City's total long-term liabilities for the year ended September 30, 2011. In general, the City uses the general and debt service funds to liquidate long-term liabilities.

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental Activities:					
Compensated absences	\$ 182,260	\$ 214,064	\$ 191,933	\$ 204,391	\$ 183,952
General obligation debt:					
Certificates of obligation					
Series 2002	136,791	-	31,776	105,015 *	33,339
Series 2006	510,000	-	85,000	425,000 *	85,000
Series 2007	700,000	-	90,000	610,000 *	90,000
Series 2008	925,000	-	115,000	810,000 *	120,000
Tax anticipation notes					
Series 2006	200,000	-	65,000	135,000 *	65,000
Total	<u>2,654,051</u>	<u>-</u>	<u>578,709</u>	<u>2,289,406</u>	<u>577,291</u>
Obligations under capital leases					
Oshkosh Capital	568,997	-	82,627	486,370 *	87,163
Ford Motor Credit Company	22,235	-	14,559	7,676 *	7,676
Total	<u>591,232</u>	<u>-</u>	<u>97,186</u>	<u>494,046</u>	<u>94,839</u>
Total Governmental Activities	<u>\$ 3,245,283</u>	<u>\$ -</u>	<u>\$ 675,895</u>	<u>\$ 2,783,452</u>	<u>\$ 672,130</u>
				<u>\$ 2,111,322</u>	
				<u>\$ 2,579,061</u>	
Business-type Activities:					
Compensated absences	\$ 25,072	\$ 18,836	\$ 17,167	\$ 26,741	\$ 24,067
Certificates of obligation					
Series 2011	-	2,445,000	-	2,445,000 *	85,000
Total Business-Type Activities	<u>\$ 25,072</u>	<u>\$ 2,463,836</u>	<u>\$ 17,167</u>	<u>\$ 2,471,741</u>	<u>\$ 109,067</u>
				<u>\$ 2,362,674</u>	
				<u>\$ 2,445,000</u>	

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

Long-term liabilities applicable to the City's governmental activities are not due and payable in the current period and, accordingly, are not reported as fund liabilities in the governmental funds. The governmental activities compensated absences are generally liquidated by the general fund. Interest on long-term debt is not accrued in governmental funds, but rather is recognized as an expenditure when due.

Long-term governmental debt at year end was comprised of the following debt issues:

Description	Interest Rates (%)	Balance
General obligation debt:		
Certificates of obligation		
Series 2002	4.80	\$ 105,015
Series 2006	4.22-4.33	425,000
Series 2007	5.25-6.00	610,000
Series 2008	3.09	810,000
Total Certificates of Obligation		<u>1,950,015</u>
Tax anticipation notes		
Series 2006	4.008-4.212	135,000
Total Tax Notes		<u>135,000</u>
Capital Leases		
Oshkosh Capital	5.49	486,370
Ford Motor Credit Company	7.10	7,676
Total Capital Leases		<u>494,046</u>
Total General Obligation Debt		<u>\$ 2,579,061</u>

The annual requirements to amortize debt issues outstanding at year end are as follows:

Year Ending Sept. 30	Certificates of Obligation		Tax Note		Capital Leases		Total
	Principal	Interest	Principal	Interest	Principal	Interest	
2012	\$ 328,339	\$ 66,725	\$ 65,000	\$ 4,283	\$ 94,839	\$ 26,861	\$ 464,347
2013	339,978	53,932	70,000	1,474	91,949	21,916	465,384
2014	351,698	40,686	-	-	96,997	16,869	392,384
2015	330,000	27,828	-	-	102,322	11,543	357,828
2016	340,000	15,399	-	-	107,939	5,926	355,399
2017	260,000	4,546	-	-	-	-	264,546
Total	<u>\$ 1,950,015</u>	<u>\$ 209,116</u>	<u>\$ 135,000</u>	<u>\$ 5,757</u>	<u>\$ 494,046</u>	<u>\$ 83,115</u>	<u>\$ 2,299,888</u>

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

Long-term business-type debt at year end was comprised of the following debt issues:

Description	Interest Rates (%)	Balance
General obligation debt:		
Certificates of obligation		
Series 2011	1.94-5.29	\$ 2,445,000
Total Certificates of Obligation		\$ 2,445,000

The annual requirements to amortize debt issues outstanding at year end are as follows:

Year Ending Sept. 30	Certificates of Obligation	
	Principal	Interest
2012	\$ 85,000	\$ 104,321
2013	85,000	102,545
2014	90,000	100,495
2015	90,000	98,119
2016	95,000	95,373
2017 - 2021	525,000	423,888
2022 - 2026	645,000	296,677
2027 - 2031	830,000	113,311
Total	\$ 2,445,000	\$ 1,334,729

Machinery and equipment acquired under current capital lease obligations was a total of \$697,589. This is from the issuance of two capital leases through Oshkosh Capital to acquire a new fire truck and Ford Motor Credit Company to acquire a new Ford Expedition. At year end, the fire truck had associated depreciation of \$100,613 and a net value of \$570,142, and the Expedition of \$8,945 and \$8,945, respectively.

Certificates of obligation are direct obligations of the City for which its full faith and credit are pledged. Repayment is from taxes levied on all taxable property located within the City and from the water and sewer system revenues. Series 2006 tax notes repayment is from sales tax from the Nassau Bay Economic Development Corporation.

E. Interfund Transactions

Transfers between the primary government funds during the year were as follows:

Transfer Out	Transfer In	Amounts
Nonmajor governmental	Enterprise	\$ 232,985
Nonmajor governmental	Nonmajor governmental	227,888
		\$ 460,873

The amount transferred between nonmajor funds relates to a transfer of revenue from the TIRZ to the RDA as part of a tri-party agreement between the two funds and the City.

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

IV. OTHER INFORMATION

A. Risk Management

The City is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters for which the City participates along with 2,617 other entities in the Texas Municipal League's Intergovernmental Risk Pools. The Pool purchases commercial insurance at group rates for participants in the Pool. The City has no additional risk or responsibility to the Pool, outside of the payment of insurance premiums. The City has not significantly reduced insurance coverage or had settlements, which exceeded coverage amounts for the past three years.

B. Contingent Liabilities

Amounts received or receivable from granting agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount of expenditures which may be disallowed by the grantor cannot be determined at this time although the City expects such amounts, if any, to be immaterial.

The City is a defendant in several lawsuits. Although the outcome of the lawsuits is not presently determinable, it is the opinion of the City's counsel that resolution of these matters will not have a material adverse effect on the financial condition of the City.

Liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amount of payouts, and other economic and social factors. No claim liabilities are reported at year end.

C. Pension Plans

Texas Municipal Retirement System

Plan Description

The City provides pension benefits for all of its full-time employees through a non-traditional, joint contributory, hybrid defined benefit plan in the state-wide Texas Municipal Retirement System (TMRS), one of 837 administered by TMRS, an agent multiple-employer public employee retirement system. The plan provisions that have been adopted by the City are within the options available in the governing state statutes of TMRS.

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

TMRS issues a publicly available comprehensive annual financial report that includes financial statements and Required Supplementary Information (RSI) for TMRS. The report also provides detailed explanations of the contributions, benefits and actuarial methods and assumptions used by TMRS. This report may be obtained from TMRS' website at www.TMRS.com.

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

	2011	2010
Employee deposit rate	5.00%	5.00%
Matching ratio (city to employee)	2 to 1	2 to 1
Years required for vesting	5	5
Service requirement eligibility (expressed as age/yrs of service)	60/5, 0/25	60/5, 0/25
Updated service credit		
	50% Repeating, Transfers	50% Repeating, Transfers
Annuity increase (to retirees)	70% of CPI Repeating	70% of CPI Repeating

Benefits

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

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

Contributions

Under the state law governing TMRS, the contribution rate for each city is determined annually by the actuary, using the Projected Unit Credit actuarial cost method. This rate consists of the normal cost contribution and the prior service cost contribution rate, which is calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the portion of an active member's projected benefit allocated annually; the prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the remainder of the plan's 30-year amortization period. Both the normal cost and prior service contribution rates include recognition of the projected impact of annually repeating benefits such as Updated Service Credits and Annuity Increases.

The City contributes to the TMRS plan at an actuarially determined rate. Both the employees and the City make contributions monthly. Since the City needs to know its contribution rate in advance for budgetary purposes, there is a one year delay between the actuarial valuation that serves as the basis for the rate and the calendar year when the rate goes into effect (i.e., December 31, 2010 valuation is effective for rates beginning January 2012).

Three-year trend information for the annual pension cost (APC) is as follows:

<u>Fiscal year</u>	<u>Annual Pension Cost (APC)</u>	<u>Actual Contribution Made</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
2009	\$ 243,149	243,149	100.00%	\$ -
2010	\$ 252,699	252,699	100.00%	\$ -
2011	\$ 242,960	242,960	100.00%	\$ -

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

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

	<u>2011</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Actuarial Valuation Date	12/31/2010 - Restructured	12/31/2010 - Prior to Restructuring	12/31/2009	12/31/2008
Actuarial Cost Method	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit
Amortization Method	Level % of Payroll	Level % of Payroll	Level % of Payroll	Level % of Payroll
Remaining Amortization Period	27.3 Years - Closed period	27.2 Years - Closed period	28.2 Years - Closed period	29 Years - Closed period
Asset Valuation Method	10-year Smoothed Market	10-year Smoothed Market	10-year Smoothed Market	Amortized cost
Investment Rate of Return	7.0%	7.5%	7.5%	7.5%
Projected Salary Increases	Varies by age and service	Varies by age and service	Varies by age and service	Varies by age and service
Includes Inflation at	3.00%	3.00%	3.00%	3.00%
Cost of Living Adjustments	2.1%	2.1%	2.1%	2.1%

Funded Status and Funding Progress

In June, 2011, SB 350 was enacted by Texas Legislature, resulting in a restructure of the TMRS funds. This legislation provided for the actuarial valuation to be completed, as if restructuring had occurred on December 31, 2010. In addition, the actuarial assumptions were updated for the new fund structure, based on an actuarial experience study that was adopted by the TMRS Board at their May, 2011 meeting (the review compared actual to expected experience for the four-year period of January 1, 2006 through December 31, 2009). For a complete description of the combined impact of legislation and new actuarial assumptions, including the effects on TMRS city rates and funding ratios, please see the December 31, 2010 TMRS Comprehensive Annual Financial Report (CAFR).

The funded status as of December 31, 2010, under the two separate valuations, is as follows:

	<u>2011</u>	<u>2011</u>
	12/31/2010 - Restructured	12/31/2010 - Prior to Restructuring
Actuarial Valuation Date		
Actuarial Value of Assets	\$ 2,913,782	\$ 2,312,659
Actuarial Accrued Liability	4,715,222	4,096,330
Percentage Funded	61.8%	56.5%
Unfunded Actuarial Accrued Liability (UAAL)	\$ 1,801,440	\$ 1,783,671
Annual Covered Payroll	\$ 2,315,948	\$ 2,315,948
UAAL as a Percentage of Covered Payroll	77.8%	77.0%

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

Actuarial calculations are based on the benefits provided under the terms of the substantive plan in effect at the time of each valuation, and reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets. The schedule of funding progress, presented as Required Supplementary Information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability benefits.

C. Other Post Employment Benefits

TMRS - Supplemental Death Benefit Fund

Plan Description

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

The death benefit for active employees provides a lump-sum payment approximately equal to the employee's annual salary (calculated based on the employee's actual earnings, for the 12-month period preceding the month of death); retired employees are insured for \$7,500; this coverage is an "other post employment benefit," or OPEB. The obligations of this plan are payable only from the SDBF and are not an obligation of, or a claim against, the Pension Trust Fund. For the year ended September 30, 2011, the City offered the supplemental death benefit to both active and retired employees.

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 employees' entire careers.

The City's contributions to the TMRS SDBF for the fiscal years ended 2011, 2010, and 2009 were \$233, \$227, and \$222, respectively. The City's contribution rates for the past three years are shown below:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Annual Req. Contrib. (Rate)	0.01%	0.01%	0.01%
Actual Contribution Made	0.01%	0.01%	0.01%
Percentage of ARC Contrib.	100.00%	100.00%	100.00%

CITY OF NASSAU BAY, TEXAS
NOTES TO FINANCIAL STATEMENTS (Continued)
For the Year Ended September 30, 2011

D. Deferred Compensation Plan

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

The City funds all amounts of compensation deferred under the Plan, at the direction of the covered employees, through investments administered by the International City Manager Association (ICMA) Retirement Corporation.

The City has no liability for losses under the plan but does have the duty of due care that would be required of an ordinary, prudent investor. The City contributed \$37,893 during the year for participating employees.

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REQUIRED SUPPLEMENTARY INFORMATION

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CITY OF NASSAU BAY, TEXAS
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE - BUDGET AND ACTUAL
GENERAL FUND

For the Year Ended September 30, 2011

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original Budget	Budget as Amended		
Revenues				
Property taxes	\$ 2,891,883	\$ 2,672,469	\$ 2,618,415	\$ (54,054)
Sales taxes	371,400	371,400	409,282	37,882
Other taxes	397,000	397,000	466,675	69,675
Licenses and permits	168,750	168,750	226,076	57,326
Fines and forfeitures	82,040	82,040	147,815	65,775
Charges for services	528,400	528,400	495,002	(33,398)
Investment income	1,550	1,550	3,756	2,206
Other revenues	35,700	35,700	84,277	48,577
Total Revenues	<u>4,476,723</u>	<u>4,257,309</u>	<u>4,451,298</u>	<u>193,989</u>
Expenditures				
Current:				
General government	1,045,251	1,045,251	886,194	159,057
Public safety	1,821,207	1,821,207	1,806,145	15,062
Public works	1,020,045	1,118,045	1,095,995	22,050
Public services	366,569	366,569	346,376	20,193
Total Expenditures	<u>4,253,072</u>	<u>4,351,072</u>	<u>4,134,710</u>	<u>216,362</u>
Revenues Over (Under) Expenditures	<u>223,651</u>	<u>(93,763)</u>	<u>316,588</u>	<u>410,351</u>
Other Financing				
Sources (Uses)				
Sale of capital assets	-	-	64,600	64,600
Transfer Out	(219,414)	-	-	-
Total Other Financing Sources (Uses)	<u>(219,414)</u>	<u>-</u>	<u>64,600</u>	<u>64,600</u>
Net Change in Fund Balance	<u>\$ 4,237</u>	<u>\$ (93,763)</u>	<u>381,188</u>	<u>\$ 474,951</u>
Beginning fund balance			<u>1,163,653</u>	
Ending Fund Balance			<u>\$ 1,544,841</u>	

Notes to Required Supplementary Information:

- Annual budgets are adopted on a basis consistent with generally accepted accounting principles (GAAP).

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CITY OF NASSAU BAY, TEXAS
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE - BUDGET AND ACTUAL
SPECIAL REVENUE AND GRANTS FUND
For the Year Ended September 30, 2011

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original Budget	Budget as Amended		
Revenues				
Intergovernmental	\$ 568,400	\$ 678,400	\$ 705,110	\$ 26,710
Investment earnings	-	-	200	200
Total Revenues	<u>568,400</u>	<u>678,400</u>	<u>705,310</u>	<u>26,910</u>
Expenditures				
Current:				
Public safety	578,060	688,060	560,872	127,188
Total Expenditures	<u>578,060</u>	<u>688,060</u>	<u>560,872</u>	<u>127,188</u>
Net Change in Fund Balance	<u>\$ (9,660)</u>	<u>\$ (9,660)</u>	144,438	<u>\$ 154,098</u>
Beginning fund balance			<u>159,465</u>	
		Ending Fund Balance	<u>\$ 303,903</u>	

Notes to Required Supplementary Information:

1. Annual budgets are adopted on a basis consistent with generally accepted accounting principles (GAAP).

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CITY OF NASSAU BAY, TEXAS

SCHEDULE OF FUNDING PROGRESS

TEXAS MUNICIPAL RETIREMENT SYSTEM

September 30, 2011

The City's annual covered payroll and pension costs are actuarially valued on a calendar year basis. Because the City makes all the annually required contributions, no net pension obligation (NPO) exists. The information presented below represents the City's Schedule of Funding Progress.

Fiscal Year	2011 (2)	2011 (1)	2010	2009
Actuarial Valuation Date	12/31/2010	12/31/2010	12/31/2009	12/31/2008
Actuarial Value of Assets	\$ 2,913,782	\$ 2,312,659	\$ 2,043,040	\$ 1,868,790
Actuarial Accrued Liability	\$ 4,715,222	\$ 4,096,330	\$ 3,739,953	\$ 3,414,592
Percentage Funded	61.8%	56.5%	54.6%	54.7%
Unfunded Actuarial				
Accrued Liability	\$ 1,801,440	\$ 1,783,671	\$ 1,696,913	\$ 1,545,802
Annual Covered Payroll	\$ 2,315,948	\$ 2,315,948	\$ 2,261,481	\$ 2,144,159
Unfunded Actuarial Accrued Liability				
(UAAL) % of Covered Payroll	77.8%	77.0%	75.0%	72.1%
Net Pension Obligation (NPO)				
at the Beginning of Period	\$ -	\$ -	\$ -	\$ -
Annual Req. Contrib. (ARC)	242,960	242,960	252,699	243,149
Contributions Made	242,960	242,960	252,699	243,149
NPO at the End of Period	\$ -	\$ -	\$ -	\$ -

(1) Actuarial valuation performed under the original fund structure

(2) Actuarial valuation performed under the new fund structure

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COMBINING STATEMENTS AND SCHEDULES

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CITY OF NASSAU BAY, TEXAS
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE - BUDGET AND ACTUAL
DEBT SERVICE FUND

For the Year Ended September 30, 2011

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original Budget	Budget as Amended		
Revenues				
Property taxes	\$ 185,680	\$ 171,795	\$ 166,347	\$ (5,448)
Intergovernmental	71,919	71,919	71,919	-
Investment earnings	330	330	358	28
Total Revenues	<u>257,929</u>	<u>244,044</u>	<u>238,624</u>	<u>(5,420)</u>
Expenditures				
Current:				
Principal	386,776	386,776	386,776	-
Interest and fiscal charges	86,082	86,832	86,819	13
Total Expenditures	<u>472,858</u>	<u>473,608</u>	<u>473,595</u>	<u>13</u>
Revenues Over (Under) Expenditures	<u>(214,929)</u>	<u>(229,564)</u>	<u>(234,971)</u>	<u>(5,407)</u>
Other Financing				
Sources (Uses)				
Transfers in	232,985	232,985	232,985	-
Transfers (out)	(13,885)	-	-	-
Total Other Financing Sources (Uses)	<u>219,100</u>	<u>232,985</u>	<u>232,985</u>	<u>-</u>
Net Change in Fund Balance	<u>\$ 4,171</u>	<u>\$ 3,421</u>	<u>(1,986)</u>	<u>\$ (5,407)</u>
Beginning fund balance			<u>195,952</u>	
		Ending Fund Balance	<u>\$ 193,966</u>	

CITY OF NASSAU BAY, TEXAS

COMBINING BALANCE SHEET

NONMAJOR GOVERNMENTAL FUNDS

September 30, 2011

	Special Revenue Funds			
	Tourism	Streets	TIRZ #1	RDA
<u>Assets</u>				
Cash	\$ 138,782	\$ 202,992	\$ -	\$ 295,701
Receivables, net	125,386	19,360	-	-
Total Assets	\$ 264,168	\$ 222,352	\$ -	\$ 295,701
<u>Liabilities</u>				
Accounts payable and accrued liabilities	\$ 11,701	\$ -	\$ -	\$ -
Total Liabilities	11,701	-	-	-
<u>Fund Balances</u>				
Restricted for:				
Enabling legislation	252,467	-	-	-
Capital projects	-	-	-	-
Special projects	-	222,352	-	295,701
Total Fund Balances	252,467	222,352	-	295,701
Total Liabilities and Fund Balances	\$ 264,168	\$ 222,352	\$ -	\$ 295,701

<u>Capital Projects</u>	<u>Total Nonmajor Governmental Funds</u>
\$ 5,506	\$ 642,981
<u>-</u>	<u>144,746</u>
<u>\$ 5,506</u>	<u>\$ 787,727</u>
<u>\$ -</u>	<u>\$ 11,701</u>
<u>-</u>	<u>11,701</u>
-	252,467
5,506	5,506
<u>-</u>	<u>518,053</u>
<u>5,506</u>	<u>776,026</u>
<u>\$ 5,506</u>	<u>\$ 787,727</u>

CITY OF NASSAU BAY, TEXAS
COMBINING STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES
NONMAJOR GOVERNMENTAL FUNDS
For the Year Ended September 30, 2011

	Special Revenue Funds			
	Tourism	Streets	TIRZ #1	RDA
Revenues				
Property taxes	\$ -	\$ -	\$ 227,888	\$ -
Sales taxes	-	101,432	-	-
Other taxes	474,112	-	-	-
Investment earnings	380	447	-	604
Total Revenues	<u>474,492</u>	<u>101,879</u>	<u>227,888</u>	<u>604</u>
Expenditures				
General government	-	-	-	92,782
Public works	-	34,309	-	-
Economic development/tourism	540,588	-	-	-
Capital outlay	-	-	-	-
Total Expenditures	<u>540,588</u>	<u>34,309</u>	<u>-</u>	<u>92,782</u>
Revenues Over (Under) Expenditures	<u>(66,096)</u>	<u>67,570</u>	<u>227,888</u>	<u>(92,178)</u>
Other Financing Sources (Uses)				
Transfers in	-	-	-	227,888
Transfers out	-	-	(227,888)	-
Total Other Financing Sources (Uses)	<u>-</u>	<u>-</u>	<u>(227,888)</u>	<u>227,888</u>
Net Change in Fund Balances	<u>(66,096)</u>	<u>67,570</u>	<u>-</u>	<u>135,710</u>
Beginning fund balances	318,563	154,782	-	159,991
Ending Fund Balances	<u>\$ 252,467</u>	<u>\$ 222,352</u>	<u>\$ -</u>	<u>\$ 295,701</u>

Capital Projects	Total Nonmajor Governmental Funds
\$ -	\$ 227,888
-	101,432
-	474,112
107	1,538
<u>107</u>	<u>804,970</u>
-	92,782
-	34,309
-	540,588
166,800	166,800
<u>166,800</u>	<u>834,479</u>
<u>(166,693)</u>	<u>(29,509)</u>
-	227,888
<u>-</u>	<u>(227,888)</u>
-	-
<u>(166,693)</u>	<u>(29,509)</u>
172,199	805,535
<u>\$ 5,506</u>	<u>\$ 776,026</u>

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CITY OF NASSAU BAY, TEXAS
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCE - BUDGET AND ACTUAL
NONMAJOR SPECIAL REVENUE FUNDS
For the Year Ended September 30, 2011

TOURISM FUND

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original Budget	Budget as Amended		
Revenues				
Other taxes	\$ 525,000	\$ 525,000	\$ 474,112	\$ (50,888)
Investment earnings	350	350	380	30
Total Revenues	<u>525,350</u>	<u>525,350</u>	<u>474,492</u>	<u>(50,858)</u>
Expenditures				
Current:				
Economic development/tourism	569,080	569,080	540,588	28,492
Total Expenditures	<u>569,080</u>	<u>569,080</u>	<u>540,588</u>	<u>28,492</u>
Net Change in Fund Balance	<u>\$ (43,730)</u>	<u>\$ (43,730)</u>	<u>(66,096)</u>	<u>\$ (22,366)</u>
Beginning fund balance			<u>318,563</u>	
Ending Fund Balance			<u>\$ 252,467</u>	

STREETS FUND

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original Budget	Budget as Amended		
Revenues				
Sales taxes	\$ 92,900	\$ 92,900	\$ 101,432	\$ 8,532
Investment earnings	500	500	447	(53)
Total Revenues	<u>93,400</u>	<u>93,400</u>	<u>101,879</u>	<u>8,479</u>
Expenditures				
Current:				
Public works	187,625	187,625	34,309	153,316
Total Expenditures	<u>187,625</u>	<u>187,625</u>	<u>34,309</u>	<u>153,316</u>
Net Change in Fund Balance	<u>\$ (94,225)</u>	<u>\$ (94,225)</u>	<u>67,570</u>	<u>\$ 161,795</u>
Beginning fund balance			<u>154,782</u>	
Ending Fund Balance			<u>\$ 222,352</u>	

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