

This Preliminary Official Statement and the information contained herein are subject to completion or amendment. These securities may not be sold nor may offers to buy be accepted prior to the time the Official Statement is delivered in final form. Under no circumstances shall this Preliminary Official Statement constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of these securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction.

**PRELIMINARY OFFICIAL STATEMENT
DATED NOVEMBER 6, 2012**

Ratings:
Moody's: "A2"
**See ("OTHER INFORMATION -
RATINGS" herein)**

NEW ISSUE - Book-Entry-Only

In the opinion of Bond Counsel, interest on the Certificates is excludable from gross income for federal income tax purposes under existing law and the Certificates are not "private activity bonds." See "TAX MATTERS – TAX EXEMPTION" herein for a discussion of the opinion of Bond Counsel, including a description of alternative minimum tax consequences for corporations.

**THE CERTIFICATES WILL BE DESIGNATED AS "QUALIFIED TAX-EXEMPT OBLIGATIONS"
FOR FINANCIAL INSTITUTIONS**

\$2,455,000*
CITY OF CLEVELAND, TEXAS
(Liberty and Montgomery Counties)
COMBINATION TAX AND REVENUE
CERTIFICATES OF OBLIGATION, SERIES 2012A

Dated Date: December 1, 2012

Due: March 1, as shown below

PAYMENT TERMS . . . Interest on the \$2,455,000* City of Cleveland, Texas, Combination Tax and Revenue Certificates of Obligation, Series 2012A (the "Certificates") will accrue from December 1, 2012 (the "Dated Date"), and will be payable September 1 and March 1 of each year commencing March 1, 2013, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The definitive Certificates will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company ("DTC") pursuant to the Book-Entry-Only System described herein. Beneficial ownership of the Certificates may be acquired in denominations of \$5,000 or integral multiples thereof. **No physical delivery of the Certificates will be made to the owners thereof.** Principal of, premium, if any, and interest on the Certificates will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Certificates. See "THE CERTIFICATES - BOOK-ENTRY-ONLY SYSTEM" herein. The initial Paying Agent/Registrar is The Bank of New York Mellon Trust Company, N.A., Dallas, Texas (see "THE CERTIFICATES - PAYING AGENT/REGISTRAR").

AUTHORITY FOR ISSUANCE . . . The Certificates are issued pursuant to the Constitution and general laws of the State of Texas (the "State"), particularly Subchapter C of Chapter 271, Texas Local Government Code, as amended, and an ordinance adopted by the City Council of the City (the "Ordinance") and constitute direct obligations of the City of Cleveland, Texas (the "City"), payable from a combination of (i) the levy and collection of an annual ad valorem tax, within the limits prescribed by law, on all taxable property within the City, and (ii) a limited pledge, in an amount not to exceed \$1,000, of a subordinate lien on certain net revenues of the waterworks and sanitary sewer system of the City as provided in the Ordinance (see "THE CERTIFICATES - AUTHORITY FOR ISSUANCE").

PURPOSE . . . Proceeds from the sale of the Certificates will be used (i) to pay for all or any part of the costs associated with the construction of improvements to and the rehabilitation and equipment of the City's waterworks and sanitary sewer system and (ii) to pay the costs associated with the issuance of the Certificates.

SEE MATURITY SCHEDULE ON THE INSIDE COVER

OPTIONAL REDEMPTION . . . The City reserves the right, at its option, to redeem Certificates having stated maturities on and after March 1, 2022, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on March 1, 2021, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption (see "THE CERTIFICATES - OPTIONAL REDEMPTION").

MANDATORY SINKING FUND REDEMPTION . . . In addition to the foregoing optional redemption provision, if principal amounts designated in the serial maturity schedule on the inside cover page hereof are combined to create one or more Term Certificates, each such Term Certificate shall be subject to mandatory sinking fund redemption commencing on March 1 of the first year which has been combined to form such Term Certificate and continuing on March 1 in each year thereafter until the stated maturity date of such Term Certificate, and the amount required to be redeemed in any year shall be equal to the principal amount for such year set forth in the serial maturity schedule on the inside cover page hereof. Term Certificates to be redeemed in any year by mandatory sinking fund redemption shall be redeemed at par and shall be selected by lot from and among the Term Certificates then subject to redemption. The City, at its option, may credit against any mandatory sinking fund redemption requirement Term Certificates of the maturity then subject to redemption which have been purchased and canceled by the City or have been redeemed and not theretofore applied as a credit against any mandatory sinking fund redemption requirement. (See "THE CERTIFICATES – MANDATORY SINKING FUND REDEMPTION.")

LEGALITY . . . The Certificates are offered for delivery when, as and if issued and received by the underwriter listed below (the "Underwriter") and subject to the approving opinion of the Attorney General of Texas and the opinion of Bracewell and Giuliani LLP, Bond Counsel, Houston, Texas (see Appendix C – Form of Bond Counsel's Opinion"). Certain legal matters will be passed upon for the Underwriter by Petruska & Associates, PLLC, Dallas, Texas, counsel for the Underwriter.

DELIVERY . . . It is expected that the Certificates will be available for delivery through The Depository Trust Company on December 11, 2012.

SOUTHWEST SECURITIES

* Preliminary, subject to change.

MATURITY SCHEDULE*

Maturity	Principal*	Rate	Price or Yield ⁽¹⁾	CUSIP ⁽²⁾	Maturity	Principal*	Rate	Price or Yield ⁽¹⁾	CUSIP ⁽²⁾
March 1					March 1				
2014	\$ 100,000				2024 ⁽³⁾	\$ 120,000			
2015	100,000				2025 ⁽³⁾	125,000			
2016	100,000				2026 ⁽³⁾	125,000			
2017	105,000				2027 ⁽³⁾	130,000			
2018	105,000				2028 ⁽³⁾	135,000			
2019	110,000				2029 ⁽³⁾	140,000			
2020	110,000				2030 ⁽³⁾	145,000			
2021	110,000				2031 ⁽³⁾	150,000			
2022 ⁽³⁾	115,000				2032 ⁽³⁾	155,000			
2023 ⁽³⁾	115,000				2033 ⁽³⁾	160,000			

(Accrued Interest from December 1, 2012 to be added)

* Preliminary, subject to change.

- (1) The initial reoffering prices or yields on the Certificates are furnished by the Underwriter and represent the initial offering prices or yields to the public, which may be changed by the Underwriter at any time.
- (2) CUSIP numbers have been assigned to the Certificates by the CUSIP Global Services managed by Standard & Poor's Financial Services LLC on behalf of The American Banker's Association, and are included solely for the convenience of the owners of the Certificates. Neither the City nor the Underwriter is responsible for the selection or correctness of the CUSIP numbers set forth herein.
- (3) The City reserves the right, at its option, to redeem Certificates having stated maturities on and after March 1, 2022, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on March 1, 2021, or any date thereafter, at the par value thereof plus accrued interest from the most recent interest payment date to the date of redemption.

For purposes of compliance with Rule 15c2-12 of the Securities and Exchange Commission, this document constitutes an Official Statement of the City with respect to the Certificates that has been "deemed final" by the City as of its date except for the omission of no more than the information permitted by Rule 15c2-12.

This Official Statement, which includes the cover page and the Appendices hereto, does not constitute an offer to sell or the solicitation of an offer to buy in any jurisdiction to any person to whom it is unlawful to make such offer, solicitation or sale.

No dealer, broker, salesperson or other person has been authorized to give information or to make any representation other than those contained in this Official Statement, and, if given or made, such other information or representations must not be relied upon.

The information set forth herein has been obtained from the City and other sources believed to be reliable, but such information is not guaranteed as to accuracy or completeness and is not to be construed as the promise or guarantee of the Financial Advisor or the Underwriter. This Official Statement contains, in part, estimates and matters of opinion which are not intended as statements of fact, and no representation is made as to the correctness of such estimates and opinions, or that they will be realized.

The information and expressions of opinion contained herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the City or other matters described herein.

All of the summaries of the statutes, ordinances, contracts, audited financial statements, engineering and related reports set forth in this Official Statement are made subject to all of the provisions of such documents. These summaries do not purport to be complete statements of such provisions, and reference is made to such documents, copies of which are available from the City.

The Underwriter has provided the following sentence for inclusion in this Official Statement. The Underwriter has reviewed the information in this Official Statement in accordance with, and as part of its responsibilities to investors under federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information.

NEITHER THE CITY, THE FINANCIAL ADVISOR, THE UNDERWRITER NOR BOND COUNSEL MAKE ANY REPRESENTATION OR WARRANTY WITH RESPECT TO THE INFORMATION CONTAINED IN THIS OFFICIAL STATEMENT REGARDING DTC OR ITS BOOK-ENTRY-ONLY SYSTEM.

THE COVER PAGE CONTAINS CERTAIN INFORMATION FOR GENERAL REFERENCE ONLY AND IS NOT INTENDED AS A SUMMARY OF THIS OFFERING. INVESTORS SHOULD READ THIS ENTIRE OFFICIAL STATEMENT, INCLUDING THE ATTACHED APPENDICES, TO OBTAIN INFORMATION ESSENTIAL TO MAKING AN INFORMED INVESTMENT DECISION.

THE CERTIFICATES HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, IN RELIANCE UPON AN EXEMPTION CONTAINED IN SUCH ACT. THE REGISTRATION OR QUALIFICATION OF THE CERTIFICATES IN ACCORDANCE WITH APPLICABLE PROVISIONS OF SECURITIES LAW OF THE STATES IN WHICH THE CERTIFICATES HAVE BEEN REGISTERED OR QUALIFIED AND THE EXEMPTION FROM REGISTRATION OR QUALIFICATION IN OTHER STATES CANNOT BE REGARDED AS A RECOMMENDATION THEREOF.

THIS OFFICIAL STATEMENT CONTAINS "FORWARD-LOOKING" STATEMENTS WITHIN THE MEANING OF SECTION 21E OF THE SECURITIES AND EXCHANGE ACT OF 1934, AS AMENDED. SUCH STATEMENTS MAY INVOLVE KNOWN AND UNKNOWN RISKS, UNCERTAINTIES AND OTHER FACTORS WHICH MAY CAUSE THE ACTUAL RESULTS, PERFORMANCE AND ACHIEVEMENTS TO BE DIFFERENT FROM THE FUTURE RESULTS, PERFORMANCE AND ACHIEVEMENTS EXPRESSED OR IMPLIED BY SUCH FORWARD-LOOKING STATEMENTS. INVESTORS ARE CAUTIONED THAT THE ACTUAL RESULTS COULD DIFFER MATERIALLY FROM THOSE SET FORTH IN THE FORWARD-LOOKING STATEMENTS.

TABLE OF CONTENTS

<p>MATURITY SCHEDULE2</p> <p>OFFICIAL STATEMENT SUMMARY5</p> <p style="padding-left: 20px;">SELECTED FINANCIAL INFORMATION6</p> <p style="padding-left: 20px;">GENERAL FUND CONSOLIDATED STATEMENT SUMMARY6</p> <p>CITY OFFICIALS, STAFF AND CONSULTANTS7</p> <p>INTRODUCTION8</p> <p style="padding-left: 20px;">DESCRIPTION OF THE CITY8</p> <p>THE CERTIFICATES8</p> <p style="padding-left: 20px;">DESCRIPTION OF THE CERTIFICATES8</p> <p style="padding-left: 20px;">AUTHORITY FOR ISSUANCE8</p> <p style="padding-left: 20px;">SECURITY AND SOURCE OF PAYMENT8</p> <p style="padding-left: 20px;">TAX RATE LIMITATION9</p> <p style="padding-left: 20px;">OPTIONAL REDEMPTION9</p> <p style="padding-left: 20px;">MANDATORY SINKING FUND REDEMPTION9</p> <p style="padding-left: 20px;">NOTICE OF REDEMPTION9</p> <p style="padding-left: 20px;">DEFEASANCE9</p> <p style="padding-left: 20px;">BOOK-ENTRY-ONLY SYSTEM10</p> <p style="padding-left: 20px;">PAYING AGENT/REGISTRAR11</p> <p style="padding-left: 20px;">TRANSFER, EXCHANGE AND REGISTRATION11</p> <p style="padding-left: 20px;">RECORD DATE FOR INTEREST PAYMENT12</p> <p style="padding-left: 20px;">BONDHOLDERS’ REMEDIES12</p> <p style="padding-left: 20px;">SOURCES AND USE OF CERTIFICATE PROCEEDS12</p> <p>TAX INFORMATION13</p> <p style="padding-left: 20px;">AD VALOREM TAX LAW13</p> <p style="padding-left: 20px;">EFFECTIVE TAX RATE AND ROLLBACK TAX RATE14</p> <p style="padding-left: 20px;">PROPERTY ASSESSMENT AND TAX PAYMENT14</p> <p style="padding-left: 20px;">PENALTIES AND INTEREST15</p> <p style="padding-left: 20px;">CITY APPLICATION OF TAX CODE15</p> <p style="padding-left: 20px;">TABLE 1 - VALUATION, EXEMPTIONS AND GENERAL OBLIGATION DEBT16</p> <p style="padding-left: 20px;">TABLE 2 - TAXABLE ASSESSED VALUATIONS BY CATEGORY .17</p> <p style="padding-left: 20px;">TABLE 3 - VALUATION AND GENERAL OBLIGATION DEBT HISTORY18</p> <p style="padding-left: 20px;">TABLE 4 - TAX RATE, LEVY AND COLLECTION HISTORY18</p> <p style="padding-left: 20px;">TABLE 5 - TEN LARGEST TAXPAYERS18</p> <p style="padding-left: 20px;">TABLE 6 - TAX ADEQUACY19</p> <p style="padding-left: 20px;">TABLE 7 - ESTIMATED OVERLAPPING DEBT19</p> <p>DEBT INFORMATION20</p> <p style="padding-left: 20px;">TABLE 8 - PRO-FORMA GENERAL OBLIGATION DEBT SERVICE REQUIREMENTS20</p> <p style="padding-left: 20px;">TABLE 9 - INTEREST AND SINKING FUND BUDGET PROJECTION21</p> <p style="padding-left: 20px;">TABLE 10 - COMPUTATION OF SELF-SUPPORTING DEBT21</p> <p style="padding-left: 20px;">AUTHORIZED BUT UNISSUED GENERAL OBLIGATION BONDS ..21</p> <p style="padding-left: 20px;">TABLE 11 - OTHER OBLIGATIONS21</p> <p style="padding-left: 20px;">PENSION FUND22</p> <p style="padding-left: 20px;">OTHER POST-EMPLOYMENT BENEFITS22</p>	<p>FINANCIAL INFORMATION 23</p> <p style="padding-left: 20px;">TABLE 12 - CHANGES IN NET ASSETS 23</p> <p style="padding-left: 20px;">TABLE 12A - GENERAL FUND REVENUES AND EXPENDITURE HISTORY 24</p> <p style="padding-left: 20px;">TABLE 13 - MUNICIPAL SALES TAX HISTORY 25</p> <p style="padding-left: 20px;">INVESTMENTS 25</p> <p style="padding-left: 20px;">LEGAL INVESTMENTS 25</p> <p style="padding-left: 20px;">INVESTMENT POLICIES 26</p> <p style="padding-left: 20px;">ADDITIONAL PROVISIONS 26</p> <p style="padding-left: 20px;">TABLE 14 - CURRENT INVESTMENTS 27</p> <p>TAX MATTERS 27</p> <p style="padding-left: 20px;">TAX EXEMPTION 27</p> <p style="padding-left: 20px;">PURCHASE OF TAX-EXEMPT OBLIGATIONS BY FINANCIAL INSTITUTIONS 28</p> <p style="padding-left: 20px;">ADDITIONAL FEDERAL INCOME TAX CONSIDERATIONS 28</p> <p style="padding-left: 20px;">TAX LEGISLATIVE CHANGES 29</p> <p>OTHER INFORMATION 29</p> <p style="padding-left: 20px;">RATINGS 29</p> <p style="padding-left: 20px;">LITIGATION 29</p> <p style="padding-left: 20px;">REGISTRATION AND QUALIFICATION OF CERTIFICATES FOR SALE 29</p> <p style="padding-left: 20px;">LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS 30</p> <p style="padding-left: 20px;">LEGAL MATTERS 30</p> <p style="padding-left: 20px;">AUTHENTICITY OF FINANCIAL DATA AND OTHER INFORMATION 30</p> <p>CONTINUING DISCLOSURE OF INFORMATION 30</p> <p style="padding-left: 20px;">ANNUAL REPORTS 31</p> <p style="padding-left: 20px;">NOTICE OF CERTAIN EVENTS 31</p> <p style="padding-left: 20px;">LIMITATIONS AND AMENDMENTS 31</p> <p style="padding-left: 20px;">COMPLIANCE WITH PRIOR UNDERTAKINGS 32</p> <p>MISCELLANEOUS 32</p> <p style="padding-left: 20px;">FINANCIAL ADVISOR 32</p> <p style="padding-left: 20px;">UNDERWRITER 32</p> <p style="padding-left: 20px;">FORWARD-LOOKING STATEMENTS DISCLAIMER 32</p> <p>APPENDICES</p> <p style="padding-left: 20px;">GENERAL INFORMATION REGARDING THE CITY A</p> <p style="padding-left: 20px;">EXCERPTS FROM THE ANNUAL FINANCIAL REPORT B</p> <p style="padding-left: 20px;">FORM OF BOND COUNSEL’S OPINION C</p> <p>The cover page hereof, this page, the appendices included herein and any addenda, supplement or amendment hereto, are part of this Official Statement.</p>
--	--

OFFICIAL STATEMENT SUMMARY

This summary is subject in all respects to the more complete information and definitions contained or incorporated in this Official Statement. The offering of the Certificates to potential investors is made only by means of this entire Official Statement. No person is authorized to detach this summary from this Official Statement or to otherwise use it without this entire Official Statement.

- THE CITY**..... The City of Cleveland is a political subdivision and municipal corporation of the State, located in Liberty and Montgomery Counties, Texas. The City covers approximately 4.81 square miles (see "INTRODUCTION - DESCRIPTION OF CITY").
- THE CERTIFICATES** The Certificates are issued as \$2,455,000* Combination Tax and Revenue Certificates of Obligation, Series 2012A. The Certificates are issued as serial certificates maturing 2014 through 2033, inclusive, unless the Underwriter designates one or more maturities as a Term Certificate (see "THE CERTIFICATES -DESCRIPTION OF THE CERTIFICATES" and "- MANDATORY SINKING FUND REDEMPTION").
- PAYMENT OF INTEREST** Interest on the Certificates accrues from December 1, 2012, and is payable March 1, 2013, and each March 1 and September 1 thereafter until maturity or prior redemption (see "THE CERTIFICATES - DESCRIPTION OF THE CERTIFICATES" and "THE CERTIFICATES - OPTIONAL REDEMPTION").
- AUTHORITY FOR ISSUANCE** The Certificates are issued pursuant to the general laws of the State, particularly Subchapter C of Chapter 271, Texas Local Government Code, as amended, and an Ordinance passed by the City Council of the City (see "THE CERTIFICATES - AUTHORITY FOR ISSUANCE").
- SECURITY FOR THE CERTIFICATES** The Certificates constitute direct obligations of the City, payable from a combination of (i) the levy and collection of an annual ad valorem tax, within the limits prescribed by law, on all taxable property within the City, and (ii) a limited pledge of a subordinate lien on certain net revenues of the waterworks and sanitary sewer system of the City (see "THE CERTIFICATES - SECURITY AND SOURCE OF PAYMENT").
- REDEMPTION** The City reserves the right, at its option, to redeem Certificates having stated maturities on and after March 1, 2022, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on March 1, 2021, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption. Additionally, the Certificates may be subject to mandatory redemption in the event the Underwriter elects to aggregate one or more maturities as a Term Certificate (see "THE CERTIFICATES - MANDATORY SINKING FUND REDEMPTION").
- TAX EXEMPTION** In the opinion of Bond Counsel, the interest on the Certificates is excludable from gross income for federal income tax purposes under existing law and the Certificates are not "private activity bonds." See "TAX MATTERS - TAX EXEMPTION" for a discussion of the opinion of Bond Counsel including a description of alternative minimum tax consequences for corporations.
- QUALIFIED TAX-EXEMPT OBLIGATIONS**..... The City will designate the Certificates as "qualified tax-exempt obligations" for financial institutions (see "TAX MATTERS - PURCHASE OF TAX-EXEMPT OBLIGATIONS BY FINANCIAL INSTITUTIONS").
- USE OF PROCEEDS** Proceeds from the sale of the Certificates will be used (i) to pay for all or any part of the costs associated with the construction of improvements to and the rehabilitation and equipment of the City's waterworks and sanitary sewer system and (ii) to pay the costs associated with the issuance of the Certificates.
- RATINGS** The Bonds have been rated "A2" by Moody's Investors Service, Inc. ("Moody's"). The presently outstanding tax supported debt of the City is rated "A2" by Moody's and "A-" by Standard & Poor's Ratings Services, a Standard & Poor's Financial Services LLC business ("S&P"), without regard to credit enhancement. (See "OTHER INFORMATION - RATINGS").
- BOOK-ENTRY-ONLY SYSTEM**..... The definitive Certificates will be initially registered and delivered only to Cede & Co., the nominee of DTC pursuant to the Book-Entry-Only System described herein. Beneficial ownership of the Certificates may be acquired in denominations of \$5,000 or integral multiples thereof. No physical delivery of the Certificates will be made to the beneficial owners thereof. Principal of, premium, if any, and interest on the Certificates will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Certificates (see "THE CERTIFICATES - BOOK-ENTRY-ONLY SYSTEM").
- PAYMENT RECORD** The City has never defaulted in payment of its general obligation tax debt.

* Preliminary, subject to change.

SELECTED FINANCIAL INFORMATION

Fiscal Year Ended 9/30	Estimated City Population ⁽¹⁾	Taxable Assessed Valuation ⁽²⁾	Per Capita Taxable Assessed Valuation	General Obligation (G.O.) Tax Debt ⁽³⁾	Per Capita G.O. Tax Debt	Ratio Tax Debt to Taxable Assessed Valuation	Percent Of Total Tax Collections
2008	7,605	\$ 280,734,243	\$ 36,914	\$ 8,140,000	\$ 1,070	2.90%	98.51%
2009	7,605	300,068,613	39,457	8,390,000	1,103	2.80%	97.27%
2010	7,675	323,275,945	42,121	8,045,000	1,048	2.49%	95.14% ⁽⁶⁾
2011	7,675	326,210,866	42,503	10,045,000	1,309	3.08%	93.60% ⁽⁶⁾
2012	7,675	334,736,518	43,614	13,345,000	1,739	3.99%	97.28% ⁽⁶⁾⁽⁷⁾
2013	7,695	333,423,632 ⁽⁴⁾	43,330	14,940,000 ⁽⁵⁾	1,942	4.48%	⁽⁸⁾

- (1) Actual 2000 Census population data held constant for years 2008 and 2009 and actual 2010 Census population data held constant for years 2010 through 2013.
- (2) As reported by the Montgomery County and Liberty County Appraisal Districts, subject to change during the ensuing year.
- (3) Includes self-supporting debt. See "TABLE 10 – COMPUTATION OF SELF SUPPORTING DEBT".
- (4) Includes \$8,267,928 of uncertified value that is subject to change due to protest and arbitration process.
- (5) Projected, includes the Certificates.
- (6) Decrease in taxes paid due to the general downturn in the economy and a principal taxpayer that filed for bankruptcy. See "TABLE 5 – TEN LARGEST TAXPAYERS."
- (7) Collections through August 31, 2012.
- (8) The 2012 tax year began October 1, 2012. Taxes are due January 31, 2013.

GENERAL FUND CONSOLIDATED STATEMENT SUMMARY

	For Fiscal Year Ended September 30				
	2012 ⁽¹⁾	2011	2010	2009	2008
Beginning Balance	\$ 740,807	\$ 896,401	\$ 799,441	\$ 679,712	\$ 559,110
Total Revenue	5,039,361	7,048,387	6,513,731	6,117,262	6,773,505
Total Expenditures	(5,125,408)	(7,783,133)	(6,944,459)	(6,431,792)	(7,016,307)
Other Financing Sources (Uses)	489,750	579,152	527,688	551,859	363,404
Prior Period Adjustment		-	-	(117,600)	-
Ending Balance	\$ 740,807	\$ 896,401	\$ 799,441	\$ 679,712	\$ 679,712

(1) Unaudited, provided by the City as of August 31, 2012.

For additional information regarding the City, please contact:

Mr. Dion Miller
 City of Cleveland
 907 E. Houston Street
 Cleveland, Texas 77327
 (281) 592-2667

or

Mr. Joe Morrow
 First Southwest Company
 700 Milam Street, Suite 500
 Houston, Texas 77002
 (713) 654-8690

CITY OFFICIALS, STAFF AND CONSULTANTS

ELECTED OFFICIALS

City Council	Term Expires	Occupation
Jill Kirkonis, Mayor	May 2013	Owner, J&B Medical
Niki Coats, Position 1/Mayor Pro-Tem	May 2013	Owner, Construction Company
Brian C. Eoff, Position 2	May 2013	Self Employed
Carolyn McWaters, Position 3	May 2014	Retired
Jorge Cuellar, Position 4	May 2014	Sam's Warehouse
Delores Terry, Position 5	May 2014	Teacher's Aide

SELECTED ADMINISTRATIVE STAFF

Name	Position	Length of Service to City
Dion Miller ⁽¹⁾	City Manager	< 1 Year
Kelly McDonald	City Secretary	20 Years
Becky Roseberry	Director of Finance	6.5 Years
Mike Ulbig	Public Works Director	8 Years
Darrel Broussard ⁽²⁾	Police Chief	25 Years
David Olson	City Attorney	15.5 Years

(1) Mr. Miller started his position with the City on February 21, 2012. He has 25 years of experience in municipal government.
 (2) Mr. Broussard has served on the police force of the City since 1987 and became Chief of Police during 2012.

CONSULTANTS AND ADVISORS

Auditors	Hereford, Lynch, Sellars & Kirkham Cleveland, Texas
Bond Counsel.....	Bracewell & Giuliani LLP Houston, Texas
Financial Advisor.....	First Southwest Company Houston, Texas

PRELIMINARY OFFICIAL STATEMENT
RELATING TO
CITY OF CLEVELAND, TEXAS
\$2,455,000*
COMBINATION TAX AND REVENUE
CERTIFICATES OF OBLIGATION, SERIES 2012A

INTRODUCTION

This Official Statement, which includes the Appendices hereto, provides certain information regarding the issuance of \$2,455,000* City of Cleveland, Texas, Combination Tax and Revenue Certificates of Obligation, Series 2012A. Capitalized terms used in this Official Statement have the same meanings assigned to such terms in the ordinance to be adopted on the date of sale of the Certificates which will authorize the issuance of the Certificates (the "Ordinance"), except as otherwise indicated herein.

There follows in this Official Statement descriptions of the Certificates and certain information regarding the City and its finances. All descriptions of documents contained herein are only summaries and are qualified in their entirety by reference to each such document. Copies of such documents may be obtained from the City's Financial Advisor, First Southwest Company, Houston, Texas.

DESCRIPTION OF THE CITY

The City is a political subdivision and municipal corporation of the State of Texas (the "State"), duly organized and existing under the laws of the State, including the City's Home Rule Charter. The City was incorporated in 1935, and first adopted its Home Rule Charter in 1981. The City operates under a Council/Manager form of government with a City Council comprised of the Mayor and five Councilmembers. The term of office is two years with the terms of the Mayor and two of the Councilmembers' terms expiring in odd-numbered years and the terms of the other three Councilmembers expiring in even-numbered years. The City Manager is the chief administrative officer for the City. Some of the services that the City provides are: public safety, streets, waterworks and sanitary sewer utilities, recreation, public improvements, planning and zoning, and general administrative services. The 2010 Census population for the City was 7,675. The City covers approximately 4.81 square miles.

THE CERTIFICATES

DESCRIPTION OF THE CERTIFICATES

The Certificates are dated December 1, 2012, and mature on March 1 in each of the years and in the amounts shown on the cover page hereof. Interest will be computed on the basis of a 360-day year of twelve 30-day months, and will be payable on September 1 and March 1, commencing March 1, 2013. The definitive Certificates will be issued only in fully registered form in any integral multiple of \$5,000 for any one maturity and will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company ("DTC") pursuant to the Book-Entry-Only System described herein. **No physical delivery of the Certificates will be made to the owners thereof.** Principal of, premium, if any, and interest on the Certificates will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Certificates. See "BOOK-ENTRY-ONLY SYSTEM" herein.

AUTHORITY FOR ISSUANCE

The Certificates are being issued pursuant to the Constitution and general laws of the State of Texas, particularly Subchapter C of Chapter 271, Texas Local Government Code, as amended, and the Ordinance.

SECURITY AND SOURCE OF PAYMENT

The Certificates are payable from and secured by a combination of (i) the levy and collection of an annual ad valorem tax, within the limits prescribed by law, on all taxable property within the City, and (ii) a limited pledge, in the amount not to exceed \$1,000, of a subordinate lien on certain net revenues of the waterworks and sanitary sewer system of the City as provided in the Ordinance.

TAX RATE LIMITATION

All taxable property within the City is subject to the assessment, levy and collection by the City of a continuing, direct annual ad valorem tax sufficient to provide for the payment of principal of and interest on all ad valorem tax debt within the limits prescribed by law. Article XI, Section 5, of the Texas Constitution is applicable to the City, and limits its maximum ad valorem tax rate to \$2.50 per \$100 Taxable Assessed Valuation for all City purposes. The Home Rule Charter of the City adopts the constitutionally authorized maximum tax rate of \$2.50 per \$100 Taxable Assessed Valuation. Administratively, the Attorney General of the State of Texas will permit allocation of \$1.50 of the \$2.50 maximum tax rate for all general obligation debt service, as calculated at the time of issuance of new money obligations.

OPTIONAL REDEMPTION

The City reserves the right, at its option, to redeem Certificates having stated maturities on and after March 1, 2022, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on March 1, 2021, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption. If less than all of the Certificates are to be redeemed, the City may select the maturities of Certificates to be redeemed. If less than all the Certificates of any maturity are to be redeemed, the Paying Agent/Registrar (or DTC while the Certificates are in Book-Entry-Only form) shall determine by lot the Certificates, or portions thereof, within such maturity to be redeemed. If a Certificate (or any portion of the principal sum thereof) shall have been called for redemption and notice of such redemption shall have been given, such Certificate (or the principal amount thereof to be redeemed) shall become due and payable on such redemption date and interest thereon shall cease to accrue from and after the redemption date, provided funds for the payment of the redemption price and accrued interest thereon are held by the Paying Agent/Registrar on the redemption date.

MANDATORY SINKING FUND REDEMPTION

In addition to the foregoing optional redemption provision, if principal amounts designated in the serial maturity schedule on the inside cover page hereof are combined to create Term Certificates, each such Term Certificate shall be subject to mandatory sinking fund redemption commencing on March 1 of the first year which has been combined to form such Term Certificate and continuing on March 1 in each year thereafter until the stated maturity date of such Term Certificate. The Paying Agent/Registrar will select by lot or by any other customary method that results in a random selection the specific Term Certificates (or with respect to Term Certificates having a denomination in excess of \$5,000, each \$5,000 portion thereof) to be redeemed by mandatory redemption. The principal amount of Term Certificates required to be redeemed on any redemption date pursuant to the foregoing mandatory sinking fund redemption provisions hereof shall be reduced, at the option of the City, by the principal amount of any Term Certificates which, at least forty-five (45) days prior to the mandatory sinking fund redemption date (i) shall have been acquired by the City at a price not exceeding the principal amount of such Term Certificates plus accrued interest to the date of purchase thereof, and delivered to the Paying Agent/Registrar for cancellation, or (ii) shall have been redeemed pursuant to the optional redemption provisions hereof and not previously credited to a mandatory sinking fund redemption.

NOTICE OF REDEMPTION

Not less than 30 days prior to a redemption date for the Certificates, the City shall cause a notice of redemption to be sent by United States mail, first class, postage prepaid, to the registered owners of the Certificates to be redeemed, in whole or in part, at the address of the registered owner appearing on the registration books of the Paying Agent/Registrar at the close of business on the business day next preceding the date of mailing such notice. ANY NOTICE SO MAILED SHALL BE CONCLUSIVELY PRESUMED TO HAVE BEEN DULY GIVEN, WHETHER OR NOT THE REGISTERED OWNER RECEIVES SUCH NOTICE. NOTICE HAVING BEEN SO GIVEN, THE CERTIFICATES CALLED FOR REDEMPTION SHALL BECOME DUE AND PAYABLE ON THE SPECIFIED REDEMPTION DATE, AND NOTWITHSTANDING THAT ANY CERTIFICATE OR PORTION THEREOF HAS NOT BEEN SURRENDERED FOR PAYMENT, INTEREST ON SUCH CERTIFICATE OR PORTION THEREOF SHALL CEASE TO ACCRUE.

The City reserves the right, in the case of a redemption, to give notice of its election or direction to redeem Certificates conditioned upon the occurrence of subsequent events. Such notice may state (i) that the redemption is conditioned upon the deposit of moneys and/or authorized securities, in an amount equal to the amount necessary to effect the redemption, with the Paying Agent/Registrar, or such other entity as may be authorized by law, no later than the redemption date, or (ii) that the City retains the right to rescind such notice at any time on or prior to the scheduled redemption date if the City delivers a certificate of the City to the Paying Agent/Registrar instructing the Paying Agent/Registrar to rescind the redemption notice and such notice and redemption shall be of no effect if such moneys and/or authorized securities are not so deposited or if the notice is rescinded. The Paying Agent/Registrar shall give prompt notice of any such rescission of a conditional notice of redemption to the affected Owners. Any Certificate that is subject to conditional redemption and such redemption has been rescinded shall remain outstanding.

DEFEASANCE

The Ordinance provides that the City may defease, refund or discharge the Certificates in any manner now or hereafter permitted by law.

BOOK-ENTRY-ONLY SYSTEM

This section describes how ownership of the Certificates is to be transferred and how the principal of, premium, if any, and interest on the Certificates are to be paid to and credited by The Depository Trust Company ("DTC"), New York, New York, while the Certificates are registered in its nominee name. The information in this section concerning DTC and the Book-Entry-Only System has been provided by DTC for use in disclosure documents such as this Official Statement. The City believes the source of such information to be reliable, but takes no responsibility for the accuracy or completeness thereof.

The City cannot and does not give any assurance that (1) DTC will distribute payments of debt service on the Certificates, or redemption or other notices, to DTC Participants, (2) DTC Participants or others will distribute debt service payments paid to DTC or its nominee (as the registered owner of the Certificates), or redemption or other notices, to the Beneficial Owners, or that they will do so on a timely basis, or (3) DTC will serve and act in the manner described in this Official Statement. The current rules applicable to DTC are on file with the Securities and Exchange Commission, and the current procedures of DTC to be followed in dealing with DTC Participants are on file with DTC.

The Depository Trust Company ("DTC") New York, New York, will act as securities depository for the Certificates. The Certificates will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered security certificate will be issued for each maturity of the Certificates, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC, the world's largest depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing City ("DTCC"). DTCC is the holding company for DTC, National Securities Clearing City and Fixed Income Clearing City, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing companies that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has a Standard & Poor's rating of "AA+." The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com and www.dtc.org.

Purchases of Certificates under the DTC system must be made by or through Direct Participants, which will receive a credit for the Certificates on DTC's records. The ownership interest of each actual purchaser of each Obligation ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Certificates are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Certificates, except in the event that use of the book-entry system for the Certificates is discontinued.

To facilitate subsequent transfers, all Certificates deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Certificates with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Certificates; DTC's records reflect only the identity of the Direct Participants to whose accounts such Certificates are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of Certificates may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Certificates, such as redemptions, tenders, defaults, and proposed amendments to the Certificate documents. For example, Beneficial Owners of Certificates may wish to ascertain that the nominee holding the Certificates for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the register and request that copies of the notices be provided directly to them.

Redemption notices for the Certificates shall be sent to DTC. If less than all of the Certificates of a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such maturity to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Certificates unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the City as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Certificates are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Certificates will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or the Paying Agent/Registrar of each series, on the payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC nor its nominee, the Paying Agent/Registrar of each series, or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, principal and interest payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or Paying Agent/Registrar of each series, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

Use of Certain Terms in Other Sections of this Official Statement . . . In reading this Official Statement it should be understood that while the Certificates are in the Book-Entry-Only System, references in other sections of this Official Statement to registered owners should be read to include the person for which the Participant acquires an interest in the Certificates, but (i) all rights of ownership must be exercised through DTC and the Book-Entry-Only System, and (ii) except as described above, notices that are to be given to registered owners under the Ordinance will be given only to DTC.

Information concerning DTC and the Book-Entry-Only System has been obtained from DTC and is not guaranteed as to accuracy or completeness by, and is not to be construed as a representation by the City, the Financial Advisor, or the Underwriter.

Effect of Termination of Book-Entry-Only System . . . In the event that the Book-Entry-Only System of the Certificates is discontinued, printed Certificates will be issued to the DTC Participants or the holder, as the case may be, and such Certificates will be subject to transfer, exchange and registration provisions as set forth in the Ordinance and summarized under "The Certificates - Transfer, Exchange and Registration" below.

PAYING AGENT/REGISTRAR

The initial Paying Agent/Registrar is The Bank of New York Mellon Trust Company, N.A., Dallas, Texas. In the Ordinance, the City retains the right to replace the Paying Agent/Registrar and covenants to maintain and provide a Paying Agent/Registrar at all times until the Certificates are duly paid and any successor Paying Agent/Registrar shall be a commercial bank or trust company organized under the laws of the State of Texas or other entity duly qualified and legally authorized to serve as and perform the duties and services of Paying Agent/Registrar for the Certificates. Upon any change in the Paying Agent/Registrar for the Certificates, the City agrees to promptly cause a written notice thereof to be sent to each registered owner of the Certificates by United States mail, first class, postage prepaid, which notice shall also give the address of the new Paying Agent/Registrar.

TRANSFER, EXCHANGE AND REGISTRATION

In the event the Book-Entry-Only System is discontinued, the Certificates may be transferred and exchanged on the registration books of the Paying Agent/Registrar only upon presentation and surrender to the Paying Agent/Registrar and such transfer or exchange shall be without expense or service charge to the registered owner, except for any tax or other governmental charges required to be paid with respect to such registration, exchange and transfer. Certificates may be assigned by the execution of an assignment form on the respective Certificates or by other instrument of transfer and assignment acceptable to the Paying Agent/Registrar. New Certificates will be delivered by the Paying Agent/Registrar, in lieu of the Certificates being transferred or exchanged, at the designated office of the Paying Agent/Registrar, or sent by United States mail, first class, postage prepaid, to the new registered owner or his designee. To the extent possible, new Certificates issued in an exchange or transfer of Certificates will be delivered to the registered owner or assignee of the registered owner in not more than three business days after the receipt of the Certificates to be canceled, and the written instrument of transfer or request for exchange duly executed by the registered owner or his duly authorized agent, in form satisfactory to the Paying Agent/Registrar. New Certificates registered and delivered in an exchange or transfer shall be in any integral multiple of \$5,000 for any one maturity and for a like aggregate principal amount as the Certificates surrendered for exchange or transfer. See "Book-Entry-Only System" herein for a description of the system to be utilized initially in regard to ownership and transferability of the Certificates. Neither the City nor the Paying Agent/Registrar shall be required to transfer or exchange any Certificate called for redemption, in whole or in part, within 45 days of the date fixed for redemption; provided, however, such limitation of transfer shall not be applicable to an exchange by the registered owner of the uncalled balance of a Certificate.

RECORD DATE FOR INTEREST PAYMENT

The record date ("Record Date") for the interest payable on the Certificates on any interest payment date means the close of business on the 15th day of the preceding month. In the event of a non payment of interest on a scheduled payment date, and for 30 days thereafter, a new record date for such interest payment (a "Special Record Date") will be established by the Paying Agent/Registrar, if and when funds for the payment of such interest have been received from the City. Notice of the Special Record Date and of the scheduled payment date of the past due interest ("Special Payment Date", which shall be 15 days after the Special Record Date) shall be sent at least five business days prior to the Special Record Date by United States mail, first class postage prepaid, to the address of each Holder of a Certificate appearing on the registration books of the Paying Agent/Registrar at the close of business on the business day next preceding the date of mailing of such notice.

BONDHOLDERS' REMEDIES

The Ordinance does not provide for the appointment of a trustee to represent the interests of the holders of the Certificates upon any failure of the City to perform in accordance with the terms of the Ordinance or upon any other condition and, in the event of any such failure to perform, the registered owners would be responsible for the initiation and cost of any legal action to enforce performance of the Ordinance. Furthermore, the Ordinance does not establish specific events of default with respect to the Certificates and, under State law, there is no right to the acceleration of maturity of the Certificates upon the failure of the City to observe any covenant under the Ordinance. A registered owner of the Certificates could seek a judgment against the City if a default occurred in the payment of principal or interest on any such Certificate; however, such judgment could not be satisfied by execution against any property of the City and a suit for monetary damages could be vulnerable to the defense of sovereign immunity. A registered owner's only practical remedy, if a default occurs, is a mandamus or mandatory injunction proceeding to compel the City to levy, assess and collect an annual ad valorem tax sufficient to pay principal of and interest on the Certificates as it becomes due or perform other material terms and covenants contained in the Ordinance. However, the enforcement of any such remedy may be difficult and time consuming and a registered owner could be required to enforce such remedy on a periodic basis.

The City is also eligible to seek relief from its creditors under Chapter 9 of the U.S. Bankruptcy Code ("Chapter 9"). Although Chapter 9 provides for the recognition of a security interest represented by a specifically pledged source of revenues, the pledge of taxes in support of a general obligation of a bankrupt entity is not specifically recognized as a security interest under Chapter 9. Chapter 9 also includes an automatic stay provision that would prohibit, without Bankruptcy Court approval, the prosecution of any other legal action by creditors or Certificate holders of an entity which has sought protection under Chapter 9. Therefore, should the City avail itself of Chapter 9 protection from creditors, the ability to enforce would be subject to the approval of the Bankruptcy Court (which could require that the action be heard in Bankruptcy Court instead of another federal or state court); and the Bankruptcy Code provides for broad discretionary powers of a Bankruptcy Court in administering any proceeding brought before it. The opinion of Bond Counsel will note that all opinions relative to the enforceability of the Ordinance and the Certificates are qualified with respect to the customary rights of debtors relative to their creditors, including rights afforded to creditors under the Bankruptcy Code.

SOURCES AND USE OF CERTIFICATE PROCEEDS

Proceeds from the sale of the Certificates are expected to be expended as follows:

Sources of Funds	
Par Amount	
Net Premium	
Accrued Interest	
Total Sources	\$ <u> -</u>
 Uses of Funds	
Deposit to the Project Fund	
Deposit to I&S Fund	
Underwriter's Discount	
Costs of Issuance	
Total Uses of Funds	\$ <u> -</u>

TAX INFORMATION

AD VALOREM TAX LAW

The appraisal of property within the City is the responsibility of the Montgomery County and Liberty County Appraisal Districts (the "Appraisal Districts"). Excluding agricultural and open-space land, which may be taxed on the basis of productive capacity, the Appraisal Districts are required under the Property Tax Code to appraise all property within the Appraisal Districts on the basis of 100% of their market value and are prohibited from applying any assessment ratios. In determining market value of property, different methods of appraisal may be used, including the cost method of appraisal, the income method of appraisal and market data comparison method of appraisal, and the method considered most appropriate by the chief appraiser is to be used. State law further limits the appraised value of a residence homestead for a tax year to an amount that would not exceed the lesser of (1) the property's market value in the most recent tax year in which the market value was determined by the Appraisal Districts or (2) the sum of (a) 10% of the property's appraised value in the preceding tax year, plus (b) the property's appraised value the preceding tax year, plus (c) the market value of all new improvements to the property. The value placed upon property within the Appraisal Districts is subject to review by an Appraisal Review Board, consisting of five assessors appointed by the Boards of Directors of the Appraisal Districts. The Appraisal Districts are required to review the value of property within the Appraisal Districts at least every three years. The City may require annual review at its own expense, and is entitled to challenge the determination of appraised value of property within the City by petition filed with the Appraisal Review Board.

Reference is made to the Property Tax Code, for identification of property subject to taxation; property exempt or which may be exempted from taxation, if claimed; the appraisal of property for ad valorem taxation purposes; and the procedures and limitations applicable to the levy and collection of ad valorem taxes.

Article VIII of the State Constitution ("Article VIII") and State law provide for certain exemptions from property taxes, the valuation of agricultural and open-space lands at productivity value, and the exemption of certain personal property from ad valorem taxation.

Under Section 1-b, Article VIII, and State law, the governing body of a political subdivision, at its option, may grant: (1) An exemption of not less than \$3,000 of the market value of the residence homestead of persons 65 years of age or older and the disabled from all ad valorem taxes thereafter levied by the political subdivision; (2) An exemption of up to 20% of the market value of residence homesteads. The minimum exemption under this provision is \$5,000.

In the case of residence homestead exemptions granted under Section 1-b, Article VIII, ad valorem taxes may continue to be levied against the value of homesteads exempted where ad valorem taxes have previously been pledged for the payment of debt if cessation of the levy would impair the obligation of the contract by which the debt was created.

State law and Section 2, Article VIII, mandate an additional property tax exemption for disabled veterans or the surviving spouse or children of a deceased veteran who died while on active duty in the armed forces; the exemption applies to either real or personal property with the amount of assessed valuation exempted ranging from \$5,000 to a maximum of \$12,000; provided, however, that disabled veterans (and their surviving spouses) who receive from the United States Department of Veterans Affairs or its successor 100 percent disability compensation due to a service-connected disability and a rating of 100 percent disabled or of individual unemployability are entitled to an exemption from taxation of the total appraised value of the veteran's residence homestead.

Under Article VIII and State law, the governing body of a county, municipality or junior college district, may freeze the total amount of ad valorem taxes levied on the residence homestead of a disabled person or persons 65 years of age or older to the amount of taxes imposed in the year such residence qualified for such exemption. Also, upon receipt of a petition signed by five percent of the registered voters of the county, municipality or junior college district, an election must be held to determine by majority vote whether to establish such a limitation on taxes paid on residence homesteads of persons 65 years of age or who are disabled. Upon providing for such exemption, such freeze on ad valorem taxes is transferable to a different residence homestead and to a surviving spouse living in such homestead who is disabled or is at least 55 years of age. If improvements (other than maintenance or repairs) are made to the property, the value of the improvements is taxed at the then current tax rate, and the total amount of taxes imposed is increased to reflect the new improvements with the new amount of taxes then serving as the ceiling on taxes for the following years. Once established, the tax rate limitation may not be repeated or rescinded.

Article VIII provides that eligible owners of both agricultural land (Section 1-d) and open-space land (Section 1-d-1), including open-space land devoted to farm or ranch purposes or open-space land devoted to timber production, may elect to have such property appraised for property taxation on the basis of its productive capacity. The same land may not be qualified under both Section 1-d and 1-d-1.

Nonbusiness personal property, such as automobiles or light trucks, are exempt from ad valorem taxation unless the governing body of a political subdivision elects to tax this property. Boats owned as nonbusiness property are exempt from ad valorem taxation.

Article VIII, Section 1-j, provides for "freeport property" to be exempted from ad valorem taxation. Freeport property is defined as goods detained in Texas for 175 days or less for the purpose of assembly, storage, manufacturing, processing or fabrication. Decisions to continue to tax may be reversed in the future; decisions to exempt freeport property are not subject to reversal.

Article VIII, Section 1-n of the Texas Constitution provides for the exemption from taxation of "goods in transit." "Goods in transit" is defined by a provision in the Tax Code, which is effective for tax years 2008 and thereafter, as personal property acquired or imported into Texas and transported to another location in the State or outside of the State within 175 days of the date the property was acquired or imported into Texas. The exemption excludes oil, natural gas, petroleum products, aircraft and special inventory, including motor vehicle, vessel and out board motor, heavy equipment and manufactured housing inventory. The Tax Code provision permits local governmental entities, on a local option basis, to take official action by January 1 of the year preceding a tax year, after holding a public hearing, to tax goods in transit during the following tax year. A taxpayer may receive only one of the freeport exemptions or the goods in transit exemptions for items of personal property.

The City and the other taxing bodies within its territory may agree to jointly create tax increment financing zones, under which the tax values on property in the zone are "frozen" at the value of the property at the time of creation of the zone. The City also may enter into tax abatement agreements to encourage economic development. Under the agreements, a property owner agrees to construct certain improvements on its property. The City in turn agrees not to levy a tax on all or part of the increased value attributable to the improvements until the expiration of the agreement. The abatement agreement could last for a period of up to 10 years.

Cities are also authorized, pursuant to Chapter 380, Texas Local Government Code ("Chapter 380") to establish programs to promote state or local economic development and to stimulate business and commercial activity in the City. In accordance with a program established pursuant to Chapter 380, the City may make loans or grants of public fund for economic development purposes, however, no obligations secured by ad valorem taxes may be issued for such purposes unless approved by voters of the City.

EFFECTIVE TAX RATE AND ROLLBACK TAX RATE

By each September 1 or as soon thereafter as practicable, the City Council adopts a tax rate per \$100 taxable value for the current year. The City Council will be required to adopt the annual tax rate for the City before the later of September 30 or the 60th day after the date the certified appraisal roll is received by the City. If the City Council does not adopt a tax rate by such required date the tax rate for that tax year is the lower of the effective tax rate calculated for that tax year or the tax rate adopted by the City for the preceding tax year. The tax rate consists of two components: (1) a rate for funding of maintenance and operation expenditures, and (2) a rate for debt service.

Under the Property Tax Code, the City must annually calculate and publicize its "effective tax rate" and "rollback tax rate". Effective 2005, a tax rate cannot be adopted by the City Council that exceeds the lower of the rollback tax rate or the effective tax rate until two public hearings have been held on the proposed tax rate following notice of such public hearings (including the requirement that notice be posted on the City's website if the City owns, operates or controls an internet website and public notice be given by television if the City has free access to a television channel) and the City Council has otherwise complied with the legal requirements for the adoption of such tax rate. If the adopted tax rate exceeds the rollback tax rate the qualified voters of the City by petition may require that an election be held to determine whether or not to reduce the tax rate adopted for the current year to the rollback tax rate.

"Effective tax rate" means the rate that will produce last year's total tax levy (adjusted) from this year's total taxable values (adjusted). "Adjusted" means lost values are not included in the calculation of last year's taxes and new values are not included in this year's taxable values.

"Rollback tax rate" means the rate that will produce last year's maintenance and operation tax levy (adjusted) from this year's values (adjusted) multiplied by 1.08 plus a rate that will produce this year's debt service from this year's values (unadjusted) divided by the anticipated tax collection rate.

The Property Tax Code provides that certain cities and counties in the State may submit a proposition to the voters to authorize an additional one-half cent sales tax on retail sales of taxable items. If the additional tax is levied, the effective tax rate and the rollback tax rate calculations are required to be offset by the revenue that will be generated by the sales tax in the current year.

Reference is made to the Property Tax Code for definitive requirements for the levy and collection of ad valorem taxes and the calculation of the various defined tax rates.

PROPERTY ASSESSMENT AND TAX PAYMENT

Property within the City is generally assessed as of January 1 of each year. Business inventory may, at the option of the taxpayer, be assessed as of September. Oil and gas reserves are assessed on the basis of a valuation process which uses an average of the daily price of oil and gas for the prior year. Taxes become due October 1 of the same year, and become delinquent on February 1 of the following year. Taxpayers 65 years old or older are permitted by State law to pay taxes on homesteads in four installments with the first due on February 1 of each year and the final installment due on August 1.

PENALTIES AND INTEREST

Charges for penalty and interest on the unpaid balance of delinquent taxes are made as follows:

<u>Month</u>	<u>Cumulative Penalty</u>	<u>Cumulative Interest</u>	<u>Total</u>
February	6%	1%	7%
March	7	2	9
April	8	3	11
May	9	4	13
June	10	5	15
July	12	6	18

After July, a cumulative penalty remains at 12%, and interest increases at the rate of 1% each month. In addition, if an account is delinquent in July, a 15% attorney's collection fee is added to the total tax penalty and interest charge. Under certain circumstances, taxes which become delinquent on the homestead of a taxpayer 65 years old or older incur a penalty of 8% per annum with no additional penalties or interest assessed. In general, property subject to the City's lien may be sold, in whole or in parcels, pursuant to court order to collect the amounts due. Federal law does not allow for the collection of penalty and interest against an estate in bankruptcy. Federal bankruptcy law provides that an automatic stay of action by creditors and other entities, including governmental units, goes into effect with the filing of any petition in bankruptcy. The automatic stay prevents governmental units from foreclosing on property and prevents liens for post-petition taxes from attaching to property and obtaining secured creditor status unless, in either case, an order lifting the stay is obtained from the bankruptcy court. In many cases post-petition taxes are paid as an administrative expense of the estate in bankruptcy or by order of the bankruptcy court.

CITY APPLICATION OF TAX CODE

The City grants an exemption to the market value of the residence homestead of persons 65 years of age or older of \$10,000; the disabled are also granted an exemption of \$5,000.

The City has granted an additional exemption of 20% of the market value of residence homesteads; minimum exemption of \$5,000.

See Table 1 for a listing of the aggregate amounts of the exemptions described above.

The City has adopted the tax freeze for citizens who are disabled or are 65 years of age or older.

Ad valorem taxes are not levied by the City against the exempt value of residence homesteads for the payment of debt.

The City does tax nonbusiness personal property; and the Liberty County Tax Assessor/Collector collects taxes for the City.

The City does permit split payments, and discounts are not allowed.

The City does tax freeport property.

The City does tax goods-in-transit.

The City does collect the additional one-half cent sales tax for reduction of ad valorem taxes.

TABLE 1 - VALUATION, EXEMPTIONS AND GENERAL OBLIGATION DEBT

2012/2013 Appraised Valuation Established by Liberty and Montgomery County Appraisal Districts ⁽¹⁾		\$ 432,540,607
Less Exemptions/Reductions at 100% Market Value:		
Homestead Exemption	\$ 5,469,370	
Over 65 or Disabled	4,660,940	
Disabled Veterans	1,416,110	
Productivity Loss	6,592,365	
Cap Loss	477,169	
House Bill 366	4,330	
Abatement	1,322,226	
Charity Exemption	180,840	
Tax Exempt Property	<u>78,993,625</u>	<u>\$ 99,116,975</u>
2012/2013 Taxable Assessed Valuation ⁽¹⁾		\$ 333,423,632
General Obligation Debt Payable from Ad Valorem Taxes (as of 12/1/2012)		
Outstanding Certificates of Obligation	\$ 12,925,000	
Outstanding Tax Notes	420,000	
Plus: The Certificates*	<u>2,455,000</u>	<u>* \$ 15,800,000</u>
Less: Self-Supporting Debt Service (as of 12/1/2012)		\$ 8,150,000 ⁽²⁾
Less: General Obligation Interest and Sinking Fund Balance as of 8/31/2012		178,063 ⁽³⁾
Net General Obligation Debt Payable from Ad Valorem Taxes		\$ 7,471,937
Ratio Net General Obligation Debt to Taxable Assessed Valuation ⁽¹⁾		2.24%

2010 Census Population - 7,695
Per Capita Taxable Assessed Valuation - \$43,330
Per Capita Funded Debt - \$1,348

* Preliminary, subject to change.

(1) Includes \$8,267,928 of uncertified value that is subject to change due to protest and arbitration process.

(2) Includes debt service on the Certificates, the Combination Tax and Revenue Certificates of Obligation, Series 2009, the Combination Tax and Revenue Certificates of Obligation, Series 2011 and a portion of the Combination Tax and Revenue Certificates of Obligation, Series 2012. The revenue available to support general obligation debt is shown in "TABLE 10 – COMPUTATION OF SELF-SUPPORTING DEBT". It is the City's current policy to provide these payments from waterworks and sanitary system revenues or payments from the Cleveland Economic Development Corporation; this policy is subject to change in the future.

(3) Unaudited, provided by the City.

TABLE 2 - TAXABLE ASSESSED VALUATIONS BY CATEGORY

Category	Taxable Appraised Value, Fiscal Year Ending September 30					
	2013 ⁽¹⁾		2012		2011	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Real, Residential, Single-Family	122,943,220	28.42%	124,109,621	28.33%	\$ 124,752,091	29.10%
Real, Residential, Multi-Family	14,741,850	3.41%	14,801,160	3.38%	13,194,680	3.08%
Real, Vacant Lots/Tracts	12,603,410	2.91%	12,825,318	2.93%	12,750,948	2.97%
Real, Acreage (Land Only)	10,414,414	2.41%	11,400,998	2.60%	11,045,818	2.58%
Real Farm and Ranch Improvements	145,994	0.03%	117,000	0.03%	261,780	0.06%
Real, Commercial	114,693,345	26.52%	115,517,510	26.37%	112,514,670	26.25%
Real, Industrial	982,198	0.23%	488,969	0.11%	488,969	0.11%
Real and Tangible Personal, Utilities	11,943,601	2.76%	11,926,081	2.72%	12,486,661	2.91%
Tangible Personal, Commercial	51,900,260	12.00%	55,031,870	12.56%	51,101,630	11.92%
Tangible Personal, Industrial	5,474,330	1.27%	4,348,450	0.99%	4,278,390	1.00%
Tangible Personal, Mobile Home	4,131,510	0.96%	3,473,990	0.79%	2,880,490	0.67%
Real Property & Special Inventory	3,387,680	0.78%	2,936,240	0.67%	2,651,110	0.62%
Totally Exempt Property	79,178,795	18.31%	81,162,539	18.52%	80,255,199	18.72%
Total Appraised Value Before Exemptions	\$ 432,540,607	100.00%	\$ 438,139,746	100.00%	\$ 428,662,436	100.00%
Less: Total Exemptions/Reductions	99,116,975		103,403,228		102,451,570	
Taxable Assessed Value	<u>\$ 333,423,632</u>		<u>\$ 334,736,518</u>		<u>\$ 326,210,866</u>	

Category	Taxable Appraised Value, Fiscal Year Ending September 30			
	2010		2009	
	Amount	% of Total	Amount	% of Total
Real, Residential, Single-Family	\$ 122,992,722	29.06%	\$ 121,884,652	30.64%
Real, Residential, Multi-Family	12,946,482	3.06%	13,346,980	3.36%
Real, Vacant Lots/Tracts	11,763,719	2.78%	11,730,780	2.95%
Real, Acreage (Land Only)	9,159,577	2.16%	6,716,362	1.69%
Real Farm and Ranch Improvements	289,210	0.07%	120,320	0.03%
Real, Commercial	109,032,862	25.76%	92,640,078	23.29%
Real, Industrial	415,900	0.10%	415,900	0.10%
Real and Tangible Personal, Utilities	12,265,610	2.90%	13,052,430	3.28%
Tangible Personal, Commercial	57,226,900	13.52%	51,389,460	12.92%
Tangible Personal, Industrial	2,778,830	0.66%	2,326,420	0.58%
Tangible Personal, Mobile Home	2,492,450	0.59%	2,059,640	0.52%
Real Property & Special Inventory	2,968,150	0.70%	4,778,970	1.20%
Totally Exempt Property	78,890,259	18.64%	77,299,809	19.43%
Total Appraised Value Before Exemptions	\$ 423,222,671	100.00%	\$ 397,761,801	100.00%
Less: Total Exemptions/Reductions	99,946,726		97,693,188	
Taxable Assessed Value	<u>\$ 323,275,945</u>		<u>\$ 300,068,613</u>	

(1) Includes \$8,267,928 of uncertified value that is subject to change due to protest and arbitration process.

NOTE: Valuations shown are certified taxable assessed values reported by the Montgomery County and Liberty County Appraisal Districts to the State Comptroller of Public Accounts. Certified values are subject to change throughout the year as contested values are resolved and the Appraisal Districts update records.

TABLE 3 - VALUATION AND GENERAL OBLIGATION DEBT HISTORY

Fiscal Year Ended 9/30	Estimated Population ⁽¹⁾	Taxable Assessed Valuation ⁽²⁾	Taxable Assessed Valuation Per Capita	G.O. Tax Debt Outstanding at End of Year ⁽³⁾	Ratio of G.O. Tax Debt to Taxable Assessed Valuation	G.O. Tax Debt Per Capita
2008	7,605	\$ 280,734,243	\$ 36,914	\$ 8,140,000	2.90%	\$ 1,070
2009	7,605	300,068,613	39,457	8,390,000	2.80%	1,103
2010	7,675	323,275,945	42,121	8,045,000	2.49%	1,048
2011	7,675	326,210,866	42,503	10,045,000	3.08%	1,309
2012	7,675	334,736,518	43,614	13,345,000	3.99%	1,739
2013	7,695	333,423,632 ⁽⁴⁾	43,330	14,940,000 ⁽⁵⁾	4.48%	1,942

- (1) Population from 2000 Census held constant for fiscal years 2007-2009. 2010 Census population held constant for fiscal years 2010-2012. 2013 estimate provided by the City.
- (2) As reported by the Montgomery County and Liberty County Appraisal Districts on City's annual Report of Property Value; subject to change during the ensuing year.
- (3) Includes self-supporting debt. The revenue available to support general obligation debt is shown in "TABLE 10 – COMPUTATION OF SELF-SUPPORTING DEBT." It is the City's current policy to provide these payments from waterworks and sanitary sewer system revenues or payments from the Cleveland Economic Development Corporation; this policy is subject to change in the future.
- (4) Includes \$8,267,928 of uncertified value that is subject to change due to protest and arbitration process.
- (5) Projected, includes the Certificates.

TABLE 4 - TAX RATE, LEVY AND COLLECTION HISTORY

Fiscal Year Ended 9/30	Tax Rate	General Fund	Interest and Sinking Fund	Tax Levy	% Current Collections	% Total Collections
2008	\$ 0.700000	\$ 0.456500	\$ 0.243500	\$ 1,945,638	93.66%	98.51%
2009	0.690000	0.437700	0.252300	2,028,515	93.79%	97.27%
2010	0.685000	0.506600	0.178400	2,179,965	91.37% ⁽¹⁾	95.14% ⁽¹⁾
2011	0.685000	0.480300	0.204700	2,216,589	90.20% ⁽¹⁾	93.60% ⁽¹⁾
2012	0.685000	0.472000	0.213000	2,249,792	91.25% ⁽²⁾	97.28% ⁽²⁾
2013	0.780000	0.483100	0.296900	2,470,669	⁽³⁾	⁽³⁾

- (1) Decrease in taxes paid due to the general downturn in the economy and a principal taxpayer has filed for bankruptcy. See "TABLE 5 – TEN LARGEST TAXPAYERS."
- (2) Collections as of August 31, 2012
- (3) The 2013 tax year began October 1, 2012. Taxes are due January 31, 2013.

TABLE 5 - TEN LARGEST TAXPAYERS

Name of Taxpayer	Nature of Property	2012/2013 Taxable Assessed Valuation	% of Total Taxable Assessed Valuation
NHCI of Hillsboro Inc.	Hospital	\$ 9,762,130	3.00%
Walmart Real Estate	Real Estate	8,127,150	2.50%
Cleveland Diagnostics Plaza ⁽¹⁾	Hospital	7,589,950	2.33%
Walmart Store	Retail	6,590,880	2.03%
Campbell Concrete & Materials, LP	Concrete Manufacturer	5,165,860	1.59%
Entergy Texas, Inc.	Energy Provider	4,546,810	1.40%
Southwestern Bell Telephone LP	Telephone Communications	4,169,010	1.28%
Cleveland Regional Medical Corp.	Hospital	3,617,140	1.11%
Tobin Ben Co.	Shopping Center	3,009,370	0.93%
Sleepy Hollow Holdings LP	Apartments	2,821,660	0.87%
		<u>\$ 55,399,960</u>	<u>17.04%</u>

- (1) Cleveland Diagnostics Plaza has filed for bankruptcy protection. They are delinquent on ad valorem tax payments to the City for the last three years. The amount due the City is \$92,516.51 in base taxes and \$45,504.25 in penalty and interest as of August 31, 2012.

GENERAL OBLIGATION DEBT LIMITATION . . . No general obligation debt limitation is imposed on the City under current State law or the City's Home Rule Charter (see "TAX RATE LIMITATION"). Administratively, the Attorney General of the State of Texas will permit allocation of up to \$1.50 of the \$2.50 maximum tax rate for the purpose of paying all general obligation debt service, as measured against the maximum annual debt service on all City ad valorem tax debt and calculated at the time of issuance.

TABLE 6 - TAX ADEQUACY

2013 Net Principal and Interest Requirements	\$	924,581 ⁽¹⁾
\$0.3048 Tax Rate at 91% Collection Produces	\$	924,810
Net Average Principal and Interest Requirements (2013-2023)	\$	857,069 ⁽¹⁾
\$0.2825 Tax Rate at 91% Collection Produces	\$	857,149
Net Maximum Principal and Interest Requirements (2014)	\$	967,570 ⁽¹⁾
\$0.3189 Tax Rate at 91% Collection Produces	\$	967,592

(1) Projected, includes the Certificates and excludes self-supporting debt. The revenue available to support general obligation debt is shown in "TABLE 10 – COMPUTATION OF SELF-SUPPORTING DEBT". It is the City's current policy to provide these payments from the waterworks and sanitary sewer system revenues or payments from the Cleveland Economic Development Corporation; this policy is subject to change in the future. It is the current expectation of the City that a portion of the Certificates will be treated as self-supporting debt.

TABLE 7 - ESTIMATED OVERLAPPING DEBT

Expenditures of the various taxing entities within the territory of the City are paid out of ad valorem taxes levied by such entities on properties within the City. Such entities are independent of the City and may incur borrowings to finance their expenditures. This statement of direct and estimated overlapping ad valorem tax bonds ("Tax Debt") was developed from information contained in "Texas Municipal Reports" published by the Municipal Advisory Council of Texas. Except for the amounts relating to the City, the City has not independently verified the accuracy or completeness of such information, and no person should rely upon such information as being accurate or complete. Furthermore, certain of the entities listed may have issued additional bonds since the date hereof, and such entities may have programs requiring the issuance of substantial amounts of additional bonds, the amount of which cannot be determined. The following table reflects the estimated share of overlapping Tax Debt of the City.

	2011/2012 Taxable Assessed Value	Total G.O. Debt	Estimated % Applicable	City's Overlapping G.O. Debt as of 8/31/2012
City of Cleveland	\$ 333,423,632 ⁽¹⁾	\$ 15,800,000 ⁽²⁾	100.00%	15,800,000 ⁽²⁾
Cleveland ISD	675,769,357	37,866,509	43.44%	16,449,212
Liberty County	4,000,125,544	18,075,000	7.59%	1,371,893
Montgomery County	35,124,516,885	452,950,000	⁽³⁾	176,651
Total Direct and Overlapping Funded Debt				\$ 33,797,755
Ratio of Direct and Overlapping Funded Debt to Taxable Assessed Valuation				10.14%
Per Capita Overlapping Funded Debt				4,392

(1) 2012/2013 Tax Assessed Valuation

(2) Projected, includes the Certificates and self-supporting debt. The revenue available to support general obligation debt is shown in "TABLE 10 – COMPUTATION OF SELF-SUPPORTING DEBT". It is the City's current policy to provide these payments from waterworks and sanitary sewer system revenues or payments from the Cleveland Economic Development Corporation; this policy is subject to change in the future.

(3) Represents less than one percent (1%) of Tax Assessed Valuation.

DEBT INFORMATION

TABLE 8 - PRO-FORMA GENERAL OBLIGATION DEBT SERVICE REQUIREMENTS

Year End 9/30	Outstanding Debt Service ⁽¹⁾	The Certificates*			Total General Obligation Debt Service	Less: Self- Supporting Debt Service ⁽³⁾	Total Net General Obligation Debt Service	% of Total Net Debt Service Retired
		Principal	Interest ⁽²⁾	Total				
2013	\$ 1,329,641		\$ 49,013	\$ 49,013	\$ 1,378,654	\$ 454,073	\$ 924,581	
2014	1,374,795	\$ 100,000	64,350	164,350	1,539,145	571,575	967,570	
2015	1,367,064	100,000	62,350	162,350	1,529,414	566,255	963,159	
2016	1,372,804	100,000	60,350	160,350	1,533,154	570,394	962,761	
2017	1,262,561	105,000	58,300	163,300	1,425,861	568,925	856,936	49.59%
2018	1,172,029	105,000	56,200	161,200	1,333,229	566,874	766,355	
2019	1,204,004	110,000	54,050	164,050	1,368,054	568,639	799,415	
2020	1,193,038	110,000	51,850	161,850	1,354,888	569,175	785,713	
2021	1,214,690	110,000	49,650	159,650	1,374,340	568,728	805,613	
2022	1,203,989	115,000	47,400	162,400	1,366,389	567,301	799,088	91.55%
2023	1,206,668	115,000	44,813	159,813	1,366,480	569,905	796,575	100.00%
2024	409,666	120,000	41,875	161,875	571,541	571,541	-	
2025	403,806	125,000	38,813	163,813	567,619	567,619	-	
2026	407,451	125,000	35,375	160,375	567,826	567,826	-	
2027	405,119	130,000	31,550	161,550	566,669	566,669	-	
2028	411,635	135,000	27,575	162,575	574,210	574,210	-	
2029	407,435	140,000	23,450	163,450	570,885	570,885	-	
2030	363,633	145,000	18,813	163,813	527,445	527,445	-	
2031	365,123	150,000	13,650	163,650	528,773	528,773	-	
2032	209,100	155,000	8,313	163,313	372,413	372,413	-	
2033	-	160,000	2,800	162,800	162,800	162,800	-	
	<u>\$ 17,284,249</u>	<u>\$ 2,455,000</u>	<u>\$ 840,538</u>	<u>\$ 3,295,538</u>	<u>\$ 20,579,787</u>	<u>\$ 11,152,023</u>	<u>\$ 9,427,764</u>	

* Preliminary, subject to change.

(1) Does not include note obligations, see "TABLE 11 – OTHER OBLIGATIONS."

(2) Interest on the Certificates has been calculated at current market rates for the purpose of illustration.

(3) Includes the Certificates, the Combination Tax and Revenue Certificates of Obligation, Series 2009, the Combination Tax and Revenue Certificates of Obligation, Series 2011 and the Combination Tax and Revenue Certificates of Obligation, Series 2012. See "TABLE 10 – COMPUTATION OF SELF-SUPPORTING DEBT". The revenue available to support general obligation debt is shown in "TABLE 10 – COMPUTATION OF SELF-SUPPORTING DEBT". It is the City's current policy to provide these payments from waterworks and sanitary sewer system revenues or payments from the Cleveland Economic Development Corporation; this policy is subject to change in the future.

TABLE 9 - INTEREST AND SINKING FUND BUDGET PROJECTION

Total General Obligation Debt Service Requirements, Fiscal Year Ending 9/30/2013 ⁽¹⁾		\$ 1,378,654
Interest and Sinking Fund Balance as of August 31, 2012 ⁽²⁾	\$ 178,063	
Calculated Interest and Sinking Fund Tax Levy Collection	881,612	
Estimated Transfer from Waterworks and Sanitary System Fund	248,698	
Estimated Transfer from Economic Development Corp. Fund	205,375	
Budgeted Delinquent Taxes, Penalties and Interest	53,000	
Budgeted Investment Income	1,500	\$ 1,568,248
Estimated Balance, 9/30/2012		\$ 189,594

- (1) Projected, includes the Certificates. The revenue available to support general obligation debt is shown in "TABLE 10 – COMPUTATION OF SELF-SUPPORTING DEBT". It is the City's current policy to provide these payments from waterworks and sanitary sewer system revenues or payments from the Cleveland Economic Development Corporation; this policy is subject to change in the future.
- (2) Unaudited, provided by the City.

TABLE 10 - COMPUTATION OF SELF-SUPPORTING DEBT

Net Water and Sewer System Revenue Available	\$ 2,639,741
Less: Requirements for Water and Sewer Revenue Bonds, 9/30/2013	362,598
Balance Available for Other Purposes	2,277,144
Requirements for Ad Valorem Tax Debt Supported by the Waterworks and Sanitary Sewer System ⁽¹⁾	\$ 248,698
Percentage of Water and Sewer System General Obligation Bonds, Self-Supporting	100%
Net Economic Development Corporation Revenue Available	\$ 2,412,232
Less: Requirements for Economic Development Corporation Revenue Bonds, 9/30/2013	-
Balance Available for Other Purposes	2,412,232
Requirements for Park and Economic Development Projects contract payments to the City ⁽²⁾	\$ 205,375
Percentage of Park and Economic Project related ad valorem tax debt, Self-Supporting	100%

- (1) Includes the Certificates. The treatment of this ad valorem tax debt as self-supporting is a policy decision by the City that is subject to change.
- (2) The contract payments from the Economic Development Corporation are not pledged to the payment of the park and economic project related to ad valorem tax debt. The treatment of this ad valorem tax debt as self-supporting is a policy decision by the City that is subject to change.

AUTHORIZED BUT UNISSUED GENERAL OBLIGATION BONDS . . . The City has no authorized but unissued general obligation debt. However, under State law, the City is authorized to issue various types of indebtedness, including tax-supported debt, such as the Certificates, without seeking voter approval.

ANTICIPATED ISSUANCE OF GENERAL OBLIGATION DEBT . . . The City plans to issue general obligation refunding bonds in the first quarter of calendar year 2013. The planned issue of refunding bonds may refund obligations payable solely from waterworks and sanitary sewer system revenues and thereby increase the total par amount of general obligation ad valorem tax debt of the City. The City currently intends to treat such bonds as self-supporting from revenues of the waterworks and sanitary sewer system. The City does not anticipate the issuance of additional new money general obligation debt within the next 12 months.

TABLE 11 – OTHER OBLIGATIONS**Notes Payable: Governmental Activities**

The City issued notes payable to provide funds for the purchase of equipment. The notes payable are secured by the equipment purchased. The notes are issued as 3-4 year current interest notes.

Fiscal Year Ended 9/30	Principal	Interest	Total
2013	\$ 42,379	\$ 4,395	\$ 46,774
2014	28,994	2,273	31,267
2015	21,190	960	22,150
	<u>\$ 92,563</u>	<u>\$ 7,628</u>	<u>\$ 100,191</u>

PENSION FUND

The City provides pension benefits for all of its full-time employees through the Texas Municipal Retirement System ("TMRS"), a State-wide administered pension plan. The City makes annual contributions to the plan equal to the amounts accrued for pension expense. (For more detailed information concerning the retirement plan, see Appendix B, "Excerpts from the City's Annual Financial Report" - Note # I.)

OTHER POST-EMPLOYMENT BENEFITS

In addition to providing pension benefits through the Texas Municipal Retirement System, the City has opted to provide eligible retired employees with the following post-employment benefits:

- Eligible retirees may purchase health insurance from the City's healthcare provider at the City's cost to cover current employees
- Eligible retirees may purchase health insurance from the City's healthcare provider at the City's cost to cover current employees for dependents if the dependents were covered at the point of retirement

The City recognizes its share of the costs of providing these benefits when paid, on a "pay-as-you-go" basis. These payments are budgeted annually. The amount budgeted for the fiscal year ending September 30, 2013, is \$1,848. The appropriation for the fiscal year ending September 30, 2012, was \$1,668. At September 30, 2011, there were approximately 6 participants eligible to receive such benefits.

For more information concerning the City's post-employment benefits, see Appendix B, "Excerpts from the City's Annual Financial Report" - Note #J.

[Remainder of Page Intentionally Left Blank]

FINANCIAL INFORMATION

TABLE 12 - CHANGES IN NET ASSETS

	For Fiscal Year Ended September 30				
	2012 ⁽¹⁾	2011	2010	2009	2008
Revenues:					
Charges for Services	\$ 929,042	\$ 1,918,739	\$ 1,152,058	\$ 1,845,793	\$ 1,478,947
Operating Grants and Contributions	22,145	135,575	388,312	70,097	1,397,703
Capital Grants and Contributions	-	1,437,552	466,613	220,444	-
Property Taxes	1,575,406	2,232,954	2,225,907	2,060,953	1,905,762
Sales and Other Taxes	2,132,957	2,316,293	2,457,479	2,644,130	2,802,077
Franchise Taxes	446,455	483,970	540,596	382,186	336,451
Earnings on Investment	13,355	10,889	11,826	9,639	48,982
Proceeds from Insurance	750	29,392	66,903	82,511	14,328
Gain on sale of Assets	-	15,500	-	56,627	17,985
Miscellaneous	-	15,459	61,797	105,494	50,674
Total Revenues	<u>\$ 5,120,110</u>	<u>\$ 8,596,323</u>	<u>\$ 7,371,491</u>	<u>\$ 7,477,874</u>	<u>\$ 8,052,909</u>
Expenditures:					
General Government	\$ 944,532	\$ 800,884	\$ 941,093	\$ 1,041,737	\$ 1,049,947
Public Safety	2,502,599	4,108,437	3,711,673	3,653,792	3,750,982
Public Works	255,849	284,069	281,045	234,484	254,191
Transportation	643,733	820,878	812,646	578,481	571,532
Culture and Recreation	764,377	1,034,176	894,707	885,924	645,228
Grants	800	39,731	324,674	50,183	216,186
Economic Development	98,982	86,902	75,233	72,367	253,396
Debt Service	352,301	326,958	343,649	364,868	373,457
Total Expenditures	<u>\$ 5,563,173</u>	<u>\$ 7,502,035</u>	<u>\$ 7,384,720</u>	<u>\$ 6,881,836</u>	<u>\$ 7,114,919</u>
Change in Net Assets Before Transfers	\$ (443,063)	\$ 1,094,288	\$ (13,229)	\$ 596,038	\$ 937,990
Transfers	489,000	400,000	450,367	400,000	300,000
Change in Net Assets	<u>\$45,937</u>	<u>\$1,494,288</u>	<u>\$ 437,138</u>	<u>\$ 996,038</u>	<u>\$ 1,237,990</u>
Beginning in Net Assets	9,868,928	8,374,640	7,937,502	7,059,064 ⁽²⁾	7,075,210
Prior Period Adjustment	-	-	-	(117,600)	-
Ending Net Assets	<u>\$ 9,914,865</u>	<u>\$ 9,868,928</u>	<u>\$ 8,374,640</u>	<u>\$ 7,937,502</u>	<u>\$ 8,313,200</u>

Source: The City's audited financial statements.

(1) Unaudited, provided by the City as of August 31, 2012.

(2) Restated.

TABLE 12A - GENERAL FUND REVENUES AND EXPENDITURE HISTORY

	For Fiscal Year Ended September 30				
	2012 ⁽¹⁾	2011	2010	2009	2008
Revenues:					
Property Taxes	\$ 1,575,406	\$ 1,499,148	\$ 1,573,120	\$ 1,295,859	\$ 1,298,414
Sales and Other Taxes	2,035,478	2,189,659	2,344,854	2,458,708	2,269,212
Franchise Taxes	446,455	483,970	540,596	382,186	336,451
License and Permits	57,079	60,531	83,913	83,114	55,358
Charges for Services	647,990	867,819	663,799	1,032,176	1,054,666
Fines and Forfeitures	241,453	352,990	383,142	416,802	363,877
Intergovernmental	22,145	1,535,627	824,925	337,477	1,304,022
Earnings on Investments	13,355	4,823	6,770	5,446	13,467
Contributions	-	38,361	30,831	3,713	53,372
Miscellaneous	-	15,459	61,781	101,781	24,666
Total Revenues	\$ 5,039,361	\$ 7,048,387	\$ 6,513,731	\$ 6,117,262	\$ 6,773,505
Expenditures:					
City Council	\$ 27,587	\$ 24,966	\$ 26,752	\$ 44,709	\$ 71,964
Administration	683,110	726,547	868,444	950,850	702,748
Civic / Community	210,337	242,442	182,819	169,921	159,554
Technology	233,835	-	-	-	-
Court	167,760	207,606	192,902	200,948	195,438
Police	1,807,906	2,009,753	1,975,325	1,915,781	1,910,708
Fire Department	637,023	96,573	297,862	250,871	197,747
Animal Control	57,671	203,972	60,926	67,056	64,392
Inspection	194,422	669,138	201,662	154,646	123,337
Street Department	400,678	30,401	668,296	452,580	497,133
Airport Department	43,055	76,242	28,920	37,858	23,743
Garage Department	61,427	345,773	75,529	75,983	126,999
Library Department	279,531	301,134	303,216	311,237	291,670
Cemetery and Parks	274,509	39,731	269,164	264,781	284,299
Grants	800	1,067,889	324,674	50,183	216,186
Ambulance	-	-	834,762	999,519	1,196,841
Capital Outlay	-	1,690,683	572,657	409,572	862,898
Debt Service	45,757	50,283	60,549	75,297	90,650
Total Expenditures	\$ 5,125,408	\$ 7,783,133	\$ 6,944,459	\$ 6,431,792	\$ 7,016,307
Proceeds from Insurance	\$ 750	\$ 29,392	\$ 66,903	\$ 82,511	\$ 17,985
Proceeds from Sale of Assets	-	15,500	-	-	21,280
Proceeds from Loans	-	135,010	-	69,348	23,810
Operating Transfers In (Out)	489,000	399,250	460,785	400,000	300,329
Total Other Financing Sources (Uses)	\$ 489,750	\$ 579,152	\$ 527,688	\$ 551,859	\$ 363,404
Excess (Deficit) of Revenues and Other Sources Over Expenditures and Other Financing Uses					
	\$ 403,703	\$ (155,594)	\$ 96,960	\$ 237,329	\$ 120,602
Fund Balance, Beginning of Year	740,807	896,401	799,441	679,712	559,110
Prior Period Adjustment		-	-	(117,600)	
Fund Balance, End of Year		\$ 740,807	\$ 896,401	\$ 799,441	\$ 679,712

Source: The City's audited financial statements.

(1) Unaudited, provided by the City as of August 31, 2012.

TABLE 13 - MUNICIPAL SALES TAX HISTORY

The City has adopted the Municipal Sales and Use Tax Act, Tax Code, Chapter 321, as amended, which grants the City the power to impose and levy a 1% Local Sales and Use Tax within the City; the proceeds are credited to the General Fund and are not pledged to the payment of the Certificates. Collections and enforcements are effected through the offices of the Comptroller of Public Accounts, State of Texas, who remits the proceeds of the tax, after deduction of a 2% service fee, to the City monthly. In 2001, the voters of the City approved the imposition of an additional sales and use tax of one-quarter of one percent (1/4 of 1%) for economic development and an additional one-quarter of one percent (1/4 of 1%) for property tax reduction. The sales tax for economic development is collected solely for the benefit of Cleveland Economic Development Corporation (the "Corporation"), a Type B economic development corporation, and may be pledged to secure payment of sales tax revenue bonds issued by the Corporation.

Fiscal Year Ended 9/30	Total Collected ⁽¹⁾	% of Ad Valorem Tax Levy	Equivalent of Ad Valorem Tax Rate	Per Capita
2008	\$ 2,570,628	132.12%	\$ 0.92	\$ 338
2009	2,786,644	137.37%	0.95	366
2010	2,509,238	115.10%	0.79	330
2011	2,509,419	113.21%	0.78	327
2012	2,412,232 ⁽²⁾	106.91%	0.73	314

- (1) Includes the sales tax credited to the General Fund, including for reduction of property taxes, and collected for the benefit of the Corporation for economic development.
- (2) Partial collections through August 31, 2012.

The sales tax breakdown for the City is as follows:

Economic Development Corporation	1/4 ¢
Property Relief Tax	1/4 ¢
City Sales & Use Tax	1 ¢
Liberty County Sales & Use Tax	1/2 ¢
State Sales & Use Tax	6 1/4 ¢
Total	8 1/4 ¢

INVESTMENTS

The City invests its investable funds in investments authorized by Texas law in accordance with investment policies approved by the City Council. Both state law and the City’s investment policies are subject to change.

LEGAL INVESTMENTS

Available City funds are invested as authorized by Texas law and in accordance with investment policies approved by the City. Both Texas law and the City’s investment policies are subject to change. Under Texas law, the City is authorized to invest in (1) obligations, including letters of credit, of the United States or its agencies and instrumentalities, (2) direct obligations of the State of Texas or its agencies and instrumentalities, (3) collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States, (4) other obligations, the principal and interest of which are unconditionally guaranteed, insured, or backed by the full faith and credit of the State of Texas or the United States or their respective agencies and instrumentalities, including obligations that are fully guaranteed or insured by the Federal Deposit Insurance Corporation or by the explicit full faith and credit of the United States, (5) obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent, (6) bonds issued, assumed, or guaranteed by the State of Israel, (7) certificates of deposit and share certificates (i) issued by a depository institution that has its main office or a branch office in the State of Texas, that are guaranteed or insured by the Federal Deposit Insurance Corporation or the National Credit Union Share Insurance Fund, or are secured as to principal by obligations described in clauses (1) through (6) or in any other manner and amount provided by law for City deposits, or (ii) where (a) the funds are invested by the City through (I) a broker that has its main office or a branch office in the State of Texas and is selected from a list adopted, at least annually, by the City as required by law or (II) a depository institution that has its main office or a branch office in the State of Texas that is selected by the City; (b) the broker or the depository institution selected by the City arranges for the deposit of the funds in certificates of deposit in one or more federally insured depository institutions, wherever located, for the account of the City; (c) the full amount of the principal and accrued interest of each of the certificates of deposit is insured by the United States or an instrumentality of the United States; and (d) the City appoints the depository institution selected under (a) above, a custodian as described by Section 2257.041(d) of the Texas Government Code, as amended, or a clearing broker-dealer registered with the Securities and Exchange Commission and operating pursuant to Securities and Exchange Commission Rule 15c3-3 (17 C.F.R. Section 240.15c3-3) as custodian for the City with respect

to the certificates of deposit, (8) fully collateralized repurchase agreements that have a defined termination date, are fully secured by a combination of cash and obligations described in clause (1) which are pledged to the City, held in the City's name, and deposited at the time the investment is made with the City or with a third party selected and approved by the City and are placed through a primary government securities dealer, as defined by the Federal Reserve, or a financial institution doing business in the State of Texas, (9) bankers' acceptances with a stated maturity of 270 days or less from the date of its issuance, if the short-term obligations of the accepting bank or its parent are rated at least A-1 or P-1 or the equivalent by at least one nationally recognized credit rating agency, (10) commercial 20 paper that is rated at least A-1 or P-1 or the equivalent by either (a) two nationally recognized credit rating agencies or (b) one nationally recognized credit rating agency if the paper is fully secured by an irrevocable letter of credit issued by a U.S. or state bank, (11) no-load money market mutual funds registered with and regulated by the Securities and Exchange Commission that have a dollar weighted average stated maturity of 90 days or less and include in their investment objectives the maintenance of a stable net asset value of \$1 for each share, (12) no-load mutual funds registered with the Securities and Exchange Commission that have an average weighted maturity of less than two years, invest exclusively in obligations described in the preceding clauses, and are continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than AAA or its equivalent, and (13) public funds investment pools that have an advisory board which includes participants in the pool and are continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than AAA or its equivalent. Texas law also permits the City to invest bond proceeds in a guaranteed investment contract, subject to limitations as set forth in the Public Funds Investment Act, Chapter 2256, Texas Government Code, as amended, (the "PFIA"). A political subdivision such as the City may enter into securities lending programs if (i) the securities loaned under the program are 100% collateralized, a loan made under the program allows for termination at any time and a loan made under the program is either secured by (a) obligations that are described in clauses (1) through (6) above, (b) irrevocable letters of credit issued by a state or national bank that is continuously rated by a nationally recognized investment rating firm at not less than A or its equivalent or (c) cash invested in obligations described in clauses (1) through (6) above, clauses (10) through (12) above, or an authorized investment pool; (ii) securities held as collateral under a loan are pledged to the City, held in the City's name and deposited at the time the investment is made with the City or a third party designated by the City; (iii) a loan made under the program through either a primary government securities dealer or a financial institution doing business in the State of Texas; and (iv) the agreement to lend securities has a term of one year or less. The City may invest in such obligations directly or through government investment pools that invest solely in such obligations provided that the pools are rated no lower than AAA or AAAM or an equivalent by at least one nationally recognized rating service. The City may also contract with an investment management firm registered under the Investment Advisers Act of 1940 or with the State Securities Board to provide for the investment and management of its public funds or other funds under its control for a term up to two years, but the City retains ultimate responsibility as fiduciary of its assets. The City is specifically prohibited from investing in (1) obligations whose payment represents the coupon payments on the outstanding principal balance of the underlying mortgage-backed security collateral and pays no principal, (2) obligations whose payment represents the principal stream of cash flow from the underlying mortgage-backed security and bears no interest, (3) collateralized mortgage obligations that have a stated final maturity of greater than 10 years, and (4) collateralized mortgage obligations the interest rate of which is determined by an index that adjusts opposite to the changes in a market index.

INVESTMENT POLICIES

Under Texas law, the City is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity; that address investment diversification, yield, maturity, and the quality and capability of investment management; and that include a list of authorized investments for City funds, maximum allowable stated maturity of any individual investment and the maximum average dollar-weighted maturity allowed for pooled fund groups. All City funds must be invested consistent with a formally adopted "Investment Strategy Statement" that specifically addresses each fund's investment. Each Investment Strategy Statement will describe its objectives concerning: (1) suitability of investment type, (2) preservation and safety of principal, (3) liquidity, (4) marketability of each investment, (5) diversification of the portfolio, and (6) yield.

Under Texas law, City investments must be made "with judgment and care, under prevailing circumstances, that a person of prudence, discretion, and intelligence would exercise in the management of the person's own affairs, not for speculation, but for investment, considering the probable safety of capital and the probable income to be derived." At least quarterly the investment officers of the City shall submit an investment report detailing: (1) the investment position of the City, (2) that all investment officers jointly prepared and signed the report, (3) the beginning market value, and the ending value of each pooled fund group, (4) the book value and market value of each separately listed asset at the beginning and end of the reporting period, (5) the maturity date of each separately invested asset, (6) the account or fund or pooled fund group for which each individual investment was acquired, and (7) the compliance of the investment portfolio as it relates to: (a) adopted investment strategy statements and (b) State law. No person may invest City funds without express written authority from the City.

ADDITIONAL PROVISIONS

Under Texas law the City is additionally required to: (1) annually review its adopted policies and strategies; (2) require any investment officers with personal business relationships or relatives with firms seeking to sell securities to the entity to disclose the relationship and file a statement with the Texas Ethics Commission and the City Council; (3) require the registered principal of firms seeking to sell securities to the City to: (a) receive and review the City's investment policy, (b) acknowledge that reasonable controls and procedures have been implemented to preclude imprudent investment activities, and (c) deliver a written statement attesting to these requirements; (4) perform an annual audit of the management controls on investments and adherence to the City's investment

policy; (5) provide specific investment training for the Treasurer, Chief Financial Officer and investment officers; (6) restrict reverse repurchase agreements to not more than 90 days and restrict the investment of reverse repurchase agreement funds to no greater than the term of the reverse repurchase agreement; (7) restrict its investment in mutual funds in the aggregate to no more than 15 percent of its monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service, and to invest no portion of bond proceeds, reserves and funds held for debt service, in mutual funds; and (8) require local government investment pools to conform to the new disclosure, rating, net asset value, yield calculation, and advisory board requirements.

TABLE 14 - CURRENT INVESTMENTS

As of August 31, 2012, the City's investable funds were invested in the following categories:

Type of Investments	Amount
Money Market Account	\$ 1,037,808
TexPool	808
Total	<u>\$ 1,038,616</u>

Source: The City.

TAX MATTERS

TAX EXEMPTION

In the opinion of Bracewell & Giuliani LLP, Bond Counsel, under existing law, (i) interest on the Certificates is excludable from gross income for federal income tax purposes under existing law and (ii) the Certificates are not "private activity bonds" under the Internal Revenue Code of 1986, as amended (the "Code"), and, as such, interest on the Certificates will not be subject to the alternative minimum tax on individuals and corporations, except as described below in the discussion regarding the adjusted current earnings adjustment for corporations.

The Code imposes a number of requirements that must be satisfied for interest on state or local obligations, such as the Certificates, to be excludable from gross income for federal income tax purposes. These requirements include limitations on the use of proceeds and the source of repayment, limitations on the investment of proceeds prior to expenditure, a requirement that excess arbitrage earned on the investment of proceeds be paid periodically to the United States, and requirement that the issuer file an information report with the Internal Revenue Service (the "Service"). The City has covenanted in the Ordinance that it will comply with these requirements.

Bond Counsel's opinion will assume continuing compliance with the covenants of the Ordinance pertaining to those sections of the Code that affect the exclusion from gross income of interest on the Certificates for federal income tax purposes and, in addition, will rely on representations by the City, the City's Financial Advisor and the Underwriter with respect to matters solely within the knowledge of the City, the City's Financial Advisor and the Underwriter, respectively, which Bond Counsel has not independently verified. If the City should fail to comply with the covenants in the Ordinance or if the foregoing representations should be determined to be inaccurate or incomplete, interest on the Certificates could become includable in gross income from the date of delivery of the Certificates, regardless of the date on which the event causing such inclusion occurs.

The Code also imposes a 20% alternative minimum tax on the "alternative minimum taxable income" of a corporation if the amount of such alternative minimum tax is greater than the amount of the corporation's regular income tax. Generally, the alternative minimum taxable income of a corporation (other than any S corporation, regulated investment company, REIT, or REMIC), includes 75% of the amount by which its "adjusted current earnings" exceeds its other "alternative minimum taxable income." Because interest on tax-exempt obligations, such as the Certificates, is included in a corporation's "adjusted current earnings," ownership of the Certificates could subject a corporation to alternative minimum tax consequences.

Except as stated above, Bond Counsel will express no opinion as to any federal, state or local tax consequences resulting from the receipt or accrual of interest on, or acquisition, ownership or disposition of, the Certificates.

Bond Counsel's opinions are based on existing law, which is subject to change. Such opinions are further based on Bond Counsel's knowledge of facts as of the date thereof. Bond Counsel assumes no duty to update or supplement its opinions to reflect any facts or circumstances that may thereafter come to Bond Counsel's attention or to reflect any changes in any law that may thereafter occur or become effective. Moreover, Bond Counsel's opinions are not a guarantee of result and are not binding on the Service; rather, such opinions represent Bond Counsel's legal judgment based upon its review of existing law and in reliance upon the representations and covenants referenced above that it deems relevant to such opinions. The Service has an ongoing audit program to determine compliance with rules that relate to whether interest on state or local obligations is includable in gross income for federal income tax purposes. No assurance can be given as to whether or not the Service will commence an audit of the Certificates. If an audit is commenced, in accordance with its current published procedures the Service is likely to treat the City as the taxpayer and the Owners may not have a right to participate in such audit. Public awareness of any future audit of the Certificates could adversely affect the value and liquidity of the Certificates regardless of the ultimate outcome of the audit.

PURCHASE OF TAX-EXEMPT OBLIGATIONS BY FINANCIAL INSTITUTIONS

Section 265(a) of the Code provides, in general, that a deduction for interest on indebtedness incurred to acquire or carry tax-exempt obligations is disallowed. Section 265(b) of the Code provides a specific complete disallowance of any deduction by a financial institution of its pro rata interest expense to reflect such financial institution's investment in tax-exempt obligations acquired after August 7, 1986. Section 265(b) also provides an exception for financial institutions for tax-exempt obligations that are properly designated by an issuer as "qualified tax-exempt obligations."

The City expects to designate the Certificates as "qualified tax-exempt obligations" based, in part, on the City's representation that the amount of the Certificates, when added to the amount of all other tax-exempt obligations (not including private activity bonds other than "qualified 501(c)(3) bonds") issued or reasonably anticipated to be issued by or on behalf of the City during 2012, is not expected to exceed \$10,000,000. Further, the City and entities aggregated with the City under the Code have not designated more than \$10,000,000 in "qualified tax-exempt obligations" (including the Certificates) during 2012.

Notwithstanding the designation of the Certificates as "qualified tax-exempt obligations" under this exception, financial institutions acquiring the Certificates will be subject to a 20% disallowance of allocable interest expense.

ADDITIONAL FEDERAL INCOME TAX CONSIDERATIONS

Collateral Tax Consequences . . . Prospective purchasers of the Certificates should be aware that the ownership of tax-exempt obligations may result in collateral federal income tax consequences to financial institutions, life insurance and property and casualty insurance companies, certain S corporations with Subchapter C earnings and profits, individual recipients of Social Security or Railroad Retirement benefits, taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations and individuals otherwise qualifying for the earned income credit. In addition, certain foreign corporations doing business in the United States may be subject to the "branch profits tax" on their effectively connected earnings and profits, including tax-exempt interest such as interest on the Certificates. These categories of prospective purchasers should consult their own tax advisors as to the applicability of these consequences. Prospective purchasers of the Certificates should also be aware that, under the Code, taxpayers are required to report on their returns the amount of tax-exempt interest, such as interest on the Certificates, received or accrued during the year.

Tax Accounting Treatment of Original Issue Premium . . . The issue price of all or a portion of the Certificates may exceed the stated redemption price payable at maturity of such Certificates. Such Certificates (the "Premium Certificates") are considered for federal income tax purposes to have "bond premium" equal to the amount of such excess. The basis of a Premium Certificate in the hands of an initial owner is reduced by the amount of such excess that is amortized during the period such initial owner holds such Premium Certificate in determining gain or loss for federal income tax purposes. This reduction in basis will increase the amount of any gain or decrease the amount of any loss recognized for federal income tax purposes on the sale or other taxable disposition of a Premium Certificate by the initial owner. No corresponding deduction is allowed for federal income tax purposes for the reduction in basis resulting from amortizable bond premium. The amount of bond premium on a Premium Certificate that is amortizable each year (or shorter period in the event of a sale or disposition of a Premium Certificate) is determined using the yield to maturity on the Premium Certificate based on the initial offering price of such Certificate.

The federal income tax consequences of the purchase, ownership and redemption, sale or other disposition of Premium Certificates that are not purchased in the initial offering at the initial offering price may be determined according to rules that differ from those described above. All owners of Premium Certificates should consult their own tax advisors with respect to the determination for federal, state, and local income tax purposes of amortized bond premium upon the redemption, sale or other disposition of a Premium Certificate and with respect to the federal, state, local, and foreign tax consequences of the purchase, ownership, and sale, redemption or other disposition of such Premium Certificates.

Tax Accounting Treatment of Original Issue Discount Certificates . . . The issue price of all or a portion of the Certificates may be less than the stated redemption price payable at maturity of such Certificates (the "Original Issue Discount Certificates"). In such case, the difference between (i) the amount payable at the maturity of each Original Issue Discount Certificate, and (ii) the initial offering price to the public of such Original Issue Discount Certificate constitutes original issue discount with respect to such Original Issue Discount Certificate in the hands of any owner who has purchased such Original Issue Discount Certificate in the initial public offering of the Certificates. Generally, such initial owner is entitled to exclude from gross income (as defined in Section 61 of the Code) an amount of income with respect to such Original Issue Discount Certificate equal to that portion of the amount of such original issue discount allocable to the period that such Original Issue Discount Certificate continues to be owned by such owner. Because original issue discount is treated as interest for federal income tax purposes, the discussions regarding interest on the Certificates under the captions "TAX MATTERS – TAX EXEMPTION" and "TAX MATTERS – ADDITIONAL FEDERAL INCOME TAX CONSIDERATIONS – COLLATERAL TAX CONSEQUENCES" and "—TAX LEGISLATIVE CHANGES" generally apply and should be considered in connection with the discussion in this portion of this Official Statement.

In the event of the redemption, sale or other taxable disposition of such Original Issue Discount Certificate prior to stated maturity, however, the amount realized by such owner in excess of the basis of such Original Issue Discount Certificate in the hands of such owner (adjusted upward by the portion of the original issue discount allocable to the period for which such Original Issue Discount Certificate was held by such initial owner) is includable in gross income.

The foregoing discussion assumes that (i) the Underwriter has purchased the Certificates for contemporaneous sale to the public and (ii) all of the Original Issue Discount Certificates have been initially offered, and a substantial amount of each maturity thereof has been sold, to the general public in arm's-length transactions for a price (and with no other consideration being included) not more than the initial offering prices thereof stated on the inside cover page of this Official Statement. Neither the City nor Bond Counsel has made any investigation or offers any comfort that the Original Issue Discount Certificates will be offered and sold in accordance with such assumptions.

Under existing law, the original issue discount on each Original Issue Discount Certificate accrues daily to the stated maturity thereof (in amounts calculated as described below for each six-month period ending on the date before the semiannual anniversary dates of the date of the Certificates and ratably within each such six-month period) and the accrued amount is added to an initial owner's basis for such Original Issue Discount Certificate for purposes of determining the amount of gain or loss recognized by such owner upon the redemption, sale or other disposition thereof. The amount to be added to basis for each accrual period is equal to (i) the sum of the issue price and the amount of original issue discount accrued in prior periods multiplied by the yield to stated maturity (determined on the basis of compounding at the close of each accrual period and properly adjusted for the length of the accrual period) less (ii) the amounts payable as current interest during such accrual period on such Certificate.

The federal income tax consequences of the purchase, ownership, and redemption, sale or other disposition of Original Issue Discount Certificates that are not purchased in the initial offering at the initial offering price may be determined according to rules that differ from those described above. All owners of Original Issue Discount Certificates should consult their own tax advisors with respect to the determination for federal, state, and local income tax purposes of interest accrued upon redemption, sale or other disposition of such Original Issue Discount Certificates and with respect to the federal, state, local and foreign tax consequences of the purchase, ownership, redemption, sale or other disposition of such Original Issue Discount Certificates.

TAX LEGISLATIVE CHANGES

Current law may change so as to directly or indirectly reduce or eliminate the benefit of the exclusion of interest on the Certificates from gross income for federal income tax purposes. Any proposed legislation, whether or not enacted, could also affect the value and liquidity of the Certificates. Prospective purchasers of the Certificates should consult with their own tax advisors with respect to any proposed, pending or future legislation.

OTHER INFORMATION

RATINGS

The Bonds have been rated "A2" by Moody's. The presently outstanding tax supported debt of the City is rated "A2" by Moody's and "A-" by S&P, without regard to credit enhancement. An explanation of the significance of such ratings on the Certificates and the presently outstanding tax supported debt of the City may be obtained from the company furnishing the rating. The ratings reflect only the respective view of such organization and the City makes no representation as to the appropriateness of the ratings. There is no assurance that such ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by either or both rating companies, if in the judgment of either or both companies, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Certificates.

LITIGATION

It is the opinion of the City Attorney and City Staff that there is no pending litigation against the City that would have a material adverse financial impact upon the City or its operations.

REGISTRATION AND QUALIFICATION OF CERTIFICATES FOR SALE

The sale of the Certificates has not been registered under the Federal Securities Act of 1933, as amended, in reliance upon the exemption provided thereunder by Section 3(a)(2); and the Certificates have not been qualified under the Securities Act of Texas in reliance upon various exemptions contained therein; nor have the Certificates been qualified under the securities acts of any jurisdiction. The City assumes no responsibility for qualification of the Certificates under the securities laws of any jurisdiction in which the Certificates may be sold, assigned, pledged, hypothecated or otherwise transferred. This disclaimer of responsibility for qualification for sale or other disposition of the Certificates shall not be construed as an interpretation of any kind with regard to the availability of any exemption from securities registration provisions.

LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS

Section 1201.041 of the Public Security Procedures Act (Chapter 1201, Texas Government Code, as amended) provides that the Certificates are negotiable instruments governed by Chapter 8, Texas Business and Commerce Code, as amended, and are legal and authorized investments for insurance companies, fiduciaries, and trustees, and for the sinking funds of municipalities or other political subdivisions or public agencies of the State of Texas. With respect to investment in the Certificates by municipalities or other political subdivisions or public agencies of the State of Texas, the Public Funds Investment Act, Chapter 2256, Texas Government Code, as amended, requires that the Certificates be assigned a rating of "A" or its equivalent as to investment quality by a national rating agency. See "OTHER INFORMATION - RATINGS" herein. In addition, various provisions of the Texas Finance Code provide that, subject to a prudent investor standard, the Certificates are legal investments for state banks, savings banks, trust companies with at capital of one million dollars or more, and savings and loan associations. The Certificates are eligible to secure deposits of any public funds of the State, its agencies, and its political subdivisions, and are legal security for those deposits to the extent of their market value. No review by the City has been made of the laws in other states to determine whether the Certificates are legal investments for various institutions in those states.

LEGAL MATTERS

The City will furnish a complete transcript of proceedings incident to the authorization and issuance of the Certificates, including the approving legal opinion of the Attorney General of the State of Texas to the effect that the Certificates are valid and binding obligations of the City, and based upon examination of such transcript of proceedings, the approving legal opinion of Bond Counsel in substantially the form attached hereto as Appendix C. Bond Counsel has reviewed the statements and information appearing in this Official Statement under the captions "THE CERTIFICATES" (except the subcaptions "BOOK-ENTRY-ONLY SYSTEM," "BONDHOLDERS' REMEDIES," and "SOURCES AND USES OF CERTIFICATE PROCEEDS) and "CONTINUING DISCLOSURE OF INFORMATION" (except the subcaption "COMPLIANCE WITH PRIOR UNDERTAKINGS") and Bond Counsel is of the opinion that the statements and information contained therein fairly and accurately reflect the provisions of the Ordinance; further, Bond Counsel has reviewed the statements and information contained in this Official Statement under the captions "TAX MATTERS," "OTHER INFORMATION – REGISTRATION AND QUALIFICATION OF CERTIFICATES FOR SALE," "OTHER INFORMATION – LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS," "OTHER INFORMATION – LEGAL MATTERS" (except of the last sentence of the first paragraph) and Bond Counsel is of the opinion that the statements and information contained therein fairly and accurately describe the laws and legal issues addressed therein. Bond Counsel has not independently verified any of the factual information contained in this Official Statement nor have they conducted an investigation of the affairs of the City for the purpose of passing upon the accuracy or completeness of this Official Statement. No person is entitled to rely upon such firm's limited participation as an assumption of responsibility for, or an expression of opinion of any kind with regard to, the accuracy or completeness of any of the information contained herein. The legal fees to be paid Bond Counsel for services rendered in connection with the issuance of the Certificates is contingent upon the sale and delivery of the Certificates. Certain matters will be passed upon for the Underwriter by Petruska & Associates, PLLC, Dallas, Texas, Counsel for the Underwriter, whose fee is contingent upon the sale and delivery of the Certificates.

The various legal opinions to be delivered concurrently with the delivery of the Certificates express the professional judgment of the attorneys rendering the opinions as to the legal issues explicitly addressed therein. In rendering a legal opinion, the attorney does not become an insurer or guarantor of the expression of professional judgment, of the transaction opined upon, or of the future performance of the parties to the transaction. Nor does the rendering of an opinion guarantee the outcome of any legal dispute that may arise out of the transaction.

AUTHENTICITY OF FINANCIAL DATA AND OTHER INFORMATION

The financial data and other information contained herein have been obtained from City records, audited financial statements and other sources which are believed to be reliable. There is no guarantee that any of the assumptions or estimates contained herein will be realized. All of the summaries of the statutes, documents and resolutions contained in this Official Statement are made subject to all of the provisions of such statutes, documents and resolutions. These summaries do not purport to be complete statements of such provisions and reference is made to such documents for further information. Reference is made to original documents in all respects.

CONTINUING DISCLOSURE OF INFORMATION

In the Ordinance, the City has made the following agreement for the benefit of the holders and beneficial owners of the Certificates. The City is required to observe the agreement for so long as it remains an "obligated person" with respect to the Certificates, within the meaning of the Securities and Exchange Commission's Rule 15c2-12 (the "Rule"). Under the agreement, the City will be obligated to provide certain updated financial information and operating data annually, and timely notice of specified material events, to the Municipal Securities Rulemaking Board (the "MSRB"). This information will be available free of charge from the MSRB via Electronic Municipal Market Access ("EMMA") system at www.emma.msrb.org.

ANNUAL REPORTS

The City will provide certain updated financial information and operating data to the MSRB. The information to be updated includes all quantitative financial information and operating data with respect to the City of the general type included in this Official Statement under Tables numbered 1 through 6 and 8 through 14 and in Appendix B. The City will update and provide this information within six months after the end of each fiscal year ending in and after September 30, 2012.

The financial information and operating data to be provided may be set forth in full in one or more documents or may be included by specific reference to any document available to the public on the MSRB's Internet Web site or filed with the United States Securities and Exchange Commission (the "SEC"), as permitted by SEC Rule 15c2-12 (the "Rule"). The updated information will include audited financial statements, if the City commissions an audit and it is completed by the required time. If audited financial statements are not available by the required time, the City will provide unaudited financial statements by the required time and audited financial statements when and if such audited financial statements become available. Any such financial statements will be prepared in accordance with the accounting principles described in Appendix B or such other accounting principles as the City may be required to employ from time to time pursuant to State law or regulation.

The City's current fiscal year end is September 30. Accordingly, it must provide updated information by March 31 in each year, unless the City changes its fiscal year. If the City changes its fiscal year, it will notify the MSRB of the change.

NOTICE OF CERTAIN EVENTS

The City will also provide timely notices of certain events to the MSRB. The City will provide notice of any of the following events with respect to the Certificates to the MSRB in a timely manner (but not in excess of ten business days after the occurrence of the event): (1) principal and interest payment delinquencies; (2) non-payment related defaults, if material; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB), or other material notices or determinations with respect to the tax-exempt status of the Certificates, or other material events affecting the tax status of the Certificates; (7) modifications to rights of holders of the Certificates, if material; (8) Certificate calls, if material, and tender offers; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the Certificates, if material; (11) rating changes; (12) bankruptcy, insolvency, receivership, or similar event of the City, which shall occur as described below; (13) the consummation of a merger, consolidation, or acquisition involving the City or the sale of all or substantially all of its assets, other than in the ordinary course of business, the entry into of a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; and (14) appointment of a successor or additional trustee or the change of name of a trustee, if material. In addition, the City will provide timely notice of any failure by the City to provide annual financial information in accordance with their agreement described above under "ANNUAL REPORTS".

For these purposes, any event described in (12) in the immediately preceding paragraph is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent, or similar officer for the City in a proceeding under the United States Bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the City, or if such jurisdiction has been assumed by leaving the existing governing body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement, or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the City.

LIMITATIONS AND AMENDMENTS

The City has agreed to update information and to provide notices of certain specified events only as described above. The City has not agreed to provide other information that may be relevant or material to a complete presentation of its financial results of operations, condition, or prospects or agreed to update any information that is provided, except as described above. The City makes no representation or warranty concerning such information or concerning its usefulness to a decision to invest in or sell Certificates at any future date. The City disclaims any contractual or tort liability for damages resulting in whole or in part from any breach of its continuing disclosure agreement or from any statement made pursuant to its agreement, although holders of Certificates may seek a writ of mandamus to compel the City to comply with its agreement.

The City may amend its continuing disclosure agreement from time to time to adapt to changed circumstances that arise from a change in legal requirements, a change in law, or a change in the identity, nature, status, or type of operations of the City, if (i) the agreement, as amended, would have permitted an underwriter to purchase or sell Certificates in the offering described herein in compliance with the Rule, taking into account any amendments or interpretations of the Rule to the date of such amendment, as well as such changed circumstances, and (ii) either (a) the holders of a majority in aggregate principal amount of the outstanding Certificates consent to the amendment or (b) any person unaffiliated with the City (such as nationally recognized bond counsel) determines that the amendment will not materially impair the interests of the holders and beneficial owners of the Certificates. The City may also amend or repeal the provisions of this continuing disclosure agreement if the SEC amends or repeals the applicable provisions of the SEC Rule 15c2-12 or a court of final jurisdiction enters judgment that such provisions of the SEC Rule 15c2-12 are

invalid, but only if and to the extent that the provisions of this sentence would not prevent an underwriter from lawfully purchasing or selling Certificates in the primary offering of the Certificates. If the City so amends the agreement, it has agreed to include with the next financial information and operating data provided in accordance with its agreement described under "ANNUAL REPORTS" an explanation, in narrative form, of the reasons for the amendment and of the impact of any change in the type of financial information and operating data so provided.

COMPLIANCE WITH PRIOR UNDERTAKINGS

The City became obligated to make annual disclosure of certain financial information by filing with the state information depository ("SID") and each nationally recognized municipal securities information repository ("NRMSIR") in connection with the offering of its Certificates of Obligation, Series 2003. For fiscal years ending 2007, 2008 and 2010 audited financial statements and certain required financial information were not timely filed with the SID and NRMSIRs. The City has subsequently filed the required financial information, along with a notice of late filing, for the last five years with the current NRMSIR, the MSRB via EMMA. The City has implemented procedures to ensure the timely filing of all required financial information in the future.

MISCELLANEOUS

FINANCIAL ADVISOR

First Southwest Company is employed as Financial Advisor to the City in connection with the issuance of the Certificates. The Financial Advisor's fee for services rendered with respect to the sale of the Certificates is contingent upon the issuance and delivery of the Certificates. First Southwest Company, in its capacity as Financial Advisor, does not assume any responsibility for the information, covenants and representations contained in any of the legal documents with respect to the federal income tax status of the Certificates, or the possible impact of any present, pending or future actions taken by any legislative or judicial bodies.

The Financial Advisor to the City has provided the following sentence for inclusion in this Official Statement. The Financial Advisor has reviewed the information in this Official Statement in accordance with, and as part of, its responsibilities to the City and, as applicable, to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Financial Advisor does not guarantee the accuracy or completeness of such information.

UNDERWRITER

The Underwriter has agreed, subject to certain conditions, to purchase the Certificates from the City, at an underwriting discount of \$_____. The Underwriter will be obligated to purchase all of the Certificates if any Certificates are purchased. The Certificates to be offered to the public may be offered and sold to certain dealers (including the Underwriter and other dealers depositing Certificates into investment trusts) at prices lower than the public offering prices of such Certificates and such public offering prices may be changed, from time to time, by the Underwriter.

The Underwriter has provided the following sentence for inclusion in this Official Statement. The Underwriter has reviewed the information in this Official Statement in accordance with, and as part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information.

FORWARD-LOOKING STATEMENTS DISCLAIMER

The statements contained in this Official Statement, and in any other information provided by the City, that are not purely historical, are forward-looking statements, including statements regarding the City's expectations, hopes, intentions, or strategies regarding the future. Readers should not place undue reliance on forward-looking statements. All forward-looking statements included in this Official Statement are based on information available to the City on the date hereof, and the City assumes no obligation to update any such forward-looking statements. The City's actual results could differ materially from those discussed in such forward-looking statements.

The forward-looking statements included herein are necessarily based on various assumptions and estimates and are inherently subject to various risks and uncertainties, including risks and uncertainties relating to the possible invalidity of the underlying assumptions and estimates and possible changes or developments in social, economic, business, industry, market, legal, and regulatory circumstances and conditions and actions taken or omitted to be taken by third parties, including customers, suppliers, business partners and competitors, and legislative, judicial, and other governmental authorities and officials. Assumptions related to the foregoing involve judgments with respect to, among other things, future economic, competitive, and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond the control of the City. Any of such assumptions could be inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this Official Statement will prove to be accurate.

The financial data and other information contained herein have been obtained from the City's records, audited financial statements and other sources which are believed to be reliable. There is no guarantee that any of the assumptions or estimates contained herein will be realized. All of the summaries of the statutes, documents and resolutions contained in this Official Statement are made subject to all of the provisions of such statutes, documents and resolutions. These summaries do not purport to be complete statements of such provisions and reference is made to such documents for further information. Reference is made to original documents in all respects.

The Ordinance authorizing the issuance of the Certificates will also approve the form and content of this Official Statement, and any addenda, supplement or amendment thereto, and authorize its further use in the reoffering of the Certificates by the Underwriter.

Mayor
City of Cleveland, Texas

ATTEST:

City Secretary
City of Cleveland, Texas

APPENDIX A

GENERAL INFORMATION REGARDING THE CITY

THE CITY . . . The City of Cleveland, located in Liberty and Montgomery Counties, was incorporated in 1935. The City covers approximately 4.81 square miles and its economy is centered around timber-related industries. The City's economic foundation also includes oil and gas production, sand and gravel, tourism and agriculture.

CENSUS POPULATION

	1960 Official Census	1970 Official Census	1980 Official Census	1990 Official Census	2000 Official Census	2010 Official Census
City of Cleveland	5,383	5,627	5,977	7,124	7,605	7,675
Liberty County	31,595	33,014	47,088	52,726	70,154	75,643

LOCATION . . . The major route traveling through Cleveland is U.S. Highway 59 ("US 59"), traveling southwest towards Houston and north east into East Texas to the cities of Livingston, Lufkin, and Nacogdoches, and onward to Texarkana, Texas. US 59 Business is the original route of US 59, which runs north and south through the center of Cleveland, known locally as Washington Avenue and Loop 537. SH 105 travels east and west, and Cleveland is roughly the halfway point between Beaumont and Navasota.

MEDICAL CENTER . . . Cleveland Regional Medical Center serves the City.

TOP FIVE EMPLOYERS . . . Major employers in the Cleveland area are:

Name of Firm	Type of Business	Approximate Number of Employees
Campbell Concrete	Manufacturing	650
Cleveland ISD	Education	415
Wal-Mart	Retail	400
Louisiana Pacific Corporation	Manufacturing	350
Cleveland Regional Medical Center	Hospital	305

Source: Texas Workforce Commission

RAILROADS . . . Burlington Northern Santa Fe and Union Pacific provide railroad service to the City.

AIR SERVICE . . . The City is served by Cleveland Municipal Airport which features a paved and lighted 5,000 foot runway. The nearest commercial air service is Houston Intercontinental Airport 30 miles southwest, which provides regional, national and international services.

EDUCATION . . . The City is within the Cleveland Independent School District consisting of four elementary schools, one middle school and one high school.

PARKS AND RECREATION . . . The City maintains three parks and a community swimming pool. City parks are available to the public year round with the exception of the pool which has a schedule that varies during the spring and summer months. Various amenities that the parks provide include basketball and volleyball courts, playground equipment, a covered pavilion, picnic tables and restrooms.

LABOR FORCE

Calendar Year	Labor Force	Liberty County		
		Total Employment	Total Unemployment	Unemployment Rate
2007	30,607	28,990	1,617	5.3%
2008	30,802	28,940	1,862	6.0%
2009	31,437	28,256	3,181	10.1%
2010	32,067	28,525	3,542	11.0%
2011	32,490	29,050	3,440	10.6%
2012 ⁽¹⁾	32,975	29,886	3,090	9.4%

(1) As of August 31, 2012

APPENDIX B

EXCERPTS FROM THE
CITY OF CLEVELAND, TEXAS
ANNUAL FINANCIAL REPORT

For the Year Ended September 30, 2011

The information contained in this Appendix consists of excerpts from the City of Cleveland, Texas Annual Financial Report for the Year Ended 2011, and is not intended to be a complete statement of the City's financial condition. Reference is made to the complete Report for further information.



Hereford, Lynch, Sellars & Kirkham

Certified Public Accountants • A Professional Corporation

1406 Wilson Road
Conroe, Texas 77304
(936) 756-8127
Fax (936) 756-8132

Members of the
American Institute of Certified Public Accountants
Texas Society of Certified Public Accounts
Private Companies Practice Section
of the AICPA Division for Firms

111 E. Boothe
Cleveland, Texas 77327
(281) 592-6443
Fax (281) 592-7706

INDEPENDENT AUDITORS' REPORT

The Honorable Mayor and Members of City Council
City of Cleveland, Texas
Cleveland, Texas 77327

The Honorable Mayor and Members of City Council:

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

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

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

In accordance with *Government Auditing Standards*, we have also issued our report dated January 10, 2012, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and schedule of funding progress for the Texas Municipal Retirement System, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial

statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's financial statements as a whole. The introductory section, combining and discretely presented component unit financial statements section, and other supplementary information, are presented for purposes of additional analysis and are not a required part of the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the financial statements. The combining and discretely presented component unit financial statements section, other supplementary information section, and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Respectfully submitted,

Hereford, Lynch, Sellars & Kirkham, P.C.

HEREFORD, LYNCH, SELLARS & KIRKHAM, P.C.
Certified Public Accountants

Conroe, Texas
January 10, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of City of Cleveland's annual financial report presents our discussion and analysis of the City's financial performance during the fiscal year ended September 30, 2011. Please read it in conjunction with the City's financial statements, which follow this section.

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to City of Cleveland's 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 financial 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 Financial 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 assets includes all of the government's assets 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 assets and how they have changed. Net assets—the difference between the City's assets and liabilities—is one way to measure the City's financial health or *position*.

- Over time, increases or decreases in the City's net assets 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 nonfinancial 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, public works, transportation, culture and recreation, grants, economic development, debt service, and water and sewer. Charges for services, operating grants and contributions, and taxes 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. 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.
- The City Council 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 types 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* that 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 statements, 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 HIGHLIGHTS

- The assets of the City exceeded its liabilities at the close of the fiscal year by \$16,283,470 (net assets). As required by GASB Statement No. 34, net assets also reflect \$13,111,449 that is invested in capital assets, net of related debt.
- During the year, the City's revenues of \$12,098,983 exceeded expenses of \$10,235,383 by \$1,863,600.
- The General Fund reported a fund balance this year of \$740,807, in which \$694,064 was unassigned and approximated 9% of General Fund expenditures. Total fund balance decreased \$155,594 from current year operations.
- The Debt Service Fund reported a fund balance this year of \$178,063 which was restricted for debt service fund expenditures. Total fund balance decreased \$21,062 from prior year.
- The Utility Fund reported an operating income of \$561,612, and an increase in net assets of \$369,312.
- The Component Unit – Cleveland Economic Development Corporation reported net assets of \$1,794,394, of which \$829,164 was unrestricted. Total net assets increased \$235,205 from prior year.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

Net assets. The City's combined net assets were \$16,283,470 at September 30, 2011.

Table A-1
CITY OF CLEVELAND, TEXAS NET ASSETS

	Governmental Activities		Business-type Activities		Total	
	2011	2010	2011	2010	2011	2010
Current and Other Assets	\$ 2,832,942	\$ 2,485,466	\$ 4,030,374	\$ 1,801,920	\$ 6,863,316	\$ 4,287,386
Capital Assets	15,111,032	13,908,362	7,849,797	7,525,985	22,960,829	21,434,347
Total Assets	17,943,974	16,393,828	11,880,171	9,327,905	29,824,145	25,721,733
Long-term Liabilities Outstanding	7,302,922	7,554,832	5,115,000	3,010,000	12,417,922	10,564,832
Other Liabilities	772,124	464,356	350,629	272,675	1,122,753	737,031
Total Liabilities	8,075,046	8,019,188	5,465,629	3,282,675	13,540,675	11,301,863
Net Assets:						
Invested in Capital Assets, net of Related Debt	7,808,110	6,356,700	5,303,339	5,035,958	13,111,449	11,392,658
Restricted	353,791	357,560	398,449	418,182	752,240	775,742
Unrestricted	1,707,027	1,660,380	712,754	591,090	2,419,781	2,251,470
Total Net Assets	\$ 9,868,928	\$ 8,374,640	\$ 6,414,542	\$ 6,045,230	\$ 16,283,470	\$ 14,419,870

The City's total assets of \$29,824,145 are largely comprised of capital assets, net of accumulated depreciation of \$22,960,829, or 77%. GASB Statement No. 34 requires that all capital assets, including infrastructure, be reported in the government-wide statements. Capital assets are non-liquid assets and cannot be utilized to satisfy City obligations.

Long-term liabilities of \$12,417,922 comprise the largest portion of the City's total liabilities of \$13,540,675 at 92%. Of total long-term liabilities, \$770,359 is due within one year, with the remainder \$11,647,563 being due over a period of time greater than one year. A more in-depth discussion of long-term debt can be found in the notes to the financial statements.

Approximately 80% of total net assets or \$13,111,449 represents investments in capital assets, net of related debt and approximately 5% of total net assets or \$752,240 represents restriction for debt service. The \$2,419,781 (15%) of unrestricted net assets represent resources available to fund the programs of the City next year.

Changes in net assets. The City's combined increase in current year net assets was \$1,863,600 at September 30, 2011.

**Table A-2
CITY OF CLEVELAND, TEXAS CHANGE IN NET ASSETS**

	Governmental Activities		Business-type Activities		Total	
	2011	2010	2011	2010	2011	2010
Revenues:						
Program Revenues:						
Charges for Services	\$ 1,918,739	\$ 1,152,058	\$ 3,140,654	\$ 3,407,971	\$ 5,059,393	\$ 4,560,029
Operating Grants and Contributions	135,575	388,312	-	-	135,575	388,312
Capital Grants and Contributions	1,437,552	466,613	343,560	168,186	1,781,112	634,799
General Revenues:						
Property Taxes	2,232,954	2,225,907	-	-	2,232,954	2,225,907
Sales and Other Taxes	2,316,293	2,457,479	-	-	2,316,293	2,457,479
Franchise Taxes	483,970	540,596	-	-	483,970	540,596
Earnings on Investments	10,889	11,826	7,547	6,790	18,436	18,616
Gain on Sale of Assets	15,500	-	-	-	15,500	-
Proceeds from Insurance	29,392	66,903	10,899	23,348	40,291	90,251
Miscellaneous	15,459	61,797	-	2,061	15,459	63,858
Total Revenues	8,596,323	7,371,491	3,502,660	3,608,356	12,098,983	10,979,847
Expenses:						
General Government	800,884	941,093	-	-	800,884	941,093
Public Safety	4,108,437	3,711,673	-	-	4,108,437	3,711,673
Public Works	284,069	281,045	-	-	284,069	281,045
Transportation	820,878	812,646	-	-	820,878	812,646
Culture and Recreation	1,034,176	894,707	-	-	1,034,176	894,707
Grants	39,731	324,674	-	-	39,731	324,674
Economic Development	86,902	75,233	-	-	86,902	75,233
Debt Service	326,958	343,649	-	-	326,958	343,649
Water and Sewer	-	-	2,733,348	3,029,476	2,733,348	3,029,476
Total Expenses	7,502,035	7,384,720	2,733,348	3,029,476	10,235,383	10,414,196
Excess (Deficiency) Before Transfers	1,094,288	(13,229)	769,312	578,880	1,863,600	565,651
Transfers In (Out)	400,000	450,367	(400,000)	(450,367)	-	-
Increase (Decrease) in Net Assets	1,494,288	437,138	369,312	128,513	1,863,600	565,651
Net Assets - Beginning	8,374,640	7,937,502	6,045,230	5,916,717	14,419,870	13,854,219
Net Assets - Ending	\$ 9,868,928	\$ 8,374,640	\$ 6,414,542	\$ 6,045,230	\$ 16,283,470	\$ 14,419,870

Governmental Activities

The City's total revenues were \$8,596,323 from all governmental activities. A significant portion, \$2,316,293 or 27%, of the City's revenue comes from sales and other taxes. Property tax revenue accounts for \$2,232,954, or 26%, of total revenue for governmental activities. The most significant changes in governmental revenues was the increases in capital grants and contributions and charges for services. The increase in capital grants and contributions results primarily from the receipt of grant funds for completion of the storm drainage project. The increase in charges for services results primarily from an increase in fines collected because of the red light project and forfeitures.

The total cost of all governmental programs and services was \$7,502,035. The public safety function accounted for \$4,108,437, or 55% of this total. Expenses increased \$117,315 in total, which was primarily the result of increases in public safety. The increase in public safety results from an increase expenditures associated with the red light project.

Business-type Activities

Business-type activities are financed in whole or part by fees charged to external users for goods or services (water and sewer). They are reported in the enterprise fund. Business-type activities increased the City's net assets by \$369,312. Revenue can be reported as program revenue or general revenue—all revenues are general unless they are required to be reported as program revenues. Program revenue, charges for services, which includes revenues attributable to a specific program because they result from exchange-like transactions or other events, such as charges to customers. Charges for service of \$3,140,654 are utilized to provide funds for program expenses of \$2,733,348.

The increase in net assets for business-type activities is due to an increase in federal grants for water and sewer improvements as well as a decrease in sanitation expenditures due to the City now contracts with an outside company for sanitation services.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

Governmental Funds

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

As the City completed the year, its governmental funds, as presented in the balance sheet reported combined ending fund balances of \$1,349,055, which is a decrease of \$38,526 from last year's total of \$1,387,581.

The General Fund is the operating fund of the City. At the end of the current fiscal year, unassigned fund balance of the General Fund was \$694,064, which represented 94% of total general fund balance. As a measure of the General Fund's liquidity, it may be useful to compare unassigned fund balance to total fund expenditures. Unassigned fund balance represents 9% of total General Fund expenditures. Refer to page 18 of this report for a more detailed presentation of governmental fund balances.

The debt service fund ending fund balance of \$178,063, all of which is restricted for the payment of principal and interest on debt. The debt service fund balance decreased \$21,062 during the year, primarily due to the debt service requirements exceeded the tax collections.

The capital projects ending fund balance of \$0. The net decrease in fund balance during the current year in the capital projects fund was \$3,170. The increase was due to planned expenditures exceeded interest earned.

Proprietary Funds

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

Unrestricted net assets of the Water and Sewer Funds at the end of the current fiscal year amounted to \$712,754. The total increase in net assets for the Water and Sewer Funds was \$369,312. Other factors concerning these funds have been addressed in the discussion of the City's business-type activities.

General Fund Budgetary Highlights

The City amended the budget several times throughout the year. Differences between the originally-adopted budget and the final amended budget of the general fund were to increase appropriations \$109,183. There were no significant individual variations between the original budget and final budget.

Significant differences between the final amended budget and actual amounts can be briefly summarized as follows:

- Actual Expenditures, when compared to the final budgeted amount, had a \$1,297,127 unfavorable variance primarily due to increases in spending in Street Department Capital Outlay.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of 2011, the City had invested \$22,960,829 in a broad range of capital assets. More detailed information about the City's capital assets is presented in the notes to the financial statements.

**Table A-3
CITY OF CLEVELAND, TEXAS CAPITAL ASSETS
(net of depreciation)**

	Governmental Activities		Business-type Activities		Total	
	2011	2010	2011	2010	2011	2010
Land	\$ 2,068,148	\$ 2,068,148	\$ 178,621	\$ 178,621	\$ 2,246,769	\$ 2,246,769
Buildings and Improvements	14,007,773	12,624,298	47,997	47,997	14,055,770	12,672,295
Furniture & Equipment	4,016,762	3,689,685	661,303	488,566	4,678,065	4,178,251
Water System	-	-	4,375,434	3,939,005	4,375,434	3,939,005
Sewer System	-	-	15,127,980	14,727,488	15,127,980	14,727,488
Construction in Progress	54,236	30,000	-	218,691	54,236	248,691
Totals	20,146,919	18,412,131	20,391,335	19,600,368	40,538,254	38,012,499
Total Accumulated Depreciation	(5,035,887)	(4,503,769)	(12,541,538)	(12,074,383)	(17,577,425)	(16,578,152)
Net Capital Assets	\$ 15,111,032	\$ 13,908,362	\$ 7,849,797	\$ 7,525,985	\$ 22,960,829	\$ 21,434,347

Major capital asset purchases during the year included the following:

- Improvements to Sewer System \$400,493
- Storm Drainage Project \$1,353,445
- 500k Gallon Ground Tank \$398,608

Long Term Debt

At year-end, the City had \$12,417,922 in long-term debt outstanding as shown in Table A-4. More detailed information about the City's debt is presented in the notes to the financial statements.

**Table A-4
CITY OF CLEVELAND, TEXAS LONG-TERM DEBT**

	Governmental Activities		Business-type Activities		Total	
	2011	2010	2011	2010	2011	2010
Certificates of Obligation	\$ 7,170,000	\$ 7,510,000	\$ -	\$ -	\$ 7,170,000	\$ 7,510,000
Revenue Bonds	-	-	5,115,000	3,010,000	5,115,000	3,010,000
Note Payable	132,922	44,832	-	-	132,922	44,832
Total Long-term Debt	\$ 7,302,922	\$ 7,554,832	\$ 5,115,000	\$ 3,010,000	\$ 12,417,922	\$ 10,564,832

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

- Total tax rate \$.685 per \$100 valuation in fiscal year 2012 (\$.472 for maintenance and operations and \$.213 for interest and sinking).
- These indicators were taken into account when adopting the general fund budget for 2012. Amounts available for appropriation in the general fund budget are \$694,064 at September 30, 2011. The City projects to transfer \$400,000 from the Water and Sewer Fund to the General Fund which will be used to fund expenditures of the General Fund budget.
- The City's budgetary General Fund balance is expected to increase \$82,442.
- On October 11, 2011 the City issued \$500,000 Tax Notes in the fiscal year 2011-2012.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the City's Finance Department.

(This page was intentionally left blank)

BASIC FINANCIAL STATEMENTS

(This page was intentionally left blank)

CITY OF CLEVELAND, TEXAS

EXHIBIT A-1

STATEMENT OF NET ASSETS

SEPTEMBER 30, 2011

	Governmental Activities	Business-type Activities	Total	Component Unit Cleveland EDC
ASSETS:				
Cash and Cash Equivalents	\$ 1,398,361	\$ 522,564	\$ 1,920,925	\$ 683,463
Investments	51,352	53,410	104,762	131,744
Receivables (Net of Allowances for Uncollectibles, Where Applicable):				
Property Taxes	647,068	-	647,068	-
Accounts	103,400	451,708	555,108	-
Due From Other Governments	565,888	56,421	622,309	34,647
Other	44,249	-	44,249	-
Internal Balances	20,720	(20,720)	-	-
Due From Component Unit	1,904	-	1,904	-
Deferred Charges	-	112,498	112,498	-
Restricted Assets:				
Cash - Reserve	-	398,449	398,449	-
Cash - Construction	-	2,453,649	2,453,649	-
Investment - Construction	-	2,395	2,395	-
Capital Assets:				
Land	2,068,148	178,621	2,246,769	1,228,132
Buildings and Improvements	14,007,773	47,997	14,055,770	-
Furniture & Equipment	4,016,762	661,303	4,678,065	-
Water System	-	4,375,434	4,375,434	-
Sewer System	-	15,127,980	15,127,980	-
Construction in Progress	54,236	-	54,236	88,520
Accumulated Depreciation	(5,035,887)	(12,541,538)	(17,577,425)	-
Total Assets	<u>17,943,974</u>	<u>11,880,171</u>	<u>29,824,145</u>	<u>2,166,506</u>
LIABILITIES:				
Accounts Payable	631,421	124,746	756,167	18,786
Accrued Liabilities	110,095	20,253	130,348	-
Refundable Deposits	-	182,080	182,080	-
Accrued Interest	29,357	23,550	52,907	-
Due to Primary Government	-	-	-	1,904
Unearned Revenue	1,251	-	1,251	-
Noncurrent Liabilities:				
Notes Payable - Current	40,359	-	40,359	35,567
Notes Payable - Long-term	92,563	-	92,563	315,855
Certificates of Obligation and Bonds Payable-Current	375,000	355,000	730,000	-
Certificates of Obligation and Bonds Payable-Long-term	6,795,000	4,760,000	11,555,000	-
Total Liabilities	<u>8,075,046</u>	<u>5,465,629</u>	<u>13,540,675</u>	<u>372,112</u>
NET ASSETS:				
Investment in Capital Assets, Net of Related Debt	7,808,110	5,303,339	13,111,449	965,230
Restricted for:				
Debt Services	353,791	398,449	752,240	-
Unrestricted	1,707,027	712,754	2,419,781	829,164
Total Net Assets	<u>\$ 9,868,928</u>	<u>\$ 6,414,542</u>	<u>\$ 16,283,470</u>	<u>\$ 1,794,394</u>

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

CITY OF CLEVELAND, TEXAS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2011

FUNCTIONS/PROGRAMS	Expenses	Program Revenues		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
PRIMARY GOVERNMENT:				
Governmental Activities:				
General Government:				
City Council	\$ 25,635	\$ -	\$ -	\$ -
City Administration	775,249	-	-	-
Public Safety:				
Municipal Court	207,606	34,942	-	-
Police Department	2,643,915	969,711	78,971	-
Animal Control	96,573	-	-	-
Fire and Ambulance	1,160,343	597,725	-	151,999
Public Works:				
Inspection Department	206,476	60,531	-	-
Garage Department	77,593	-	-	-
Transportation:				
Street Department	762,696	-	-	1,248,053
Airport Department	58,182	68,563	-	37,500
Culture and Recreation:				
Library	396,673	23,991	6,161	-
Cemetery and Parks	325,954	55,898	-	-
Civic/Community	311,549	107,378	-	-
Grants	39,731	-	50,443	-
Economic Development	86,902	-	-	-
Debt Service:				
Interest and Fiscal Charges	326,958	-	-	-
Total Governmental Activities	<u>7,502,035</u>	<u>1,918,739</u>	<u>135,575</u>	<u>1,437,552</u>
Business-type Activities:				
Water and Sewer	2,733,348	3,140,654	-	343,560
Total Business-Type Activities	<u>2,733,348</u>	<u>3,140,654</u>	<u>-</u>	<u>343,560</u>
Total Primary Government	\$ <u>10,235,383</u>	\$ <u>5,059,393</u>	\$ <u>135,575</u>	\$ <u>1,781,112</u>
COMPONENT UNIT:				
Cleveland Economic Development Corp.	\$ <u>200,907</u>	\$ -	\$ -	\$ -

General Revenues:
Property Taxes
Sales and Other Taxes
Franchise Taxes
Earnings on Investments
Gain on Sale of Assets
Proceeds from Insurance
Miscellaneous
Transfers
Total General Revenues and Transfers
Change in Net Assets
Net Assets - Beginning
Net Assets - Ending

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

Net (Expense) Revenue and Changes in Net Assets			Component Unit
Governmental Activities	Business-type Activities	Total	Cleveland EDC
\$ (25,635)	\$ -	\$ (25,635)	\$ -
(775,249)	-	(775,249)	-
(172,664)	-	(172,664)	-
(1,595,233)	-	(1,595,233)	-
(96,573)	-	(96,573)	-
(410,619)	-	(410,619)	-
(145,945)	-	(145,945)	-
(77,593)	-	(77,593)	-
485,357	-	485,357	-
47,881	-	47,881	-
(366,521)	-	(366,521)	-
(270,056)	-	(270,056)	-
(204,171)	-	(204,171)	-
10,712	-	10,712	-
(86,902)	-	(86,902)	-
<u>(326,958)</u>	<u>-</u>	<u>(326,958)</u>	<u>-</u>
<u>(4,010,169)</u>	<u>-</u>	<u>(4,010,169)</u>	<u>-</u>
-	750,866	750,866	-
-	750,866	750,866	-
<u>(4,010,169)</u>	<u>750,866</u>	<u>(3,259,303)</u>	
			<u>(200,907)</u>
2,232,954	-	2,232,954	-
2,316,293	-	2,316,293	429,429
483,970	-	483,970	-
10,889	7,547	18,436	6,683
15,500	-	15,500	-
29,392	10,899	40,291	-
15,459	-	15,459	-
400,000	(400,000)	-	-
<u>5,504,457</u>	<u>(381,554)</u>	<u>5,122,903</u>	<u>436,112</u>
1,494,288	369,312	1,863,600	235,205
8,374,640	6,045,230	14,419,870	1,559,189
<u>\$ 9,868,928</u>	<u>\$ 6,414,542</u>	<u>\$ 16,283,470</u>	<u>\$ 1,794,394</u>

CITY OF CLEVELAND, TEXAS
BALANCE SHEET - GOVERNMENTAL FUNDS
SEPTEMBER 30, 2011

	General Fund	Debt Service Fund
	<u> </u>	<u> </u>
ASSETS:		
<i>Cash and Cash Equivalents</i>	\$ 559,170	\$ 176,588
<i>Investments</i>	51,352	-
<i>Receivable (Net of Allowances for Uncollectible Accounts, Where Applicable):</i>		
<i>Property Taxes</i>	446,346	200,722
<i>Accounts - Ambulance</i>	94,053	-
<i>Accounts -Hotel/Motel</i>	-	-
<i>Due From Other Governments</i>	565,888	-
<i>Other</i>	44,249	-
<i>Due From Other Funds</i>	48,522	1,475
<i>Due From Component Unit</i>	1,904	-
Total Assets	\$ <u>1,811,484</u>	\$ <u>378,785</u>
 LIABILITIES AND FUND BALANCES		
LIABILITIES :		
<i>Accounts Payable</i>	\$ 415,264	\$ -
<i>Accrued Liabilities</i>	108,379	-
<i>Due To Other Funds</i>	5,385	-
<i>Deferred Revenue</i>	541,649	200,722
Total Liabilities	<u>1,070,677</u>	<u>200,722</u>
 FUND BALANCES:		
<i>Restricted for Court</i>	13,243	-
<i>Restricted for Debt</i>	-	178,063
<i>Restricted for Economic Development</i>	-	-
<i>Restricted for Police</i>	-	-
<i>Assigned Fund Balance - Capital Expenditures for Fire and Ambulance</i>	15,500	-
<i>Assigned Fund Balance - Development Services</i>	18,000	-
<i>Unassigned Fund Balances</i>	694,064	-
Total Fund Balance	<u>740,807</u>	<u>178,063</u>
 Total Liabilities and Fund Balance	 \$ <u>1,811,484</u>	 \$ <u>378,785</u>

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

EXHIBIT A-3

Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
\$ -	\$ 662,603	\$ 1,398,361
-	-	51,352
-	-	647,068
-	-	94,053
-	9,347	9,347
-	-	565,888
-	-	44,249
-	1,619	51,616
-	-	1,904
<u>\$ -</u>	<u>\$ 673,569</u>	<u>\$ 2,863,838</u>
-	-	-
-	216,157	\$ 631,421
-	1,716	110,095
-	25,511	30,896
-	-	742,371
<u>-</u>	<u>243,384</u>	<u>1,514,783</u>
-	-	-
-	-	13,243
-	-	178,063
-	278,448	278,448
-	151,737	151,737
-	-	15,500
-	-	18,000
-	-	694,064
<u>-</u>	<u>430,185</u>	<u>1,349,055</u>
<u>\$ -</u>	<u>\$ 673,569</u>	<u>\$ 2,863,838</u>

(This page was intentionally left blank)

CITY OF CLEVELAND, TEXAS

EXHIBIT A-4

*RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS
SEPTEMBER 30, 2011*

Total Fund Balance - Governmental Funds (Exhibit A-3)	\$ 1,349,055
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	15,111,032
Property taxes receivables are not available to pay for current period expenditures and, therefore, are deferred in the funds.	647,068
Ambulance receivables are not available to pay for current period expenditures and, therefore, are deferred in the funds.	94,052
Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the funds.	(7,302,922)
Other long-term liabilities, at year-end, consisted of accrued interest on the bonds and notes payable.	<u>(29,357)</u>
Total Net Assets - Governmental Activities (Exhibit A-1)	\$ <u>9,868,928</u>

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

CITY OF CLEVELAND, TEXAS
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2011

	General Fund	Debt Service Fund
	<u> </u>	<u> </u>
REVENUE:		
Taxes:		
Property Taxes	\$ 1,499,148	\$ 640,102
Sales and Other Taxes	2,189,659	-
Franchise Taxes	483,970	-
License and Permits	60,531	-
Charges for Services	867,819	-
Fines and Forfeitures	352,990	-
Intergovernmental	1,535,627	-
Earnings on Investments	4,823	2,086
Contributions	38,361	-
Miscellaneous	15,459	-
Total Revenues	<u>7,048,387</u>	<u>642,188</u>
EXPENDITURES:		
City Council	24,966	-
Administration	726,547	-
Civic / Community	242,442	-
Court	207,606	-
Police	2,009,753	-
Animal Control	96,573	-
Inspection	203,972	-
Street Department	669,138	-
Airport Department	30,401	-
Garage Department	76,242	-
Library Department	345,773	-
Cemetery and Parks	301,134	-
Grants	39,731	-
Fire and Ambulance	1,067,889	-
Economic Development	-	-
Capital Outlay:		
Administration	28,258	-
Police	-	-
Animal Control	6,740	-
Street Department	1,353,445	-
Airport Department	17,496	-
Library Department	33,984	-
Cemetery and Parks	18,903	-
Fire and Ambulance	231,857	-
Debt Service:		
Principal Retirement	46,920	340,000
Interest and Fiscal Charges	3,363	323,250
Total Expenditures	<u>7,783,133</u>	<u>663,250</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	<u>(734,746)</u>	<u>(21,062)</u>
Other Financing Sources (Uses):		
Proceeds from Sale of Assets	15,500	-
Proceeds from Insurance	29,392	-
Proceeds from Loans	135,010	-
Transfers In (Out)	399,250	-
Total Other Financing Sources (Uses)	<u>579,152</u>	<u>-</u>
Net Change in Fund Balances	(155,594)	(21,062)
Fund Balance - Beginning	896,401	199,125
Fund Balance - Ending	<u>\$ 740,807</u>	<u>\$ 178,063</u>

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

EXHIBIT A-5

Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
\$ -	\$ -	\$ 2,139,250
-	126,634	2,316,293
-	-	483,970
-	-	60,531
-	-	867,819
-	651,663	1,004,653
-	-	1,535,627
17	3,963	10,889
-	-	38,361
-	-	15,459
17	782,260	8,472,852
-	-	24,966
3,937	-	730,484
-	-	242,442
-	-	207,606
-	495,953	2,505,706
-	-	96,573
-	-	203,972
-	-	669,138
-	-	30,401
-	-	76,242
-	-	345,773
-	-	301,134
-	-	39,731
-	-	1,067,889
-	86,902	86,902
-	-	28,258
-	58,105	58,105
-	-	6,740
-	-	1,353,445
-	-	17,496
-	-	33,984
-	-	18,903
-	-	231,857
-	-	386,920
-	-	326,613
3,937	640,960	9,091,280
(3,920)	141,300	(618,428)
-	-	15,500
-	-	29,392
-	-	135,010
750	-	400,000
750	-	579,902
(3,170)	141,300	(38,526)
3,170	288,885	1,387,581
\$ -	\$ 430,185	\$ 1,349,055

CITY OF CLEVELAND, TEXAS

EXHIBIT A-6

*RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2011*

Total Net Change in Fund Balance - Governmental Funds (Exhibit A-5) \$ (38,526)

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

Some property taxes will not be collected for several months after the City's fiscal year end and are not considered "available" revenues and, therefore, are deferred in the governmental funds. Deferred tax revenues increased by this amount this year. 93,704

Some ambulance revenue will not be collected for several months after the City's fiscal year end and are not considered "available" revenues and, therefore, are deferred in the governmental funds. Deferred ambulance revenues decreased by this amount this year. (15,125)

Capital outlays are reported in governmental funds as expenditures. However, in the statement of activities, the cost of those assets are allocated over their estimated useful lives as depreciation expense.

Capital Outlay	\$ 1,748,788	
Depreciation Expense	<u>(546,118)</u>	1,202,670

Repayment of notes and certificates of obligation is an expenditure in the governmental funds but the repayment reduces long-term liabilities in the statement of net assets. 386,920

Loan proceeds provide current financial resources to governmental funds, but issuing debt increases long term liabilities in the statement of net assets. (135,010)

Interest on long-term debt in the statement of activities differs from the amount reported in the governmental funds because interest is recognized as an expenditure in the funds when it is due, and thus requires the use of current financial resources. In the statement of activities, however, interest expense is recognized as the interest accrues, regardless of when it is due. The increase of accrued interest reported in the statement of activities consist of accrued interest on notes and certificates of obligation. (345)

Change in Net Assets of Governmental Activities (Exhibit A-2) \$ 1,494,288

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

CITY OF CLEVELAND, TEXAS

EXHIBIT A-7

**GENERAL FUND
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - BUDGET (GAAP BASIS) AND ACTUAL
FOR THE YEAR ENDED SEPTEMBER 30, 2011**

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUE:				
<i>Taxes:</i>				
Property Taxes	\$ 1,517,514	\$ 1,517,514	\$ 1,499,148	\$ (18,366)
Sales and Other Taxes	2,199,582	2,199,582	2,189,659	(9,923)
Franchise Taxes	533,000	533,000	483,970	(49,030)
License and Permits	65,000	65,000	60,531	(4,469)
Charges for Services	930,300	661,500	867,819	206,319
Fines and Forfeitures	661,500	930,300	352,990	(577,310)
Intergovernmental	65,109	65,109	1,535,627	1,470,518
Earnings on Investments	6,900	6,900	4,823	(2,077)
Contributions	-	-	38,361	38,361
Miscellaneous	125,191	125,191	15,459	(109,732)
Total Revenues	<u>6,104,096</u>	<u>6,104,096</u>	<u>7,048,387</u>	<u>944,291</u>
EXPENDITURES:				
City Council	31,100	31,100	24,966	6,134
Administration	908,851	880,593	726,547	154,046
Civic/Community	223,892	234,596	242,442	(7,846)
Court	203,956	203,956	207,606	(3,650)
Police	2,039,521	2,065,608	2,009,753	55,855
Animal Control	110,894	104,154	96,573	7,581
Inspection	225,694	225,694	203,972	21,722
Street Department	655,785	669,138	669,138	-
Airport Department	33,629	30,401	30,401	-
Garage Department	76,179	76,179	76,242	(63)
Library Department	335,734	344,851	345,773	(922)
Cemetery and Parks	306,878	302,530	301,134	1,396
Grants	-	-	39,731	(39,731)
Fire and Ambulance	1,224,710	1,067,889	1,067,889	-
Capital Outlay				
Administration	-	28,258	28,258	-
Animal Control	-	6,740	6,740	-
Street Department	-	-	1,353,445	(1,353,445)
Airport Department	-	3,228	17,496	(14,268)
Library Department	-	-	33,984	(33,984)
Cemetery and Parks	-	18,903	18,903	-
Fire and Ambulance	-	156,821	231,857	(75,036)
Debt Service:				
Principal Retirement	-	32,717	46,920	(14,203)
Interest and Fiscal Charges	-	2,650	3,363	(713)
Total Expenditures	<u>6,376,823</u>	<u>6,486,006</u>	<u>7,783,133</u>	<u>(1,297,127)</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	<u>(272,727)</u>	<u>(381,910)</u>	<u>(734,746)</u>	<u>(352,836)</u>
Other Financing Sources (Uses):				
Proceeds from Sale of Assets	-	-	15,500	15,500
Proceeds from Insurance	-	-	29,392	29,392
Proceeds from Loans	-	-	135,010	135,010
Transfers In (Out)	400,000	410,704	399,250	(11,454)
Total Other Financing Sources (Uses)	<u>400,000</u>	<u>410,704</u>	<u>579,152</u>	<u>168,448</u>
Excess (Deficiency) of Revenues and Other Financing Sources Over (Under) Expenditures and Other Uses	<u>127,273</u>	<u>28,794</u>	<u>(155,594)</u>	<u>(184,388)</u>
Fund Balance - Beginning	896,401	896,401	896,401	-
Fund Balance - Ending	<u>\$ 1,023,674</u>	<u>\$ 925,195</u>	<u>\$ 740,807</u>	<u>\$ (184,388)</u>

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

CITY OF CLEVELAND, TEXAS

EXHIBIT A-8

STATEMENT OF NET ASSETS
 PROPRIETARY FUND
 SEPTEMBER 30, 2011

Water
 and Sewer
 Fund

ASSETS:

Current Assets:

Cash and Cash Equivalents	\$ 522,564
Investments	53,410
Receivables (Net of Allowances for Uncollectibles):	
Accounts - Utilities	451,708
Due from Other Governments	56,421
Due from Other Funds	2,291
Total Current Assets	<u>1,086,394</u>

Noncurrent Assets:

Restricted Assets:

Cash - Reserve	398,449
Cash - Construction	2,453,649
Investment - Construction	2,395

Deferred Charges:

Bond Issuance	112,498
---------------	---------

Capital Assets:

Land	178,621
Buildings & Improvements	47,997
Furniture & Equipment	661,303
Water System	4,375,434
Sewer System	15,127,980
Accumulated Depreciation	<u>(12,541,538)</u>
Total Noncurrent Assets	10,816,788
Total Assets	<u>\$ 11,903,182</u>

LIABILITIES:

Current Liabilities:

Accounts Payable	\$ 124,746
Accrued Liabilities	20,253
Refundable Deposits	182,080
Accrued Interest Payable	23,550
Due to Other Funds	23,011
Total Current Liabilities	<u>373,640</u>

Noncurrent Liabilities:

Bonds and Certificates of Obligation Payable - Current	355,000
Bonds and Certificates of Obligation Payable - Long-term	4,760,000
Total Noncurrent Liabilities	<u>5,115,000</u>
Total Liabilities	<u>5,488,640</u>

NET ASSETS:

Investment in Capital Assets, Net of Related Debt	5,303,339
Restricted for:	
Debt Services - Reserve (Expendable)	398,449
Unrestricted	712,754
Total Net Assets	<u>6,414,542</u>

Total Liabilities and Fund Balance	<u>\$ 11,903,182</u>
---	-----------------------------

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

CITY OF CLEVELAND, TEXAS

EXHIBIT A-9

STATEMENT OF REVENUES, EXPENSES, AND CHANGES
 IN NET ASSETS - PROPRIETARY FUND
 FOR THE YEAR ENDED SEPTEMBER 30, 2011

	Water and Sewer Fund
OPERATING REVENUES:	
<i>Charges for Services</i>	\$ 3,140,654
Total Operating Revenues	<u>3,140,654</u>
OPERATING EXPENSES:	
<i>Administrative</i>	298,393
<i>Water Production</i>	556,055
<i>Sewer Department</i>	614,807
<i>Sanitation Services</i>	642,632
<i>Depreciation</i>	467,155
Total Operating Expenses	<u>2,579,042</u>
Operating Income	<u>561,612</u>
NON-OPERATING REVENUES (EXPENSES):	
<i>Intergovernmental</i>	343,560
<i>Proceeds from Insurance</i>	10,899
<i>Earnings on Investments</i>	7,547
<i>Interest and Fees on Debt</i>	(154,306)
Total Non-Operating Revenues (Expenses)	<u>207,700</u>
Income before Other Financing Sources (Uses)	769,312
OTHER FINANCING SOURCES (USES):	
<i>Transfers Out</i>	(400,000)
Total Other Financing Sources (Uses)	<u>(400,000)</u>
Change in Net Assets	369,312
Total Net Assets - Beginning	<u>6,045,230</u>
Total Net Assets - Ending	<u>\$ 6,414,542</u>

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

CITY OF CLEVELAND, TEXAS
STATEMENT OF CASH FLOWS
PROPRIETARY FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2011

EXHIBIT A-10

	Water and Sewer Fund
CASH FLOWS FROM OPERATING ACTIVITIES:	
<i>Cash Received for Services</i>	\$ 3,197,539
<i>Cash Payments to Suppliers for Goods and Services</i>	(2,098,480)
Net Cash Provided (Used) by Operating Activities	<u>1,099,059</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:	
<i>Transfers From (To) Other Funds</i>	(400,000)
<i>Grant Contributions</i>	287,139
<i>Insurance Proceeds</i>	10,899
Net Cash Provided (Used) by Noncapital Financing Activities	<u>(101,962)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:	
<i>Proceeds from Capital Debt</i>	2,360,000
<i>Purchase of Capital Assets</i>	(790,967)
<i>Principal Paid on Capital Debt</i>	(255,000)
<i>Interest and Fees Paid on Capital Debt</i>	(150,723)
Net Cash Provided (Used) for Capital and Related Financing Activities	<u>1,163,310</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
<i>Earnings on Investments</i>	7,547
<i>Sale (Purchase) of Investments</i>	464,062
Net Cash Provided (Used) for Investing Activities	<u>471,609</u>
Net Increase (Decrease) in Cash and Cash Equivalents	2,632,016
Cash and Cash Equivalents at Beginning of Year	742,646
Cash and Cash Equivalents at End of Year	<u>\$ 3,374,662</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:	
Operating Income	\$ 561,612
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:	
<i>Depreciation</i>	467,155
<i>Change in Assets and Liabilities:</i>	
<i>Decrease (Increase) in Accounts and Other Receivables, net</i>	59,633
<i>Decrease (Increase) in Deferred Charges</i>	(77,700)
<i>Decrease (Increase) in Due to Other Funds</i>	(2,291)
<i>Increase (Decrease) in Accounts Payable</i>	70,951
<i>Increase (Decrease) in Accrued Liabilities</i>	6,168
<i>Increase (Decrease) in Refundable Deposits</i>	(2,748)
<i>Increase (Decrease) in Due to Other Funds</i>	16,279
Total Adjustments	<u>537,447</u>
Net Cash Provided (Used) by Operating Activities	<u>\$ 1,099,059</u>

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

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

A. Summary of Significant Accounting Policies

The accompanying financial statements of City of Cleveland, Texas (the "City") have been prepared in conformity with accounting principles applicable to governmental units which are generally accepted in the United States of America. The Governmental Accounting Standards Board ("GASB") is the accepted standard setting body for establishing governmental accounting and financial reporting principles.

1. Reporting Entity

The City's basic financial statements include the accounts of all its operations. The City evaluated whether any other entity should be included in these financial statements. The criteria for including organizations as component units within the City's reporting entity, as set forth in GASB Statement No. 14, "The Financial Reporting Entity," include whether:

- The organization is legally separate (can sue and be sued in its name)
- The City holds the corporate powers of the organization
- The City appoints a voting majority of the organization's board
- The City is able to impose its will on the organization
- The organization has the potential to impose a financial benefit/burden to the City
- There is fiscal dependency by the organization on the City
- The exclusion of the organization would result in misleading or incomplete financial statements

Based on the above criteria, the City reports the Cleveland Economic Development Corporation (CEDC), a component unit, which is reported as a discretely presented component unit. The CEDC was established as a non-profit industrial development corporation on November 27, 2001. The primary purpose of the Corporation is to (1) enhance appearance, housing and education, (2) envision improvements and plan for progress in the local economy and (3) create and develop opportunities for enhancing the quality of life. The Corporation receives funding primarily through sales and use taxes levied for the benefit of the Corporation. The Corporation is exempt from Federal income taxes under Section 501(c) 6 of the Internal Revenue Code. The Corporation is managed by a five member board of directors who are appointed by the City Council of the City of Cleveland, Texas.

2. Basis of Presentation, Basis of Accounting

a. Basis of Presentation

Government-wide Statements: The statement of net assets and the statement of activities include the financial activities of the overall government. Eliminations have been made to minimize the double-counting of internal activities. These statements distinguish between the governmental and business-type activities of the City. Governmental activities generally are financed through taxes, intergovernmental revenues, ambulance fees, and other nonexchange transactions. Business-type activities are financed in whole or in part by fees charged to external parties.

The statement of activities presents a comparison between direct expenses and program revenues for the business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular program or function. Depreciation expense has been allocated to all applicable functions in order to present the expenditures of the City more accurately on the Statement of Activities. Program revenues include (a) fees, fines, and charges paid by the recipients of goods or services offered by the programs and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

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

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

the enterprise fund 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.

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

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as grants, insurance proceeds and investment earnings, result from nonexchange transactions or ancillary activities.

The City reports the following *major governmental funds*:

General Fund: This is the City's primary operating fund. It accounts for all financial resources of the City except those required to be accounted for in another fund. The principal sources of revenue of the General Fund are taxes, ambulance fees, fines and intergovernmental revenues.

Debt Service Fund: This fund is used to account for the accumulation of resources and payment of general obligation bonds and contractual obligations. The primary source of revenue for Debt Service is property taxes.

Capital Projects Fund: This fund is used to account for the expenditures of resources accumulated from the issuance of debt and related interest earnings for the acquisition and construction of city facilities and utility systems.

The City reports the following *major enterprise fund*:

Water and Sewer Fund: This fund is used to account for operations that are financed and operated in a manner similar to private business enterprises where the costs (expenses, including depreciation) of providing water and sewer services to the general public on a continuing basis are financed or recovered primarily through user charges or periodic determination of revenues earned, expenses incurred, and/or net income is appropriated for capital maintenance, public policy, management control, accountability, or other purposes.

b. Measurement Focus, Basis of Accounting

Government-wide and Proprietary Fund Financial Statements: These financial statements are reported using the economic resources measurement focus. The government-wide and proprietary fund financial statements are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Nonexchange transactions, in which the City gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, sales taxes, grants, and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied and ambulance fees are recognized in the period the services are performed. Revenue from grants, entitlements, and donations are recognized in the fiscal year in which all eligibility requirements have been satisfied.

Governmental Fund Financial Statements: Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they are both measurable and available. The City considers revenues reported in the governmental funds to be available if the revenues are collected within sixty days after year-end. Revenues from local sources consist primarily of taxes and fees for ambulance services. Revenues received from grant sources and investments are recognized under the susceptible-to-accrual concept.

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

Taxes, ambulance services, and miscellaneous revenues are recorded as revenue when received. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures to the extent they have matured. Capital asset acquisitions are reported as expenditures in governmental funds. Proceeds from long-term debt agreements are reported as other financing sources.

When both restricted and unrestricted (committed, assigned, or unassigned) resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed. The City considers that committed amounts would be reduced first, followed by assigned amounts, and then unassigned amounts when expenditures are incurred for purposes for which amounts in any unrestricted fund balance classification could be used.

Under GASB Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting," all proprietary funds will continue to follow Financial Accounting Standards Board ("FASB") standards issued on or before November 30, 1989. However, from that date forward, proprietary funds will have the option of either 1) choosing not to apply future FASB standards (including amendments of earlier pronouncements), or 2) continuing to follow new FASB pronouncements unless they conflict with GASB guidance. The City has chosen not to apply future FASB standards.

3. Financial Statement Amounts

a. Deposits and Investments

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

The City is authorized to invest in obligations of the U.S. Treasury or the State of Texas, certain U.S. Agencies, certificates of deposit, money market savings accounts, certain municipal securities, repurchase agreements, or investment pools.

Investments for the City are reported at fair value. The investment pools operate in accordance with appropriate state laws and regulations. The reported value of the pools is the same as the fair value of the pool shares.

b. Cash and Cash Equivalents

The City's cash and cash equivalents are considered to be cash on hand and cash on deposit (including restricted cash).

c. Property Taxes

Property values are determined by the County Central Appraisal District as of July 31 of each year. Prior to October 1 of each year, the City sets its tax rate thus creating the tax levy. The taxes are levied and payable October 1 on property values assessed as of January 1. Taxes may be paid without penalty before February 1 of the following year and create a tax lien as of July 1 of each year. The tax assessor/collector for Liberty County bills and collects the property taxes for the City. City property tax revenues are recognized when levied to the extent that they result in current receivables. The combined current tax rate to finance general governmental services and payment of principal and interest on long-term debt for the year ended September 30, 2011 was \$0.685 per \$100, allocated \$0.4803 for the General Fund and \$0.2047 for the Debt Service Fund.

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

d. Restricted Assets

Certain proceeds of the City are classified as restricted assets on the balance sheet because they are maintained in separate bank accounts and their use is limited by applicable bond covenants or grants. The "reserve" account is used to report resources set aside to subsidize potential deficiencies from the City's operation that could adversely affect debt service payments over the next twelve months. The "construction" account is the unexpended balance from debt proceeds.

e. Deferred Charges

Debt issuance costs applicable to future accounting periods are recorded as deferred charges.

f. Capital Assets

Purchased or constructed capital assets are reported at cost or estimated historical cost. Donated fixed assets are recorded at their estimated fair value at the date of the 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. A capitalization threshold of \$5,000 is used.

Capital assets are being depreciated using the straight line method over the following estimated useful lives:

<u>Asset Class</u>	<u>Estimated Useful Lives</u>
Buildings and Improvements	10-50
Furniture and Equipment	5-15
Water System	5-50
Sewer System	5-50

g. Compensated Absences

It is the City's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. There is no liability for unpaid accumulated sick leave since the City does not have a policy to pay any amounts when employees separate from service with the government. All vacation pay is accrued when incurred in the government-wide and proprietary fund financial statements. A liability for these amounts is reported in governmental funds when the individual is eligible for the benefit.

h. Long-term Obligations

In the government-wide financial statements and proprietary fund type financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Debt issuance costs are reported as deferred charges and amortized over the term of the related debt.

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

i. Fund Equity

Beginning with fiscal year 2011, the City implemented GASB Statement No. 54, "Fund Balance Reporting and Governmental Fund Type Definitions." This Statement provides more clearly defined fund balance categories to make the nature and extent of the constraints placed on a government's

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

fund balances more transparent. The following classifications describe the relative strength of the spending constraints:

- Nonspendable fund balance – amounts that are not in spendable form (such as inventory) or are required to be maintained intact.
- Restricted fund balance – amounts constrained to specific purposes by their providers (such as grantors, bondholders, and higher levels of government), through constitutional provisions, or by enabling legislation.
- Committed fund balance – amounts constrained to specific purposes by the City itself, using its highest level of decision-making authority (i.e., Board of Trustees). To be reported as committed, amounts cannot be used for any other purpose unless the City takes the same highest level action to remove or change the constraint.
- Assigned fund balance – amounts the City intends to use for a specific purpose. Intent can be expressed by the Board or by an official or body to which the Board delegates the authority.
- Unassigned fund balance – amounts that are available for any purpose. Positive amounts are reported only in the general fund.

Beginning fund balances for the City's governmental funds have been restated to reflect the above classifications.

The Board established (and modifies or rescinds) fund balance commitments by passage of a resolution. This is typically done through adoption and amendment of the budget. A fund balance commitment is further indicated in the budget document as a designation or commitment of the fund (such as for special incentives). Assigned fund balance is established by the Director of Finance or her designee through adoption or amendment of the budget as intended for specific purpose (such as the purchase of fixed assets, construction, debt service, or for other purposes).

j. Interfund Activity

Interfund activity results from loans, services provided, reimbursements or transfers between funds. Loans are reported as interfund receivables and payables as appropriate and are subject to elimination upon consolidation. Services provided, deemed to be at market or near market rates, are treated as revenues and expenditures or expenses. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers In and Transfers Out are netted and presented as a single "Transfers" line on the government-wide statement of activities. Similarly, interfund receivables and payables are netted and presented as a single "Internal Balances" line of the government-wide statement of net assets.

k. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of management's estimates. Actual results could differ from those estimates.

4. Budgetary Data

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

- a. Prior to September 1, the City Manager submits to the City council a proposed operating budget for the fiscal year commencing the following October 1. The operating budget includes proposed expenditures and the means of financing them.
- b. Prior to October 1, the budget is legally enacted through passage of an ordinance.

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

- c. The City Manager may approve a department's request to transfer an unencumbered balance, or portion thereof within any department; however, City Council must approve a transfer of funds between departments.
- d. Budgets for the General and Debt Service Funds are adopted on a basis consistent with generally accepted accounting principles (GAAP). Special Revenue Funds (grants) are budgeted on a project period basis.

B. Compliance and Accountability

For the year ended September 30, 2011, the general fund expenditures exceeded its appropriations in the following functions:

	<u>Appropriations</u>	<u>Expenditures</u>	<u>Excess</u>
General Fund:			
Civic/Community	\$ 234,596	\$ 242,442	\$ (7,846)
Court	203,956	207,606	(3,650)
Garage Department	76,179	76,242	(63)
Library Department	344,851	345,773	(922)
Grants	-	39,731	(39,731)
Capital Outlay:			
Street Department	-	1,353,445	(1,353,445) *
Airport Department	3,228	17,496	(14,268)
Library Department	-	33,984	(33,984)
Fire and Ambulance	156,821	231,857	(75,036)
Debt Service:			
Principal Retirement	32,717	46,920	(14,203)
Interest and Fiscal Changes	2,650	3,363	(713)

(*Funded by grants reported as intergovernmental revenues)

C. Deposits and Investments

Primary Government:

As of September 30, 2011, the City had the following investments:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Weighted Average Maturity (Years)</u>
Texpool - LGIP	\$ 107,157	0.22
Total Fair Value	\$ 107,157	
Portfolio Weighted Average Maturity		0.22

Interest rate risk. Interest rate risk is the risk that changes in interest rates may adversely affect the value of the investments. The City monitors interest rate risk utilizing weighted average maturity analysis. In accordance with its investment policy, the City reduces its exposure to declines in fair values by limiting the weighted average maturity of its investment portfolio and by holding securities to maturity.

Credit risk. For fiscal year 2011, the City invested in Texpool. Texpool is duly chartered and administered by the State Comptroller's Office and was rated AAAM by Standard & Poor's Investors Service.

Concentration of credit risk. The City's investment policy does not limit an investment in any one issuer.

Custodial credit risk – deposits. In the case of deposits, this is the risk that in the event of a bank failure, the City's deposits may not be returned to it. As of September 30, 2011, City's bank balance of \$3,237,907 was not exposed to custodial credit risk because it was insured and collateralized with securities held by the City's agent and in the City's name.

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

Custodial credit risk – investments. For an investment, this is the risk that, in the event of the failure of the counterparty, the City will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The City is not exposed to custodial risk due to the investments are insured or registered, or securities are held by the City or its agent in the City's name.

Discretely Presented Component Unit:

As of September 30, 2011, the Cleveland Economic Development Corporation had the following investments:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Weighted Average Maturity (Years)</u>
Texpool - LGIP	\$ 131,744	0.22
Total Fair Value	\$ 131,744	
Portfolio Weighted Average Maturity		0.22

D. Receivables

Primary Government:

Receivables as of year end for the City's individual major governmental and proprietary funds, including the applicable allowances for uncollectible accounts, are as follows:

	<u>General</u>	<u>Debt Service Fund</u>	<u>Water and Sewer Fund</u>	<u>Total</u>
Receivables:				
Property Taxes	\$ 479,942	\$ 215,830	\$ -	\$ 695,772
Accounts	916,410	-	610,375	1,526,785
Due From Other Governments	565,888	-	-	565,888
Other	44,249	-	-	44,249
Gross Receivables	2,006,489	215,830	610,375	2,832,694
Less: Allowance for Uncollectible	(855,953)	(15,108)	(158,667)	(1,029,728)
Net Total Receivables	\$ 1,150,536	\$ 200,722	\$ 451,708	\$ 1,802,966

Tax revenues of the general and debt service fund are reported net of estimated uncollectible amounts. Ambulance revenues in the general fund are reported net of estimated uncollectible amounts. Revenues of the Water and Sewer Fund are reported net of estimated uncollectible amounts. Total uncollectible amounts related to revenues of the current period increased (decreased) revenues as follows:

Uncollectibles Related to General Fund Property Taxes	\$ (10,671)
Uncollectibles Related to Debt Service Property Taxes	(1,382)
Uncollectibles Related to General Fund Ambulance Service	(476,627)
Uncollectibles Related to Water and Sewer Fund Utilities	(15,408)
Total Uncollectibles of the Current Fiscal Year Increased (Decreased) Revenues as Follows:	\$ (504,088)

Governmental funds report deferred revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period or in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of deferred revenue reported in the governmental funds were as follows:

	<u>Unavailable</u>	<u>Unearned</u>
Delinquent Property Taxes Receivable (General Fund)	\$ 446,346	\$ -
Delinquent Property Taxes Receivable (Debt Service Fund)	200,722	-
Ambulance Receivable (General Fund)	94,052	-
Fireworks Contributions (General Fund)	-	1,251
Total Deferred/Unearned Revenue For Governmental Funds	\$ 741,120	\$ 1,251

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

E. Capital Assets

Primary Government:

Capital asset activity for the period ended September 30, 2011, was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Adjustments and Transfers</u>	<u>Ending Balance</u>
Governmental Activities:					
Capital Assets, not being Depreciated:					
Land	\$ 2,068,148	\$ -	\$ -	\$ -	\$ 2,068,148
Construction in Progress	30,000	24,236	-	-	54,236
Total Capital Assets, not being Depreciated	2,098,148	24,236	-	-	2,122,384
Capital Assets, being Depreciated:					
Building and Improvements	12,624,298	1,383,475	-	-	14,007,773
Furniture and Equipment	3,689,685	341,077	(14,000)	-	4,016,762
Total Capital Assets, being Depreciated	16,313,983	1,724,552	(14,000)	-	18,024,535
Less Accumulated Depreciation for:					
Building and Improvements	(1,913,282)	(300,333)	-	-	(2,213,615)
Furniture and Equipment	(2,590,487)	(245,785)	14,000	-	(2,822,272)
Total Accumulated Depreciation	(4,503,769)	(546,118)	14,000	-	(5,035,887)
Total Capital Assets, being Depreciated, net	11,810,214	1,178,434	-	-	12,988,648
Governmental Activities Capital Assets, net	\$ 13,908,362	\$ 1,202,670	\$ -	\$ -	\$ 15,111,032

Depreciation was charged to governmental-type activities as follows:

City Council	\$ 669
Administration	44,765
Civic Center	69,107
Police	138,209
Inspection Department	2,504
Street Department	93,558
Airport Department	27,781
Garage Department	1,351
Library Department	50,900
Cemetery and Parks	24,820
Fire and Ambulance	92,454
Total	\$ 546,118

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

	Beginning Balance	Increases	Decreases	Adjustments and Transfers	Ending Balance
Business-type Activities:					
Capital Assets, not being Depreciated:					
Land	\$ 178,621	\$ -	\$ -	\$ -	\$ 178,621
Construction in Progress	218,691	580,409	-	(799,100)	-
Total Capital Assets, not being Depreciated	397,312	580,409	-	(799,100)	178,621
Capital Assets, being Depreciated:					
Building and Improvements	47,997	-	-	-	47,997
Furniture and Equipment	488,566	172,737	-	-	661,303
Water System	3,939,005	37,821	-	398,608	4,375,434
Sewer System	14,727,488	-	-	400,492	15,127,980
Total Capital Assets, being Depreciated	19,203,056	210,558	-	799,100	20,212,714
Less Accumulated Depreciation for:					
Building and Improvements	(19,047)	(1,408)	-	-	(20,455)
Furniture and Equipment	(415,122)	(36,253)	-	-	(451,375)
Water System	(2,766,315)	(77,436)	-	-	(2,843,751)
Sewer System	(8,873,899)	(352,058)	-	-	(9,225,957)
Total Accumulated Depreciation	(12,074,383)	(467,155)	-	-	(12,541,538)
Total Capital Assets, being Depreciated, net	7,128,673	(256,597)	-	799,100	7,671,176
Business-type Activities Capital Assets, net	\$ 7,525,985	\$ 323,812	\$ -	\$ -	\$ 7,849,797

Depreciation was charged to business-type activities as follows:

Water and Sewer Fund	\$ 467,155
	<u>\$ 467,155</u>

Discretely Presented Component Unit:

The Cleveland Economic Development Corporation purchased land in the amount of \$647,808 and started an ongoing construction project in the amount of \$88,520 during the period ended September 30, 2011. The balance of total assets at fiscal year end was \$1,316,652.

F. Interfund Balances and Activity

Primary Government:

1. Due To and From Other Funds at September 30, 2011 consisted of the following:

	Interfund Receivables	Interfund Payables
General Fund	\$ 48,522	\$ 5,385
Debt Service Fund	1,475	-
Hotel/Motel Fund	-	10,704
Money Seizures Fund	1,619	14,807
Water and Sewer Fund	2,291	23,011
Totals	\$ 53,907	\$ 53,907

Interfund balances consist of short-term lending/borrowing arrangements that result primarily from expenditures that are paid by one fund and then charged back to the appropriate other fund. Additionally, some lending/borrowing may occur between two or more funds.

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

2. Transfers To and From Other Funds

Transfers to and from other funds at September 30, 2011, consisted of the following:

<u>Transfers From</u>	<u>Transfers To</u>	<u>Amount</u>
Water and Sewer Fund	General Fund	\$ 400,000
General Fund	Capital Projects Fund	750
		<u>\$ 400,750</u>

Transfers from the Water and Sewer Fund were utilized to pay budgeted expenditures of the General Fund. The transfers from the General Fund were utilized to pay expenditures of the Capital Projects.

G. Long-Term Obligations

Primary Government and Discretely Presented Component Unit (CEDC):

1. Long-term Obligation Activity

Long-term obligations include notes payable, revenue bonds and certificates of obligation. The requirements for the certificates of obligation principal and interest payments are accounted for in the Debt Service Fund. The requirements for the revenue bonds principal and interest payments are accounted for in the Water and Sewer Fund. The requirements for notes payable principal and interest payments are accounted for in the General Fund and the Discretely Presented Component Unit (CEDC).

Changes in long-term obligations for the period ended September 30, 2011 are as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>	<u>Amounts Due Within One Year</u>
Governmental Activities:					
Notes Payable	\$ 44,832	\$ 135,010	\$ 46,920	\$ 132,922	\$ 40,359
Certificates of Obligation	7,510,000	-	340,000	7,170,000	375,000
Total Governmental Activities	<u>\$ 7,554,832</u>	<u>\$ 135,010</u>	<u>\$ 386,920</u>	<u>\$ 7,302,922</u>	<u>\$ 415,359</u>
Business-type Activities:					
Revenue Bonds (RB)	\$ 3,010,000	\$ 2,360,000	\$ 255,000	\$ 5,115,000	\$ 355,000
Total Business-type Activities	<u>\$ 3,010,000</u>	<u>\$ 2,360,000</u>	<u>\$ 255,000</u>	<u>\$ 5,115,000</u>	<u>\$ 355,000</u>
Discretely Presented Component Unit (CEDC):					
Notes Payable	\$ 385,270	-	\$ 33,848	\$ 351,422	\$ 35,567
Total Discretely Presented Component Unit	<u>\$ 385,270</u>	<u>-</u>	<u>\$ 33,848</u>	<u>\$ 351,422</u>	<u>\$ 35,567</u>

2. Governmental Activities

The City issued notes payable and certificates of obligation.

Notes Payable:

The City issued notes payable to provide funds for the purchase of equipment. The notes payable are secured by the equipment purchased. The notes are issued as 3-4 year current interest notes.

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

The following is a summary of changes in the notes payable of the governmental activities for the fiscal year:

Description	Interest Rate	Maturity Date	Beginning Balance	Additions	Reductions	Ending Balance
2008 Laptops	5.94%	2011	\$ 3,313	\$ -	\$ 3,313	\$ -
2009 Police Vehicle Computers	5.91%	2012	41,519	-	13,053	28,466
2011 Tractor & Security System	4.53%	2015	-	135,010	30,554	104,456
Totals			\$ 44,832	\$ 135,010	\$ 46,920	\$ 132,922

Debt service requirements for notes payable at September 30, 2011 are as follows:

Year Ending September 30,	Governmental Activities		
	Principal	Interest	Total
2012	\$ 40,359	\$ 6,414	\$ 46,773
2013	42,379	4,395	46,774
2014	28,994	2,273	31,267
2015	21,190	960	22,150
Totals	\$ 132,922	\$ 14,042	\$ 146,964

Certificates of Obligation:

The City issues certificates of obligation to provide funds for the construction and improvement of the airport, law enforcement center, civic center, city hall, parks and various other projects. Principal and interest payments on the City's debt are secured solely by ad valorem property taxes levied on all taxable property within the city limits.

The following is a summary of changes in the certificates of obligation for the fiscal year:

Series	Interest Rate	Maturity Date	Original Issue	Beginning Balance	Additions	Reductions	Ending Balance
2001	5.10%	2012	1,800,000	\$ 440,000	\$ -	\$ 215,000	\$ 225,000
2003	6.00%	2023	7,430,000	7,070,000	-	125,000	6,945,000
Totals				\$ 7,510,000	\$ -	\$ 340,000	\$ 7,170,000

Debt service requirements for certificates of obligation at September 30, 2011 are as follows:

Year Ending September 30,	Governmental Activities		
	Principal	Interest	Total
2012	\$ 375,000	\$ 303,478	\$ 678,478
2013	440,000	280,043	720,043
2014	510,000	256,643	766,643
2015	530,000	235,843	765,843
2016	550,000	214,105	764,105
2017	575,000	191,036	766,036
2018	600,000	166,355	766,355
2019	660,000	139,415	799,415
2020	675,000	110,713	785,713
2021	725,000	80,613	805,613
2022	750,000	49,088	799,088
2023	780,000	16,575	796,575
Totals	\$ 7,170,000	\$ 2,043,907	\$ 9,213,907

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

3. Business-Type Activities

Revenue Bonds:

The City issues bonds to provide funds for the construction and improvement of the City's water and sewer system.

The City pledges the net revenues of the waterworks and sanitary sewer system for payment of principal and interest on the revenue bonds, which are equally secured by a first lien on the City's combined waterworks and sanitary sewer system.

The following is a summary of changes in the revenue bonds of business-type activities for the fiscal year:

<u>Series</u>	<u>Interest Rate</u>	<u>Maturity Date</u>	<u>Original Issue</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
1997 RB	2.65-4.45%	2017	\$ 2,250,000	\$ 1,075,000	\$ -	\$ 125,000	\$ 950,000
2000 RB	5.10-4.80%	2020	1,865,000	1,400,000	-	110,000	1,290,000
2009 TRB	0.350-4.30%	2029	555,000	535,000	-	20,000	515,000
2011 TRB	0.100-3.90%	2031	2,360,000	-	2,360,000	-	2,360,000
Totals				\$ 3,010,000	\$ 2,360,000	\$ 255,000	\$ 5,115,000

Debt service requirements for revenue bonds at September 30, 2011 are as follows:

<u>Year Ending September 30,</u>	<u>Business-type Activities</u>		
	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2012	\$ 355,000	\$ 178,584	\$ 533,584
2013	395,000	167,283	562,283
2014	410,000	154,436	564,436
2015	415,000	140,573	555,573
2016	430,000	125,734	555,734
2017	435,000	109,940	544,940
2018	300,000	97,026	397,026
2019	305,000	85,941	390,941
2020	315,000	74,190	389,190
2021	140,000	61,616	201,616
2022	145,000	57,164	202,164
2023	150,000	52,255	202,255
2024	155,000	46,992	201,992
2025	160,000	41,381	201,381
2026	165,000	35,451	200,451
2027	170,000	29,219	199,219
2028	180,000	22,535	202,535
2029	185,000	15,435	200,435
2030	150,000	8,933	158,933
2031	155,000	3,023	158,023
Totals	\$ 5,115,000	\$ 1,507,711	\$ 6,622,711

4. Discretely Presented Component Unit - CEDC

Notes Payable:

The Cleveland Economic Development Corporation (CEDC) issued notes payable to provide funds for the purchase of land. The notes payable are secured by the land purchased. The notes are issued as 10 year current interest notes.

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

The following is a summary of changes in the notes payable of the discretely presented component unit for the fiscal year:

Description	Interest Rate	Maturity Date	Beginning Balance	Additions	Reductions	Ending Balance
2010 Land	5.10%	2020	\$ 385,270	\$ -	\$ 33,848	\$ 351,422
Totals			\$ 385,270	\$ -	\$ 33,848	\$ 351,422

Discretely Presented Component Unit

Year Ending September 30,	Principal	Interest	Total
2012	\$ 35,567	\$ 17,143	\$ 52,710
2013	37,472	15,237	52,709
2014	39,428	13,281	52,709
2015	41,487	11,223	52,710
2016	43,627	9,082	52,709
2017	45,931	6,779	52,710
2018	48,328	4,381	52,709
2019	50,852	1,857	52,709
2020	8,730	56	8,786
Totals	\$ 351,422	\$ 79,039	\$ 430,461

H. 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 2011, the City purchased workers compensation and property and liability insurance at a cost that is considered to be economically justifiable by joining together with other governmental entities in the State as a member of the Texas Municipal League Intergovernmental Risk Pool ("TML"). TML is a self-funded pool operating as a common risk management and insurance program. The City pays an annual premium to TML for its above insurance coverages. The agreement for the formation of TML provides that TML will be self-sustaining through member premiums and will reinsure through commercial companies for claims in excess of acceptable risk levels; however, each category of coverage has its own level of reinsurance. The City continues to carry commercial insurance for other risks of loss. There were no significant reductions in insurance coverages in the past fiscal year and settled claims resulting from these risks have not exceeded coverage in any of the past three fiscal years.

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

I. Cost-Sharing Multiple Employer Defined Benefit Pension Plan

Plan Description:

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

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

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

	Plan Year 2010	Plan Year 2011
Employee deposit rate	5.0%	5.0%
Matching ratio (city to employee)	2 to 1	2 to 1
Years required for vesting	5	5
Service retirement eligibility (expressed as age/years of service)	60/5 , 0/20	60/5 , 0/20
Updated Service Credit	100% Repeating, Transfers	100% Repeating, Transfers
Annuity Increase (to retirees)	70% of CPI Repeating	70% of CPI Repeating

Contributions:

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

The City contributes to the TMRS Plan at an actuarially determined rate. Both the employees and the City make contributions monthly. Since the City needs to know its contribution rate in advance for budgetary purposes, there is a one-year delay between the actuarial valuation that serves as the basis for the rate and the calendar year when the rate goes into effect. The annual pension cost was \$292,035 and net pension obligation/(asset) was \$0.

Three-Year Trend Information

Fiscal Year Ending	Annual Pension Cost (APC)	Actual Contribution Made	Percentage of APC Contributed	Net Pension Obligation/ (Asset)
2011	292,035	292,035	100%	-
2010	305,660	305,660	100%	-
2009	267,819	267,819	100%	-

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

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

Valuation Date	12/31/2008	12/31/2009	12/31/2010-prior to restructuring	12/31/2010-Restructured
Actuarial Cost Method	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit
Amortization Method	Level Percent of Payroll	Level Percent of Payroll	Level Percent of Payroll	Level Percent of Payroll
GASB 25 Equivalent Single Amortization Period	29.0 years; closed period	28.1 years; closed period	27.2 years; closed period	27.2 years; closed period
Amortized Period for new Gains/Losses	30 years	30 years	30 years	30 years
Asset Valuation Method	Amortized Cost	10-year Smoothed Market	10-year Smoothed Market	10-year Smoothed Market
Actuarial Assumptions:				
Investment Rate of Return*	7.5%	7.5%	7.5%	7.0%
Projected Salary Increases*	Varies by age and service	Varies by age and service	Varies by age and service	Varies by age and service
* Includes Inflation at	3.00%	3.00%	3.00%	3.00%
Cost-of-Living Adjustments	2.1%	2.1%	2.1%	2.1%

Funded Status and Funding Progress:

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

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

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Funded Ratio	Unfunded AAL (UAAL)	Covered Payroll	UAAL as a Percentage of Covered Payroll
	(1)	(2)	(3)	(4)	(5)	(6)
			(1)/(2)	(2)-(1)		(4)/(5)
12/31/2010 ¹	4,264,622	6,210,030	68.7%	1,945,408	3,071,804	63.3%
12/31/2010 ²	6,066,467	7,735,708	78.4%	1,669,241	3,071,804	54.3%

(1) Actuarial valuation performed under the original fund structure.
(2) Actuarial valuation performed under the new fund structure

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

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

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

Texas Municipal Retirement System

Schedule of Funding Progress:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Funded Ratio	Unfunded AAL (UAAL)	Covered Payroll	UAAL as a Percentage of Covered Payroll
	(1)	(2)	(3)	(4)	(5)	(6)
			(1)/(2)	(2)-(1)		(4)/(5)
12/31/2008	3,791,698	5,603,179	67.7%	1,811,481	2,854,989	63.4%
12/31/2009	3,714,745	5,623,373	66.1%	1,908,628	3,086,771	61.8%
12/31/2010 ¹	4,264,622	6,210,030	68.7%	1,945,408	3,071,804	63.3%
12/31/2010 ²	6,066,467	7,735,708	78.4%	1,669,241	3,071,804	54.3%

(1) Actuarial valuation performed under the original fund structure.
(2) Actuarial valuation performed under the new fund structure

J. Postemployment Benefits-Supplemental Death Benefits Plan

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

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

Your city offers supplemental death to:	Plan Year 2010	Plan Year 2011
Active employees (yes or no)	Yes	Yes
Retirees (yes or no)	Yes	Yes

CITY OF CLEVELAND, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2011

Contributions:

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

The City's contributions to the TMRS SDBF for the years ended 2011, 2010 and 2009 were \$6,821, \$8,153, and \$8,632, respectively, which equaled the required contributions each year.

Schedule of Contribution Rates:

(RETIREE-only portion of the rate)

Plan/ Calendar Year	Annual Required Contribution (Rate)	Actual Contribution Made (Rate)	Percentage of ARC Contributed
2012	0.08%	0.08%	100.0%
2011	0.07%	0.07%	100.0%
2010	0.07%	0.07%	100.0%
2009	0.07%	0.07%	100.0%
2008	0.10%	0.10%	100.0%

APPENDIX C

FORM OF BOND COUNSEL'S OPINION

[LETTERHEAD OF BOND COUNSEL]

[DATE]

WE HAVE ACTED as bond counsel for the City of Cleveland, Texas (the "City"), in connection with an issue of certificates of obligation (the "Certificates") described as follows:

CITY OF CLEVELAND, TEXAS, COMBINATION TAX AND REVENUE CERTIFICATES OF OBLIGATION, SERIES 2012A, dated December 1, 2012, in the principal amount of \$_____.

The Certificates mature, bear interest, are subject to redemption prior to maturity and may be transferred and exchanged as set out in the Certificates and in the ordinance adopted by the City Council of the City authorizing their issuance (the "Ordinance").

WE HAVE ACTED as bond counsel for the sole purpose of rendering an opinion with respect to the legality and validity of the Certificates under the Constitution and laws of the State of Texas, and with respect to the exclusion of interest on the Certificates from gross income for federal income tax purposes. We have not investigated or verified original proceedings, records, data or other material, but have relied solely upon the transcript of certified proceedings described in the following paragraph. We have not assumed any responsibility with respect to the financial condition or capabilities of the City or the disclosure thereof in connection with the sale of the Certificates. Our role in connection with the City's Official Statement prepared for use in connection with the sale of the Certificates has been limited as described therein.

IN OUR CAPACITY as bond counsel, we have participated in the preparation of and have examined a transcript of certified proceedings pertaining to the Certificates which contains certified copies of certain proceedings of the City, customary certificates of officers, agents and representatives of the City and other public officials and other certified showings relating to the authorization and issuance of the Certificates. We have also examined such applicable provisions of the Internal Revenue Code of 1986, as amended (the "Code"), court decisions, Treasury Regulations and published rulings of the Internal Revenue Service (the "Service") as we have deemed relevant. We have also examined executed Certificate No. I-1 of this issue.

BASED ON SUCH EXAMINATION, IT IS OUR OPINION that the transcript of certified proceedings evidences complete legal authority for the issuance of the Certificates in full compliance with the Constitution and laws of the State of Texas presently effective and that therefore the Certificates constitute valid and legally binding obligations of the City, and that taxable property within the City is subject to the levy of ad valorem taxes, within the limits prescribed by law, to pay the Certificates and the interest thereon.

IT IS OUR FURTHER OPINION that the revenues to be derived from the operation of the City's waterworks and sanitary sewer system, after the payment of all operation and maintenance expenses thereof (the "Net Revenues"), are also pledged to the payment of the principal of and interest on the Certificates; provided, however, that such pledge of the Net

Revenues is limited to an amount not to exceed \$1,000 and is junior and subordinate in all respects to the pledge of the Net Revenues to the payment of all outstanding obligations of the City and any obligation of the City, whether authorized heretofore or hereafter, which the City designates as having a pledge senior to the pledge of the Net Revenues to the payment of the Certificates.

THE CITY has reserved the right to issue, for any lawful purpose at any time in one or more installments, bonds, certificates of obligation and other obligations of any kind payable in whole or in part from the Net Revenues, secured by a pledge of the Net Revenues that may be prior and superior in right to, on a parity with, or junior and subordinate to the pledge of the Net Revenues securing the Certificates.

THE RIGHTS OF THE OWNERS of the Certificates are subject to the applicable provisions of the federal bankruptcy laws and any other similar laws affecting the rights of creditors of political subdivisions generally, and may be limited by general principles of equity which permit the exercise of judicial discretion.

IT IS OUR FURTHER OPINION that:

- (1) Interest on the Certificates is excludable from gross income for federal income tax purposes under existing law.
- (2) The Certificates are not “private activity bonds” within the meaning of the Code, and interest on the Certificates is not subject to the alternative minimum tax on individuals and corporations, except that interest on the Certificates will be included in the “adjusted current earnings” of a corporation (other than any S corporation, regulated investment company, REIT or REMIC) for purposes of computing its alternative minimum tax.

In providing such opinions, we have relied on representations of the City, the City’s financial advisor and the underwriter of the Certificates, with respect to matters solely within the knowledge of the City, the City’s financial advisor and the underwriter of the Certificates, respectively, which we have not independently verified, and have assumed continuing compliance with the covenants in the Ordinance pertaining to those sections of the Code that affect the exclusion from gross income of interest on the Certificates for federal income tax purposes. If such representations are determined to be inaccurate or incomplete or the City fails to comply with the foregoing provisions of the Ordinance, interest on the Certificates could become includable in gross income from the date of original delivery, regardless of the date on which the event causing such inclusion occurs.

Except as stated above, we express no opinion as to any federal, state or local tax consequences resulting from the receipt or accrual of interest on, or acquisition, ownership, or disposition of the Certificates.

Owners of the Certificates should be aware that the ownership of tax-exempt obligations may result in collateral federal income tax consequences to financial institutions, life insurance and property and casualty insurance companies, certain S corporations with Subchapter C earnings and profits, individual recipients of Social Security or Railroad Retirement benefits,

taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, and individuals otherwise qualifying for the earned income credit. In addition, certain foreign corporations doing business in the United States may be subject to the “branch profits tax” on their effectively-connected earnings and profits (including tax-exempt interest such as interest on the Certificates).

The opinions set forth above are based on existing law, which is subject to change. Such opinions are further based on our knowledge of facts as of the date hereof. We assume no duty to update or supplement these opinions to reflect any facts or circumstances that may hereafter come to our attention or to reflect any changes in any law that may hereafter occur or become effective. Moreover, our opinions are not a guarantee of result and are not binding on the Service; rather, such opinions represent our legal judgment based upon our review of existing law and in reliance upon the representations and covenants referenced above that we deem relevant to such opinions. The Service has an ongoing audit program to determine compliance with rules that relate to whether interest on state or local obligations is includable in gross income for federal income tax purposes. No assurance can be given as to whether or not the Service will commence an audit of the Certificates. If an audit is commenced, in accordance with its current published procedures, the Service is likely to treat the City as the taxpayer. We observe that the City has covenanted in the Ordinance not to take any action, or omit to take any action within its control, that if taken or omitted, respectively, may result in the treatment of interest on the Certificates as includable in gross income for federal income tax purposes.