

CITY OF MERKEL, TEXAS

**ANNUAL FINANCIAL REPORT
FOR THE YEAR ENDED SEPTEMBER 30, 2018**

CATHRINE WILKS CPA LLC

**CITY OF MERKEL, TEXAS
ANNUAL FINANCIAL REPORT
YEAR ENDED SEPTEMBER 30, 2018**

TABLE OF CONTENTS

	<u>PAGE</u>
<u>Financial Section</u>	
Independent Auditor's Report	1
Management's Discussion and Analysis	3
 Basic Financial Statements:	
Government-wide Financial Statements:	
Statement of Net Position	11
Statement of Activities	12
 Fund Financial Statements:	
Balance Sheet – Governmental Funds	14
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Assets	15
Statement of Revenues, Expenditures, and Changes in Fund Balances-Governmental Funds	16
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities	17
Statement of Revenues, Expenditures, and Changes in Fund Balances - Budget and Actual - General Fund	18
Statement of Net Position – Proprietary Fund	19
Statement of Revenues, Expenses, and Changes in Fund Net Position - Proprietary Fund	20
Statement of Cash Flows - Proprietary Fund	21
Notes to the Financial Statements	23
 Required Supplementary Information:	
Schedule of Changes in Net Pension Liability and Related Ratios-TMRS	45
Schedule of Contributions and Notes to Schedule of Contributions-TMRS	46
Schedule of Changes in Total OPEB Liability and Related Ratios – TMRS	47
 <u>Reports Related to Financial Statements Required by Government Auditing Standards</u>	
Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	51
Schedule of Findings and Responses	53
Summary Schedule of Prior Audit Findings	54

INDEPENDENT AUDITOR'S REPORT

Honorable Mayor and
Members of the City Council
Merkel, Texas 79536

Report on the Financial Statements

I have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, and the aggregate remaining funds of the City of Merkel, Texas, ("City") as of and for the year ended September 30, 2018, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

My responsibility is to express opinions on these financial statements based on our audit. I conducted the 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 I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinions

In my 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 aggregate discretely presented component units, and the aggregate remaining funds of the City of Merkel, Texas, as of September 30, 2018, and the respective changes in financial position, and, where applicable, cash flows, and the respective budgetary comparison for the general fund for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the schedule of changes in net pension liability and related ratios, and the schedule of contributions and notes to schedule of contributions be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental

Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. I 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 I obtained during our audit of the basic financial statements. I do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, I have also issued our report dated December 19, 2018, on our consideration of the City of Merkel'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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.

Cathrine Wilke CPA LLC

Sweetwater, Texas

December 19, 2018

CITY OF MERKEL, TEXAS

Management's Discussion and Analysis September 30, 2018

This section of the City of Merkel's annual financial report presents our discussion and analysis of the City's financial performance during the fiscal year ended September 30, 2018. Please read it in conjunction with the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The primary government's combined net position was \$3.6 million as of September 30, 2018.
- During the year, the primary government's combined net position decreased \$86,025 from the previous year.
- The general fund reported a fund balance this year of a little over 1.5 million at year end. Of this amount, \$434,200 is available for spending at the government's discretion (unassigned fund balance).

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of two parts—*management's discussion and analysis* (this section), and the *basic financial statements*. The basic financial statements include two kinds of statements that present different views of the City:

- The first two statements are *government-wide financial statements* that provide both *long-term* and *short-term* information about the City's overall financial status.
- The remaining statements are *fund financial statements* that focus on *individual parts* of the government, reporting the City's operations in more detail than the government-wide statements.
- The *governmental funds statements* tell how *general government* services were financed in the *short term* as well as what remains for future spending.
- *Proprietary fund statements* offer *short- and long-term* financial information about the activities the government operates *like businesses*.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data.

Government-wide Statements

The government-wide statements report information about the City as a whole using accounting methods similar to those used by private-sector companies. The statement of net position includes all of the government's assets, deferred inflows of resources, and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the City's net position and how they have changed. Net position—the difference between the City's assets and liabilities—are one way to measure the City's financial health or *position*.

- Over time, increases or decreases in the City's net position are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the City, one needs to consider additional non-financial factors such as changes in the City's tax base.

The government-wide financial statements of the City include the *Governmental activities*. Most of the City's basic services are included here, such as general government, public safety, highways and streets, sanitation, economic development, culture and recreation, and interest on long-term debt. Property taxes and grants finance most of these activities.

Fund Financial Statements

The fund financial statements provide more detailed information about the City's most significant *funds*—not the City as a whole.

CITY OF MERKEL, TEXAS

Management's Discussion and Analysis September 30, 2018

Funds are accounting devices that the City uses to keep track of specific sources of funding and spending for particular purposes.

- Some funds are required by State law and by bond covenants.
- City Administration establishes other funds to control and manage money for particular purposes or to show that it is properly using certain taxes and grants.

The City has the following kinds of funds:

- *Governmental funds*—Most of the City's basic services are included in governmental funds, which focus on (1) how *cash and other financial assets* can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental fund statements provide a detailed *short-term* view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds statement, or on the subsequent page, that explain the relationship (or differences) between them.
- *Proprietary funds*—Services for which the City charges customers a fee are generally reported in proprietary funds. Proprietary funds, like the government-wide statements, provide both long-term and short-term financial information.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

The City's combined net position was nearly \$3.6 million at September 30, 2018. The components of the City's net position are shown in the table below. The \$1.6 million of unrestricted net position represents resources available to fund the programs of the City next year. This represents 44% of the total net position of the City.

Statement of Net position

	Governmental Activities		Business-type Activities		Total	
	2018	2017	2018	2017	2018	2017
Current & other assets	\$1,650,335	\$1,846,338	\$ 979,619	\$ 900,873	\$2,629,954	\$2,747,211
Capital assets	1,773,427	1,812,408	6,500,397	6,689,355	8,273,824	8,501,763
Total assets	<u>3,423,762</u>	<u>3,658,746</u>	<u>7,480,016</u>	<u>7,590,227</u>	<u>10,903,778</u>	<u>11,248,974</u>
Deferred outflows	42,172	69,602	20,126	35,143	62,298	104,745
Current liabilities	12,904	39,369	108,241	87,880	121,145	127,249
Long-term liabilities	1,746,377	1,996,269	5,239,482	5,473,114	6,985,859	7,469,383
Total Liabilities	<u>1,759,281</u>	<u>2,035,638</u>	<u>5,347,724</u>	<u>5,560,994</u>	<u>7,107,005</u>	<u>7,596,632</u>
Deferred pension inflow	142,993	-	71,839	-	214,832	-
Net position:						
Net investment in						
Capital assets	258,743	275,639	1,389,566	1,437,682	1,648,309	1,713,321
Restricted	190,802	123,591	196,436	189,907	387,239	313,498
Unrestricted	1,114,115	1,293,480	494,577	436,787	1,608,692	1,730,267
Total Net position	<u>\$1,563,660</u>	<u>\$1,692,710</u>	<u>\$2,080,579</u>	<u>\$2,064,376</u>	<u>\$3,644,239</u>	<u>\$3,757,086</u>

As the above table shows, current and other assets decreased \$117,257, and net capital assets decreased by \$227,939. The details of capital asset additions are discussed in more detail in the notes to the financial statements. Depreciation expense for the primary government for the year was \$411,804.

CITY OF MERKEL, TEXAS

Management's Discussion and Analysis September 30, 2018

Deferred pension outflows decreased \$42,447 and deferred pension inflows increased \$214,832, both related to TMRS participation changes for the year.

The City had a decrease in current liabilities in the amount of \$6,104 which was nearly entirely from a decrease in accounts payable. The City had \$34,926 in current year long-term debt additions and \$545,273 in long-term debt reductions. All debt is current, and all debt covenants have been complied with. Details of the City's debt can be found on pages 31 through 34 in the notes to the financial statements.

Statement of Activities

	Governmental Activities		Business-type Activities		Total	
	2018	2017	2018	2017	2018	2017
Program Revenues:						
Charges for services	\$ 59,502	\$ 96,995	\$1,693,207	\$1,677,934	\$1,752,709	\$1,774,929
Operating grants, contributions	2,139	36,578	-	-	2,139	36,578
Capital grants, contributions	46,163	-	-	-	46,163	-
General Revenues:						
Taxes	1,013,992	969,367	-	-	1,013,992	969,367
Other	60,905	31,889	4,298	3,268	65,203	35,157
Total Revenues	<u>1,182,701</u>	<u>1,134,829</u>	<u>1,697,505</u>	<u>1,681,202</u>	<u>2,880,206</u>	<u>2,816,031</u>
Program Expenses						
General government	146,694	210,091	-	-	146,694	210,091
Public safety	680,803	647,988	-	-	680,803	647,988
Streets	328,186	197,509	-	-	328,186	197,509
Culture and recreation	74,650	90,759	-	-	74,650	90,759
Interest on long-term debt	63,563	66,586	-	-	63,563	66,586
Water and sewer	-	-	1,419,507	1,439,268	1,419,507	1,439,268
Sanitation	-	-	252,826	250,659	252,826	250,659
Total Program Expenses	<u>1,293,896</u>	<u>1,212,934</u>	<u>1,672,333</u>	<u>1,689,927</u>	<u>2,966,229</u>	<u>2,902,861</u>
Increase (decrease) in net position	(111,196)	(78,103)	25,171	(8,725)	(86,025)	(86,828)
Beginning net position	1,692,710	1,770,813	2,064,377	2,073,101	3,757,086	3,843,914
Prior period adjustment	(17,853)	-	(8,969)	-	(26,822)	-
Ending net position	<u>\$1,563,660</u>	<u>\$1,692,710</u>	<u>\$2,080,579</u>	<u>\$2,064,377</u>	<u>\$3,644,239</u>	<u>\$3,757,086</u>

Total revenues increased from \$2,816,031 to \$2,880,206. This is a 2% increase. As indicated in the table above, the main increase is in capital grants and contributions. In fiscal year 2018 the City received a capital contribution from the volunteer fire department for improvements to a firetruck. The total program expenses increased \$63,368. The main increase was in the street department. The City had a street repair project in fiscal year 2018. The net position of the City decreased by \$86,025. At the end of the current fiscal year, the City of Merkel is able to report positive balances in all three categories of net position, both for the government as a whole, as well as for its separate governmental and business-type activities. The same situation held true for the prior fiscal year.

CITY OF MERKEL, TEXAS

Management's Discussion and Analysis September 30, 2018

FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

Governmental Activities

The focus of the City's general fund is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the City's financing requirements. In particular, *unreserved fund balance* may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. The general fund has several categories of restricted and assigned fund balances as seen on page 27. The unassigned fund balance in the general fund of \$434,200 represents approximately 4 months of operating costs.

The City's total general fund revenues were up \$2,662 from the previous year. Intergovernmental decreased due to the loss of dispatch revenue. Sales tax revenue increased \$37,542. Other revenue increased due to an easement payment from AEP. A significant portion, 87%, of the City's revenue comes from taxes that include property, sales, franchise taxes, and other taxes.

The total cost of all governmental activities program expenses was \$1,293,896 as seen on page 5. This amounts to an increase of \$80,962, which is mainly concentrated in the street department. The street department had higher paving costs in fiscal year September 30, 2018.

Business-type Activities

The City's business-type revenues increased from \$1,681,202 to \$1,697,505. This increase is mainly attributable to an increase in charges for services. Costs of business-type activities decreased \$17,594. There were no significant changes in rates or expenses in the business-type fund this past year.

General Fund Budgetary Highlights

The City had no budget amendments during the year as discussed on page 25 of the notes. Actual general fund expenditures were \$30,042 over budgeted amounts. The most significant negative variances resulted from unbudgeted ambulance department expenditures. These were due to a complete write-off of accounts receivable due to the dissolution of the ambulance service provided by the City volunteers. The police department had additional payroll and capital outlay costs were higher than originally planned. Revenues were \$38,831 more than budgeted. Nearly all revenue sources were more than budgeted amounts. The net result was a negative budget variance of \$23,612 in the net change in fund balance of the general fund.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of fiscal year 2018, the City had invested nearly \$14 million in a broad range of capital assets including land, equipment, buildings, and vehicles. The City purchased various pieces of equipment during the year. More details on capital assets are in the notes to the financial statements. The Merkel Economic Development Corporation and the Merkel Volunteer Fire Department (discretely presented component units) capital asset information is presented in the notes as well.

CITY OF MERKEL, TEXAS

Management's Discussion and Analysis September 30, 2018

Capital Assets

	Governmental Activities		Business-type Activities		Total	
	2018	2017	2018	2017	2018	2017
Land	\$ 12,500	\$ 12,500	\$ 72,080	\$ 72,080	\$ 84,580	\$ 84,580
Construction in-progress	-	-	-	-	-	-
Buildings	141,968	141,968	1,975	1,975	143,943	143,943
Water system	-	-	9,380,968	9,380,968	9,380,968	9,380,968
Infrastructure	1,912,060	1,912,060	-	-	1,912,060	1,912,060
Machinery and equipment	1,170,749	1,079,556	340,454	323,704	1,511,203	1,403,260
Vehicles	1,136,322	1,082,159	55,311	39,325	1,191,633	1,121,484
Total at historical cost	<u>4,373,599</u>	<u>4,228,242</u>	<u>9,850,788</u>	<u>9,818,051</u>	<u>14,224,387</u>	<u>14,046,293</u>
Total accumulated Depreciation	<u>(2,600,172)</u>	<u>(2,415,834)</u>	<u>(3,350,391)</u>	<u>(3,128,696)</u>	<u>(5,950,563)</u>	<u>(5,544,530)</u>
Net capital assets	<u>\$ 1,773,427</u>	<u>\$ 1,812,408</u>	<u>\$ 6,500,397</u>	<u>\$ 6,689,355</u>	<u>\$ 8,273,824</u>	<u>\$ 8,501,763</u>

Long-Term Debt

At year-end the City had a little over \$7.6 million in outstanding debt as shown in the following table. More detailed information about the City's debt is presented in the notes to the financial statements. The beginning net OPEB liability has been restated after the enactment of GASB 75.

City's Long-Term Debt

	Governmental Activities		Business-type Activities		Total	
	2018	2017	2018	2017	2018	2017
Notes	\$ 156,578	\$ 214,100	\$ 227,830	\$ 260,033	\$ 384,408	\$ 474,133
Capital leases	50,608	25,169	-	17,640	50,608	42,809
Certificate of obligation	1,375,000	1,395,000	4,883,000	4,974,000	6,258,000	6,369,000
Compensated absences	12,177	16,618	8,812	4,452	20,989	21,070
Net Pension liability	130,975	345,382	109,271	216,990	240,246	562,372
Net OPEB liability	21,039	17,853	10,569	8,969	31,608	26,822
Total Long-Term Debt	<u>\$1,746,377</u>	<u>\$2,014,122</u>	<u>\$5,239,482</u>	<u>\$5,482,084</u>	<u>\$6,985,859</u>	<u>\$7,496,206</u>

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City's budgetary general fund will not change significantly next year. Ad valorem tax rate will decrease from .7014 to .6500. There were no major changes in the number of city employees expected. Ambulance department will no longer be needed. Services will be provided by Taylor County EMS. The street department intends to add a new employee. Merit raises were budgeted as well.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the City's Administrative Office at (325) 928-4911 or by mail at 100 Kent Street, Merkel, Texas 79536.

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Government-wide Financial Statements

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CITY OF MERKEL, TEXAS

Statement of Net Position September 30, 2018

	Primary Government			Component Units
	Governmental Activities	Business-type Activities	Total	
Assets				
Current cash and cash equivalents	\$ 1,199,685	\$ 714,872	\$ 1,914,557	\$ 19,600
Investments	23,696	-	23,696	144,524
Receivables (net of allowance for uncollectibles)	96,280	167,670	263,950	15,425
Inventory	-	28,311	28,311	-
Internal balances	127,669	(127,669)	-	-
Cash - temporarily restricted	138,004	196,436	334,440	541,554
Note receivable	65,000	-	65,000	209,900
Capital assets (net of accumulated depreciation):				
Land	12,500	72,080	84,580	-
Construction in-progress	-	-	-	-
Buildings and improvements	34,152	-	34,152	-
Utility system	-	6,326,726	6,326,726	-
Machinery and equipment	148,399	86,138	234,537	51,019
Furniture and fixtures	595	-	595	-
Vehicles	233,800	15,453	249,253	-
Infrastructure	1,343,981	-	1,343,981	-
Total assets	3,423,762	7,480,016	10,903,778	982,022
Deferred Outflows of Resources				
Deferred pension outflow	40,582	19,327	59,909	-
Deferred OPEB outflow	1,590	799	2,389	-
Total deferred outflows of resources	42,172	20,126	62,298	-
Liabilities				
Accounts payable	7,475	64,131	71,606	-
Customer deposits	-	26,161	26,161	-
Accrued liabilities	5,429	17,949	23,378	-
Short-term note payable	-	-	-	-
Long-term Liabilities:				
Due Within one year	97,959	125,406	223,365	-
Due in More than one year	1,648,418	5,114,076	6,762,494	-
Total liabilities	1,759,281	5,347,724	7,107,005	-
Deferred Inflows of Resources				
Deferred pension inflow	142,993	71,839	214,832	-
Total deferred inflows of resources	142,993	71,839	214,832	-
Net Position				
Net Investment in Capital Assets	258,743	1,389,566	1,648,309	51,019
Restricted for Debt service	25,504	196,436	221,940	-
Restricted for Public safety	73,842	-	73,842	-
Restricted for Tourism development	75,164	-	75,164	-
Restricted for Court Technology and Security	16,293	-	16,293	-
Restricted for Streets	-	-	-	-
Restricted for Economic development	-	-	-	819,652
Unrestricted	1,114,115	494,577	1,608,692	111,351
Total Net Position	\$ 1,563,660	\$ 2,080,579	\$ 3,644,239	\$ 982,022

The notes to the financial statements are an integral part of this statement.

CITY OF MERKEL, TEXAS

Statement of Activities
For the Year Ended September 30, 2018

Function/Program Activities	Net (Expenses) Revenues and Changes in Net Position						Component Units
	Program Revenues			Primary Government			
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	
Primary Government Activities:							
Governmental Activities:							
General government	\$ 146,694	\$ 5,545	\$ -	\$ -	\$ (141,149)	\$ -	\$ (141,149)
Public safety	680,803	49,899	1,839	46,163	(582,902)	-	(582,902)
Streets	328,186	-	-	-	(328,186)	-	(328,186)
Culture and recreation	74,650	4,058	300	-	(70,292)	-	(70,292)
Interest on long-term debt	63,563	-	-	-	(63,563)	-	(63,563)
Total governmental activities	1,293,896	59,502	2,139	46,163	(1,186,092)	-	(1,186,092)
Business-type Activities:							
Water and sewer	1,419,507	1,375,087	-	-	-	(44,420)	(44,420)
Sanitation	252,826	318,120	-	-	-	65,294	65,294
Total business-type activities	1,672,333	1,693,207	-	-	-	20,874	20,874
Total Primary Government	\$ 2,966,229	\$ 1,752,709	\$ 2,139	\$ 46,163	\$ (1,186,092)	\$ 20,874	\$ (1,165,218)
Component Units:							
Volunteer Fire Department	122,765	-	58,848	-	-	-	(63,917)
Merkel Economic Development Corporation	8,233	-	-	-	-	-	(8,233)
Total Component Units	\$ 130,998	\$ -	\$ 58,848	\$ -	\$ -	\$ -	\$ (72,150)
General revenues:							
Taxes:							
Property taxes, levied for general purposes					591,379	-	591,379
Sales tax					354,356	-	354,356
Occupancy					9,858	-	9,858
Franchise tax					58,399	-	58,399
Investment earnings					3,774	4,298	8,072
Gain on sale of capital assets					-	-	-
Other					57,131	-	57,131
Total general revenues					1,074,897	4,298	1,079,195
Change in net position					(111,196)	25,171	(86,025)
Net Position - beginning					1,692,710	2,064,377	3,757,086
Prior Period Adjustment					(17,853)	(8,969)	(26,822)
Net Position - ending					\$ 1,563,660	\$ 2,080,579	\$ 3,644,239

The notes to the financial statements are an integral part of this statement.

Fund Financial Statements

CITY OF MERKEL, TEXAS

Balance Sheet Governmental Funds September 30, 2018

	General	Other Governmental Funds	Total Governmental Funds
Assets			
Current cash and cash equivalents	\$ 1,158,885	\$ 40,799	\$ 1,199,684
Investments	11,311	12,384	23,695
Receivables, net of allowance for uncollectibles	96,280	-	96,280
Due from other funds	127,669	-	127,669
Cash - restricted	138,004	-	138,004
	<u>1,532,150</u>	<u>53,183</u>	<u>1,585,333</u>
Total Assets	<u>\$ 1,532,150</u>	<u>\$ 53,183</u>	<u>\$ 1,585,333</u>
Liabilities			
Accounts payable	7,091	384	7,475
Total Liabilities	<u>7,091</u>	<u>384</u>	<u>7,475</u>
Deferred inflows of Resources			
Unavailable revenue - property taxes	48,649	-	48,649
Total Deferred Inflows of Resources	<u>48,649</u>	<u>-</u>	<u>48,649</u>
Fund Balances:			
Restricted	138,004	52,799	190,803
Assigned	904,207	-	904,207
Unassigned	434,200	-	434,200
Total fund balances	<u>1,476,410</u>	<u>52,799</u>	<u>1,529,209</u>
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	<u>\$ 1,532,150</u>	<u>\$ 53,183</u>	<u>\$ 1,585,333</u>

The notes to the financial statements are an integral part of this statement.

CITY OF MERKEL, TEXAS

Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Position September 30, 2018

Total Fund Balances - Governmental Funds	\$ 1,529,209
Capital assets, receivables and deferred outflows used in governmental activities are not financial resources and therefore are not reported in governmental funds. At the beginning of the year, the cost of these assets was \$4,228,243 and accumulated depreciation was \$2,415,835. In addition, long-term liabilities are not due and payable in the current period, and therefore are not reported as liabilities in the funds. At the beginning of the year, this balance was \$2,001,698. Also added are notes receivable and deferred outflows of resources. The net effect of including the beginning balances for capital assets (net of depreciation) and long-term debt in the governmental activities is to increase (decrease) net assets.	(24,688)
Current year capital outlays of \$152,862, including donated assets, and long-term debt reductions and increases of \$56,524 net, are expenditures in the fund financial statements, but they should be shown as increases in capital assets and reductions/additions in long-term debt in the government-wide financial statements along with changes in other liabilities. The net effect of including these changes is to increase (decrease) net assets.	207,649
Included in the items related to debt is the recognition of the City's proportionate share of the net pension liability required by GASB 68 and 75 in the amount of \$193,368, a deferred resource outflow related to pensions in the amount of \$50,673, and a deferred resource inflow related to pensions in the amount of \$119,750. This amounted to a change in Net Position in the amount of \$22,945.	22,945
The current year depreciation expense increases accumulated depreciation. The net effect of the current year's depreciation is to decrease net assets.	(190,104)
Various other reclassifications and eliminations are necessary to convert from the modified accrual basis of accounting to accrual basis accounting. These include recognizing deferred revenue as revenue, and eliminating interfund transactions. The net effect of these reclassifications and recognitions is to increase (decrease) net assets.	18,649
Net Position of Governmental Activities	<u>\$ 1,563,660</u>

The notes to the financial statements are an integral part of this statement.

CITY OF MERKEL, TEXAS

Statement of Revenues, Expenditures, and Changes in Fund Balances Governmental Funds For the Year Ended September 30, 2018

	General	Other Governmental Funds	Total Governmental Funds
Revenues			
Taxes:			
Property	\$ 586,197	\$ -	\$ 586,197
Sales	354,356	-	354,356
Occupancy	9,858	-	9,858
Franchise Fees	58,399	-	58,399
Licenses and permits	5,100	-	5,100
Charges for services	2,793	681	3,474
Fines	47,173	-	47,173
Contributions and donations	300	-	300
Intergovernmental	1,839	-	1,839
Rents and royalties	3,755	-	3,755
Investment earnings	3,548	225	3,773
Other	88,867	-	88,867
Total revenues	<u>1,162,186</u>	<u>906</u>	<u>1,163,092</u>
Expenditures			
Current:			
General government	149,166	-	149,166
Public safety	561,873	575	562,448
Streets	263,529	-	263,529
Culture and recreation	70,531	-	70,531
Debt Service:			
Principal	77,863	-	77,863
Interest	63,563	-	63,563
Capital outlay:			
Public safety	56,144	-	56,144
Streets	11,100	-	11,100
Culture and recreation	13,675	-	13,675
Total expenditures	<u>1,267,444</u>	<u>575</u>	<u>1,268,019</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(105,259)</u>	<u>331</u>	<u>(104,928)</u>
Other financing sources (uses)			
Debt Advances	<u>-</u>	<u>-</u>	<u>-</u>
Total other financing sources and uses	<u>-</u>	<u>-</u>	<u>-</u>
Net change in fund balances	<u>(105,259)</u>	<u>331</u>	<u>(104,928)</u>
Fund balances - beginning	1,581,669	52,468	1,634,137
Fund balances - ending	<u>\$ 1,476,410</u>	<u>\$ 52,799</u>	<u>\$ 1,529,209</u>

The notes to the financial statements are an integral part of this statement.

CITY OF MERKEL, 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, 2018

Amounts reported for governmental activities in the statement of activities (page 12) are different because:

Net change in fund balances - total governmental funds (page 16)	\$ (104,928)
--	--------------

Current year capital outlays of \$106,699 plus donated assets of \$46,163 and long-term debt changes of \$56,524 are expenditures in the fund financial statements, but they should be shown as increases in capital assets and reductions/additions in long-term debt in the government-wide financial statements along with changes in other liabilities. The net effect of including these changes is to increase (decrease) net assets.

	207,649
--	---------

Included in the items related to debt is the recognition of the City's proportionate share of the net pension and OPEB expenses required by GASB 68 and 75

	40,798
--	--------

The current year depreciation expense increases accumulated depreciation. The net effect of the current year's depreciation is to decrease net assets.

	(190,104)
--	-----------

Reclassification entries to convert modified accrual basis of accounting to accrual basis of accounting. These include recognizing deferred revenue as revenue, and adjusting current year revenue to show revenue earned from the current year's tax levy, as well as revenue earned on a current year contract yet not available in the current year.

	<u>(64,612)</u>
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Change in net position of governmental activities (page 12)

	<u><u>\$ (111,196)</u></u>
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CITY OF MERKEL, TEXAS

General Fund

Statement of Revenues, Expenditures, and Changes in Fund Balances - Budget and Actual For the Year Ended September 30, 2018

	Budgeted Amounts		Actual Amounts	Variance with Final budget- Positive (Negative)
	Original	Final		
Revenues				
Taxes:				
Property	\$ 563,441	\$ 563,441	\$ 586,197	\$ 22,756
Sales	306,750	306,750	354,356	47,606
Occupancy	5,600	5,600	9,858	4,258
Franchise tax	60,000	60,000	58,399	(1,601)
Licenses and permits	6,000	6,000	5,100	(900)
Charges for services	21,200	21,200	2,793	(18,407)
Fines	62,000	62,000	47,173	(14,827)
Contributions and donations	850	850	300	(550)
Intergovernmental	33,063	33,063	1,839	(31,224)
Rents and royalties	3,650	3,650	3,755	105
Investment earnings	3,500	3,500	3,548	48
Other	57,300	57,300	88,867	31,567
Total revenues	<u>1,123,355</u>	<u>1,123,355</u>	<u>1,162,186</u>	<u>38,831</u>
Expenditures				
Current:				
General government	212,099	212,099	149,166	62,933
Public safety:				
Ambulance	23,000	23,000	83,025	(60,025)
Fire department	29,112	29,112	41,579	(12,468)
Police department	411,384	411,384	437,772	(26,388)
Municipal Court	49,357	49,357	55,640	(6,283)
Streets	301,057	301,057	277,204	23,852
Culture and Recreation:				
Heritage Hall	21,272	21,272	38,151	(16,879)
Library	29,335	29,335	30,683	(1,348)
Parks	18,916	18,916	12,796	6,120
Debt Service:				
Principal	78,100	78,100	77,863	237
Interest	63,770	63,770	63,563	207
Total expenditures	<u>1,237,402</u>	<u>1,237,402</u>	<u>1,267,444</u>	<u>(30,042)</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(114,047)</u>	<u>(114,047)</u>	<u>(105,259)</u>	<u>8,788</u>
Other financing sources (uses)				
Transfer in	-	-	-	-
Debt Advances	32,400	32,400	-	(32,400)
Total other financing sources and uses	<u>32,400</u>	<u>32,400</u>	<u>-</u>	<u>(32,400)</u>
Net change in fund balances	<u>(81,647)</u>	<u>(81,647)</u>	<u>(105,259)</u>	<u>(23,612)</u>
Fund balances - beginning	1,581,669	1,581,669	1,581,669	-
Fund balances - ending	<u>\$ 1,500,022</u>	<u>\$ 1,500,022</u>	<u>\$ 1,476,410</u>	<u>\$ (23,612)</u>

The notes to the financial statements are an integral part of this statement.

CITY OF MERKEL, TEXAS

Statement of Net Position Proprietary Funds September 30, 2018

	Business-type Activities- Enterprise Fund
Assets	
Current assets:	
Cash and cash equivalents	\$ 714,872
Restricted cash	196,436
Accounts receivable (net of allowance for uncollectibles)	167,670
Inventory	28,311
Total current assets	<u>1,107,288</u>
Capital assets:	
Land	72,080
Construction in-progress	-
Buildings	1,975
Machinery and equipment	340,454
Vehicles	55,311
Utility system	9,380,968
Less accumulated depreciation	<u>(3,350,391)</u>
Total capital assets (net of accumulated depreciation)	<u>6,500,397</u>
Total assets	<u>7,607,685</u>
Deferred Outflows of Resources	
Deferred pension outflow	19,327
Deferred OPEB outflow	799
Total deferred outflows of resources	<u>20,126</u>
Liabilities	
Current Liabilities:	
Accounts payable	64,131
Due to other funds	127,669
Accrued expenses	17,949
Customer deposits	26,161
Compensated absences	2,203
Note payable	32,203
Certificates of obligation	91,000
Total current liabilities	<u>361,316</u>
Noncurrent liabilities:	
Compensated absences	6,609
Net pension liability	109,271
Net OPEB liability	10,569
Note payable	195,628
Certificates of obligation	4,792,000
Total noncurrent liabilities	<u>5,114,077</u>
Total liabilities	<u>5,475,393</u>
Deferred Inflow of Resources	
Deferred pension inflow	71,839
Total deferred inflows of resources	<u>71,839</u>
Net Position	
Net investment in capital assets	1,389,566
Restricted for debt service (expendable)	196,436
Unrestricted	494,577
Total net position	<u>\$ 2,080,579</u>

The notes to the financial statements are an integral part of this statement.

CITY OF MERKEL, TEXAS

Statement of Revenues, Expenses, and Changes in Fund Net Position Proprietary Funds For the Year Ended September 30, 2018

	Business-type Activities- Enterprise Fund
Operating revenues:	
Charges for sales and services:	
Water	\$ 1,020,248
Sewer	343,785
Sanitation	318,120
Other operating revenue	11,054
Total operating revenue	<u>1,693,207</u>
Operating expenses:	
Personal services	249,733
Maintenance and supplies	130,524
Other services and charges	820,668
Depreciation	221,700
Total operating expenses	<u>1,422,625</u>
Operating income (loss)	<u>270,582</u>
Nonoperating revenues (expenses):	
Interest income	4,298
Interest expense	<u>(249,709)</u>
Total nonoperating revenue (expense)	<u>(245,411)</u>
Change in net position	25,171
Total net position - beginning	2,064,377
Prior period adjustment	(8,969)
Total net position - ending	<u><u>\$ 2,080,579</u></u>

The notes to the financial statements are an integral part of this statement.

CITY OF MERKEL, TEXAS

Statement of Cash Flows Proprietary Funds For the Year Ended September 30, 2018

	Business-type Activities- Enterprise Fund
Cash Flows From Operating Activities	
Receipts from customers and users	\$ 1,676,013
Payments to suppliers	957,865
Payments to employees	264,634
Net cash provided by operating activities	<u>453,514</u>
Cash Flows From Capital and Related Financing Activities	
Acquisition and construction of capital assets	(32,740)
Principal paid on debt	(140,843)
Interest paid on debt	(249,709)
Net cash provided (used) by capital and related financing activities	<u>(423,292)</u>
Cash Flows From Investing Activities	
Interest and dividends received	4,298
Net cash provided (used) by investing activities	<u>4,298</u>
Net increase in cash and cash equivalents	34,519
Cash and cash equivalents at beginning of year	876,789
Cash and cash equivalents at end of year	<u>\$ 911,308</u>
As reported on the balance sheet:	
Cash and cash equivalents	714,872
Restricted cash	196,436
Total cash and equivalents at end of year	<u>\$ 911,308</u>
Reconciliation of operating income to net cash provided (used) by operating activities:	
Operating income (loss)	<u>270,582</u>
Adjustments to reconcile operating income to net cash provided (used) by operating activities:	
Depreciation expense	221,700
(Increase) decrease in accounts receivable	(10,228)
(Increase) decrease in inventory	(28,311)
(Increase) decrease in deferred outflows of resources	15,017
Increase (decrease) in accounts payable	27,327
Increase (decrease) in due to other funds	(5,689)
Increase (decrease) in customer deposits	(6,966)
Increase (decrease) in compensated absences	4,360
Increase (decrease) in net pension and OPEB liability	(106,117)
Increase (decrease) in deferred inflows of resources	71,839
Total adjustments	<u>182,932</u>
Net cash provided by operating activities	<u>\$ 453,514</u>

The notes to the financial statements are an integral part of this statement.

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CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

(1) Summary of Significant Accounting Policies

A. General Statement

The City of Merkel, Texas, is a Type A General Law City with a council-manager form of government and provides the following services: Police and Fire, Streets, Sanitation, Water, Sewer, Social Services, Recreation, Public Improvements, and General Administrative Services.

B. Financial Reporting Entity

The governmental reporting entity consists of the City (Primary Government) and its component units. Component units are legally separate organizations for which the Board is financially accountable or other organizations whose nature and significant relationship with the City are such that exclusion would cause the City's financial statements to be misleading. Financial accountability is defined as the appointment of a voting majority of the component unit's board, and (i) either the City's ability to impose its will on the organization or (ii) there is potential for the organization to provide a financial benefit to or impose a financial burden on the City. Organizations for which the City is not financially accountable are also included when doing so is necessary in order to prevent the City's financial statements from being misleading.

The basic financial statements include both blended and discretely presented component units. The blended component unit, although a legally separate entity is, in substance, part of the City's operations and so data from this unit is combined with data of the primary government. The discretely presented component units, on the other hand, are reported in a separate column in the government-wide financial statements to emphasize they are legally separate from the government.

Discretely presented component units.

Based on these criteria, Merkel Economic Development Corporation is reported as a discretely presented component unit of the City. The corporation is fiscally dependent upon the City and the City is able to impose its will on the organization. The EDC does not have separately issued financial statements.

The Merkel Volunteer Fire Department is reported as a discretely presented component unit of the City. They are fiscally dependent on the City and a financial benefit exists. The Volunteer Firemen provide services to the City as well as the surrounding area. They do not prepare separate financial statements.

Blended component unit.

The Emergency Medical Services, Inc. is reported as a blended component unit of the City. They are fiscally dependent upon the City, the City is able to impose its will on the organization, and they are nearly exclusively funded by the City. Exclusion of the organization would result in misleading or incomplete financial statements. The funds of the Emergency Medical Services, Inc. have been included in the Governmental Activities in the financial statements. They do not prepare separate financial statements.

Resource flows(except those affecting the statement of net assets/balance sheet only) between a primary government and its discretely presented component unit are reported as external transactions – that is, as revenues and expenses. Resource flows between the primary government and blended component units are classified as interfund transactions in the financial statements. Neither of these entities issue separate financial statements.

C. Government-wide and Fund Financial Statements

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

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

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

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

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

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

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

Property taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Only the portion of special assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The government reports the following major governmental fund:

The *general fund* is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The government reports the following major proprietary fund:

The *water, sewer and sanitation fund* accounts for the activities of the City. The City of Merkel supplies water to city residents, disposal of wastewater is primarily limited to the citizens of Merkel. The City also provides for solid waste collection and disposal within the City.

The City has one non-major governmental fund. The Emergency Medical Services is a blended component unit; therefore, it is a special revenue fund.

As a rule, the effect of interfund activity has been eliminated from the government-wide financial statements.

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

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City enterprise fund and the government's internal service funds are charges to customers for sales and services. The City also recognizes as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the system. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

E. Budgetary Control

The departments submit to the City Manager a budget of estimated expenditures for the ensuing fiscal year after which the City Manager subsequently submits a budget of estimated expenditures and revenues to the City Council by August 15. The City has one governmental fund with a legally adopted budget and it is the General Operating fund.

Upon receipt of the budget estimates, the Council holds a first reading on the Budget Ordinance and Tax Rate Ordinance. Information about the Budget Ordinance is then published in the official newspaper of the City. The Council is precluded from passing the Budget Ordinance (second reading) until ten days have passed after the Ordinance Publication and after the first Monday in September.

Prior to October 1, the budget is legally adopted or is amended by the City Council on a basis consistent with generally accepted accounting principles. The City Manager is authorized to transfer budgeted amounts between line items and departments within any fund; however, any revisions that alter the total expenditures of any fund must be approved by the City Council. The City did not have any budget amendments for the year ending September 30, 2018.

F. Cash and Investments

The government's cash and cash equivalents are considered to be cash on hand, demand deposits, and certificates of deposit. In accordance with GASBS No. 3, all governmental certificates of deposit are classified as deposits. All investments for the government as well as for its component units are recorded at fair value. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties.

For purposes of the statement of cash flows, the Enterprise Fund consider all highly liquid investments, with a maturity of three months or less when purchased, to be cash equivalents.

G. Prepaid Items

Prepaid balances are for payments made by the City in the current year to provide services occurring in the subsequent fiscal year.

H. Receivables and Payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as "due to/from other funds". Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances".

I. Inventory

Inventories are valued at cost using the first in/first-out (FIFO) method. The costs of inventories are recorded as expenditures when purchased.

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

J. Restricted Assets

Certain cash balances in the water sewer and sanitation fund are set aside for the repayment of debt. They are maintained in separate bank accounts and their use is limited by applicable bond or lending covenants. The general fund has cash that is restricted for debt service and restricted by legislative mandates such as hotel/motel tax monies, drug seizure monies, and court security and technology monies. The general fund restricted cash is \$138,004. Of this amount, \$110,189 is restricted by legislative mandates. The water sewer and sanitation fund has \$196,436 restricted cash for debt service. The City's discretely presented component unit, EDC, had restricted cash of \$541,554 as of September 30, 2018. This entire amount is restricted by legislative mandates.

K. 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. Capital assets are defined by the government as assets with an initial, individual cost of more than \$500 and an estimated useful life in excess of three years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

Property, plant, infrastructure, and equipment of the primary government, as well as the component units, is depreciated using the straight line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Vehicles	3 – 5
Machinery and Equipment	6 – 30
Buildings	40 – 60
Infrastructure	40 – 60
Improvements	27.5 – 60

L. Deferred Outflows/Inflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. The City has two items that qualifies for reporting in this category; the deferred outflow related to pensions and also OPEB reported in the government-wide Statement of Net Position.

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (revenue) until that time. The City has one type which arise only under a modified accrual basis of accounting that qualifies for reporting in this category.

Accordingly, the item, unavailable revenue, is reported only in the fund balance sheet. This amount is deferred and recognized as an inflow of resources in the period that the amount becomes available.

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

M. Compensated Absences

It is the government's policy to permit employees to accumulate earned but unused vacation, sick, and comp pay benefits. Employees are allowed to carryover 5 days for unused vacation time. Employees are allowed to accumulate 30 days of sick time. However, no payment for unused sick pay would be made in the event of termination or death. The estimated liability for accumulated time as of September 30, 2018 is recorded as an accrued payable in the appropriate fund. Governmental fund liabilities are paid by the general fund. Business-type compensated absences are paid by the water, sewer and sanitation fund.

N. Long-term Obligations

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

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

O. Fund Balance

In the fund financial statements, governmental funds report the following classifications of fund balance:

Restricted - amounts that can be spent only for specific purposes because of constitutional provisions or enabling legislation or because of City Charter, City Code, state or federal laws, or externally imposed conditions by grantors or creditors.

Assigned - amounts the City intends to use for a specific purpose. Intent can be expressed by the City Council or the City Manager when the City Council has delegated that authority. Modifications or rescissions of the constraints can also be removed by the same action that limited the funds.

Unassigned - all other spendable amounts.

As of September 30, 2018, fund balances are composed of the following:

	General Fund	Nonmajor Funds	Total Governmental Funds
Restricted:			
Public Safety	\$ 21,043	52,799	\$ 73,842
Tourism Development	75,164	-	75,164
Court Technology and Security	16,293	-	16,293
Debt	25,504	-	25,504
Assigned:			
Street Improvements	581,473	-	581,473
Debt	298,839	-	298,839
Senior Nutrition	23,765	-	23,765
Crime Prevention	130	-	130
Unassigned Fund Balances	434,200	-	434,200
Total Fund Balances	<u>\$ 1,476,410</u>	<u>\$ 52,799</u>	<u>\$1,529,209</u>

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

When an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available, the City considers restricted funds to have been spent first. 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 funds, then assigned funds, and finally unassigned funds, as needed, unless the City Council has provided otherwise in its commitment or assignment actions.

Net Position

In the government-wide financial statements and proprietary fund financial statements, the net position is reported in three components: (1) net investment in capital assets; (2) restricted; and (3) unrestricted. Net investment in capital assets represents the City's total investment in capital assets, net of depreciation, reduced by the outstanding balances of any borrowing used for the acquisition, construction or improvement of those assets. Net position is reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the City or through external restriction imposed by creditors, grantors or laws or regulations of other governments.

The government-wide statement of net position of the primary government reported restricted net position of \$387,239 of which, \$165,299 is restricted by enabling legislation.

Net Investment in Capital Assets

Net investment in capital assets is composed of the following:

	Capital Assets - Net	Related Debt	Unspent Debt Proceeds	Total
Governmental Fund	\$ 1,773,427	\$ 1,514,684	\$ -	\$ 258,743
Business-Type Fund				
Water and Sewer Fund	\$ 6,500,397	\$ 5,110,831	\$ -	\$ 1,389,566

(3) Deposits and Investments

As of September 30, 2018, the Primary Government and both discretely presented component units had investments in certificates of deposit.

Interest rate risk. In accordance with its investment policy, the City manages its exposure to declines in fair values by staggering the maturity dates of its certificates of deposit.

Credit risk. It is the City's policy to limit their investments to certificates of deposit thus the City is not significantly exposed to credit risk.

Concentration of credit risk. The City recognizes that investment risks can result from issuer defaults, market price changes or various technical complications leading to temporary illiquidity. Risk is controlled through portfolio diversification, however, they are allowed to have 100% of the investment portfolio in either certificates of deposit or authorized pools.

Custodial credit risk - deposits and investments. State statutes require that all deposits in financial institutions be fully collateralized by U.S. Government obligations or obligations of Texas and its agencies that have a fair value of not less than the principal amount of the deposits. The Primary Government's deposits and Certificates of Deposits, were fully insured or collateralized as required by the state statutes at September 30, 2018. At year-end, the carrying amount of the Primary Government's deposits totaled \$2,248,997 and the bank balances totaled \$2,297,515. The collateral is held by Prosperity Bank of Lubbock, Texas and is held in the City's name. The City's discretely presented component units had

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

carrying amounts of \$561,154 and bank balances were \$551,832. The cash and cash equivalents of both were also fully secure at year end.

(4) Receivables

Receivables as of year-end for the government's individual major funds, and non-major funds, in the aggregate, including the applicable allowances for uncollectible accounts, are as follows:

	General Fund	Water Sewer Fund	Total
Accounts	\$ 1,349	\$ 220,802	\$ 222,151
Taxes	100,336	-	100,336
Gross Receivables	101,685	220,802	322,487
Less: allowance for Uncollectibles	(5,405)	(53,132)	(58,537)
Net total receivables	<u>\$ 96,280</u>	<u>\$ 167,670</u>	<u>\$ 263,950</u>

The City's component unit, Merkel Economic Development Corporation, had taxes receivable of \$15,425 and notes receivable of \$209,900 for a total of \$225,325.

All receivables are expected to be collected within one year.

The City's capital lease receivable consists of a lease/purchase agreement with McElroy Metals, Inc. ("the Company") for land and improvements constructed for the Company pursuant to a contract between the City and the Texas Department of Economic Development. The purpose of this contract was to provide partial funding for the construction of a manufacturing facility through the Texas Capital Fund (TCF). Under the terms of the lease/purchase agreement the Company makes lease payments of \$2,500 per month over the 20 year term of the lease. Beginning five years after the closing of the TCF contract, the Company has the option to purchase merchantable title to the property for the original amount of the lease obligation less the aggregate amount of rent paid by the Company under the lease. The City is obligated to remit the amount of the lease payments received to the Texas Department of Housing and Community Affairs in repayment of the construction costs reimbursed under the City's agreements with the Texas Department of Economic Development. The total minimum lease payments to be received under the lease as of September 30, 2018 is \$65,000.

As of September 30, 2018 the minimum lease payments are as follows:

Year	Amount
2018	\$ 30,000
2019	30,000
2020	5,000
	<u>\$ 65,000</u>

(5) Capital Assets

Capital asset activity for the year ended September 30, 2018 was as follows:

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

Primary Government

Governmental activities:	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$ 12,500	\$ -	\$ -	\$ 12,500
Construction in-progress	-	-	-	-
Total capital assets not being depreciated	12,500	-	-	12,500
Capital assets, being depreciated:				
Buildings and improvements	141,968	-	-	141,968
Equipment	1,031,211	98,699	(7,506)	1,122,404
Infrastructure	1,912,060	-	-	1,912,060
Motor vehicles	1,082,159	54,163	-	1,136,322
Furniture and fixtures	48,345	-	-	48,345
Total capital assets being depreciated	4,215,743	152,862	(7,506)	4,361,099
Less accumulated depreciation for:				
Buildings and improvements	102,805	5,011	-	107,816
Equipment	929,804	49,969	(5,769)	974,006
Infrastructure	508,015	60,064	-	568,079
Motor vehicles	828,544	73,978	-	902,522
Furniture and fixtures	46,667	1,082	-	47,749
Total accumulated depreciation	2,415,834	190,104	(5,769)	2,600,172
Total capital assets, being depreciated, net	1,799,909	(37,242)	(1,737)	1,760,927
Governmental activities capital assets, net	\$ 1,812,409	\$ (37,242)	\$ (1,737)	\$ 1,773,427

Business-type activities:	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$ 72,080	\$ -	\$ -	\$ 72,080
Construction in-progress	-	-	-	-
Total capital assets not being depreciated	72,080	-	-	72,080
Capital assets, being depreciated:				
Equipment	323,700	16,754	-	340,454
Buildings	1,975	-	-	1,975
Motor vehicles	39,325	15,986	-	55,311
Water system	9,380,968	-	-	9,380,968
Total capital assets being depreciated	9,745,972	32,740	-	9,778,712
Less accumulated depreciation for:				
Equipment	235,220	19,096	-	254,316
Buildings	1,975	-	-	1,975
Motor vehicles	39,325	533	-	39,858
Water system	2,852,175	202,071	-	3,054,242
Total accumulated depreciation	3,128,695	221,700	-	3,350,395
Total capital assets, being depreciated, net	6,617,277	(188,960)	-	6,428,317
Business-type activities capital assets, net	\$ 6,689,357	\$ (188,960)	\$ -	\$ 6,500,397

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

Depreciation expense was charged to functions as follows:

Governmental activities:	
General government	\$ 2,740
Public safety	107,990
Streets	73,042
Culture and recreation	6,333
Total depreciation expense – governmental activities	<u>\$190,104</u>

Component Unit

Merkel Volunteer Fire Department	Beginning <u>Balance</u>	<u>Increases</u>	<u>Decreases</u>	Ending <u>Balance</u>
Capital assets, being depreciated:				
Equipment	\$ 243,010	\$ 20,000	\$ -	\$ 263,010
Total capital assets being depreciated	<u>243,010</u>	<u>20,000</u>	<u>-</u>	<u>263,010</u>
Less accumulated depreciation for:	160,909	51,082	-	211,991
Total accumulated depreciation	<u>160,909</u>	<u>51,082</u>	<u>-</u>	<u>211,991</u>
Total capital assets being depreciated, net	82,101	(31,082)	-	51,019
capital assets, net	<u>\$ 82,101</u>	<u>\$(31,082)</u>	<u>\$ -</u>	<u>\$ 51,019</u>

(6) Capital Lease

Governmental Type Activities:

The City has entered into an agreement to lease police department equipment. This agreement is in substance a purchase and is reported as a capital lease obligation. The following schedule presents future minimum lease payments as of September 30, 2018. The value of equipment leased at September 30, 2018 was \$50,608 and amortization on leased equipment is included with depreciation expense.

Year Ending September 30,	Governmental <u>Leases</u>
2019	18,150
2020	18,150
2021	18,150
Net minimum lease payments	<u>54,450</u>
Less: interest	<u>3,844</u>
Present Value of Minimum Lease payments	<u>\$ 50,608</u>

(7) Long-Term Notes and Certificates of Obligation

At September 30, 2018, long-term debt consisted of the following:

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

Governmental-Type Activities:

A Texas Department of Housing and Community Affairs loan for \$600,000 bearing an interest rate of 0% payable in 240 monthly installments of \$2,500. Final maturity of the loan is in November 2019.	\$ 67,500
A First Financial Bank note for \$143,759 bearing an interest rate of 3.52% payable in five annual payments of \$31,816. Final maturity is January 1, 2021. The note is for three police vehicles.	89,078
Combination Tax & Revenue Certificates of Obligation, Series 2011 in the amount of \$1,500,000. The certificates bear interest of 4.25%. and have a final maturity in 2050. Property taxes, waterworks and sewer revenues are pledged for payments of the obligations. This bond issue is for street and pavement improvements.	<u>1,375,000</u>
Total Governmental-Type Activities debt	<u>\$1,531,578</u>

Business-Type Activities:

1994 Combination Tax & Revenue Certificates of Obligation, dated September 1994 in the original amount of \$383,000 due in annual installments through September 2024, bearing interest rate of 4.5%. Property taxes, waterworks and sewer revenues are pledged for payments of the obligations.	\$ 129,000
2008 Combination Tax & Revenue Certificates of Obligation, dated November 2008 for \$2,300,000 due in annual installments through September 2047, bearing interest rate of 4.5%. Property taxes, and surplus revenues of the City's waterworks and sewer system are pledged for payment of the obligations. This bond issue is for improvements and extensions of the City's waterworks and sewer system.	2,039,000
2009 Combination Tax and Waterworks and Sewer System Surplus Revenue C.O., dated January 2009 in the original amount of \$3,000,000 due in annual installments through September 2048, bearing interest from 3.948% to 5.22% increasing annually. Property taxes, and surplus revenues of the City's waterworks and sewer system are pledged for payment of the obligations. This bond issue is for replacing existing water and sewer lines, construction, acquisition and installation of new water and sewer lines, pumping and storage facilities, and lift stations.	<u>2,715,000</u>
Total Certificates of Obligation	<u>\$ 4,883,000</u>
Note payable to Prosperity Bank for water line replacement. Loan advance in the amount of \$397,000 with 3.150% interest due in monthly installments of \$3,322 through January 2025. This note is unsecured.	<u>\$ 227,830</u>

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

Annual Requirements to Retire Debt Obligations

The annual aggregate maturities for the years subsequent to September 30, 2018 are as follows:

Governmental Activities:

Year Ending September 30	Principal	Interest	Total Obligation
2019	79,679	61,574	141,253
2020	81,689	59,672	141,361
2021	61,210	57,692	118,902
2022	24,000	55,633	79,633
2023	25,000	54,613	79,613
2024-2028	140,000	256,275	396,275
2029-2033	174,000	223,848	397,848
2034-2038	213,000	183,643	396,643
2039-2043	262,000	134,470	396,470
2044-2048	322,000	73,866	395,866
2049-2050	149,000	9,563	158,563
Total	<u>\$ 1,531,578</u>	<u>\$ 1,170,846</u>	<u>\$ 2,702,424</u>

Business-Type Activities:

Year Ending September 30	Principal	Interest	Total Obligation
2019	127,058	244,397	371,455
2020	131,129	239,008	370,138
2021	139,235	233,419	372,654
2022	143,377	227,437	370,814
2023	152,556	221,265	373,822
2024-2028	595,475	1,017,182	1,612,657
2029-2033	666,000	876,176	1,542,176
2034-2038	851,000	696,981	1,547,981
2039-2043	1,076,000	467,609	1,543,609
2044-2048	1,229,000	177,329	1,406,329
Total	<u>\$ 5,110,830</u>	<u>\$ 4,400,804</u>	<u>\$ 9,511,634</u>

Changes in Outstanding Long-Term Debt

Transactions for the year ended September 30, 2018 are summarized as follows:

	Balance September 30, 2017	Issues or Additions	Payments or Expenditures	Balance September 30, 2018	Due Within One Year
Governmental Activities					
Notes Payable	\$ 214,100	\$ -	\$ 57,522	\$ 156,578	\$ 58,663
Capital Lease	25,169	25,780	341	50,608	16,252
Certificates of Obligation	1,395,000	-	20,000	1,375,000	20,000
Compensated Absences	16,618		4,441	12,177	3,044
Net Pension Liability	345,382		214,407	130,975	-
Net OPEB Liability	17,853	3,186		21,039	
Total Governmental	<u>\$ 2,014,122</u>	<u>\$ 28,966</u>	<u>\$ 296,711</u>	<u>\$ 1,746,377</u>	<u>\$ 97,959</u>

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

	Balance September 30, 2017	Issues or Additions	Payments or Expenditures	Balance September 30, 2018	Due Within One Year
<u>Business-type Activities</u>					
Note Payable	\$ 260,033	\$ -	\$ 32,203	\$ 227,830	\$ 32,203
Capital Lease	17,640	-	17,640	-	-
Certificates of Obligation	4,974,000	-	91,000	4,883,000	91,000
Compensated Absences	4,452	4,360	-	8,812	2,203
Net Pension Liability	216,990	-	107,719	109,271	-
Net OPEB Liability	8,969	1,600	-	10,569	-
Total Business-type Activities	\$ 5,482,084	\$ 5,960	\$ 248,562	\$ 5,239,482	\$ 125,406

Direct Interest

The debt listed for business-type activities above was issued for the creation or continuing existence of specific programs for the City's water and sewer system. Interest on the debt is reported in the water and sewer fund as direct expenses on the Statement of Activities. In governmental fund financial statements, interest is reported by the department responsible for the debt and making the payment.

(9) Operating Lease

Commitments under operating (noncapitalized) lease agreements for equipment provide for the minimum future rental payments as of September 30, 2018, are as follows:

Year Ending <u>September 30,</u>	
2019	\$ 3,137
2020	3,137
2021	3,137
2022	3,137
2023	262
Total Minimum Rentals	\$ 12,810
 Rental Expenditures in Fiscal Year 2018	 \$ 2,876

(10) Property Tax

The City's property tax is levied and becomes a lien each October 1, on 100 percent of assessed value listed for all real and personal property located in the City as of the prior January 1. Assessed values are established by the Taylor County Central Appraisal District and certified by the Board of Review.

The City is permitted by Article II, Section 5 of the State of Texas constitution to levy taxes up to \$2.50 per \$100 of assessed valuation for general governmental services including the payment of principal and interest on general obligation long-term debt. Taxes are due on the levy date and are delinquent on January 31, following the October 1, levy date. Current tax collections for the year ended September 30, 2018 were 96 percent of the tax levy.

Property tax revenues are recognized when they become available. Available means collected within the current period and the amount expected to be collected soon after year-end to pay liabilities of the current period not to exceed 60 days. The amount of taxes collected in the balance of taxes receivable, net of allowance, is recorded as unavailable revenue.

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

Beginning in 1982, the Appraisal District is required under the Property Tax Code to assess all property within the Appraisal District on the basis of 100 percent of its appraised market value and is prohibited from applying any assessment ratios. The value of property within the Appraisal District must be reviewed every four years; however, the City may, at its own expense, require annual reviews of appraised values. The City may challenge appraised values established by the Appraisal District through various appeals and if necessary, legal action. Under this legislation the City continues to set tax rates on City property. However, if the effective tax rates, excluding tax rates for bonds and other contractual obligations, adjusted for new improvements, exceeds the rate for the previous year by more than 8 percent, qualified voters of the City may petition for an election to determine whether to limit the tax rate to no more than 8 percent above the calculated tax rate of the previous year levy and the current year valuation.

(11) Employee Retirement Systems
Texas Municipal Retirement System (TMRS)

A. Plan Description

The City participates as one of 883 member cities in the nontraditional, joint contributory, hybrid defined benefit pension plan administered by the Texas Municipal Retirement System (TMRS). TMRS is an agency created by the State of Texas and administered in accordance with the TMRS Act, Subtitle G, Title 8, Texas Government Code (the TMRS Act) as an agent multiple-employer retirement system for municipal employees in the State of Texas. The TMRS Act places the general administration and management of the System with a six-member Board of Trustees. Although the Governor, with the advice and consent of the Senate, appoints the Board, TMRS is not fiscally dependent on the State of Texas. TMRS's defined benefit pension plan is a tax-qualified plan under Section 401 (a) of the Internal Revenue Code. TMRS issues a publicly available comprehensive annual financial report (CAFR) that can be obtained at www.tmrs.com.

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

B. Benefits Provided

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

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

TMRS members vest after 5 years of service. If a vested member leaves covered employment before reaching retirement eligibility, the member may leave his or her deposits with TMRS, earn interest on the deposits, and, upon reaching age 60, apply for and receive a monthly retirement payment. A member becomes eligible for service retirement based on various combinations of age and service, depending on which provisions have been adopted by the employing municipality. The City of Merkel has adopted a 5 yrs/age 60, 25 yrs/any age provision for their service retirement eligibilities.

A member city may elect to increase the annuities of its retirees (grant a cost-of-living adjustment, or COLA), either annually or on an annually repeating basis, effective January 1 of a calendar year. For cities that adopted annuity increases since January 1, 2000, the adjustment is either 30%, 50%, or 70% of the increase (if any) in the Consumer Price Index - All Urban Consumers (CPI-U) between the December preceding the member's retirement date and the December 13 months before the effective date of the increase, applied to the original monthly annuity.

Employees covered by benefit terms.

At the December 31, 2017 valuation and measurement date, the following employees were covered by the benefit terms:

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

Inactive employees or beneficiaries currently receiving benefits	8
Inactive employees entitled to but not yet receiving benefits	14
Active employees	<u>16</u>
	38

C. Contributions

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

Employees for the City of Merkel were required to contribute 6% of their annual gross earnings during the fiscal year. The contribution rates for the City were 13.23% and 13.66% in calendar years 2017 and 2018, respectively. The City's contributions to TMRS for the year ended September 30, 2018 were \$70,824 and were equal to the required contributions.

D. Net Pension Liability

The City's Net Pension Liability (NPL) was measured as of December 31, 2016, and the Total Pension Liability (TPL) used to calculate the Net Pension Liability was determined by an actuarial valuation as of that date.

Actuarial assumptions:

The Total Pension Liability in the December 31, 2017 actuarial valuation was determined using the following actuarial assumptions:

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

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

The actuarial assumptions were developed primarily from the actuarial investigation of the experience of TMRS over the four year period from December 31, 2010 to December 31, 2014. They were adopted in 2015 and first used in the December 31, 2015 actuarial valuation. The post-retirement mortality assumption for healthy annuitants and Annuity Purchase Rate (APRs) are based on the Mortality Experience Investigation Study covering 2009 through 2011 and dated December 31, 2013. In conjunction with these changes first used in the December 31, 2013 valuation, the System adopted the Entry Age Normal actuarial cost method and a one-time change to the amortization policy. Plan assets are managed on a total return basis with an emphasis on both capital appreciation as well as the production of income, in order to satisfy the short-term and long-term funding needs of TMRS.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best estimate ranges of expected future real rates of return (expected returns, net

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. In determining their best estimate of a recommended investment return assumption under the various alternative asset allocation portfolios, GRS focused on the area between (1) arithmetic mean (aggressive) without an adjustment for time (conservative) and (2) the geometric mean (conservative) with an adjustment for time (aggressive).

The target allocation and best estimates of arithmetic real rates of return for each major asset class in fiscal year 2018 are summarized in the following table:

Asset Class	Target Allocation	Long-term Expected Real Rate of Return
Domestic Equity	17.5%	4.55%
International Equity	17.5%	6.35%
Core Fixed Income	10.0%	1.00%
Non-Core Fixed Income	20.0%	3.90%
Real Return	10.0%	3.80%
Real estate	10.0%	4.50%
Absolute Return	10.0%	3.75%
Private Equity	<u>5.0%</u>	7.50%
Total	<u>100%</u>	

Changes in the Net Pension Liability

	Increase (Decrease)		
	Total Pension Liability	Plan Fiduciary Net Position	Net Pension Liability
	[a]	[b]	[a] – [b]
Balance at 12/31/2016	\$ 1,824,431	\$ 1,262,059	\$ 562,372
Changes for the year:			
Service cost	65,072	-	65,072
Interest	120,182	-	120,182
Difference between expected and actual experience	(243,261)	-	(243,261)
Changes in assumptions	-	-	-
Contributions – employer	-	61,935	(61,935)
Contributions – employee	-	28,129	(28,129)
Net investment income	-	175,007	(175,007)
Benefit payments, including refunds of employee contributions	(152,995)	(152,995)	-
Administrative expense	-	(906)	906
Other changes	-	(46)	46
Net changes	\$ (211,002)	\$ 111,124	\$ (322,126)
Balance at 12/31/2017	\$ 1,613,429	\$ 1,373,183	\$ 240,246

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

Discount Rate

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

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

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

	Disc out rate	Net pension liability
1% decrease	5.75 %	\$ 475,173
Current discount rate	6.75 %	\$ 240,246
1% increase	7.75 %	\$ 50,547

Pension Plan Fiduciary Net Position

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

E. Pension Expense, Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended September 30, 2018 the city recognized pension expense of \$7,183.

At September 30, 2018, the City reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ -	\$ 176,731
Changes in actuarial assumptions	6,703	-
Difference between projected and actual investment earnings	-	38,102
Contributions subsequent to the measurement date	53,207	-
Total	\$ 59,910	\$ 214,833

\$53,207 reported as deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability for the year ending September 30, 2018. Other amounts reported as deferred outflows and inflows of resources

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

related to pensions will be recognized in pension expense as follows:

Year ending Dec 31:	
2018	\$ (60,866)
2019	(59,386)
2020	(69,916)
2021	(17,962)
2022	-
Thereafter	-

**(12) Employee Retirement Systems - Volunteer Fire Department
Texas Emergency Services Retirement System (TESRS)**

A. Plan Description

The Texas Emergency Services Retirement System is an agency of the State of Texas and its financial records comply with state statutes and regulations. The nine Board of Trustees, appointed by the Governor, establishes policy for the administration of the Texas Emergency Services Retirement System.

The TESTS was created as a standalone agency by the 83rd Legislature via the passage of SB 220, effective September 1, 2013, to assume the related functions of the abolished Office of the Fire Fighters' Pension Commissioner. While the agency is new, the System has been in existence since 1977. TESRS, which is under the authority of Title 8, Subtitle H, Chapters 861-865 of the Texas Government Code, provides death and disability benefits to active volunteer fire fighters and first responders, and a pension to members with vested service, as well as to their survivor/beneficiaries. For financial reporting purposes, the State of Texas is considered the primary reporting government. TESRS' financial statements are included in the State's Comprehensive Annual Financial Report. TESRS issues a publicly available Annual Financial Report, which includes financial statements, notes, and required supplementary information, which can be obtained at www.tesrs.org. The separately issued actuarial valuations which may be of interest are also available at the same link.

Information that is available in the annual financial report is not repeated in the allocation schedules and related notes.

The preparation of the schedules of participating department allocations and collective pension amounts in conformity with accounting principles generally accepted in the United States of America requires management to make significant estimates and assumptions that affect the reporting amounts during the reporting period. Actual results could differ from those estimates.

B. Benefits Provided

The benefit provision include retirement benefits as well as death and disability benefits. Members are 50% vested after the tenth year of service, with the vesting percent increasing 10% for each of the next five years of service so that a member becomes 100% vested with 15 years of service.

Upon reaching age 55, each vested member may retire and receive a monthly pension equal to his vested percent multiplied by six times the governing body's average monthly contribution over the member's year of qualified service. For years of service in excess of 15 years, this monthly benefit is increased at the rate of 6.2% compounded annually. There is no provision for automatic postretirement benefit increases.

On and off-duty death benefits and on-duty disability benefits are dependent on whether or not the member was engaged in the performance of duties at the time of death or disability. Death benefits

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

include a lump sum amount or continuing monthly payments to a member's surviving spouse and dependent children.

C. Contributions

Contributions are made by governing bodies for the participating departments. No contributions are required from the individuals who are members of the system, nor are they allowed. The governing bodies of each participating department are required to make contributions for each month a member performs emergency services for a department (this contribution is \$36 per member and the department may make a higher monthly contribution for its members). This is referred to as a Part One contribution, which is the legacy portion of the System contribution that directly impacts future retiree annuities. The state is required to contribute an amount necessary to make the System "actuarially sound" each year, which may not exceed one-third of the total of all contributions made by participating governing bodies in a particular year.

The board rule defining contributions was amended effective July 27, 2014 to add the potential for actuarially determined Part Two contributions that would be required only if the expected future annual contributions from the state are not enough with the Part One contributions to provide an adequate contribution arrangement as determined by the most recent actuarial valuation. This Part Two portion, which is actuarially determined as a percent of the Part One portion (not to exceed 15%), is to be actuarially adjusted near the end of each even-numbered calendar year based on the most recent actuarial valuation. Based on the actuarial valuation as of August 31, 2017, the Part Two contribution rate was 0%, since the first actuarial valuation report after adoption of the rules showed the System to have an adequate contribution arrangement without any Part Two contributions.

The contributions to TESRS for the year ended September 30, 2018 were \$2,203, and were equal to the required contributions.

D. Net Pension Liability

The Volunteer Fire Department's Net Pension obligations are not recorded on the financial statements because of their materiality.

(13) Other Post-Employment Benefits

A. Plan Description

The City also participates in an optional cost sharing multiple-employer defined benefit group life insurance plan operated by the Texas Municipal Retirement System (TMRS) known as the Supplemental Death Benefits Fund (SDBF). It provides death benefits to both active and retired members, and each participating municipality can elect to cover just active members, or active and retired members. A supplemental death contribution rates is determined annually for each participating municipality as a percentage of that city's covered payroll. The contribution rate finances the expected benefit payments each year on a pay-as-you-go basis.

As stated in the previous paragraph, the SDBF covers both active and retiree benefits with no segregation of assets, and therefore doesn't meet the definition of a trust under GASB no. 75, paragraph 4b, (i.e., no assets are accumulated for OPEB). As such the SDBF is considered to be a single-employer unfunded OPEB plan (and not a cost sharing plan) with benefit payments treated as being equal to the employer's yearly contributions for retirees. In accordance with paragraph 155, the applicable discount rate for an unfunded OPEB is based on an index of tax exempt 20-year municipal bond rates rated as AA or higher. As of December 31, 2017, the discount rate used in the development of the Total OPEB Liability was 3.31% compared to 3.78% as of December 31, 2016.

B. Benefits Provided

The death benefit for active employees provides a lump-sum payment approximately equal to the

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

employee's annual salary (calculated based on the employee's actual earnings, for the 12-month period preceding the month of death). The death benefit for retirees is a fixed amount of \$7,500.

Employees covered by benefit terms.

At the December 31, 2017 valuation and measurement date, the following employees were covered by the benefit terms:

Inactive employees or beneficiaries currently receiving benefits	5
Inactive employees entitled to but not yet receiving benefits	2
Active employees	<u>16</u>
	23

C. Contributions

The employer contribution rates for the municipalities participating in the SDBF are certified annually by the Board of Trustees which is responsible for establishing and maintaining the funding policy. These rates are determined actuarially, based on the plan provisions in effect as of April 1, 2018 and the actuarial assumptions and methodology adopted by the Board. The Board's current policy is that the contribution rates determined by a given actuarial valuation become effective one (1) year after the valuation date. For example, the rates determined by the December 31, 2017 actuarial valuation will be applicable for the calendar year beginning January 1, 2019 and ending December 31, 2019.

D. Net OPEB Liability

The total OPEB Liability (TOL) as of December 31, 2017 was "rolled back" to December 31, 2016 for the purposes of developing a beginning of the year TOL

Actuarial assumptions:

The actuarial assumptions were developed primarily from the actuarial investigation of the experience of TMRS over the four-year period from December 31, 2010 to December 31, 2014. They were adopted in 2015 and first used in the December 31, 2015 actuarial valuation. The post-retirement mortality assumption for healthy annuitants and Annuity Purchase Rate (APRs) are based on the Mortality Experience Investigation Study covering 2009 through 2011 and dated December 31, 2013.

Economic Assumptions:

- General Inflation – General Inflation is assumed to be 2.50% per year.
- Discount Rates – Because the Supplemental Death Benefits Fund is considered an unfunded trust under GASB Statement No. 75, the relevant discount rate for calculating the Total OPEB Liability is based on the Fidelity Index's "20-Year Municipal GO AA Index" rate as of the measurement date.
- Individual Salary Increases – Salary increases are assumed to occur once a year, on January 1. Therefore, the pay used for the period year following the valuation date is equal to the reported pay for the prior year, increased by the salary increase assumption. Salaries are assumed to increase by the following graduated service-based scale.

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

Years of Service	Rate (%)
1	10.50%
2	7.50%
3	7.00%
4	6.50%
5	6.00%
6	5.50%
7	5.25%
8-10	4.75%
11	4.50%
12-13	4.25%
14-16	4.00%
17-24	3.75%
25+	3.50%

Changes in the Total OPEB Liability

Total OPEB Liability – beginning of year	\$ 26,925
Changes for the year:	
Service cost	1,125
Interest	1,036
Changes in benefit terms	-
Differences between expected and actual experience	-
Changes in assumptions or other inputs	2,663
Benefit payments**	(141)
Net changes	<u>\$ 4,683</u>
Total OPEB Liability - end of year	<u>\$ 31,608</u>

** Due to the SDBF considered an unfunded OPEB plan under GASB 75, benefit payments are treated as being equal to the employer's yearly contributions for retirees.

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net OPEB liability of the City, calculated using the discount rate of 3.31%, as well as what the City's net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (2.31%) or 1-percentage-point higher (4.31%) than the current rate:

	Discount rate	Net pension liability
1% decrease	2.31%	\$ 38,559
Current discount rate	3.31%	\$ 31,608
1% increase	4.31%	\$ 26,329

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

E. OPEB Expense, Deferred Outflows of Resources and Deferred Inflows of Resources

For the year ended September 30, 2018 the city recognized OPEB expense of \$2,598.

At September 30, 2018, the City reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between expected and actual experience	\$ -	\$ -
Changes in assumptions and other inputs	2,226	-
Contributions subsequent to the measurement date	163	-
Total	<u>\$ 2,389</u>	<u>\$ -</u>

\$163 reported as deferred outflows of resources related to OPEB resulting from contributions subsequent to the measurement date will be recognized as a reduction of the net OPEB liability for the year ending September 30, 2018. Other amounts reported as deferred outflows and inflows of resources related to OPEB will be recognized in pension expense as follows:

Year ending Dec 31:

2018	\$ 437
2019	437
2020	437
2021	437
2022	437
Thereafter	41

(14) Individual Fund Disclosures

For fiscal year ended September 30, 2018, the City has expended funds in excess of appropriations at the level of control in the following areas:

<u>Fund</u>	<u>Excess Amount</u>
Ambulance Department	60,025
Fire Department	12,468
Police Department	26,388
Municipal Court	6,283
Heritage Hall	16,879
Library	1,348

These over-expenditures were funded by greater than anticipated revenues, under-budget expenditures in other departments and fund balance.

(15) Interfund Receivables, Payables, and Transfers

The composition of interfund balances as of September 30, 2018, is as follows:

	<u>Due From</u>	<u>Due To</u>
General fund	\$ 127,669	\$ -
Major business-type fund	-	127,669
	<u>\$ 127,669</u>	<u>\$ 127,669</u>

CITY OF MERKEL, TEXAS
Notes to the Financial Statements
September 30, 2018

The general fund pays all city employees and the water sewer fund reimburses the general fund. This balance due is scheduled to be collected in the subsequent year.

(16) Health Care Coverage

During the year ended September 30, 2018, employees of the City were covered by a health insurance plan (the Plan). The City paid premiums for full time employee to the Plan. Employees at their option, authorized payroll withholdings to pay premiums for dependents. All premiums were paid to a third party administrator, acting on behalf of the licensed insurer. The Plan was authorized by Article 3.51-2, Texas Insurance Code and was documented by contractual agreement.

The contract between the City and the third party administrator is renewable January 1, and terms of coverage and premium costs are included in the contractual provisions.

Latest financial statements for First Care are available for the year ended December 31, 2017, and have been filed with the Texas State Board of Insurance, Austin, Texas and are public record.

(17) Risk Management

The City is exposed to various risks of loss related to torts, theft, damage or destruction of assets, errors and omissions, injuries to employees, and natural disasters. During fiscal year 2017, the City obtained general liability coverage at a cost that is considered to be economically justifiable by joining together with other governmental entities in the State as a member of the Texas Municipal League Intergovernmental Risk Pool ("TMLIRP"). TMLIRP is a self-funded pool operating as a common risk management and insurance program. The City pays an annual premium to TMLIRP for its above insurance coverage. During the last three years, no program has had settlements or judgments that exceeded pooled or insured coverage. There have been no significant reductions in coverage from coverage in the prior years.

(18) Contingent Liabilities

Amounts received or receivable from grantor 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, if any, 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 a lawsuit that has arisen in the normal course of business. While substantial damages are alleged in this action, the outcome cannot be predicted with certainty. In the opinion of the City's legal team, this action when finally adjudicated will not have a material adverse effect on the financial position of the City.

(19) Impact of Recently Implemented Accounting Principles and Resulting Prior Period Adjustment

Implemented

Statement No. 75, "Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions" - This statement changes the focus of accounting of postemployment benefits other than pensions from whether they are responsibility funding the benefits over time to a point-in-time liability that is reflected on the employer's financial statements for any actuarially unfunded portion of benefits earned to date. This statement will become effective for the City in fiscal year 2018. The prior period adjustment related to the implementation of GASB 75 was \$26,822.

CITY OF MERKEL, TEXAS

Schedule of Changes in Net Pension Liability and Related Ratios - TMRS
 Last 10 years (will ultimately be displayed)

	Measurement Year 2014	Measurement Year 2015	Measurement Year 2016	Measurement Year 2017
Total pension liability				
Service Cost	\$ 64,854	\$ 66,494	\$ 70,767	\$ 65,072
Interest (on the Total Pension Liability)	106,830	111,355	113,433	120,182
Changes of benefit terms	-	-	-	-
Difference between expected and actual experience	(27,992)	(37,710)	31,577	(243,261)
Change of assumptions	-	21,935	-	-
Benefit payments, including refunds of employee contributions	(83,630)	(76,096)	(72,913)	(152,995)
Net Change in Total Pension Liability	60,062	85,978	142,864	(211,002)
Total Pension Liability - Beginning	1,535,527	1,595,589	1,681,567	1,824,431
Total Pension Liability - Ending (a)	<u>\$ 1,595,589</u>	<u>\$ 1,681,567</u>	<u>\$ 1,824,431</u>	<u>\$ 1,613,429</u>
 Plan Fiduciary Net Position				
Contributions - Employer	\$ 63,243	\$ 68,792	\$ 68,655	\$ 61,935
Contributions - Employee	28,408	30,043	30,903	28,129
Net Investment Income	61,010	1,674	78,295	175,007
Benefit payments, including refunds of employee contributions	(83,630)	(76,096)	(72,913)	(152,995)
Administrative Expense	(637)	(1,020)	(884)	(906)
Other	(52)	(50)	(48)	(46)
Net change in Plan Fiduciary Net Position	68,342	23,342	104,008	111,124
Plan Fiduciary Net Position - Beginning	1,066,367	1,134,709	1,158,051	1,262,059
Plan Fiduciary Net Position - Ending (b)	<u>\$ 1,134,709</u>	<u>\$ 1,158,051</u>	<u>\$ 1,262,059</u>	<u>\$ 1,373,183</u>
Net Pension Liability - Ending (a) - (b)	<u>\$ 460,880</u>	<u>\$ 523,516</u>	<u>\$ 562,372</u>	<u>\$ 240,246</u>
Plan Fiduciary Net Position as a % of Total Pension Liability	71.12%	68.87%	69.18%	85.11%
Covered Employee Payroll	\$ 473,464	\$ 500,712	\$ 515,044	\$ 468,821
Net Pension Liability as a % of Covered Employee Payroll	97.34%	104.55%	109.19%	51.24%

Notes to Schedule:

N/A

CITY OF MERKEL, TEXAS

Schedule of Contributions - TMRS Last 10 years (will ultimately be displayed)

	9/30/2015	9/30/2016	9/30/2017	9/30/2018
Actuarially Determined Contribution	\$ 66,909	\$ 69,196	\$ 63,574	\$ 70,824
Contributions in relation to the actuarially determined contribution	\$ 66,909	\$ 69,196	\$ 63,574	\$ 70,824
Contribution deficiency (excess)	\$ -	\$ -	\$ -	\$ -
Covered employee payroll	\$ 490,528	\$ 514,947	\$ 479,127	\$ 523,392
Contributions as a percentage of covered employee payroll	13.64%	13.44%	13.27%	13.53%

Notes to Schedule of Contributions

Valuation Date:

Notes

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

Methods and Assumptions Used to Determine Contribution Rates:

Actuarial Cost Method	Entry Age Normal
Amortization Method	Level Percentage of Payroll, closed
Remaining Amortization Period	26 years
Asset Valuation Method	10 Year smoothed market; 15% soft corridor
Inflation	2.5%
Salary Increases	3.50% to 10.5% including inflation
Investment Rate of Return	6.75%
Retirement Age	Experience-based table of rates that are specific to the City's plan of benefits. Last updated for the 2010 valuation pursuant to an experience study of the period 2010-2014.
Mortality	RP2000 Combined Mortality Table with Blue Collar Adjustment with male rates multiplied by 109% and female rates multiplied by 103% and projected on a fully generational basis with scale BB.

Other information:

Notes

There were no benefit changes during the year.

CITY OF MERKEL, TEXAS

Schedule of Changes in Total OPEB Liability and Related Ratios - TMRS Last 10 years (will ultimately be displayed)

	Measurement Year 2017
Total OPEB liability	
Service Cost	\$ 1,125
Interest (on the Total OPEB Liability)	1,036
Changes of benefit terms	-
Difference between expected and actual experience	-
Change of assumptions	2,663
Benefit payments **	<u>(141)</u>
Net Change in Total Pension Liability	4,683
Total Pension Liability - Beginning	<u>26,925</u>
Total Pension Liability - Ending (a)	<u><u>\$ 31,608</u></u>
Covered employee payroll	\$ 523,392
Total OPEB Liability as a percentage of covered payroll	6.74%

** Due to the SDBF being considered an unfunded OPEB plan under GASB 75, benefit payments are treated as being equal to the employer's yearly contributions for retirees.

Notes to RSI:

No assets are accumulated in a trust that meets the criteria in paragraph 4 of GASB No. 75 to pay related benefits.

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Other Information Required by Government Auditing Standards

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

Honorable Mayor and
Members of the City Council
Merkel, TX 79536

I have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, business-type activities, aggregate discretely presented component units, and the aggregate remaining funds of the City of Merkel, Texas ("City"), as of and for the year ended September 30, 2018, and the related notes to the financial statements, which collectively comprise the City's basic financial statements and have issued my report thereon dated December 19, 2018.

Internal Control Over Financial Reporting

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

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

My consideration of internal control was for the limited purposes described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies in internal control may exist that were not identified. Given these limitations, during the audit I did identify one deficiency in internal control that I consider to be a material weakness. It is described in the accompanying Schedule of Findings and Responses as 2018-001.

Compliance and Other Matters

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

Response to Findings

The City's response to the findings identified in the audit is described in the accompanying schedule of findings and responses. The response is not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, I express no opinion on it.

Purpose of this Report

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

Cathrine Wilks CPA LLC

Sweetwater, Texas
December 19, 2018

CITY OF MERKEL, TEXAS

Schedule of Findings and Responses For the Year Ended September 30, 2018

I. Summary of the Auditor's Results:

- a. The type of report issued on the general purpose financial statements of the City of Merkel was an unmodified opinion.
- b. There were material deficiencies in internal control detected by the audit.
- c. The audit disclosed no instances of noncompliance which would be material to the financial statements.

II. Findings Relating to the Financial Statements Which Are Required To Be Reported in Accordance with *Generally Accepted Government Auditing Standards*.

Financial Reporting Finding

2018-001 *Criteria:* Management should have adequate procedures to ensure that the financial statements are free of material misstatements.

Condition: Several adjustments were required to correct material misstatements.

Cause: City staff need additional training in order to properly understand and complete year-end closing entries.

Effect: The financial records as presented were materially misstated.

Recommendation: I recommend that staff responsible for the financial transactions receive additional training and possibly additional assistance when getting the year-end closing entries made and assembling all necessary documentation required to support all adjustments made.

Management Response: The City Secretary has already enrolled in governmental accounting classes and will receive the necessary training before year-end.

CITY OF MERKEL, TEXAS

Summary Schedule of Prior Audit Findings For the Year Ended September 30, 2018

Finding/Recommendation	Current Status	Management's Explanation If not Implemented
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There were no findings in the prior year.