FirstSouthwest
Continuing Disclosure Services
(See "Continuing Disclosure Information" herein)

PRELIMINARY OFFICIAL STATEMENT

Dated February 21, 2013

Ratings:
Moody's: "Applied For"
S&P: "Applied For"
PSF Guarantee: "Conditional Approval Received"
(See "OTHER INFORMATION - Ratings" and "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" herein)

In the opinion of Bond Counsel, interest on the Bonds will be excludable from gross income for federal income tax purposes under statutes, regulations, published rulings and court decisions existing on the date thereof, subject to the matters described under "TAX MATTERS" herein, including the alternative minimum tax on corporations.

THE BONDS **WILL NOT** BE DESIGNATED AS "QUALIFIED TAX-EXEMPT OBLIGATIONS" FOR FINANCIAL INSTITUTIONS

$84,789,982.55*
KELLER INDEPENDENT SCHOOL DISTRICT
(Tarrant County, Texas)
UNLIMITED TAX REFUNDING BONDS, SERIES 2013

Dated Date: March 1, 2013 | **Due: As shown on Page 2**
Interest Accrual Date: Delivery Date

PAYMENT TERMS . . . The $84,789,982.55* Keller Independent School District Unlimited Tax Refunding Bonds, Series 2013 (the "Bonds") will be issued in part as current interest bonds (the "Current Interest Bonds") and in part as premium capital appreciation bonds (the "Premium Capital Appreciation Bonds" and, collectively with the Current Interest Bonds, the "Bonds"), as shown on Page 2 hereof. Interest on the Current Interest Bonds will accrue from March 28, 2013* (the "Delivery Date"), and will be payable February 15 and August 15 of each year commencing August 15, 2013, until maturity or prior redemption, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. Interest on the Premium Capital Appreciation Bonds will accrete from the Delivery Date and such interest will compound semiannually on February 15 and August 15 of each year beginning August 15, 2013, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The sum of the principal of, premium, if any, and accreted/compounded interest on the Premium Capital Appreciation Bonds (the "Maturity Amount") is payable only at maturity. The Current Interest Bonds will be issued as fully registered obligations in denominations of $5,000 of principal amount or any integral multiple thereof for any one stated maturity, and the Premium Capital Appreciation Bonds will be issued in denominations of integral multiples of $5,000 of the Maturity Amount. The definitive Bonds 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 Bonds may be acquired in authorized denominations thereof. **No physical delivery of the Bonds will be made to the beneficial owners thereof.** The principal and Maturity Amounts of the Bonds and interest on the Current Interest Bonds 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 Bonds (see "THE BONDS - Book-Entry-Only System"). The initial Paying Agent/Registrar is Regions Bank, Dallas, Texas (see "THE BONDS - Paying Agent/Registrar").

AUTHORITY FOR ISSUANCE . . . The Bonds are issued pursuant to the Constitution and general laws of the State of Texas (the "State"), including Chapter 1207 of the Texas Government Code, as amended, and an order (the "Bond Order") adopted by the Board of Trustees (the "Board") of the Keller Independent School District (the "District") in which the Board delegated to certain officers of the District authority to complete the sale of the Bonds through the execution of a "Pricing Certificate". The Bonds are direct obligations of the District, payable from an annual ad valorem tax levied, without legal limitation as to rate or amount, on all taxable property located within the District, as provided in the Bond Order (see "THE BONDS - Authority for Issuance"). **An application has been filed and the District has received conditional approval for the payment of the Bonds to be guaranteed by the Permanent School Fund of Texas (see "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM").**

PURPOSE . . .Proceeds from the sale of the Bonds will be used (1) to refund a portion of the District's Unlimited Tax School Building and Refunding Bonds, Series 2005 (the "Refunded Bonds") for debt service savings (see "PLAN OF FINANCING"; also see Schedule I for a detailed listing of the Refunded Bonds and their call date) and (2) to pay the costs associated with the sale and issuance of the Bonds.

LEGALITY . . . The Bonds are offered for delivery when, as and if issued and received by the Underwriters and subject to the approving opinion of the Attorney General of Texas and the opinion of McCall, Parkhurst & Horton L.L.P., Dallas, Texas, Bond Counsel (see Appendix C, "Form of Bond Counsel's Opinion"). Certain legal matters will be passed upon for the Underwriters by Fulbright & Jaworski L.L.P., Dallas, Texas, Counsel for the Underwriters.

DELIVERY . . . It is expected that the Bonds will be available for delivery through DTC on or about March 28, 2013*.

MATURITY SCHEDULE
See Schedules on Page 2

RAYMOND JAMES

BAIRD | **SOUTHWEST SECURITIES**

* Preliminary, subject to change.

MATURITY SCHEDULE* **CUSIP(1) Prefix: ______**

$4,154,982.55* Premium Capital Appreciation Bonds

Maturity (8/15)	Principal Amount	Initial Offering Price per $5,000 Amount	Initial Yield to Maturity	Total Payment at Maturity	CUSIP(1) Suffix
2013	$ 1,124,141.15			$1,255,000	
***	***	***	***	***	***
2016	1,492,113.00			3,075,000	
2017	1,538,728.40			3,890,000	

(Interest to accrete from the Delivery Date)

$80,635,000* Current Interest Bonds

Maturity (8/15)	Principal Amount	Interest Rate	Initial Yield	CUSIP(1) Suffix	Maturity (8/15)	Principal Amount	Interest Rate	Initial Yield	CUSIP(1) Suffix
2018	$ 3,935,000				2025	$ 11,495,000			
2019	3,475,000				2026	2,700,000			
2020	3,900,000				2027	7,065,000			
2021	4,135,000				2028	7,700,000			
2022	4,595,000				2029	7,750,000			
2023	5,110,000				2030	8,055,000			
2024	10,720,000								

(Interest to accrue from the Delivery Date)

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* Preliminary, subject to change.

(1) CUSIP is a registered trademark of the American Bankers Association. CUSIP data is provided by CUSIP Global Services, managed by Standard & Poor's Financial Services LLC on behalf of the American Bankers Association. This data is not intended to create a database and does not serve in any way as a substitute for the CUSIP services. Neither the District, the Financial Advisor, nor the Underwriters take any responsibility for the accuracy of CUSIP numbers.

OPTIONAL REDEMPTION . . . The District reserves the right, at its option, to redeem Current Interest Bonds having stated maturities on and after August 15, 20__, in whole or in part in principal amounts of $5,000 or any integral multiple thereof, on August 15, 20__, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption (see "THE BONDS – Optional Redemption").

The Premium Capital Appreciation Bonds are not subject to redemption prior to maturity.

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

No dealer, broker, salesman or other person has been authorized by the District or the Underwriters to give any information, or to make any representations other than those contained in this Official Statement, and, if given or made, such other information or representations must not be relied upon as having been authorized by the District or the Underwriters. This Official Statement does not constitute an offer to sell Bonds in any jurisdiction to any person to whom it is unlawful to make such offer in such jurisdiction.

Certain information set forth herein has been obtained from the District and other sources which are believed to be reliable but is not guaranteed as to accuracy or completeness, and is not to be construed as a representation by the Financial Advisor or the Underwriters. Any information and expressions of opinion herein contained 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 District or other matters described herein since the date hereof. See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM - PSF Continuing Disclosure Undertaking" and "CONTINUING DISCLOSURE INFORMATION" for a description of the undertakings of the Texas Education Agency (the "TEA") and the District, respectively, to provide certain information on a continuing basis.

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

The cover page contains certain information for general reference only and is not intended as a summary of this offering. Investors should read the entire Official Statement, including all schedules and appendices attached hereto, to obtain information essential to making an informed investment decision.

IN CONNECTION WITH THE OFFERING OF THE BONDS, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICES OF THE BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

NEITHER THE DISTRICT, ITS FINANCIAL ADVISOR, NOR THE UNDERWRITERS MAKE ANY REPRESENTATION OR WARRANTY WITH RESPECT TO THE INFORMATION CONTAINED IN THIS OFFICIAL STATEMENT REGARDING THE DEPOSITORY TRUST COMPANY OR ITS BOOK-ENTRY ONLY SYSTEM OR THE AFFAIRS OF THE TEXAS EDUCATION AGENCY ("TEA") DESCRIBED UNDER "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM", AS SUCH INFORMATION HAS BEEN PROVIDED BY THE DEPOSITORY TRUST COMPANY AND THE TEA, RESPECTIVELY.

THE BONDS ARE EXEMPT FROM REGISTRATION WITH THE SECURITIES AND EXCHANGE COMMISSION AND CONSEQUENTLY HAVE NOT BEEN REGISTERED THEREWITH. THE REGISTRATION, QUALIFICATION, OR EXEMPTION OF THE BONDS IN ACCORDANCE WITH APPLICABLE SECURITIES LAW PROVISIONS OF THE JURISDICTIONS IN WHICH THE BONDS HAVE BEEN REGISTERED, QUALIFIED, OR EXEMPTED SHOULD NOT 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.

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The cover page hereof, this page, the schedules and appendices included herein and any addenda, supplement or amendment hereto, are part of the Official Statement.

PRELIMINARY 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 Bonds 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 the entire Official Statement.

THE DISTRICT.............................. The District is a political subdivision located in Tarrant County, Texas. The District is approximately 51 square miles in area (see "INTRODUCTION - Description of the District").

THE BONDS.................................. The $84,789,982.55* Unlimited Tax Refunding Bonds, Series 2013 (the "Bonds") are issued in part as Premium Capital Appreciation Bonds maturing on August 15 in the years 2013, 2016 and 2017; and in part as Current Interest Bonds maturing on August 15 in the years 2018 through 2030 (see "THE BONDS - Description of the Bonds").

PAYMENT OF INTEREST .... Interest on the Current Interest Bonds accrues from the date of their delivery to the Underwriters and is payable on August 15, 2013 and each February 15 and August 15 thereafter until maturity or prior redemption. Interest on the Premium Capital Appreciation Bonds will accrete from the date of their delivery to the Underwriters and such interest will compound semiannually on February 15 and August 15 of each year beginning on August 15, 2013. The accreted interest on the Premium Capital Appreciation Bonds is payable only at maturity.

AUTHORITY FOR ISSUANCE.......... The Bonds are being issued pursuant to the Constitution and general laws of the State of Texas, including Chapter 1207 of the Texas Government Code, as amended, and an order (the "Bond Order") passed by the Board. In the Bond Order, the Board delegated to certain officers of the District, pursuant to certain provisions of Chapter 1207 of the Texas Government Code, as amended, authority to complete the sale of the Bonds. The terms of the sale will be included in a "Pricing Certificate," which will complete the sale of the Bonds (the Bond Order and the Pricing Certificate are jointly referred to herein as the "Order") (see "THE BONDS - Authority for Issuance").

SECURITY FOR THE BONDS .... The Bonds constitute direct obligations of the District, payable from a continuing direct annual ad valorem tax levied by the District, without legal limit as to rate or amount, on all taxable property within the District. Additionally, an application has been filed and the District has received conditional approval for the payment of the Bonds to be guaranteed by the corpus of the Permanent School Fund of Texas (see "THE BONDS - Security and Source of Payment").

PERMANENT SCHOOL FUND GUARANTEE .... The District has applied for and has received conditional approval from the Texas Education Agency for the payment of the Bonds to be guaranteed by the corpus of the Permanent School Fund of the State of Texas (see "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM").

OPTIONAL REDEMPTION .... The District reserves the right, at its option, to redeem Current Interest Bonds having stated maturities on and after August 15, 20__, in whole or in part in principal amounts of $5,000 or any integral multiple thereof, on August 15, 20__, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption. If less than all of the Current Interest Bonds are to be redeemed, the District may select the maturities of the Current Interest Bonds to be redeemed. If less than all the Current Interest Bonds of any maturity are to be redeemed, the Paying Agent/Registrar (or DTC while the Bonds are in Book-Entry-Only form) shall determine by lot the Current Interest Bonds, or portions thereof, within such maturity to be redeemed (see "THE BONDS - Optional Redemption").

The Premium Capital Appreciation Bonds are not subject to redemption prior to maturity.

NOT QUALIFIED TAX-EXEMPT OBLIGATIONS............................... The Bonds will not be designated as "Qualified Tax-Exempt Obligations" for financial institutions.

TAX EXEMPTION............................ In the opinion of Bond Counsel, the interest on the Bonds will be excludable from gross income for federal income tax purposes under statutes, regulations, published rulings and court decisions existing on the date thereof. See "TAX MATTERS" for a discussion of the opinion of Bond Counsel, including a description of the alternative minimum tax consequences for corporations.

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* Preliminary, subject to change.

USE OF PROCEEDS .... Proceeds from the sale of the Bonds will be used (1) to refund a portion of the District's Unlimited Tax School Building and Refunding Bonds, Series 2005 (the "Refunded Bonds") for debt service savings and (2) to pay the costs associated with the sale and issuance of the Bonds. See "PLAN OF FINANCING – Purpose"; also see Schedule I for a detailed listing of the Refunded Bonds and their call date.

RATINGS .... The presently outstanding tax supported debt of the District is rated "Aa2" by Moody's Investors Service, Inc. ("Moody's") and "AA" by Standard & Poor's Ratings Services, a Standard & Poor's Financial Services LLC business ("S&P") without regard to credit enhancement. The District also has issues outstanding which are rated "Aaa" by Moody's and "AAA" by S&P by virtue of the guarantee of the Permanent School Fund of the State of Texas. Applications for contract ratings on the Bonds have been made to Moody's and S&P (see "OTHER INFORMATION - Ratings" and "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM").

BOOK-ENTRY-ONLY SYSTEM .... The definitive Bonds 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 Bonds may be acquired in denominations of $5,000 or integral multiples thereof. No physical delivery of the Bonds will be made to the beneficial owners thereof. Principal and Maturity Amount of, premium, if any, and interest on the Bonds 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 Bonds (see "THE BONDS - Book-Entry-Only System").

PAYMENT RECORD .... The District has never defaulted in payment of its tax supported debt.

SELECTED FINANCIAL INFORMATION

Fiscal Year Ended 8/31	Estimated District Population [(1)]	Taxable Assessed Valuation [(2)]	Per Capita Taxable Assessed Valuation	Tax Supported Debt at End of Fiscal Year [(3)]	Per Capita Tax Supported Debt	Ratio Tax Supported Debt to Taxable Assessed Valuation	% of Total Tax Collections
2009	132,430	$ 10,212,543,961	77,117	$ 735,369,467	5,553	7.20%	99.85%
2010	132,705	10,518,985,594	79,266	725,718,459	5,469	6.90%	99.49%
2011	136,038	10,838,009,000	79,669	712,856,753	5,240	6.58%	101.02%
2012	154,320	11,200,638,123	72,581	700,087,011	4,537	6.25%	100.73%
2013	159,500	11,171,019,961	70,038	684,454,009 [(4)]	4,291 [(4)]	6.13% [(4)]	62.96% [(5)]

(1) Source: The District.
(2) As reported by the Tarrant Appraisal District on the District's annual State Property Tax Reports and such values are subject to change during the ensuing year.
(3) Excludes interest accreted on outstanding capital appreciation bonds.
(4) Projected, includes the Bonds but excludes the Refunded Bonds.
(5) Partial year collections through December 31, 2012.

For additional information regarding the District, please contact:

Mark Youngs Deputy Superintendent Keller Independent School District 350 Keller Parkway Keller, Texas 76248 (817) 744-1014	or	Jeff W. Robert Managing Director First Southwest Company 325 N. St. Paul Street, Suite 800 Dallas, Texas 75201 (214) 953-8744

DISTRICT OFFICIALS, STAFF AND CONSULTANTS

ELECTED OFFICIALS

Board of Trustees	Board Member Since	Term Expires	Occupation
Kevin Stevenson President	2007	May, 2013	Director of Business Development, Encore Healthcare
Craig Allen Vice President	2008	May, 2014	Director of Residential Services, Texas Christian University
Cindy Lotton Secretary	2004	May, 2013	Elementary School Counselor
Lara Lee Hogg Member	2007	May, 2014	Health Care Administrator
Ruthie Keyes Secretary	2012	May, 2015	Retired Educator
Brad Schofield Member	2012	May, 2015	Certified Public Accountant
Jim Stitt Member	2010	May, 2013	Retired Educator

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SELECTED ADMINISTRATIVE STAFF

Name	Position	Years of Service - Keller ISD	Years of Service - Education
Dr. Randy Reid	Superintendent	(1)	31
Amanda Bigbee	General Counsel	3	3
R. Mark Youngs	Deputy Superintendent	4	10
Charles Carroll	Assistant Superintendent, Administrative Services	3	20
Vicki Burris	Assistant Superintendent, Business	4	33
Deana Lopez	Assistant Superintendent, Curriculum/Instruction	4	19
Penny Benz	Assistant Superintendent, Human Resources	6	13
Joe Griffin	Chief Technology Officer	14	26
Amanda Barrios-Harris	Director, Assessment and Accountability	11	24
Bob DeJonge	Director, Athletics	20	31
Sheri Rich	Director, HR Benefits	6	22
Shellie Johnson	Director, Communications	4	4
Hudson Huff	Director, Construction and Planning	9	14
Kristin Williams, CPA	Director, Finance	9	9
Kimberly Blann	Director, Fine Arts	4	4
Cindy Harton	Director, Health Services	19	22
Johjania Najera	Director, Human Resources	3	18
Victoria Miles	Director, Intervention Support	3	28
Mary Martin	Director, Language Acquisition	5	16
Dustin Blank	Director, Leadership	6	7
Kevin Hood	Director, Leadership	5	11
John Gann	Director, Maintenance	5	5
Vaughan Hamblen	Director, Network Services	13	13
Frank DiNella	Director, Operations and Distribution	6	6
Michelle Howard-Schwind	Director, Organization Improvement	0	0
Marlene Rutledge	Director, Payroll	8	8
Lori Tudor	Director, Purchasing	5	5
Kevin Kinley	Director, Safety and Security	0	0
Janette Hahn	Director, Special Education	0	26
Lisa Ham	Director, Technology Integration	28	31
Chris Maggard	General Manager, Child Nutrition (Sodexo)	3	11
Dana Chandler	General Manager, Transportation Services (Durham)	9	19

(1) Dr. Reid began his tenure as Superintendent on August 9, 2012.

CONSULTANTS AND ADVISORS

Auditors .... Weaver and Tidwell, L.L.P.
Fort Worth, Texas

Bond Counsel .... McCall, Parkhurst & Horton L.L.P.
Dallas, Texas

Financial Advisor .... First Southwest Company
Dallas, Texas

PRELIMINARY OFFICIAL STATEMENT
RELATING TO

$84,789,982.55*
KELLER INDEPENDENT SCHOOL DISTRICT
UNLIMITED TAX REFUNDING BONDS, SERIES 2013

INTRODUCTION

This Official Statement, which includes the Appendices hereto, provides certain information regarding the issuance of $84,789,982.55* Keller Independent School District Unlimited Tax Refunding Bonds, Series 2013 (the "Bonds"). Capitalized terms used in this Official Statement have the same meanings assigned to such terms in the Order (defined herein), except as otherwise indicated herein.

There follows in this Official Statement, descriptions of the Bonds and certain information regarding the District 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 District's Financial Advisor, First Southwest Company, Dallas, Texas.

DESCRIPTION OF THE DISTRICT . . . The District is a political subdivision located in Tarrant County, Texas. The District is governed by a seven-member Board of Trustees (the "Board") who serve staggered three-year terms with elections being held in May of each year. Policy-making and supervisory functions are the responsibility of, and are vested in, the Board. The Board delegates administrative responsibilities to the Superintendent of Schools who is the chief administrative officer of the District. Support services are supplied by consultants and advisors. The District covers approximately 51 square miles in Tarrant County, encompassing the City of Keller. Additional information with respect to the District is contained in Appendix A hereto.

PLAN OF FINANCING

PURPOSE . . . Proceeds from the sale of the Bonds will be used (1) to refund a portion of the District's Unlimited Tax School Building and Refunding Bonds, Series 2005 (the "Refunded Bonds") for debt service savings and (2) to pay the costs associated with the sale and issuance of the Bonds. See Schedule I for a detailed listing of the Refunded Bonds and their call date.

REFUNDED BONDS . . . The principal and interest due on the Refunded Bonds are to be paid on the respective interest payment dates, maturity dates and redemption date of such Refunded Bonds from funds to be deposited pursuant to a certain Escrow Agreement (the "Escrow Agreement") between U.S. Bank National Association, Dallas, Texas (the "Escrow Agent"). The Order provides that from the proceeds of the sale of the Bonds received from the Underwriters and other available District funds, if any are necessary, the District will deposit with the Escrow Agent the amount that, together with investment earnings thereon, will be sufficient to pay all amounts coming due on the Refunded Bonds to their redemption date and to accomplish the discharge and final payment of the Refunded Bonds on their redemption date. Such funds will be held by the Escrow Agent in a special escrow account (the "Escrow Fund") and used to purchase direct obligations of the United States of America (the "Federal Securities"). Under the Escrow Agreement, the Escrow Fund is irrevocably pledged to the payment of the principal of and interest on the Refunded Bonds.

Grant Thornton LLP, a nationally recognized accounting firm, will verify at the time of delivery of the Bonds to the Underwriters thereof the mathematical accuracy of the schedules that demonstrate the Federal Securities will mature and pay interest in such amounts which, together with uninvested funds, if any, in the Escrow Fund, will be sufficient to pay, when due, the principal of and interest on the Refunded Bonds. **Such maturing principal of and interest on the Federal Securities will not be available to pay the Bonds** (see "OTHER INFORMATION - Verification of Arithmetical and Mathematical Computations").

By the deposit of the Federal Securities and cash, if necessary, with the Escrow Agent pursuant to the Escrow Agreement, the District will have effected the defeasance of all of the Refunded Bonds in accordance with State law. It is the opinion of Bond Counsel that as a result of such deposit and in reliance upon the report of Grant Thornton LLP, the Refunded Bonds will be defeased and outstanding only for the purpose of receiving payments from the Federal Securities and any cash held for such purpose by the Escrow Agent and such Refunded Bonds will not be deemed as being outstanding obligations of the District payable from taxes nor for the purpose of applying any limitation on the issuance of debt. Upon defeasance of the Refunded Bonds, the payment of such Refunded Bonds will no longer be guaranteed by the Permanent School Fund of Texas.

The District will covenant in the Escrow Agreement to make timely deposits to the Escrow Fund, from lawfully available funds, of any additional amounts required to pay the principal of and interest on the Refunded Bonds, if for any reason, the cash balances on deposit or scheduled to be on deposit in the Escrow Fund are insufficient to make such payment.

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* Preliminary, subject to change.

Sources and Uses of Proceeds . . . The proceeds from the sale of the Bonds will be applied approximately as follows:

Sources of Funds		
Principal Amount of the Bonds	$	-
Net Reoffering Premium		-
Total Sources of Funds	$	-

Uses of Funds		
Deposit to Escrow Fund	$	-
Deposit of Rounding Amount to Interest and Sinking Fund		-
Underwriter's Discount and Costs of Issuance		-
Total Uses of Funds	$	-

THE BONDS

Description of the Bonds . . . The Bonds will be dated March 1, 2013. The Current Interest Bonds will accrue interest from the date of their delivery to the Underwriters, and such interest is payable on February 15 and August 15 in each year, commencing on August 15, 2013, until maturity or prior redemption. Interest on the Premium Capital Appreciation Bonds will accrete from the date of their delivery to the Underwriters and such interest will compound semiannually on February 15 and August 15 of each year beginning August 15, 2013, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The sum of the principal of the Premium Capital Appreciation Bonds, the initial premium thereon, if any, and accreted/compounded interest to maturity (the "Maturity Amount") is payable only at maturity. The Current Interest Bonds will mature on the dates, in the principal amounts, and will bear interest at the rates set forth on page 2 of this Official Statement, and such interest will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The Premium Capital Appreciation Bonds will mature on the dates, in the Maturity Amounts and interest will accrete thereon at the approximate yields based upon the initial offering prices to the public, which are set forth on page 2 of this Official Statement.

Interest on the Current Interest Bonds is payable to the registered owner appearing on the bond registration books of the Paying Agent/Registrar on the Record Date (as defined below) and such interest shall be paid by the Paying Agent/Registrar (i) by check sent by United States Mail, first class postage prepaid, to the address of the registered owner recorded in the bond register or (ii) by such other method, acceptable to the Paying Agent/Registrar, requested by, and at the risk and expense of, the registered owner. The principal and Maturity Amount of the Bonds is payable at maturity or, with respect to the Current Interest Bonds, upon prior redemption, upon their presentation and surrender to the Paying Agent/Registrar; provided, however, that so long as Cede & Co. (or other DTC nominee) is the registered owner of the Bonds, all payments will be made as described under "THE BONDS - Book-Entry-Only System" herein. If the date for the payment of the Maturity Amount, principal of or interest on the Bonds shall be a Saturday, Sunday, a legal holiday, or a day when banking institutions in the city where the designated corporate office of the Paying Agent/Registrar is located is authorized by law or executive order to close, then the date for such payment shall be the next succeeding day which is not such a Saturday, Sunday, legal holiday, or day when banking institutions are authorized to close; and payment on such date shall have the same force and effect as if made on the original date payment was due.

The Bonds will be issued only in fully registered form 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. The Current Interest Bonds will be issued in denominations of $5,000 of principal amount or any integral thereof within a maturity. The Premium Capital Appreciation Bonds will be issued in denominations of $5,000 of Maturity Amount or any integral multiple thereof within a maturity. **No physical delivery of the Bonds will be made to the beneficial owners thereof.** The Maturity Amount of the Premium Capital Appreciation Bonds and the principal of and interest on the Current Interest Bonds 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 Bonds. See "THE BONDS - Book-Entry-Only System" herein.

Authority for Issuance . . . The Bonds are issued and the tax levied for their payment pursuant to authority conferred by the Constitution and the laws of the State of Texas, including Chapter 1207, Texas Government Code, as amended, and by the order (the "Bond Order") passed by the Board.

In the Bond Order, the Board delegated to certain officers of the District, pursuant to certain provisions of Chapter 1207 of the Texas Government Code, as amended, authority to complete the sale of the Bonds. The terms of the sale will be included in a "Pricing Certificate," which will complete the sale of the Bonds (the Bond Order as supplemented by the Pricing Certificate is referred to herein as the "Order").

SECURITY AND SOURCE OF PAYMENT . . . All taxable property within the District is subject to a continuing direct annual ad valorem tax levied by the District, without legal limit as to rate or amount, sufficient to provide for the payment of principal of and interest on the Bonds. Additionally, the District has received conditional approval for the payment of the Bonds to be guaranteed by the corpus of the Permanent School Fund of Texas.

PERMANENT SCHOOL FUND GUARANTEE . . . In connection with the sale of the Bonds, the District has submitted an application to the Texas Education Agency and has received conditional approval from the Commissioner of Education for guarantee of the Bonds under the Permanent School Fund Guarantee Program (Chapter 45, Subchapter C of the Texas Education Code). Subject to satisfying certain conditions discussed under the heading "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" herein, the payment of the Bonds will be absolutely and unconditionally guaranteed by the corpus of the Permanent School Fund of the State of Texas. In the event of default by the District in the scheduled payments of the Bonds, registered owners will receive all payments due from the corpus of the Permanent School Fund.

OPTIONAL REDEMPTION . . . The District reserves the right, at its option, to redeem Current Interest Bonds having stated maturities on and after August 15, 20__, in whole or in part in principal amounts of $5,000 or any integral multiple thereof, on August 15, 20__, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption. If less than all of the Current Interest Bonds are to be redeemed, the District may select the maturities of the Current Interest Bonds to be redeemed. If less than all the Current Interest Bonds of any maturity are to be redeemed, the Paying Agent/Registrar (or DTC while the Bonds are in Book-Entry-Only form) shall determine by lot the Current Interest Bonds, or portions thereof, within such maturity to be redeemed.

The Premium Capital Appreciation Bonds are not subject to redemption prior to maturity.

NOTICE OF REDEMPTION . . . Not less than 30 days prior to a redemption date for the Current Interest Bonds, the District shall cause a notice of redemption to be sent by United States mail, first class, postage prepaid, to the registered owners of the Current Interest Bonds 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 AND ANY OTHER CONDITION TO REDEMPTION SATISFIED, THE CURRENT INTEREST BONDS CALLED FOR REDEMPTION SHALL BECOME DUE AND PAYABLE ON THE SPECIFIED REDEMPTION DATE, AND NOTWITHSTANDING THAT ANY CURRENT INTEREST BOND OR PORTION THEREOF HAS NOT BEEN SURRENDERED FOR PAYMENT, INTEREST ON SUCH CURRENT INTEREST BOND OR PORTION THEREOF SHALL CEASE TO ACCRUE.

With respect to any optional redemption of the Current Interest Bonds, unless certain prerequisites to such redemption required by the Order have been met and money sufficient to pay the principal of and premium, if any, and interest on the Current Interest Bonds to be redeemed will have been received by the Paying Agent/Registrar prior to the giving of such notice of redemption, such notice may state that said redemption is conditional upon the satisfaction of such prerequisites and receipt of such money by the Paying Agent/Registrar on or prior to the date fixed for such redemption or upon any prerequisite set forth in such notice of redemption. If a conditional notice of redemption is given and such prerequisites to the redemption are not fulfilled, such notice will be of no force and effect, the District will not redeem such Current Interest Bonds, and the Paying Agent/Registrar will give notice in the manner in which the notice of redemption was given, to the effect that such Current Interest Bonds have not been redeemed.

The Paying Agent/Registrar and the District, so long as a Book-Entry-Only System is used for the Bonds, will send any notice of redemption (with respect to the Current Interest Bonds), notice of proposed amendment to the Order or other notices only to DTC. Any failure by DTC to advise any DTC participant, or of any DTC participant or indirect participant to notify the beneficial owner, shall not affect the validity of the redemption of the Current Interest Bonds called for redemption or any other action premised on any such notice. Redemption of portions of the Current Interest Bonds by the District will reduce the outstanding principal amount of such Current Interest Bonds held by DTC. In such event, DTC may implement, through its Book-Entry-Only System, a redemption of such Current Interest Bonds held for the account of DTC participants in accordance with its rules or other agreements with DTC participants and then DTC participants and indirect participants may implement a redemption of such Current Interest Bonds from the beneficial owners. Any such selection of Current Interest Bonds to be redeemed will not be governed by the Order and will not be conducted by the District or the Paying Agent/Registrar. Neither the District nor the Paying Agent/Registrar will have any responsibility to DTC participants, indirect participants or the persons for whom DTC participants act as nominees, with respect to the payments on the Bonds or the providing of notice to DTC participants, indirect participants, or beneficial owners of the selection of portions of the Current Interest Bonds for redemption (see "THE BONDS - Book-Entry-Only System").

DEFEASANCE . . . The Order provides for the defeasance of the Bonds when payment of the principal amount of the Current Interest Bonds and the Maturity Amount of the Premium Capital Appreciation Bonds, plus interest accrued on the Current Interest Bonds to their due date (whether such due date be by reason of maturity, redemption, or otherwise), is provided by irrevocably depositing with a paying agent, or other authorized escrow agent, in trust (1) money in an amount sufficient to make such payment and/or (2) Defeasance Securities, that will mature as to principal and interest in such amounts and at such times to insure the availability, without reinvestment, of sufficient money to make such payment, and all necessary and proper fees, compensation and expenses of the paying agent for the Bonds. The District has additionally reserved the right, subject to satisfying the requirements of (1) and (2) above, to substitute other Defeasance Securities originally deposited, to reinvest the uninvested moneys on deposit for such defeasance and to withdraw for the benefit of the District moneys in excess of the amount required for such defeasance. The Order provides that "Defeasance Securities" means any securities and obligations now or hereafter authorized by State law that are eligible to discharge obligations such as the Bonds. Current State law permits defeasance with the following types of securities: (a) direct, noncallable obligations of the United States of America, including obligations that are unconditionally guaranteed by the United States of America, (b) noncallable obligations of an agency or instrumentality of the United States of America, including obligations that are unconditionally guaranteed or insured by the agency or instrumentality and that, on the date of the purchase thereof, are rated as to investment quality by a nationally recognized investment rating firm not less than AAA or its equivalent, and (c) noncallable obligations of a state or an agency or a county, municipality, or other political subdivision of a state that on the date the District purchases such securities have been refunded and are rated as to investment quality by a nationally recognized investment rating firm not less than AAA or its equivalent. There is no assurance that the current law will not be changed in a manner which would permit investments other than those described above to be made with amounts deposited to defease the Bonds. Because the Order does not contractually limit such investments, registered owners will be deemed to have consented to defeasance with such other investments, notwithstanding the fact that such investments may not be of the same investment quality as those currently permitted under State law. There is no assurance that the ratings for U.S. Treasury securities used for defeasance purposes or that for any other Defeasance Security will be maintained at any particular rating category.

Upon such deposit as described above, such Bonds shall no longer be regarded to be outstanding or unpaid. After firm banking and financial arrangements for the discharge and final payment or redemption of Bonds have been made as described above, all rights of the District to initiate proceedings to call such Current Interest Bonds for redemption or take any other action amending the terms of such Bonds are extinguished; provided, however, that the right to call such Current Interest Bonds for redemption is not extinguished if the District: (i) in the proceedings providing for the firm banking and financial arrangements, expressly reserves the right to call such Current Interest Bonds for redemption; (ii) gives notice of the reservation of that right to the owners of such Current Interest Bonds immediately following the making of the firm banking and financial arrangements; and (iii) directs that notice of the reservation be included in any redemption notices that it authorizes. Furthermore, the Permanent School Fund Guarantee will terminate with respect to the Bonds defeased in the manner provided above.

AMENDMENTS . . . The District may amend the Order without the consent of or notice to any registered owner in any manner not detrimental to the interests of the registered owners, including the curing of any ambiguity, inconsistency, or formal defect or omission therein. In addition, the District may, with the written consent of the holders of a majority in aggregate principal amount and Maturity Amount of the Bonds then outstanding and affected thereby, amend, add to, or rescind any of the provisions of the Order; except that, without the consent of the registered owners of all of the Bonds affected, no such amendment, addition or rescission may (1) make any change in the maturity of any of the outstanding Bonds; (2) reduce the rate of interest borne by any of the outstanding Bonds; (3) reduce the amount of the principal of, or redemption premium, if any, or Maturity Amount payable on any outstanding Bonds; (4) modify the terms of payment of principal or of interest or redemption premium or Maturity Amount on outstanding Bonds or any of them or impose any condition with respect to such payment; or (5) change the minimum percentage of the principal amount and Maturity Amount of the Bonds necessary for consent to such amendment.

BOOK-ENTRY-ONLY SYSTEM . . . *This section describes how ownership of the Bonds is to be transferred and how the principal and Maturity Amount of, premium, if any, and interest on the Bonds are to be paid to and credited by The Depository Trust Company ("DTC"), New York, New York, while the Bonds 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 District, the Financial Advisor and the Underwriters believe the source of such information to be reliable, but take no responsibility for the accuracy or completeness thereof.*

The District, the Financial Advisor and the Underwriters cannot and do not give any assurance that (1) DTC will distribute payments of debt service on the Bonds or any 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 Bonds) or any 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.

DTC will act as securities depository for the Bonds. The Bonds will be issued as fully-registered Bonds 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 Bond certificate will be issued for each maturity of the Bonds, each in the aggregate principal amount or Maturity Amount, as applicable, of such maturity, and will be deposited with DTC.

DTC, the world's largest securities 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 Corporation ("DTCC"). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, 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 corporations 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.

Purchases of Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC's records. The ownership interest of each actual purchaser of each Bond ("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 Bonds 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 Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds 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 Bonds 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 Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds 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 Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Bond documents. For example, Beneficial Owners of Bonds may wish to ascertain that the nominee holding the Bonds 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 registrar and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Current Interest Bonds within 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 Bonds unless authorized by a Direct Participant in accordance with DTC's MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the District 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 Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

All payments on the Bonds 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 District or the Paying Agent/Registrar, on 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 Bonds 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, the Paying Agent/Registrar, or the District, subject to any statutory or regulatory requirements as may be in effect from time to time. All payments on the Bonds to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) are the responsibility of the District or the Paying Agent/Registrar, 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.

DTC may discontinue providing its services as depository with respect to the Bonds at any time by giving reasonable notice to the District or the Paying Agent/Registrar. Under such circumstances, in the event that a successor depository is not obtained, Bond certificates are required to be printed and delivered.

The District may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered to DTC.

The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that the District and the Underwriters believe to be reliable, but neither the District nor the Underwriters take any responsibility for the accuracy thereof.

Effect of Termination of Book-Entry-Only System…In the event that the Book-Entry-Only System is discontinued, printed certificates will be issued to the holders and the Bonds will be subject to transfer, exchange and registration provisions as set forth in the Order and summarized under "THE BONDS - Transfer, Exchange and Registration" below.

Use of Certain Terms in Other Sections of this Official Statement . . . In reading this Official Statement it should be understood that while the Bonds 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 Direct or Indirect Participant acquires an interest in the Bonds, 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 Order will be given only to DTC.

PAYING AGENT/REGISTRAR . . . The initial Paying Agent/Registrar is Regions Bank, Dallas, Texas. In the Order, the District retains the right to replace the Paying Agent/Registrar. The District covenants to maintain and provide a Paying Agent/Registrar at all times until the Bonds are duly paid, and any successor Paying Agent/Registrar shall be a bank or trust company or other entity duly qualified and legally authorized to serve as and perform the duties and services of Paying Agent/Registrar for the Bonds. Upon any change in the Paying Agent/Registrar for the Bonds, the District agrees to promptly cause a written notice thereof to be sent to each registered owner of the Bonds by United States mail, first class, postage prepaid, which notice shall also give the address of the new Paying Agent/Registrar.

In the event the Book-Entry-Only System should be discontinued, interest on the Current Interest Bonds will be paid to the registered owners appearing on the registration books of the Paying Agent/Registrar at the close of business on the Record Date (hereinafter defined), and such interest will be paid (i) by check sent United States mail, first class postage prepaid to the address of the registered owner recorded in the registration books of the Paying Agent/Registrar or (ii) by such other method, acceptable to the Paying Agent/Registrar requested by, and at the risk and expense of, the registered owner. Principal and Maturity Amount of the Bonds will be paid to the registered owner at the stated maturity or, with respect to the Current Interest Bonds, upon prior redemption, upon presentation to the designated payment/transfer office of the Paying Agent/Registrar; provided, however, that so long as Cede & Co. (or other DTC nominee) is the registered owner of the Bonds, payments of principal and Maturity Amount of the Bonds and interest on the Current Interest Bonds will be made as described in "THE BONDS - Book-Entry-Only System," above.

TRANSFER, EXCHANGE AND REGISTRATION . . . In the event the Book-Entry-Only System should be discontinued, printed Bond certificates will be delivered to registered owners and thereafter the Bonds may be transferred and exchanged on the registration books of the Paying Agent/Registrar only upon presentation and surrender of such printed certificates 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. Bonds may be assigned by the execution of an assignment form on the respective Bonds or by other instrument of transfer and assignment acceptable to the Paying Agent/Registrar. New Bonds will be delivered by the Paying Agent/Registrar, in lieu of the Bonds 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 Bonds issued in an exchange or transfer of Bonds 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 Bonds 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 Bonds registered and delivered in an exchange or transfer shall be in any integral multiple of $5,000 of principal or Maturity Amount, as applicable, for any one maturity and for a like aggregate principal amount or Maturity Amount, as the case may be, as the Bonds surrendered for exchange or transfer. See "THE BONDS - Book-Entry-Only System" herein for a description of the system to be utilized initially in regard to ownership and transferability of the Bonds. Neither the District nor the Paying Agent/Registrar shall be required to transfer or exchange any Current Interest Bond 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 Current Interest Bond.

Record Date for Interest Payment . . . The record date ("Record Date") for the interest payable on the Current Interest Bonds on any interest payment date means the close of business on the last business 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 District. 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 registered owner of a Current Interest Bond appearing on the registration books of the Paying Agent/Registrar at the close of business on the last business day next preceding the date of mailing of such notice.

Yield on Premium Capital Appreciation Bonds. . . The "Accreted Value" for the Premium Capital Appreciation Bonds means the original principal amount of a Premium Capital Appreciation Bond plus the initial premium, if any, paid therefor with interest thereon compounded semiannually to February 15 or August 15 (each, an "Accretion Date"), as the case may be, next preceding the date of such calculation (or the date of calculation, if such calculation is made on February 15 or August 15), using the respective yields to maturity stated on page 2. Based on the initial offering prices for the Premium Capital Appreciation Bonds, a schedule of Accreted Values per $5,000 Maturity Amount on the respective Accretion Dates, using the yields stated on page 2 of this Official Statement, is set forth in Schedule II attached hereto. Such Accreted Value table is provided for informational purposes only and may not reflect prices for the Premium Capital Appreciation Bonds in the secondary market. The respective yields on the Premium Capital Appreciation Bonds to a particular purchaser may differ depending upon the price paid by that purchaser. For various reasons, securities that do not pay interest periodically, such as the Premium Capital Appreciation Bonds, have traditionally experienced greater price fluctuation in the secondary market than securities that pay interest on a periodic basis.

Bondholders' Remedies . . . The Order does not specify events of default with respect to the Bonds. If the District defaults in the payment of principal, interest, or redemption price on the Bonds when due or the State fails to honor the Permanent School Fund Guarantee as hereinafter discussed, or the District defaults in the observation or performance of any other covenants, conditions, or obligations set forth in the Order, the registered owners may seek a writ of mandamus to compel the District or District officials to carry out the legally imposed duties with respect to the Bonds if there is no other available remedy at law to compel performance of the Bonds or the Order and the District's obligations are not uncertain or disputed, as well as to enforce the rights of payment under the Permanent School Fund Guarantee. The issuance of a writ of mandamus is controlled by equitable principles, so rests with the discretion of the court, but may not be arbitrarily refused. There is no acceleration of maturity of the Bonds in the event of default and, consequently, the remedy of mandamus may have to be relied upon from year to year. The Order does not provide for the appointment of a trustee to represent the interest of the Bondholders upon any failure of the District to perform in accordance with the terms of the Order, or upon any other condition and accordingly all legal actions to enforce such remedies would have to be undertaken at the initiative of, and be financed by, the registered owners. On June 30, 2006, the Texas Supreme Court ruled in *Tooke v. City of Mexia*, 197 S.W. 3rd 325 (Tex. 2006), that a waiver of sovereign immunity in a contractual dispute must be provided for by statute in "clear and unambiguous" language. Because it is unclear whether the Texas legislature has effectively waived the District's sovereign immunity from a suit for money damages, Bondholders may not be able to bring such a suit against the District for breach of the Bonds or Order covenants in the absence of District action. Chapter 1371, Texas Government Code ("Chapter 1371"), which pertains to the issuance of public securities by issuers such as the District, permits the District to waive sovereign immunity in the proceedings authorizing its bonds, but in connection with the issuance of the Bonds, the District has not waived sovereign immunity and is not using the legal authority provided by Chapter 1371. Even if a judgment against the District could be obtained, it could not be enforced by direct levy and execution against the District's property. Further, the registered owners cannot themselves foreclose on property within the District or sell property within the District to enforce the tax lien on taxable property to pay the principal of and interest on the Bonds. Furthermore, the District is 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 ad valorem 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 Bondholders of an entity which has sought protection under Chapter 9. Therefore, should the District 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 other 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 Bonds are qualified with respect to the customary rights of debtors relative to their creditors. See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" herein for a description of the procedures to be followed for payment of the Bonds by the Permanent School Fund in the event the District fails to make a payment on the Bonds when due. Also see "Book-Entry-Only System" herein for a description of the duties of DTC with regard to ownership of the Bonds.

THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM

The information below concerning the Texas Permanent School Fund and the Guarantee Program for School District Bonds has been provided by the Texas Education Agency and is not guaranteed as to accuracy or completeness by, and is not to be construed as a representation by the District or the Underwriters.

This disclosure statement provides information relating to the program administered by the Texas Education Agency (the "TEA") with respect to the Texas Permanent School Fund guarantee of Texas school district bonds, which program is referred to, and defined herein, as the Guarantee Program.

Some of the information contained in this Section may include projections or other forward-looking statements regarding future events or the future financial performance of the Texas Permanent School Fund (the "PSF" or the "Fund"). Actual results may differ materially from those contained in any such projections or forward-looking statements.

HISTORY AND PURPOSE

The PSF was created with a $2,000,000 appropriation by the Texas Legislature (the "Legislature") in 1854 expressly for the benefit of the public schools of Texas. The Constitution of 1876 stipulated that certain lands and all proceeds from the sale of these lands should also constitute the PSF. Additional acts later gave more public domain land and rights to the PSF. In 1953, the U.S. Congress passed the Submerged Lands Act that relinquished to coastal states all rights of the U.S. navigable waters within state boundaries. If the state, by law, had set a larger boundary prior to or at the time of admission to the Union, or if the boundary had been approved by Congress, then the larger boundary applied. After three years of litigation (1957-1960), the U. S. Supreme Court on May 31, 1960, affirmed Texas' historic three marine leagues (10.35 miles) seaward boundary. Texas proved its submerged lands property rights to three leagues into the Gulf of Mexico by citing historic laws and treaties dating back to 1836. All lands lying within that limit belong to the PSF. The proceeds from the sale and the mineral-related rental of these lands, including bonuses, delay rentals and royalty payments, become the corpus of the Fund. Prior to the approval by the voters of the State of an amendment to the constitutional provision under which the Fund is established and administered, which occurred on September 13, 2003 (the "Total Return Constitutional Amendment"), and which is further described below, the PSF had as its main sources of revenues capital gains from securities transactions and royalties from the sale of oil and natural gas. The Total Return Constitutional Amendment provides that interest and dividends produced by Fund investments will be additional revenue to the PSF. The State School Land Board ("SLB") maintains the land endowment of the Fund on behalf of the Fund and is authorized to manage the investments of the capital gains, royalties and other investment income relating to the land endowment. The SLB is a three member board, the membership of which consists of the Commissioner of the Texas General Land Office (the "Land Commissioner") and two citizen members, one appointed by the Governor and one by the Texas Attorney General (the "Attorney General").

The Texas Constitution describes the PSF as "permanent" and "perpetual." Prior to the approval by Total Return Constitutional Amendment, only the income produced by the PSF was to be used to complement taxes in financing public education.

On November 8, 1983, the voters of the State approved a constitutional amendment that provides for the guarantee of school district bonds by the PSF. On approval by the State Commissioner of Education (the "Commissioner"), bonds properly issued by a school district are fully guaranteed by the corpus of the PSF. See "The Guarantee Program."

The sole purpose of the PSF is to assist in the funding of public education for present and future generations. Prior to the adoption of the Total Return Constitutional Amendment, all interest and dividends produced by Fund investments flowed into the Available School Fund (the "ASF"), where they are distributed to local school districts based on average daily attendance. Any net gains from investments of the Fund accrue to the corpus of the PSF. Prior to the approval by the voters of the State of the Total Return Constitutional Amendment, costs of administering the PSF were allocated to the ASF. With the approval of the Total Return Constitutional Amendment, the administrative costs of the Fund have shifted from the ASF to the PSF. In fiscal year 2012, distributions to the ASF amounted to $221.04 per student and the total amount distributed to the ASF was $1.021 billion.

Audited financial information for the PSF is provided annually through the PSF Annual Report (the "Annual Report"), which is filed with the Municipal Securities Rulemaking Board ("MSRB"). The Annual Report includes the Message of the Executive Administrator of the Fund (the "Message") and the Management's Discussion and Analysis ("MD&A"). The Annual Report for the year ended August 31, 2012, when filed with the MSRB in accordance with the PSF undertaking and agreement made in accordance with Rule 15c2-12 ("Rule 15c2-12") of the federal Securities and Exchange Commission (the "SEC"), as described herein, and simultaneously posted to the PSF web site, as described below, is hereby incorporated by reference into this disclosure. Information included herein for the year ended August 31, 2012 is derived from the audited financial statements of the PSF, which are included in the Annual Report when it is filed and posted. Reference is made to the Annual Report, when filed, for the complete Message and MD&A for the year ended August 31, 2012 and for a description of the financial results of the PSF for the year ended August 31, 2012, the most recent year for which audited financial information regarding the Fund is available. The 2012 Annual Report speaks only as of its date and the TEA has not obligated itself to update the 2012 Annual Report or any other Annual Report. The TEA posts each Annual Report, which includes statistical data regarding the Fund as of the close of each fiscal year, the most recent disclosure for the Guarantee Program, the Statement of Investment Objectives, Policies and Guidelines of the Texas Permanent School Fund, which is codified at 19 Texas Administrative Code, Chapter 33 (the "Investment Policy"), monthly updates with respect to the capacity of the Guarantee Program (collectively, the "Web Site Materials") on the TEA web site at www.tea.state.tx.us/psf and with the MSRB at www.emma.msrb.org. Such monthly updates regarding the Guarantee Program are also incorporated herein and made a part hereof for all purposes. In addition to the Web Site Materials, the Fund is required to make quarterly filings with the SEC under Section 13(f) of the Securities Exchange Act of 1934. Such filings, which consist of a list of the Fund's holdings of securities specified in Section 13(f), including exchange-traded (*e.g.,* NYSE) or NASDAQ-quoted stocks, equity options and warrants, shares of closed-end investment companies and certain convertible debt securities, is available from the SEC at www.sec.gov/edgar.shtml. A list of the Fund's equity and fixed income holdings as of August 31 of each year is posted to the TEA web site and filed with the MSRB. Such list excludes holdings in the Fund's securities lending program. Such list, when filed, is incorporated herein and made a part hereof for all purposes.

THE TOTAL RETURN CONSTITUTIONAL AMENDMENT

The Total Return Constitutional Amendment approved a fundamental change in the way that distributions are made to the ASF from the PSF. The Total Return Constitutional Amendment requires that PSF distributions to the ASF be determined using a total-return-based formula instead of the current-income-based formula, which was used from 1964 to the end of the 2003 fiscal year. The Total Return Constitutional Amendment provides that the total amount distributed from the Fund to the ASF: (1) in each year of a State fiscal biennium must be an amount that is not more than 6% of the average of the market value of the Fund, excluding real property (the "Distribution Rate"), on the last day of each of the sixteen State fiscal quarters preceding the Regular Session of the Legislature that begins before that State fiscal biennium (the "Distribution Measurement Period"), in accordance with the rate adopted by: (a) a vote of two-thirds of the total membership of the State Board of Education ("SBOE"), taken before the Regular Session of the Legislature convenes or (b) the Legislature by general law or appropriation, if the SBOE does not adopt a rate as provided by clause (a); and (2) over the ten-year period consisting of the current State fiscal year and the nine preceding state fiscal years may not exceed the total return on all investment assets of the Fund over the same ten-year period (the "Ten Year Total Return"). In April 2009, the Attorney General issued a legal opinion, Op. Tex. Att'y Gen. No. GA-0707 (2009) ("GA-0707"), at the request of the Chairman of the SBOE with regard to certain matters pertaining to the Distribution Rate and the determination of the Ten Year Total Return. In GA-0707 the Attorney General opined, among other advice, that (i) the Ten Year Total Return should be calculated on an annual basis, (ii) a contingency plan adopted by the SBOE, to permit monthly transfers equal in aggregate to the annual Distribution Rate to be halted and subsequently made up if such transfers temporarily exceed the Ten Year Total Return, is not prohibited by State law, provided that such contingency plan applies only within a fiscal year time basis, not on a biennium basis, and (iii) that the amount distributed from the Fund in a fiscal year may not exceed 6% of the average of the market value of the Fund or the Ten Year Total Return. In accordance with GA-0707, in the event that the Ten Year Total Return is exceeded during a fiscal year, transfers to the ASF will be halted. However, if the Ten Year Total Return subsequently increases during that biennium, transfers may be resumed, if the SBOE has provided for that contingency, and made in full during the remaining period of the biennium, subject to the limit of 6% in any one fiscal year. Any shortfall in the transfer that results from such events from one biennium may not be paid over to the ASF in a subsequent biennium as the SBOE would make a separate payout determination for that subsequent biennium.

In determining the Distribution Rate, the SBOE has adopted the goal of maximizing the amount distributed from the Fund in a manner designed to preserve "intergenerational equity." Intergenerational equity is the maintenance of endowment purchasing power to ensure that endowment spending keeps pace with inflation, with the ultimate goal being to ensure that current and future generations are given equal levels of purchasing power. In making this determination, the SBOE takes into account various considerations, and relies particularly upon its external investment consultant, which undertakes a probability analysis for long term projection periods that includes certain assumptions. Among the assumptions used in the analysis are a projected rate of growth of the average daily scholastic attendance State-wide, the projected contributions and expenses of the Fund, projected returns in the capital markets and a projected inflation rate.

The SBOE established the Distribution Rate from the Fund to the ASF for fiscal years 2008 and 2009 at 3.5% and for fiscal years 2010 and 2011 at 2.5% of the average of the PSF market value during the respective Distribution Measurement Periods, which ended in November 2006 and November 2008, respectively. The decision of the SBOE regarding the Distribution Rate for 2008 through 2011 took into account a commitment by the SLB to transfer at least $100 million per year in fiscal years 2008 through 2011. The distribution rate for fiscal years 2010 and 2011 produced total transfers of $1.1535 billion to the ASF from the PSF during those years. The SBOE has set the Distribution Rate for the 2012-13 biennium at 4.2%, which rate was determined after the SLB authorized the release of a total of $500 million to the PSF in quarterly installments during the 2012-13 biennium. In November 2012, the SBOE set the Distribution Rate for the 2014-15 biennium at 3.3%, which is expected to produce an effective rate of 3.5% taking into account the broadening of the calculation base for the Fund that was effected by a 2011 State constitutional amendment, which amendment did not increase Fund revenues. See "2011 Constitutional Amendment" below for a description of amendments made to the Texas Constitution on November 8, 2011 that permits the SLB to make transfers directly to the ASF up to the amount of $300 million in each fiscal year.

Since the enactment of a prior amendment to the Texas Constitution in 1964, the investment of the Fund has been managed with the dual objectives of producing current income for transfer to the ASF and growing the Fund for the benefit of future generations. As a result of this prior constitutional framework, prior to the adoption of the 2004 Asset Allocation Policy (as defined below) the investment of the Fund historically included a significant amount of fixed income investments and dividend-yielding equity investments, to produce income for transfer to the ASF.

With respect to the management of the Fund's investment portfolio, the single most significant change made to date as a result of the Total Return Constitutional Amendment has been new asset allocation policies adopted by the SBOE in February 2004 (the "2004 Asset Allocation Policy"), in July 2006 (as subsequently reaffirmed in July 2008 such asset allocation is referred to herein as the "2008 Asset Allocation Policy") and in July 2010 (the "2010 Asset Allocation Policy"), which have significantly altered the asset allocations of the Fund. The SBOE further modified the asset allocation policy for the Fund in July 2012 (the "2012 Asset Allocation"). The Fund's investment policy provides for minimum and maximum ranges among the components of each of the three general asset classifications: equities, fixed income and alternative asset investments. The 2004 Asset Allocation Policy decreased the fixed income target from 45% to 25% of Fund investment assets and increased the allocation for equities from 55% to 75% of investment assets. In July 2006, the SBOE modified its asset allocation to reduce the equity allocation, including both domestic and foreign equity portfolios, to a target of 53% of Fund assets, further reduced the fixed income allocation target to 19% and added an alternative asset allocation, which included real estate, real return, absolute return and private equity components, totaling 28% of the Fund's asset target. Alternative asset classes diversify the SBOE-managed assets and are not as correlated to traditional asset classes, which is intended to increase investment returns over the long run while reducing risk and return volatility of the portfolio. In July 2010, the SBOE modified the 2008 Asset Allocation Policy by decreasing the equity allocation to 50%, and the fixed income allocation to 15%, while increasing the alternative asset allocation (which may include equity and fixed income investments as part of a variety of alternative investment strategies) to 35%. In July 2012, the SBOE modified the 2010 Asset Allocation Policy by decreasing the equity allocation to 46%, increasing the fixed income allocation to 17%, and increasing the alternative asset allocation (which may include equity and fixed income investments as part of a variety of alternative investment strategies) to 37%. The 2012 Asset Allocation changes decreased the target for large cap equity investments from 21% to 18%, replaced a 4% allocation for international small cap equities with a 3% allocation for emerging international equities, reduced core fixed income bond investments from 15% to 12% and added a new 5% allocation for emerging market debt in the fixed income portfolio. In July 2012, the SBOE also realigned the management of certain of the five investment portfolios within the absolute return allocation of the alternative investments, which include hedge fund investments within externally managed portfolios. As a result of that investment strategy, the Fund pays a double layer of fees, to external managers and to the underlying hedge fund managers. The new alignments in two of the portfolios will create a strategic relationship between the external manager and investment staff of the PSF. In time, those relationships may result in internal management of those portfolios by the PSF, which would reduce management fees. The Chair of the SBOE has filed a request with the Attorney General with respect to the authority of the SBOE to select certain investments and select and contract with investment managers and other third party providers of investment services in connection with the direct management of alternative investments through investment vehicles to be created by the SBOE, in lieu of contracting with external managers for such services, as has been the recent practice of the PSF. In particular, the SBOE Chair has presented questions pertaining to whether the SBOE can undertake such activities without complying with the competitive process required by the State Purchasing and General Services Act, given the unique nature of such investments and services. The opinion request is available for review at https://www.oag.state.tx.us/opinions/opinions/50abbott/rq/2012/pdf/RQ1092GA.pdf. The PSF Staff and the Fund's investment advisor are tasked with advising the SBOE with respect to the implementation of the 2010 Asset Allocation Policy, including the timing and manner of the selection of any external managers and other consultants. For a variety of reasons, each change in asset allocation for the Fund, including the 2012 Asset Allocation Policy, has been, and is being, implemented in phases. At August 31, 2012, the Fund was invested as follows: 54.33% in public market equity investments; 21.33% in fixed income investments; 10.04% in absolute return assets; 1.71% in private equity assets; 2.45% in real estate assets; 7.13% in risk parity assets; 2.96% in real return assets; and 0.05% in cash.

In accordance with the Texas Constitution, the SBOE views the PSF as a perpetual institution, and the Fund is managed as an endowment fund with a long-term investment horizon. Under the total-return investment objective, the Investment Policy provides that the PSF shall be managed consistently with respect to the following: generating income for the benefit of the public free schools of Texas, the real growth of the corpus of the PSF, protecting capital, and balancing the needs of present and future generations of Texas school children. As described above, the Total Return Constitutional Amendment restricts the annual pay out from the Fund to the total-return on all investment assets of the Fund over a rolling ten-year period. State law provides that each transfer of funds from the PSF to the ASF is made monthly, with each transfer to be in the amount of one-twelfth of the annual distribution. The heavier weighting of equity securities relative to fixed income investments has resulted in greater volatility of the value of the Fund. Given the greater weighting in the overall portfolio of passively managed investments, it is expected that the Fund will reflect the general performance returns of the markets in which the Fund is invested.

The asset allocation of the Fund is subject to change by the SBOE from time to time based upon a number of factors, including recommendations to the SBOE made by internal investment staff and external consultants, changes made by the SBOE without regard to such recommendations and directives of the Legislature. Fund performance may also be affected by factors other than asset allocation, including, without limitation, the general performance of the securities markets in the United States and abroad;

political and investment considerations including those relating to socially responsible investing; application of the prudent person investment standard, which may eliminate certain investment opportunities for the Fund; management fees paid to external managers and embedded management fees for some fund investments; and limitations on the number and compensation of internal and external investment staff, which is subject to Legislative oversight. The Guarantee Program could also be impacted by changes in State or federal law or the implementation of new accounting standards.

MANAGEMENT AND ADMINISTRATION OF THE FUND

The Texas Constitution and applicable statutes delegate to the SBOE the authority and responsibility for investment of the PSF's financial assets. In investing the Fund, the SBOE is charged with exercising the judgment and care under the circumstances then prevailing which persons of ordinary prudence, discretion and intelligence exercise in the management of their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income therefrom as well as the probable safety of their capital. The SBOE has adopted a "Statement of Investment Objectives, Policies, and Guidelines of the Texas Permanent School Fund," which is codified in the Texas Administrative Code beginning at 19 TAC section 33.1.

The Total Return Constitutional Amendment provides that expenses of managing the PSF are to be paid "by appropriation" from the PSF. In January 2005, at the request of the SBOE, the Attorney General issued a legal opinion, Op. Tex. Att'y Gen. No. GA-0293 (2005) ("GA-0293"), that the Total Return Constitutional Amendment requires that SBOE expenditures for managing or administering PSF investments, including payments to external investment managers, be paid from appropriations made by the Legislature, but that the Total Return Constitutional Amendment does not require the SBOE to pay from such appropriated PSF funds the indirect management costs deducted from the assets of a mutual fund or other investment company in which PSF funds have been invested.

Texas law assigns control of the Fund's land and mineral rights to the three-member SLB, which consists of the elected Commissioner of the General Land Office ("GLO"), an appointee of the Governor, and an appointee of the Attorney General. Administrative duties related to the land and mineral rights reside with the GLO, which is under the guidance of the Commissioner of the GLO. In 2007, the Legislature established the real estate special fund account of the PSF (the "Real Estate Account") consisting of the land, mineral or royalty interest, real estate investment, or other interest, including revenue received from those sources, that is set apart to the PSF under the Texas Constitution and laws, together with the mineral estate in riverbeds, channels, and the tidelands, including islands. The investment of the Real Estate Account is subject to the sole and exclusive management and control of the SLB and the Land Commissioner, who is also the head of the GLO. The 2007 legislation presented constitutional questions regarding the respective roles of the SBOE and the SLB relating to the disposition of proceeds of real estate transactions to the ASF, among other questions. Amounts in the investment portfolio of the PSF are taken into account by the SBOE for purposes of determining the Distribution Rate. An amendment to the Texas Constitution was approved by State voters on November 8, 2011, which permits the SLB to make transfers directly to the ASF, see "2011 Constitutional Amendment" below.

The SBOE contracts with its securities custodial agent to measure the performance of the total return of the Fund. A consultant is typically retained for the purpose of providing consultation with respect to strategic asset allocation decisions and to assist the SBOE in selecting external fund management advisors. The SBOE also contracts with financial institutions for custodial and securities lending services. The SBOE has established the Committee of Investment Advisors, which consists of independent investment experts each appointed by a member of the SBOE to closely advise the respective SBOE member on investment issues.

As noted above, the Texas Constitution and applicable statutes make the SBOE responsible for investment of the PSF's financial assets. By law, the Commissioner is appointed by the Governor, with Senate confirmation, and assists the SBOE, but the Commissioner can neither be hired nor dismissed by the SBOE. The Executive Administrator of the Fund is also hired by and reports to the Commissioner. Moreover, although the Fund's Executive Administrator and his staff implement the decisions of and provide information to the School Finance/PSF Committee of the SBOE and the full SBOE, the SBOE can neither select nor dismiss the Executive Administrator. TEA's General Counsel provides legal advice to the Executive Administrator and to the SBOE. The SBOE has also engaged outside counsel to advise it as to its duties over the Fund, including specific actions regarding the investment of the PSF to ensure compliance with fiduciary standards, and to provide transactional advice in connection with the investment of Fund assets in non-traditional investments.

THE GUARANTEE PROGRAM

The Guarantee Program for School District Bonds (the "Guarantee Program") was authorized by an amendment to the Texas Constitution in 1983 and by Subchapter C of Chapter 45 of the Texas Education Code (the "Act"). If the conditions for the Guarantee Program are satisfied, the guarantee becomes effective upon approval of the Bonds by the Attorney General and remains in effect until the guaranteed bonds are paid or defeased, by a refunding or otherwise.

In the event of default, holders of guaranteed bonds will receive all payments due from the corpus of the PSF. Following a determination that a district will be or is unable to pay maturing or matured principal or interest on any guaranteed bond, the Act requires the district to notify the Commissioner not later than the fifth day before the stated maturity date of such bond or interest payment. Immediately following receipt of such notice, the Commissioner must cause to be transferred from the appropriate account in the PSF to the Paying Agent/Registrar an amount necessary to pay the maturing or matured principal and interest. Upon receipt of funds for payment of such principal or interest, the Paying Agent/Registrar must pay the amount due and forward the canceled bond or evidence of payment of the interest to the State Comptroller of Public Accounts (the "Comptroller"). The Commissioner will instruct the Comptroller to withhold the amount paid, plus interest, from the first State money payable to the district. The amount withheld will be deposited to the credit of the PSF. The Comptroller must hold such canceled bond or evidence of payment of the interest on behalf of the PSF. Following full reimbursement of such payment by the district to the PSF with interest, the Comptroller will cancel the bond or evidence of payment of the interest and forward it to the district. The Act permits the Commissioner to order a school district to set a tax rate sufficient to reimburse the Fund for any payments made with respect to guaranteed bonds, and also sufficient to pay future payments on guaranteed bonds, and provides certain enforcement mechanisms to the Commissioner, including the appointment of a board of managers or annexation of a defaulting district to another district.

If a district fails to pay principal or interest on a bond as it is stated to mature, other amounts not due and payable are not accelerated and do not become due and payable by virtue of the district's default. The Guarantee Program does not apply to the payment of principal and interest upon redemption of bonds, except upon mandatory sinking fund redemption, and does not apply to the obligation, if any, of a school district to pay a redemption premium on bonds.

In the event that two or more payments are made from the PSF on behalf of a district, the Commissioner shall request the Attorney General to institute legal action to compel the district and its officers, agents and employees to comply with the duties required of them by law in respect to the payment of guaranteed bonds.

For a discussion of legislative developments that have authorized the use of the Fund to guarantee revenue bonds issued by certain open-enrollment charter schools, see "Other 2011 Legislative Actions – Charter School Guarantee Program" below.

CAPACITY LIMITS FOR THE GUARANTEE PROGRAM

The capacity of the Fund to guarantee bonds under the Guarantee Program is limited in two ways: by State law (the "State Capacity Limit") and by regulations and a notice issued by the Internal Revenue Service (the "IRS" and the "IRS Limit," respectively). Prior to May 20, 2003, the State Capacity Limit was equal to two times the lower of cost or fair market value of the Fund's assets, exclusive of real estate. During the 78th Regular Session of the Legislature in 2003, legislation was enacted that increased the State Capacity Limit by 25%, to two and one half times the lower of cost or fair market value of the Fund's assets as estimated by the SBOE and certified by the State Auditor, and eliminated the real estate exclusion from the calculation. Prior to the issuance of the IRS Notice (defined below), the capacity of the program under the IRS Limit was limited to two and one-half times the lower of cost or fair market value of the Fund's assets adjusted by a factor that excluded additions to the Fund made since May 14, 1989. During the 2007 Texas Legislature, Senate Bill 389 ("SB 389") was enacted providing for additional increases in the capacity of the Guarantee Program, and specifically providing that the SBOE may by rule increase the capacity of the Guarantee Program from two and one-half times the cost value of the PSF to an amount not to exceed five times the cost value of the PSF, provided that the increased limit does not violate federal law and regulations and does not prevent bonds guaranteed by the Guarantee Program from receiving the highest available credit rating, as determined by the SBOE. SB 389 further provides that the SBOE shall at least annually consider whether to change the capacity of the Guarantee Program. Since 2005, the Guarantee Program has twice reached capacity under the IRS Limit, and in each instance the Guarantee Program was closed to new bond guarantee applications until relief was obtained from the IRS. The most recent closure of the Guarantee Program commenced in March 2009 and the Guarantee Program reopened in February 2010 on the basis of receipt of the IRS Notice.

On December 16, 2009, the IRS published Notice 2010-5 (the "IRS Notice") stating that the IRS will issue proposed regulations amending the existing regulations to raise the IRS limit to 500% of the total cost of the assets held by the PSF as of December 16, 2009. In accordance with the IRS Notice, the amount of any new bonds to be guaranteed by the PSF, together with the then outstanding amount of bonds previously guaranteed by the PSF, must not exceed the IRS limit on the sale date of the new bonds to be guaranteed. The IRS Notice further provides that the IRS Notice may be relied upon for bonds sold on or after December 16, 2009, and before the effective date of future regulations or other public administrative guidance affecting funds like the PSF.

The IRS Notice establishes a static capacity for the Guarantee Program based upon the cost value of Fund assets on December 16, 2009 multiplied by five. On December 16, 2009, the cost value of the Guarantee Program was $23,463,730,608 (estimated and unaudited), thereby producing an IRS Limit of approximately $117.3 billion. The State Capacity Limit is determined on the basis of the cost value of the Fund from time to time multiplied by the capacity multiplier determined annually by the SBOE, but not to exceed a multiplier of five. The capacity of the Guarantee Program will be limited to the lower of the State Capacity Limit and the IRS Limit. On May 21, 2010, the SBOE modified the regulations that govern the Guarantee Program (the "Guarantee Program Rules"), and increased the State Law Capacity to an amount equal to three times the cost value of the PSF.

Such modified regulations, including the revised capacity rule, became effective on July 1, 2010. The Guarantee Program Rules provide that the Commissioner may reduce the multiplier to maintain the AAA credit rating of the Guarantee Program, but provide that any changes to the multiplier made by the Commissioner are to be ratified or rejected by the SBOE at the next meeting following the change. See "Valuation of the PSF and Guaranteed Bonds," below.

Since July 1991, when the SBOE amended the Guarantee Program Rules to broaden the range of bonds that are eligible for guarantee under the Guarantee Program to encompass most Texas school district bonds, the principal amount of bonds guaranteed under the Guarantee Program has increased sharply. In addition, in recent years a number of factors have caused an increase in the amount of bonds issued by school districts in the State. See the table "Permanent School Fund Guaranteed Bonds" below. The SBOE has approved and modified the Guarantee Program Rules in recent years, most recently in May 2010. Generally, the Guarantee Program Rules limit guarantees to certain types of notes and bonds, including, with respect to refunding bonds, a requirement that the bonds produce debt service savings, and that bonds issued for capital facilities must have been voted as unlimited tax debt of the issuing district. The Guarantee Program regulations include certain accreditation criteria for districts applying for a guarantee of their bonds, and limit guarantees to districts that have less than the amount of annual debt service per average daily attendance that represents the 90th percentile of annual debt service per average daily attendance for all districts, but such limitation will not apply to school districts that have enrollment growth of at least 25% over the previous five school years. Effective September 1, 2009, the Act provides that the SBOE may annually establish a percentage of the cost value of the Fund to be reserved from use in guaranteeing bonds. The capacity of the Guarantee Program in excess of any reserved portion is referred to herein as the "Capacity Reserve." The Guarantee Program Rules provide for a minimum Capacity Reserve of no less than 5%, and provide that the amount of the Capacity Reserve may be increased by a majority vote of the SBOE. The Commissioner is authorized to change the Capacity Reserve, which decision must be ratified or rejected by the SBOE at its next meeting following any change made by the Commissioner. The Guarantee Program Rules are codified in the Texas Administrative Code at 19 TAC sections 33.65 et seq., and are available on the TEA web site at www.tea.state.tx.us/rules/tac/chapter033/index.html. The current Capacity Reserve is noted in the monthly updates with respect to the capacity of the Guarantee Program on the TEA web site at www.tea.state.tx.us/psf, which are also filed with the MSRB.

Based upon historical performance of the Fund, the legal restrictions relating to the amount of bonds that may be guaranteed has generally resulted in a lower ratio of guaranteed bonds to available assets as compared to many other types of credit enhancements that may be available for Texas school district bonds. However, changes in the value of the Fund due to changes in securities markets, investment objectives of the Fund, an increase in bond issues by school districts in the State or legal restrictions on the Fund, the implementation of a guarantee program for revenue bonds issued by certain open-enrollment charter schools, or an increase in the calculation base of the Fund for purposes of making transfers to the ASF (see "Other 2011 Legislative Actions – Charter School Guarantee Program" below), among other factors, could adversely affect the ratio of Fund assets to guaranteed bonds and the growth of the Fund in general. It is anticipated that the issuance of the IRS Notice will substantially increase the amount of bonds guaranteed under the Guarantee Program.

The Act requires that the Commissioner prepare, and the SBOE approve, an annual report on the status of the Guarantee Program (the Annual Report). The State Auditor audits the financial statements of the PSF, which are separate from other State financial statements.

RATINGS OF BONDS GUARANTEED UNDER THE GUARANTEE PROGRAM

Moody's Investors Service, Standard & Poor's Rating Service, a Standard & Poor's Financial Service LLC business, and Fitch Ratings rate bonds guaranteed by the PSF "Aaa," "AAA" and "AAA," respectively. Not all districts apply for multiple ratings on their bonds, however. See "Ratings" herein.

VALUATION OF THE PSF AND GUARANTEED BONDS

Permanent School Fund Valuations

Fiscal Year Ended 8/31	Book Value[1]	Market Value[1]
2008	$ 22,926,299,922	$ 29,336,248,611
2009	23,117,052,793	25,443,104,623
2010	23,653,185,489	27,066,200,259
2011	24,701,156,685	29,643,439,794
2012	25,161,994,845[2]	31,284,851,266[2]

[1] SLB SLB managed assets are included in the market value and book value of the Fund. In determining the market value of the PSF from time to time during a fiscal year, the TEA uses current, unaudited values for TEA managed investment portfolios and cash held by the SLB. Market values of land and mineral interests, and investments in externally managed real estate funds managed by the SLB are based upon information reported to the PSF by the SLB. Beginning in fiscal year 2009, the SLB

reported that information to the PSF on a quarterly basis. The valuation of such assets at any point in time is dependent upon a variety of factors, including economic conditions in the State and nation in general, and the values of these assets, and, in particular, the valuation of mineral holdings administered by the SLB, can be volatile and subject to material changes from period to period. At August 31, 2012, land, external real estate investments, mineral assets and cash managed by the SLB had book values of approximately $341.10 million, $1.65 billion, $13.40 million and $1.38 billion, respectively, and market values of approximately $673.92 million, $1.55 billion, $2.18 billion and $1.34 billion, respectively.
(2) At November 30, 2012, the PSF had a book value of $25,171,202,517 and a market value of $31,674,486,091 (in each case, based on unaudited data).

Permanent School Fund Guaranteed Bonds

At 8/31	Principal Amount(1)
2008	$ 49,860,572,025
2009	50,032,724,439
2010	49,301,683,338
2011	52,653,930,546
2012	53,634,455,141(2)

(1) Represents original principal amount; does not reflect any subsequent accretions in value for compound interest bonds (zero coupon securities). The amount shown excludes bonds that have been refunded and released from the Guarantee Program. The TEA does not maintain records of the accreted value of capital appreciation bonds that are guaranteed under the Guarantee Program.
(2) As of August 31, 2012, the TEA expected that the principal and interest to be paid by school districts over the remaining life of the bonds guaranteed by the Guarantee Program is $90,343,555,115, of which $36,709,099,974 represents interest to be paid. At November 30, 2012, there were $54,016,477,578 of bonds guaranteed under the Guarantee Program and the capacity of the Guarantee Program was $75,513,607,551 based on the three times cost value multiplier approved by the SBOE on May 21, 2010. Such capacity figures include the Reserve Capacity.

DISCUSSION AND ANALYSIS PERTAINING TO FISCAL YEAR ENDED AUGUST 31, 2012

The following discussion is derived from the Annual Report for the year ended August 31, 2012, including the Message of the Executive Administrator of the Fund and the Management's Discussion and Analysis contained therein. Reference is made to the Annual Report, when filed, for the complete Message and MD&A. Investment assets managed by the fifteen member SBOE are referred to throughout this MD&A as the PSF(SBOE) assets. As of August 31, 2012, the Fund's land, mineral rights and certain real assets are managed by the three-member SLB and these assets are referred to throughout as the PSF(SLB) assets. The 2012 Asset Allocation Policy includes an allocation for real estate investments, and as such investments are made, and become a part of the PSF investment portfolio, those investments will be managed by the SBOE and not the SLB.

At the end of fiscal 2012, the total Fund balance was $28.8 billion. Fund balance increased $1.86 billion from the prior year primarily attributable to the increase in the fair value of the PSF(SBOE) equities and alternative investments, the (PSF(SLB) real assets investments and the recovering markets. During the year, the SBOE continued implementing its revised long term strategic asset allocation to diversify and strengthen the PSF(SBOE) investment assets of the Fund. The revised allocation is projected to increase returns over the long run while reducing risk and return volatility of the portfolio. The one year, three year, five year and ten year annualized total returns for the PSF(SBOE) assets were 9.45%, 10.17%, 2.80% and 7.30% respectively (total return takes into consideration the change in the market value of the Fund during the year as well as the interest and dividend income generated by the Fund's investments). In addition, the SLB continued its shift into externally managed real asset investment funds and the one year, three year, and five year annualized total returns for the PSF(SLB) real assets, including cash, are 12.20%, 6.08%, and 1.25% respectively.

The market value of the Fund's assets is directly impacted by the performance of the various financial markets in which the assets are invested. The most important factors affecting investment performance are the asset allocation decisions made by the SBOE and SLB. The current SBOE long term asset allocation policy allows for diversification of the PSF(SBOE) portfolio into alternative asset classes whose returns are not as correlated to traditional asset classes. The implementation of the long term asset allocation will occur over several fiscal years and is expected to provide incremental total return at reduced risk. As of August 31, 2012, the PSF(SBOE) portion of the Fund had diversified into emerging market large cap international equities, absolute return funds, real estate, private equity, risk parity and real return Treasury Inflation-Protected Securities. Other asset classes such as real return commodities, emerging market debt and emerging international equities securities will be strategically added commensurate with the economic environment and the goals and objectives of the SBOE. As of August 31, 2012, the SBOE had approved and the PSF(SBOE) made capital commitments to externally managed real estate funds in the amount of $926.4 million and capital commitments to two private equity limited partnerships in the total amount of $1.3 billion. Unfunded commitments at August 31, 2012, were $344.4 million in real estate and $878.99 billion in private equity.

The PSF(SLB) portfolio is generally characterized by three broad categories: (1) discretionary real assets investments, (2) sovereign and other lands, and (3) mineral interests. Discretionary real assets investments consist of externally managed real

estate, infrastructure, and energy/minerals investment funds; internally managed direct real estate investments, and cash. Sovereign and other lands consist primarily of the lands set aside to the PSF when it was created. Mineral interests consist of all of the minerals that are associated with PSF lands. The investment focus of PSF(SLB) discretionary real assets investments has shifted from internally managed direct real estate investments to externally managed real assets investment funds. The PSF(SLB) makes investments in certain limited partnerships that legally commit it to possible future capital contributions. At August 31, 2012, the remaining commitments totaled
approximately $761.

The PSF(SBOE)'s investment in equity securities experienced a return of 11.29% during the fiscal year ended August 31, 2012. The PSF(SBOE)'s investment in fixed income securities produced a return of 6.57% during the fiscal year and absolute return investments yielded a return of 3.69%. The PSF(SBOE) real estate and private equity investments returned 7.38% and 5.43%, respectively. Risk parity assets produced a return of 13.11%, while real return assets yielded 8.49%. Combined, all PSF(SBOE) asset classes produced an investment return of 9.44% for the fiscal year ended August 31, 2012, outperforming the target index by approximately 57 basis points. All PSF(SLB) real assets (including cash) returned 12.20% for the fiscal year ending August 31, 2012.

For fiscal year 2012, total revenues, inclusive of unrealized gains and losses and net of security lending rebates and fees, totaled $2.95 billion, a decrease of $782.1 million from fiscal year 2011 earnings of $3.73 billion. This decrease reflects the performance of the securities markets in which the Fund was invested in fiscal year 2012 In fiscal year 2012, revenues earned by the Fund included lease payments, bonuses and royalty income received from oil, gas and mineral leases; lease payments from commercial real estate; surface lease and easement revenues; revenues from the resale of natural and liquid gas supplies; dividends, interest, and securities lending revenues; the net change in the fair value of the investment portfolio; and, other miscellaneous fees and income.

Expenditures are paid from the Fund before distributions are made under the total return formula. Such expenditures include the costs incurred by the SLB to manage the land endowment, as well as operational costs of the Fund, including external management fees paid from appropriated funds. Total operating expenditures, net of security lending rebates and fees, decreased 6.6% for the fiscal year ending August 31, 2012. This decrease is primarily attributable to the decrease in the costs of gas supplies purchased for resale under the State Energy Marketing Program.

The Fund supports the public school system in the State by distributing a predetermined percentage of its asset value to the ASF. For fiscal years 2011 and 2012, this distribution to the ASF totaled $1.093 billion and $1.021 billion, respectively.

At the end of the 2012 fiscal year, PSF assets guaranteed $53.634 billion in bonds issued by 800 local school districts. Since its inception in 1983, the Fund has guaranteed 4,587 school district bond issues totaling $103.4 billion in principal amount. During the 2012 fiscal year, the number of outstanding issues guaranteed under the Guarantee Program increased by 98, or 3.9%. The dollar amount of guaranteed school bond issues outstanding increased by $980.6 million or 1.9%. The guarantee capacity of the Fund increased by $1.125 billion, or 1.5%, during fiscal year 2012 due to the investment performance of the Fund.

2011 CONSTITUTIONAL AMENDMENT

During the Regular Session of the 82nd Legislature, which concluded May 30, 2011, a joint resolution ("HJR 109") was enacted proposing amendments to various sections of the Texas Constitution that pertain to the PSF. In accordance with HJR 109, a referendum was held in the State on November 8, 2011. At that referendum, voters of State approved non-substantive changes to the Texas Constitution to clarify references to the Fund, and, in addition, approved an amendment that effects an increase to the base amount used in calculating the Distribution Rate from the Fund to the ASF. The amendments approved at the referendum include an increase to the base used to calculate the Distribution Rate by adding to the calculation base certain discretionary real assets and cash in the Fund that is managed by entities other than the SBOE (at present, by the SLB). The value of those assets were already included in the value of the Fund for purposes of the Guarantee Program, but prior to the amendment had not been included in the calculation base for purposes of making transfers from the Fund to the ASF. While the amendment provides for an increase in the base for the calculation of approximately $2 billion, no new resources were provided for deposit to the Fund. As described under "The Total Return Constitutional Amendment" the SBOE is prevented from approving a Distribution Rate or making a pay out from the Fund if the amount distributed would exceed 6% of the average of the market value of the Fund, excluding real property in the Fund, but including discretionary real asset investments on the last day of each of the sixteen State fiscal quarters preceding the Regular Session of the Legislature that begins before that State fiscal biennium or if such pay out would exceed the Ten Year Total Return. The new calculation base is required to be used to determine all payments to the ASF from the Fund beginning with the 2012-13 biennium. As described under "The Total Return Constitutional Amendment" the SBOE approved a Distribution Rate of 4.2% in January 2011 based on a commitment of the SLB to transfer $500 million to the PSF during the biennium. In November 2012, the SBOE established a 3.3% Distribution Rate for the 2014-15 biennium.

The constitutional amendments approved on November 8, 2011 also provides authority to the GLO or other entity other than the SBOE that has responsibility for the management of land or other properties of the Fund to determine in its sole discretion whether to transfer each year from Fund assets to the ASF revenue derived from such land or properties, an amount not to exceed

$300 million. Any amount transferred to the ASF by an entity other than the SBOE is excluded from the 6% Distribution Rate limitation applicable to SBOE transfers.

The impact of the increase in the base against which the Distribution Rate is applied will be an increase in the distributions from the PSF to the ASF, provided that there are no reductions in the percentage established biennially by the SBOE to be the Distribution Rate. For the 2012-13 biennium, the Distribution Rate has been set by the SBOE at 4.2%. Given the increase in the calculation base effected by the November 8, 2011 constitutional amendment, the effect on transfers made by the SBOE in 2012-13 will be an increase in the total return distribution by an estimated $73.7 million in each year of the biennium. Going forward, it may be necessary for the SBOE to reduce the Distribution Rate in order to preserve the corpus of the Fund in accordance with its management objective of preserving intergenerational equity, and the Distribution Rate for the 2014-15 biennium has been reduced to 3.3%, as described above. If the SBOE were to maintain a Distribution Rate in future years at the level set for 2012-13, prior to the enactment of the 2011 constitutional amendment, as the value of the real assets investments increase annually, distributions to the ASF would increase in the out years. The increased amounts distributed from the Fund will be a loss to either the investment corpus of the PSF managed by SBOE or, should the SLB increase its transfers to the SBOE to cover this share of the distribution, to the assets managed by the SLB. In addition, the changes made by the amendment will reduce the compounding interest in the Fund that would be derived from these assets remaining in the corpus of the Fund. Other factors that may affect the corpus of the Fund that are associated with this change include the decisions that are made by the SLB or others that are or may in the future be authorized to make transfers of funds from the PSF to the ASF. While the SBOE has oversight of the Guarantee Program, it will not have the decision making power with respect to all transfers to the ASF, as it has had in the past, which could adversely affect the ability of the SBOE to optimally manage its portion of the PSF assets.

OTHER 2011 LEGISLATIVE ACTIONS – CHARTER SCHOOL GUARANTEE PROGRAM

During the First Called Session of the 82nd Texas Legislature, which ended June 29, 2011, Senate Bill 1 ("SB 1") was enacted. Among other provisions, SB 1 authorizes the use of the PSF to guarantee revenue bonds issued by certain open-enrollment charter schools that are designated as "charter districts" by the Commissioner. The program authorized by SB 1 is referred to herein as the "Charter School Guarantee Program." It is anticipated that the Charter School Guarantee Program will not become effective until certain contingent requirements are satisfied, including the establishment of regulations by the Commissioner for the administration of the program. It is also expected that the new program will not be implemented until the SBOE has received a response from the IRS with respect to certain federal tax law matters concerning the Charter School Guarantee Program that have been submitted to the IRS for review. As a result, the date of implementation and the ultimate structure of the Charter School Guarantee Program are presently unknown, although the program could be implemented in calendar year 2013.

In general, the Charter School Guarantee Program has been authorized through the enactment of amendments to the Act. As amended, the Act provides that a qualified charter district may make application to the Commissioner under the Act for a guarantee of its bonds, including refunding bonds, by the PSF. The capacity of the Charter School Guarantee Program is limited to the total amount that equals the result of the percentage that is equal to the ratio of the number of students enrolled in open-enrollment charter schools in the State compared to the total number of students enrolled in all public schools in the State multiplied by the combined capacities of the Guarantee Program and Charter School Guarantee Program. As of March 1, 2012 (the most recent date for which data is available), the percentage of students enrolled in open-enrollment charter schools to the total State scholastic census was approximately 3.09%. For the capacity of the Guarantee Program, see "Capacity Limits for the Guarantee Program."

The amendments to the Act further provide that the Commissioner may not approve charter district bonds for guarantee if such guarantees will result in lower bond ratings for public school district bonds that are guaranteed under the Guarantee Program. To be eligible for a guarantee, the Act provides that a charter district's bonds must be approved by the Attorney General, rated without the guarantee as investment grade by a nationally recognized investment rating firm, and satisfy an investigation conducted by the TEA as to the charter district's accreditation.

The amendments to the Act further provide for the establishment of a reserve fund in the State treasury. Each charter district that has a bond guaranteed must annually remit to the Commissioner, for deposit in the charter district bond guarantee reserve fund, an amount equal to 10% (or such higher amount as may be determined by the Commissioner) of the savings to the charter district that result from the lower interest rate on the bond due to the guarantee by the PSF.

The Act provides that immediately following receipt of notice that a charter district will be or is unable to pay maturing or matured principal or interest on a guaranteed bond, the Commissioner is required to instruct the transfer from the charter district bond guarantee reserve fund to the district's paying agent an amount necessary to pay the maturing or matured principal or interest. If money in the charter district bond guarantee reserve fund is insufficient to pay the amount due on a bond for which a notice of default has been received, the Commissioner shall instruct the transfer from the PSF to the district's paying agent the amount necessary to pay the balance of the unpaid maturing or matured principal or interest. If a total of two or more payments are made under the Charter School Guarantee Program on charter district bonds and the Commissioner determines that the charter district is acting in bad faith under the program, the Commissioner may request the Attorney General to institute appropriate legal action to compel the charter district and its officers, agents, and employees to comply with the duties required of them by law in regard to the guaranteed bonds.

OTHER EVENTS AND DISCLOSURES

The State Investment Ethics Code governs the ethics and disclosure requirements for financial advisors and other service providers who advise certain State governmental entities, including the PSF. In accordance with the provisions of the State Investment Ethics Code, the SBOE periodically modifies its code of ethics, which occurred most recently in May 2010. The SBOE code of ethics includes prohibitions on sharing confidential information, avoiding conflict of interests and requiring disclosure filings with respect to contributions made or received in connection with the operation or management of the Fund. The code of ethics applies to members of the SBOE as well as to persons who are responsible by contract or by virtue of being a TEA PSF staff member for managing, investing, executing brokerage transactions, providing consultant services, or acting as a custodian of the PSF, and persons who provide investment and management advice to a member of the SBOE, with or without compensation under certain circumstances. The code of ethics is codified in the Texas Administrative Code at 19 TAC sections 33.5 et seq., and is available on the TEA web site at www.tea.state.tx.us/rules/tac/chapter033/index.html.

Since 2007, TEA has made supplemental appropriation requests to the Legislature for the purpose of funding the implementation of the 2008 Asset Allocation Policy, but those requests have been denied or partly funded. In the 2011 legislative session, the Legislature approved an increase of 31 positions in the full-time equivalent employees for the administration of the Fund, which was funded as part of an $18 million appropriation for each year of the 2012-13 biennium, in addition to the operational appropriation of $11 million for each year of the biennium. The TEA has begun increasing the PSF administrative staff in accordance with the 2011 legislative appropriation.

As of August 31, 2012, certain lawsuits were pending against the State and/or the GLO, which challenge the Fund's title to certain real property and/or past or future mineral income from that property, and other litigation arising in the normal course of the investment activities of the PSF. Reference is made to the Annual Report, when filed, for a description of such lawsuits that are pending, which may represent contingent liabilities of the Fund.

The SBOE is a named defendant in litigation described in the Official Statement pertaining to the Bonds that has been filed in State District Court that has challenged the constitutionality of the Texas public school finance system, and which, among other relief requested, seeks an injunction to prohibit the State and its officials from distributing any funds under the current finance system until a constitutional system is created. The TEA does not anticipate that the security for payment of the Bonds, including the PSF guarantee of school district bonds, would be adversely affected by such litigation.

PSF CONTINUING DISCLOSURE UNDERTAKING

The SBOE has adopted an investment policy rule (the "TEA Rule") pertaining to the PSF and the Guarantee Program. The TEA Rule is codified in Section I of the TEA Investment Procedure Manual, which relates to the Guarantee Program. The most recent amendment to the TEA Rule was adopted by the SBOE on November 19, 2010, and is summarized below. Through the adoption of the TEA Rule and its commitment to guarantee the Bonds, the SBOE has made the following agreement for the benefit of the District and holders and beneficial owners of the Bonds. The TEA (or its successor with respect to the management of the Guarantee Program) is required to observe the agreement for so long as it remains an "obligated person," within the meaning of Rule 15c2-12, with respect to the Bonds. Nothing in the TEA Rule obligates the Agency to make any filings or disclosures with respect to guaranteed bonds, as the obligations of the Agency under the TEA Rule pertain solely to the Guarantee Program. The district issuing the guaranteed bonds has assumed the applicable obligation under Rule 15c-12 to make all disclosures and filings relating directly to guaranteed bonds, and the TEA takes no responsibility with respect to such district undertakings. Under the TEA agreement, the TEA will be obligated to provide annually certain updated financial information and operating data, and timely notice of specified material events, to the MSRB.

The MSRB has established the Electronic Municipal Market Access ("EMMA") system, and the TEA is required to file its continuing disclosure information using the EMMA system. Investors may access continuing disclosure information filed with the MSRB at www.emma.msrb.org.

ANNUAL REPORTS

The TEA will annually 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 Guarantee Program and the PSF of the general type included in this Official Statement under the heading "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM." The information also includes the Annual Report. The TEA will update and provide this information within six months after the end of each fiscal year.

The TEA may provide updated information in full text or may incorporate by reference certain other publicly-available documents, as permitted by Rule 15c2-12. The updated information includes audited financial statements of, or relating to, the

State or the PSF, when and if such audits are commissioned and available. Financial statements of the State will be prepared in accordance with generally accepted accounting principles as applied to state governments, as such principles may be changed from time to time, or such other accounting principles as the State Auditor is required to employ from time to time pursuant to State law or regulation. The financial statements of the Fund were prepared to conform to U.S. Generally Accepted Accounting Principles as established by the Governmental Accounting Standards Board.

The Fund is reported by the State of Texas as a permanent fund and accounted for on a current financial resources measurement focus and the modified accrual basis of accounting. Measurement focus refers to the definition of the resource flows measured. Under the modified accrual basis of accounting, all revenues reported are recognized based on the criteria of availability and measurability. Assets are defined as available if they are in the form of cash or can be converted into cash within 60 days to be usable for payment of current liabilities. Amounts are defined as measurable if they can be estimated or otherwise determined. Expenditures are recognized when the related fund liability is incurred.

The State's current fiscal year end is August 31. Accordingly, the TEA must provide updated information by the last day of February in each year, unless the State changes its fiscal year. If the State changes its fiscal year, the TEA will notify the MSRB of the change.

MATERIAL EVENT NOTICES

The TEA will also provide timely notices of certain events to the MSRB. Such notices will be provided not more than ten business days after the occurrence of the event. The TEA will provide notice of any of the following events with respect to the Guarantee Program: (1) principal and interest payment delinquencies; (2) non-payment related defaults, if such event is material within the meaning of the federal securities laws; (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 IRS 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 Guarantee Program, or other material events affecting the tax status of the Guarantee Program; (7) modifications to rights of holders of Bonds guaranteed by the Guarantee Program, if such event is material within the meaning of the federal securities laws; (8) Bond calls, if such event is material within the meaning of the federal securities laws, and tender offers; (9) defeasances; (10) release, substitution, or sale of property securing repayment of Bonds guaranteed by the Guarantee Program, if such event is material within the meaning of the federal securities laws; (11) rating changes; (12) bankruptcy, insolvency, receivership, or similar event of the Guarantee Program (which is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent, or similar officer for the Guarantee Program 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 Guarantee Program, 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 Guarantee Program); (13) the consummation of a merger, consolidation, or acquisition involving the Guarantee Program 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) the appointment of a successor or additional trustee with respect to the Guarantee Program or the change of name of a trustee, if such event is material within the meaning of the federal securities laws. (Neither the Act nor any other law, regulation or instrument pertaining to the Guarantee Program make any provision with respect to the Guarantee Program for bond calls, debt service reserves, credit enhancement, liquidity enhancement, early redemption or the appointment of a trustee with respect to the Guarantee Program.) In addition, the TEA will provide timely notice of any failure by the TEA to provide information, data, or financial statements in accordance with its agreement described above under "Annual Reports."

AVAILABILITY OF INFORMATION

The TEA has agreed to provide the foregoing information only to the MSRB and to transmit such information electronically to the MSRB in such format and accompanied by such identifying information as prescribed by the MSRB. The information is available from the MSRB to the public without charge at www.emma.msrb.org.

LIMITATIONS AND AMENDMENTS

The TEA has agreed to update information and to provide notices of material events only as described above. The TEA 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 TEA makes no representation or warranty concerning such information or concerning its usefulness to a decision to invest in or sell Bonds at any future date. The TEA 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 Bonds may seek a writ of mandamus to compel the TEA to comply with its agreement.

The continuing disclosure agreement of the TEA is made only with respect to the PSF and the Guarantee Program. The District may make a continuing disclosure undertaking in accordance with Rule 15c2-12 with respect to its obligations arising under Rule 15c2-12 pertaining to financial and operating data concerning the District and notices of material events relating to the Bonds. A description of the District's undertaking, if any, is included elsewhere in the Official Statement relating to the Bonds.

This continuing disclosure agreement may be amended by the TEA 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 TEA, but only if (1) the provisions, as so amended, would have permitted an underwriter to purchase or sell guaranteed bonds in the primary offering of such bonds in compliance with Rule 15c2-12, taking into account any amendments or interpretations of Rule 15c2-12 since such offering as well as such changed circumstances and (2) either (a) the holders of a majority in aggregate principal amount of the outstanding bonds guaranteed by the Guarantee Program consent to such amendment or (b) a person that is unaffiliated with the TEA (such as nationally recognized bond counsel) determines that such amendment will not materially impair the interest of the holders and beneficial owners of the bonds guaranteed by the Guarantee Program. The TEA may also amend or repeal the provisions of its continuing disclosure agreement if the SEC amends or repeals the applicable provision of Rule 15c2-12 or a court of final jurisdiction enters judgment that such provisions of the Rule 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 bonds guaranteed by the Guarantee Program in the primary offering of such bonds.

COMPLIANCE WITH PRIOR UNDERTAKINGS

The TEA has not previously failed to substantially comply with its previous continuing disclosure agreements in accordance with Rule 15c2-12.

SEC EXEMPTIVE RELIEF

On February 9, 1996, the TEA received a letter from the Chief Counsel of the SEC that pertains to the availability of the "small issuer exemption" set forth in paragraph (d)(2) of Rule 15c2-12. The letter provides that Texas school districts which offer municipal securities that are guaranteed under the Guarantee Program may undertake to comply with the provisions of paragraph (d)(2) of Rule 15c2-12 if their offerings otherwise qualify for such exemption, notwithstanding the guarantee of the school district securities under the Guarantee Program. Among other requirements established by Rule 15c2-12, a school district offering may qualify for the small issuer exemption if, upon issuance of the proposed series of securities, the school district will have no more than $10 million of outstanding municipal securities.

STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS

LITIGATION RELATING TO THE TEXAS PUBLIC SCHOOL FINANCE SYSTEM

On April 9, 2001, four property wealthy districts filed suit in the 250th District Court of Travis County, Texas (the "District Court") against the Texas Education Agency, the Texas State Board of Education, the Texas Commissioner of Education (the "Commissioner") and the Texas Comptroller of Public Accounts in a case styled *West Orange-Cove Consolidated Independent School District, et al. v. Neeley, et al.* The plaintiffs alleged that the $1.50 maximum maintenance and operations ("M&O") tax rate had become in effect a state property tax, in violation of Article VIII, Section 1-e of the Texas Constitution, because it precluded them and other school districts from having meaningful discretion to tax at a lower rate. Forty school districts intervened alleging that the Texas public school finance system (the "Finance System") was inefficient, inadequate, and unsuitable, in violation of Article VII, Section 1 of the Texas Constitution, because the State of Texas (the "State") did not provide adequate funding. As described below, this case has twice reached the Texas Supreme Court (the "Supreme Court"), which rendered decisions in the case on May 29, 2003 ("West Orange-Cove I") and November 22, 2005 ("West Orange-Cove II"). After the remand by the Supreme Court back to the District Court in West Orange-Cove I, 285 other school districts were added as plaintiffs or intervenors. The plaintiffs joined the intervenors in their Article VII, Section 1 claims that the Finance System was inadequate and unsuitable, but not in their claims that the Finance System was inefficient.

On November 30, 2004, the final judgment of the District Court was released in connection with its reconsideration of the issues remanded to it by the Supreme Court in West Orange-Cove I. In that case, the District Court rendered judgment for the plaintiffs on all of their claims and for the intervenors on all but one of their claims, finding that (1) the Finance System was unconstitutional in that the Finance System violated Article VIII, Section 1-e of the Texas Constitution because the statutory limit of $1.50 per $100.00 of taxable assessed valuation on property taxes levied by school districts for maintenance and operation purposes had become both a floor and a ceiling, denying school districts meaningful discretion in setting their tax rates; (2) the constitutional mandate of adequacy set forth in Article VII, Section 1, of the Texas Constitution exceeded the maximum amount of funding available under the funding formulas administered by the State; and (3) the Finance System was financially inefficient, inadequate, and unsuitable in that it failed to provide sufficient access to revenue to provide for a general diffusion of knowledge as required by Article VII, Section 1, of the Texas Constitution.

The intervening school district groups contended that funding for school operations and facilities was inefficient in violation of Article VII, Section 1 of the Texas Constitution, because children in property-poor districts did not have substantially equal access to education revenue. All of the plaintiff and intervenor school districts asserted that the Finance System could not achieve "a general diffusion of knowledge" as required by Article VII, Section 1 of the Texas Constitution, because the Finance System was underfunded. The State, represented by the Texas Attorney General, made a number of arguments opposing the positions of the school districts, as well as asserting that school districts did not have standing to challenge the State in these matters.

In West Orange-Cove II, the Supreme Court's holding was twofold: (1) that the local M&O tax had become a state property tax in violation of Article VIII, Section 1-e of the Texas Constitution and (2) the deficiencies in the Finance System did not amount to a violation of Article VII, Section 1 of the Texas Constitution. In reaching its first holding, the Supreme Court relied on evidence presented in the District Court to conclude that school districts did not have meaningful discretion in levying the M&O tax. In reaching its second holding, the Supreme Court, using a test of arbitrariness determined that: the public education system was "adequate," since it is capable of accomplishing a general diffusion of knowledge; the Finance System was not "inefficient," because school districts have substantially equal access to similar revenues per pupil at similar levels of tax effort, and efficiency does not preclude supplementation of revenues with local funds by school districts; and the Finance System does not violate the constitutional requirement of "suitability," since the Finance System was suitable for adequately and efficiently providing a public education.

In reversing the District Court's holding that the Finance System was unconstitutional under Article VII, Section 1 of the Texas Constitution, the Supreme Court stated:

> Although the districts have offered evidence of deficiencies in the public school finance system, we conclude that those deficiencies do not amount to a violation of Article VII, Section 1. We remain convinced, however, as we were sixteen years ago, that defects in the structure of the public school finance system expose the system to constitutional challenge. Pouring more money into the system may forestall those challenges, but only for a time. They will repeat until the system is overhauled.

In response to the intervenor districts' contention that the Finance System was constitutionally inefficient, the West Orange-Cove II decision states that the Texas Constitution does not prevent the Finance System from being structured in a manner that results in gaps between the amount of funding per student that is available to the richest districts as compared to the poorest district, but reiterated its statements in *Edgewood Independent School District v. Meno,* 917 S.W.2d 717 (Tex. 1995) ("Edgewood IV") that such funding variances may not be unreasonable. The Supreme Court further stated that "the standards of Article VII, Section 1 - adequacy, efficiency, and suitability - do not dictate a particular structure that a system of free public schools must have." The Supreme Court also noted that "efficiency requires only substantially equal access to revenue for facilities necessary for an adequate system," and the Supreme Court agreed with arguments put forth by the State that the plaintiffs had failed to present sufficient evidence to prove that there was an inability to provide for a "general diffusion of knowledge" without additional facilities.

FUNDING CHANGES IN RESPONSE TO WEST ORANGE-COVE II

In response to the decision in West Orange-Cove II, the Texas Legislature (the "Legislature") enacted House Bill 1 ("HB 1"), which made substantive changes in the way the Finance System is funded, as well as other legislation which, among other things, established a special fund in the State treasury to be used to collect new tax revenues that are dedicated under certain conditions for appropriation by the Legislature to reduce M&O tax rates, broadened the State business franchise tax, modified the procedures for assessing the State motor vehicle sales and use tax and increased the State tax on tobacco products (HB 1 and other described legislation are collectively referred to herein as the "Reform Legislation"). The Reform Legislation generally became effective at the beginning of the 2006–07 fiscal year of each district.

CURRENT LITIGATION RELATED TO THE TEXAS PUBLIC SCHOOL FINANCE SYSTEM

As described below, during 2011 and 2012, several lawsuits were filed in District Courts of Travis County, Texas, which alleged that the Finance System, as modified by legislation enacted by the Legislature since the decision in West Orange Cove II, and in particular, as modified by Senate Bill 1 in 2011 (see “CURRENT PUBLIC SCHOOL FINANCE SYSTEM - 2011 Legislation”), has resulted in a funding system that violates principles established in West Orange Cove I and West Orange Cove II, and prior decisions of the Supreme Court relating to the constitutionality of the Finance System, and several provisions of the Texas Constitution. In general, each suit presented the legal perspectives and arguments of the different coalitions of school districts represented, but as a general matter, each group challenged the adequacy of funding provided by the Legislature for the Finance System, and the plaintiffs in each suit sought to have an injunction issued to the State and its officials to prevent the distribution of any funds under the current Finance System until a constitutional system is created and sought a declaration that changes in funding for the Finance System since the enactment of HB 1 have effectively converted the local M&O tax into a State property tax in violation of the Texas Constitution. The defendants in the suits include State officials and the State Board of Education (the “State Defendants”). The first suit was filed on October 10, 2011, styled “*The Texas Taxpayer & Student Fairness Coalition*, *et al. vs. Robert Scott, Commissioner of Education et al.*" A second suit was filed on December 9, 2011, styled "*Calhoun County Independent School District, et al. v Robert Scott, Commissioner of Education, et al.*" A third suit was filed on December 13, 2011, styled "*Edgewood Independent School District, et al. v. Robert Scott, Commissioner of Education, et al.*" A fourth suit was filed on December 23, 2011, styled "*Fort Bend Independent School District, et al. v. Robert Scott, Commissioner of Education, et al.*" (the "Fort Bend Suit"). The State Defendants filed an answer with respect to the each of the first four suits filed, denying the plaintiff's allegations, and all of such suits were assigned to the 250th District Court of Travis County. On February 24, 2012 a plea of intervention to the Fort Bend Suit was filed by seven parents and a group named "*Texans for Real Efficiency and Equity in Education.*" The intervenors asserted that the Finance System is qualitatively inefficient, and that the Finance System is unconstitutional, in part based on arguments made by other plaintiffs. A fifth suit was filed on June 26, 2012 by individuals and the Texas Charter School Association, styled "*Flores, et al. v. Robert Scott, Commissioner of Education, et al.*" (the "Charter School Suit"). The petition for the Charter School Suit agreed with the arguments of the school districts in the first four suits filed that the Finance System is unconstitutional and also sought to have an injunction issued against the State Defendants in the same manner as the first four suits. The Charter School Suit added additional grounds that relate to the circumstances of charter schools as a basis for holding the Finance System unconstitutional, including that charter schools receive no funding for facilities and that the statutory cap on charter schools is unconstitutionally arbitrary. The State Defendants also filed a general denial in the Charter School Suit.

All five suits were consolidated by the 250th District Court of Travis County (the "District Court"), and the trial commenced on October 22, 2012. On February 4, 2013, the District Court rendered a preliminary ruling generally as follows: (i) the Finance System is inefficient "in that it fails to provide substantially equal access to revenues necessary to provide a general diffusion of knowledge;" (ii) the Finance System is not "adequately funded" and arbitrarily funds districts at different levels below the amount required to provide for a general diffusion of knowledge; (iii) the Finance System has created a Statewide property tax in violation of the Texas Constitution because districts lack "meaningful discretion" in setting their tax rates, as exemplified by the ruling that low property wealth districts are forced to tax at or near the maximum M&O tax rate of $1.17 to meet State education standards and other districts cannot lower their M&O tax rate without compromising their ability to meet State education standards nor can they raise their M&O tax rate because they are either legally or practically unable to do so.

In the preliminary ruling, the District Court did not grant nor address the injunctive relief sought by any of the plaintiffs, and the Court declined any relief to Texans for Real Efficiency and Equity in Education, who had argued that greater competition could result in a more efficient public school finance system. In response to arguments on behalf of the State's charter schools, the District Court held that it is within the discretion of the Legislature, and not unconstitutional, to fund charter schools differently from other public schools.

The February 4, 2013 ruling of the District Court is preliminary, and the District Court indicated that it would be four to six weeks before the ruling is finalized by an omnibus order of the District Court containing findings of fact and conclusions of law. The District Court's ruling is qualified for direct appeal to the Texas Supreme Court, and commentary by the Texas Education Commissioner shortly after the District Court's ruling was released on February 4, 2013 suggested that the State Defendants will appeal the final District Court order directly to the Texas Supreme Court.

If any of the Constitutional findings in the District Court's ruling are upheld after exhausting all appeals, it is the responsibility of the Legislature to modify the Finance System in accordance with court findings. The Legislature meets in regular session for a 140-day period every two years, and the Legislature is currently in a regular session, which is scheduled to conclude May 27, 2013; therefore it may be necessary for the Texas Governor to call a special legislative session if a final appeal of the District Court's ruling is not complete by end of the current regular session, and such appeal requires legislative action.

The District can make no representations or predictions concerning the effect this litigation or the current ruling by the District Court, and any appeals, may have on the District's financial condition, revenues or operations. See "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS – Possible Effects of Litigation and Changes in Law on District Bonds."

POSSIBLE EFFECTS OF LITIGATION AND CHANGES IN LAW ON DISTRICT BONDS

The Reform Legislation and the changes made by the State Legislature to the Reform Legislation since its enactment did not alter the provisions of Chapter 45, Texas Education Code, that authorize districts to secure their bonds by pledging the receipts of an unlimited ad valorem debt service tax as security for payment of such bonds (including the Bonds). Reference is made, in particular, to the information under the heading "THE BONDS - Security and Source of Payment".

In the future, the Legislature could enact additional changes to the Finance System which could benefit or be a detriment to a school district depending upon a variety of factors, including the financial strategies that the district has implemented in light of past State funding systems. Among other possibilities, a district's boundaries could be redrawn, taxing powers restricted, State funding reallocated, or local ad valorem taxes replaced with State funding subject to biennial appropriation. In Edgewood IV, the Supreme Court stated that any future determination of unconstitutionality "would not, however, affect the district's authority to levy the taxes necessary to retire previously issued bonds, but would instead require the Legislature to cure the system's unconstitutionality in a way that is consistent with the Contract Clauses of the U.S. and Texas Constitutions" (collectively, the

"Contract Clauses"). Consistent with the Contract Clauses, in the exercise of its police powers, the State may make such modifications in the terms and conditions of contractual covenants related to the payment of the Bonds as are reasonable and necessary for the attainment of important public purposes.

Although, as a matter of law, the Bonds, upon issuance and delivery, will be entitled to the protections afforded previously existing contractual obligations under the Contract Clauses, the District can make no representations or predictions concerning the effect of future legislation or litigation, or how such legislation or future court orders may affect the District's financial condition, revenues or operations. While the disposition of any possible future litigation or the enactment of future legislation to address school funding in Texas could substantially adversely affect the financial condition, revenues or operations of the District, as noted herein, the District does not anticipate that the security for payment of the Bonds, specifically, the District's obligation to levy an unlimited debt service tax and the Permanent School Fund guarantee of the Bonds would be adversely affected by any such litigation or legislation. See "CURRENT PUBLIC SCHOOL FINANCE SYSTEM."

CURRENT PUBLIC SCHOOL FINANCE SYSTEM

OVERVIEW

The following description of the Finance System is a summary of the Reform Legislation and the changes made by the State Legislature to the Reform Legislation since its enactment, including modifications made during the regular through third called sessions of the 79th Texas Legislature (collectively, the "2006 Legislative Session"), the regular session of the 81st Texas Legislature (the "2009 Legislative Session") and the regular and first called sessions of the 82nd Texas Legislature (collectively, the "2011 Legislative Session"). For a more complete description of school finance and fiscal management in the State, reference is made to Vernon's Texas Codes Annotated, Education Code, Chapters 41 through 46, as amended.

Funding for school districts in the State is provided primarily from State and local sources. State funding for all school districts is provided through a set of funding formulas comprising the "Foundation School Program," as well as two facilities financing programs. Generally, the Finance System is designed to promote wealth equalization among school districts by balancing State and local sources of funds available to school districts. In particular, because districts with relatively high levels of property wealth per student can raise more local funding, such districts receive less State aid, and in some cases, are required to disburse local funds to equalize their overall funding relative to other school districts. Conversely, because districts with relatively low levels of property wealth per student have limited access to local funding, the Finance System is designed to provide more State funding to such districts. Thus, as a school district's property wealth per student increases, State funding to the school district is reduced. As a school district's property wealth per student declines, the Finance System is designed to increase its State funding. A similar equalization system exists for facilities funding wherein districts with the same tax rate for debt service raise the same amount of combined State and local funding. Facilities funding for debt incurred in prior years is expected to continue in future years; however, State funding for new school facilities was not appropriated by the 82nd Texas Legislature for the 2012–13 fiscal biennium.

Local funding is derived from collections of ad valorem taxes levied on property located within each district's boundaries. School districts are authorized to levy two types of property taxes: a limited M&O tax to pay current expenses and an unlimited interest and sinking fund ("I&S") tax to pay debt service on bonds. Under current law, M&O tax rates are subject to a statutory maximum rate of $1.17 per $100 of taxable value for most school districts. Current law also requires school districts to demonstrate their ability to pay debt service on outstanding indebtedness through the levy of an ad valorem tax at a rate of not to exceed $0.50 per $100 of taxable property at the time bonds are issued. Once bonds are issued, however, districts may levy a tax to pay debt service on such bonds unlimited as to rate or amount (see "TAX INFORMATION – Tax Rate Limitations" herein). As noted above, because property values vary widely among school districts, the amount of local funding generated by the same tax rate is also subject to wide variation among school districts.

The Reform Legislation, which generally became effective at the beginning of the 2006–07 fiscal year of each school district in the State, made substantive changes to the Finance System, which are summarized below. While each school district's funding entitlement was calculated based on the same formulas that were used prior to the 2006–07 fiscal year, the Reform Legislation effected changes to the manner in which school districts are funded that were intended to reduce local M&O tax rates by one-third over two years through the introduction of the "State Compression Percentage," with M&O tax levies declining by approximately 11% in fiscal year 2006–07 and approximately another 22% in fiscal year 2007–08. (Prior to the Reform Legislation, the maximum M&O tax rate for most school districts was $1.50 per $100 of taxable assessed valuation.) Subject to local referenda, a district may increase its local M&O tax levy up to $0.17 above the district's compressed tax rate. Based on the current State Compression Percentage, the maximum M&O tax rate is $1.17 per $100 of taxable value for most school districts (see "TAX INFORMATION – Tax Rate Limitations" herein).

LOCAL FUNDING FOR SCHOOL DISTRICTS

The primary source of local funding for school districts is collections from ad valorem taxes levied against the taxable property located in each school district. As noted above, prior to the Reform Legislation, the maximum M&O tax rate for most school districts was generally limited to $1.50 per $100 of taxable value, and the majority of school districts were levying an M&O tax rate of $1.50 per $100 of taxable value at the time the Reform Legislation was enacted. The Reform Legislation required each school district to "compress" its tax rate by an amount equal to the "State Compression Percentage." For fiscal years 2007–08 through 2012–13, the State Compression Percentage has been set at 66.67%, effectively setting the maximum compressed M&O tax rate for most school districts at $1.00 per $100 of taxable value. The State Compression Percentage is set by legislative appropriation for each State fiscal biennium or, in the absence of legislative appropriation, by the Commissioner. School districts are permitted, however, to generate additional local funds by raising their M&O tax rate by $0.04 above the compressed tax rate without voter approval (for most districts, up to $1.04 per $100 of taxable value). In addition, if the voters approve the tax rate increase, districts may, in general, increase their M&O tax rate by an additional two or more cents and receive State equalization funds for such taxing effort up to a maximum M&O tax rate of $1.17 per $100 of taxable value (see "TAX INFORMATION – Public Hearing and Rollback Tax Rate" herein). Elections held in certain school districts under older laws, however, may subject M&O tax rates in such districts to other limitations (See "TAX INFORMATION – Tax Rate Limitations" herein).

STATE FUNDING FOR SCHOOL DISTRICTS

State funding for school districts is provided through the Foundation School Program, which provides each school district with a minimum level of funding (a "Basic Allotment") for each student in average daily attendance ("ADA"). The Basic Allotment is calculated for each school district using various weights and adjustments. This basic level of funding is referred to as "Tier One" of the Foundation School Program. The basic level of funding is then "enriched" with additional funds known as "Tier Two" of the Foundation School Program. Tier Two provides a guaranteed level of funding for each cent of local tax effort that exceeds the compressed tax rate (for most districts, M&O tax rates above $1.00 per $100 of taxable value). The Finance System also provides an Existing Debt Allotment ("EDA") to subsidize debt service on eligible outstanding school district bonds and an Instructional Facilities Allotment ("IFA") to subsidize debt service on newly issued bonds. IFA primarily addresses the debt service needs of property-poor school districts. A New Instructional Facilities Allotment ("NIFA") also is available to help pay operational expenses associated with the opening of a new instructional facility. Future-year IFA and NIFA awards, however, were not funded by the Legislature for the 2012–13 fiscal biennium, although funding awards for IFA made in prior years will continue to be funded (but not the second year for NIFA for the 2012–13 fiscal biennium for districts that first became eligible for NIFA in the 2010–11 fiscal year).

Tier One and Tier Two allotments represent the State's share of the cost of M&O expenses of school districts, with local M&O taxes representing the district's local share. EDA and IFA allotments supplement a school district's local I&S taxes levied for debt service on eligible bonds issued to construct, acquire and improve facilities. Tier One and Tier Two allotments and existing EDA and IFA allotments are generally required to be funded each year by the Legislature. Since future-year IFA awards were not funded by the Legislature for the 2012–13 fiscal biennium, and debt service assistance on school district bonds that are not yet eligible for EDA is not available, debt service on new bonds issued by districts to construct, acquire and improve facilities must be funded solely from local I&S taxes. State funding allotments may be adjusted in certain circumstances to account for shortages in State appropriations or to allocate available funds in accordance with wealth equalization goals.

Tier One allotments are intended to provide all districts a basic level of education necessary to meet applicable legal standards. Tier Two allotments are intended to guarantee each school district that is not subject to the wealth transfer provisions described below an opportunity to supplement that basic program at a level of its own choice; however, Tier Two allotments may not be used for the payment of debt service or capital outlay.

The cost of the basic program is based on an allotment per student known as the "Basic Allotment". The Basic Allotment is adjusted for all districts by a cost adjustment factor intended to address competitive labor markets for teachers known as the "cost of education index." In addition, district-size adjustments are made for small- and mid-size districts. The cost of education index and district-size adjustments applied to the Basic Allotment, create what is referred to as the "Adjusted Allotment". The Adjusted Allotment is used to compute a "regular program allotment," as well as various other allotments associated with educating students with other specified educational needs. For fiscal year 2007–08, the Basic Allotment was $3,135, and for fiscal year 2008–09, the Basic Allotment was increased to $3,218. For a discussion of the Basic Allotment in fiscal years 2009–10 and beyond, see "2009 Legislation" below.

Tier Two currently provides two levels of enrichment with different guaranteed yields depending on the district's local tax effort. For the 2012–13 State fiscal biennium, the first six cents of tax effort that exceeds the compressed tax rate (for most districts, M&O tax rates ranging from $1.01 to $1.06 per $100 of taxable value) will, for most districts, generate a guaranteed yield of $59.97 per cent per weighted student in average daily attendance ("WADA"). The second level of Tier Two is generated by tax effort that exceeds the compressed tax rate plus six cents (for most districts eligible for this level of funding, M&O tax rates ranging from $1.07 to $1.17 per $100 of taxable value) and has a guaranteed yield per cent per WADA of $31.95. Property-wealthy school districts are subject to recapture at the equivalent wealth per student of $319,500 (see "Wealth Transfer Provisions" below). For school districts that adopted an M&O tax rate of $1.17 per $100 in taxable value for the 2010–11 fiscal year, the $31.95 guaranteed yield is increased to $33.95, but only for the 2011–12 fiscal year.

The IFA guarantees each awarded school district a specified amount per student (the "IFA Guaranteed Yield") in State and local funds for each cent of tax effort to pay the principal of and interest on eligible bonds issued to construct, acquire, renovate or improve instructional facilities. The guaranteed yield per cent of local tax effort per student in ADA has been $35 since this program first began. To receive an IFA award, a school district must apply to the Commissioner in accordance with rules adopted by the Commissioner before issuing the bonds to be paid with IFA state assistance. The total amount of debt service assistance over a biennium for which a district may be awarded is limited to the lesser of (1) the actual debt service payments made by the district in the biennium in which the bonds are issued; or (2) the greater of (a) $100,000 or (b) $250 multiplied by the number of students in ADA. The IFA is also available for lease-purchase agreements and refunding bonds meeting certain prescribed conditions. Once a district receives an IFA award for bonds, it is entitled to continue receiving State assistance for such bonds without reapplying to the Commissioner. The guaranteed level of State and local funds per student per cent of local tax effort applicable to the bonds may not be reduced below the level provided for the year in which the bonds were issued. For the 2012–13 State biennium, however, no funds are appropriated for new IFA awards, although all current obligations are funded through the biennium.

State financial assistance is provided for certain existing eligible debt issued by school districts (referred to herein as EDA). The EDA guaranteed yield (the "EDA Yield") is the same as the IFA Guaranteed Yield ($35 per cent of local tax effort per student in ADA), subject to adjustment as described below. For bonds that became eligible for EDA funding after August 31, 2001, and prior to August 31, 2005, EDA assistance was less than $35 in revenue per student for each cent of debt service tax, as a result of certain administrative delegations granted to the Commissioner under State law. Effective September 1, 2003, the portion of the local debt service rate that has qualified for EDA assistance is limited to the first 29 cents of debt service tax or a greater amount for any year provided by appropriation by the Legislature. In general, a district's bonds are eligible for EDA assistance if (i) the district made payments on the bonds during the final fiscal year of the preceding State fiscal biennium or (ii) the district levied taxes to pay the principal of and interest on the bonds for that fiscal year. Each biennia, access to EDA funding is determined by the debt service taxes collected in the final year of the preceding biennium. A district may not receive EDA funding for the principal and interest on a series of otherwise eligible bonds for which the district receives IFA funding.

Prior to the 2012–13 biennium, a district could also qualify for a NIFA allotment, which provided assistance to districts for operational expenses associated with opening new instructional facilities. As previously mentioned, this program was not funded for the 2012–13 State fiscal biennium.

2006 LEGISLATION

Since the enactment of the Reform Legislation in 2006, most school districts in the State have operated with a "target" funding level per student ("Target Revenue") that is based upon the "hold harmless" principles embodied in the Reform Legislation. This system of Target Revenue was superimposed on the Foundation School Program and made existing funding formulas substantially less important for most school districts. As noted above, the Reform Legislation was intended to lower M&O tax rates in order to give school districts "meaningful discretion" in setting their M&O tax rates, while holding school districts harmless by providing them with the same level of overall funding they received prior to the enactment of the Reform Legislation. Under the Target Revenue system, each school district is generally entitled to receive the same amount of revenue per student as it did in either the 2005–2006 or 2006–07 fiscal year (under existing laws prior to the enactment of the Reform Legislation), as long as the district adopted an M&O tax rate that was at least equal to its compressed rate. The reduction in local M&O taxes resulting from the mandatory compression of M&O tax rates under the Reform Legislation, by itself, would have significantly reduced the amount of local revenue available to fund the Finance System. To make up for this shortfall, the Reform Legislation authorized Additional State Aid for Tax Reduction ("ASATR") for each school district in an amount equal to the difference between the amount that each district would receive under the Foundation School Program and the amount of each district's Target Revenue funding level.

2009 LEGISLATION

During the 2009 Legislative Session, legislation was enacted that increased the Basic Allotment for the 2009–10 fiscal year from $3,218 to $4,765. In addition, each district's Target Revenue was increased by $120 per WADA. Target Revenue amounts were also adjusted to provide for mandatory employee pay raises and to account for changes in transportation and NIFA costs since the original Target Revenues were set. Overall, the Legislature allocated approximately $1.9 billion in new State aid for school districts.

2011 LEGISLATION

During the 2011 Legislative Session, the Legislature enacted a budget that cut $4 billion from the Foundation School Program for the 2012–13 State fiscal biennium, as compared to the funding level school districts were entitled to under the current formulas, including Target Revenue, and also cut approximately $1.3 billion in various grants (i.e., pre-kindergarten grant program, student success initiative, etc.) that were previously available. Such cuts were made in light of a projected State deficit of up to $27 billion for the 2012–13 State fiscal biennium. In order to reduce formula funding, a Regular Program Adjustment Factor ("RPAF") was applied to the formula that determines a district's regular program allotment. RPAF is multiplied by a school district's count of students in ADA (not counting the time a student spends in special education and career & technology education) and its Adjusted Allotment, which is the $4,765 Basic Allotment adjusted for the cost of education index and the small- and mid-sized district adjustments. The RPAF is set at 0.9239 for the 2011–12 fiscal year and 0.98 for the 2012–13 fiscal year. In order to balance these reductions across the two years for formula funded districts, such districts have the option to request that an RPAF value of 0.95195 be applied for both the 2011–12 and 2012–13 fiscal years. In order to be granted the request by the Commissioner, the district must demonstrate that using the 0.9239 RPAF will cause the district a financial hardship in 2011–12. By applying the RPAF only to the Adjusted Allotment, other Tier One allotments, such as special education, career and technology, gifted and talented, bilingual and compensatory education, were not affected. The State Board of Education however, was directed to decrease funding for these programs in proportion to the reductions to the Basic Allotment. The Legislature also established an RPAF value of 0.98 for the 2013–15 State fiscal biennium, subject to increases by subsequent legislative appropriation not to exceed an RPAF value of 1.0. The RPAF factor and its related provisions are scheduled to expire on September 1, 2015.

The RPAF is the primary mechanism for formula reductions in the 2011–12 fiscal year. In the 2012–13 fiscal year, the RPAF of 0.98 is combined with a percentage reduction in each school district's Target Revenue per WADA to 92.35% of its formula amount. For the 2013–14 and subsequent fiscal years, the percentage reduction will be set by legislative appropriation. With regard to this adjustment, the ASATR relief that funds the Target Revenue system is phased out between the 2013–14 and 2017–18 fiscal years.

2013 LEGISLATIVE SESSION

On January 8, 2013, the 83rd Texas Legislature convened in general session, which is scheduled to end May 27, 2013. Thereafter, the Governor may call one or more additional special sessions. During this time, the Texas Legislature may enact laws that materially change current public school finance or affect ad valorem tax matters. The District can make no representation regarding any actions the Texas Legislature may take.

THE SCHOOL FINANCE SYSTEM AS APPLIED TO THE DISTRICT

The District's wealth per student for the current school year is less than the equalized wealth value. Accordingly, the District has not been required to exercise one of the permitted wealth equalization options. As a district with wealth per student less than the equalized wealth value, the District may benefit in the future by agreeing to accept taxable property or funding assistance from or agreeing to consolidate with a property-rich district to enable such district to reduce its wealth per student to the permitted level.

A district's wealth per student must be tested for each future school year and, if it exceeds the maximum permitted level, must be reduced by exercise of one of the permitted wealth equalization options. Accordingly, if the District's wealth per student should exceed the maximum permitted level in future school years, it will be required each year to exercise one or more of the wealth reduction options. If the District were to consolidate (or consolidate its tax base for all purposes) with a property-poor district, the outstanding debt of each district could become payable from the consolidated district's combined property tax base, and the District's ratio of taxable property to debt could become diluted. If the District were to detach property voluntarily, a portion of its outstanding debt (including the Bonds) could be assumed by the district to which the property is annexed, in which case timely payment of the Bonds could become dependent in part on the financial performance of the annexing district.

As described above under "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - 2011 Legislation", during the 82nd legislative sessions in 2011, the Texas Legislature adopted SB 1, which failed to fully fund the Finance System for the 2012-13 State biennium. As a result of the funding action in the 2011 Legislature, and as compared to State funding for fiscal year 2010-11, the District's State funding was reduced by approximately $13.8 million during the 2011-12 fiscal year and approximately $15.1 million during the 2012-13 fiscal year. The District began preparing for a potential loss in State funding in the years leading up to such State funding cuts by building its General Operating fund balance (see "Table 11-A - General Fund Revenues and Expenditure History"). In addition to building its fund balance, the District took certain measures to reduce expenditures, including, among others, a reduction in annual personnel costs through a reduction in force as well as the elimination of several positions through attrition, a change from the modified block classroom schedule to a straight seven-period day classroom schedule, and budget reductions in various departments (primarily non-instructional). In addition, the District received approximately $4.6 million in federal "Edujobs" funds in fiscal year 2011-12, which allowed the District to free up local funds for other purposes. As a result of the foregoing and other one time receipts in 2011-2012, the District was able to increase its general operating fund balance in fiscal year 2011-12 by $18.84 million (see "Table 11-A - General Fund Revenues and Expenditure History"). As anticipated and planned, the District adopted a deficit budget for fiscal year 2012-13 of 12.1 million. The District's policy is to maintain a general fund balance of at least 20% of annual operating expenditures.

The District is unable to predict the future actions of courts and the Texas legislature with respect to funding of the Finance System. Changes made to the Finance System as a result of on-going litigation or otherwise could materially affect the financial condition of the District. See "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS - Current Litigation Related to the Texas Public School Finance System."

TAX INFORMATION

AD VALOREM TAX LAW . . . The appraisal of property within the District is the responsibility of the Tarrant Appraisal District (the "Appraisal District") in which the District is located. Excluding agricultural and open-space land, which may be taxed on the basis of productive capacity, the Appraisal District is required under Title I of the Texas Tax Code (the "Property Tax Code") to appraise all property within the Appraisal District on the basis of 100% of its market value and is prohibited from applying any assessment ratios. In determining the market value of property, different methods of appraisal may be used, including the cost method of appraisal, the income method of appraisal and the market data comparison method of appraisal, and the method considered most appropriate by the chief appraiser is to be used. Effective January 1, 2010, State law requires the appraised value of a residence homestead to be based solely on the property's value as a residence homestead, regardless of whether residential use is considered to be the highest and best use of the property. 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 market value of the property for the most recent tax year that the market value was determined by the appraisal office 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 in the preceding tax year, plus (c) the market value of all new improvements to the property. The value placed upon property within the Appraisal District is subject to review by an Appraisal Review Board, consisting of members appointed by the Board of Directors of the Appraisal District. The Appraisal District is required to review the value of property within the Appraisal District at least every three years. The District may require annual review at its own expense, and is entitled to challenge the determination of appraised value of property within the District 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 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.

Certain residence homestead exemptions from ad valorem taxes for public school purposes are mandated by Section 1-b, Article VIII, and State law and apply to the market value of residence homesteads in the following sequence:

$15,000; and an additional

$10,000 for those 65 years of age or older, or the disabled. A person over 65 and disabled may receive only one $10,000 exemption, and only one such exemption may be received per family, per residence homestead. State law also mandates a freeze on taxes paid on residence homesteads of persons who are 65 years of age or older or disabled, to the extent that such persons are eligible for the $10,000 exemption. Such residence homesteads shall be appraised and taxes calculated as on any other property, but taxes shall never exceed the amount imposed in the first year in which the property received the $10,000 exemption. The freeze on ad valorem taxes on the homesteads of persons who are 65 years of age or older or disabled is also transferable to a different residence homestead. If improvements (other than repairs or improvements required to comply with governmental requirements) 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. A "disabled" person is one who is "under a disability for purposes of payment of disability insurance benefits under the Federal Old Age, Survivors and Disability Insurance". Also, a surviving spouse of a taxpayer who qualifies for the freeze on ad valorem taxes is entitled to the same exemption so long as the property was the residence homestead of the surviving spouse when the deceased spouse died and remains the residence homestead of the surviving spouse and the spouse was at least 55 years of age at the time of the death of the individual's spouse. Pursuant to a constitutional amendment approved by the voters on May 12, 2007, legislation was enacted to reduce the school property tax limitation imposed by the freeze on taxes paid on residence homesteads of persons who are 65 years of age or over or disabled to correspond to reductions in local school district tax rates from the 2005 tax year to the 2006 tax year and from the 2006 tax year to the 2007 tax year (see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM – General"). The school property tax limitation provided by the constitutional amendment and enabling legislation apply to the 2007 and subsequent tax years.

In addition, under Section 1-b, Article VIII, and State law, the governing body of a political subdivision, at its option, may grant either or both of the following:

(i) 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;

(ii) An exemption of up to 20% of the market value of residence homesteads; minimum exemption $5,000.

After the exemption described in (i) above is authorized, such exemption may be repealed or decreased or increased in amount (a) by the governing body of the political subdivision or (b) by a favorable vote of a majority of the qualified voters at an election called by the governing body of the political subdivision, which election must be called upon receipt of a petition signed by at least 20% of the number of qualified voters who voted in the preceding election of the political subdivision. In the case of a decrease, the amount of the exemption may not be reduced to less than $3,000 of the market value.

The surviving spouse of an individual who qualifies for the exemption listed in (i) above for the residence homestead of a person 65 or older (but not the disabled) is entitled to an exemption for the same property in an amount equal to that of the exemption for which the deceased spouse qualified if (i) the deceased spouse died in a year in which the deceased spouse qualified for the exemption, (ii) the surviving spouse was at least 55 years of age at the time of the death of the individual's spouse and (iii) the property was the residence homestead of the surviving spouse when the deceased spouse died and remains the residence homestead of the surviving spouse.

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 beginning in the 2009 tax year, a disabled veteran who receives from the 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 is entitled to an exemption from taxation of the total appraised value of the veteran's residence homestead. In addition, effective January 1, 2012, and subject to certain conditions, surviving spouses of a deceased veteran who had received a disability rating of 100% will be entitled to receive a residential homestead exemption equal to the exemption received by the deceased spouse until such surviving spouse remarries.

Article VIII provides that eligible owners of both agricultural land (Section l-d) and open-space land (Section l-d-l), 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 of the Texas Constitution 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. Notwithstanding such exemption, counties, school districts, junior college districts and cities may tax such tangible personal property provided official action to tax the same was taken before April 1, 1990. 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 Section 11.253 of 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. Section 11.253 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 exemption or the goods-in-transit exemption for items of personal property.

A city or county may create a tax increment financing district ("TIF") within the city or county with defined boundaries and establish a base value of taxable property in the TIF at the time of its creation. Overlapping taxing units, including school districts, may agree with the city or county to contribute all or part of future ad valorem taxes levied and collected against the "incremental value" (taxable value in excess of the base value) of taxable real property in the TIF to pay or finance the costs of certain public improvements in the TIF, and such taxes levied and collected for and on behalf of the TIF are not available for general use by such contributing taxing units. Prior to September 1, 2001, school districts were allowed to enter into tax abatement agreements to encourage economic development. Under such agreements, a property owner agrees to construct certain improvements on its property. The school district 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. School districts have been prohibited from entering into new tax abatement agreements since September 1, 2001. In addition, credit will not be given by the Commissioner of Education in determining a district's property value wealth per student for (1) the appraised value, in excess of the "frozen" value, of property that is located in a TIF created after May 31, 1999 (except in certain limited circumstances where the municipality creating the tax increment financing zone gave notice prior to May 31, 1999 to all other taxing units that levy ad valorem taxes in the TIF of its intention to create the TIF and the TIF was created and had its final project and financing plan approved by the municipality prior to August 31, 1999), or (2) for the loss of value of abated property under any abatement agreement entered into after May 31, 1993. Notwithstanding the foregoing, in 2001 the Legislature enacted legislation known as the Texas Economic Development Act, which provides incentives for school districts to grant limitations on appraised property values and provide ad valorem tax credits to certain corporations and limited liability companies to encourage economic development within the district. Generally, during the last eight years of the ten-year term of a tax limitation agreement, the school district may only levy and collect ad valorem taxes for maintenance and operation purposes on the agreed-to limited appraised property value. The taxpayer is entitled to a tax credit from the school district for the amount of taxes imposed during the first two years of the tax limitation agreement on the appraised value of the property above the agreed-to limited value. Additional State funding is provided to a school district for each year of such tax limitation in the amount of the tax credit provided to the taxpayer. During the first two years of a tax limitation agreement, the school district may not adopt a tax rate that exceeds the district's rollback tax rate (see "TAX INFORMATION - Public Hearing and Rollback Tax Rate" and "TAX INFORMATION – District Application of Tax Code").

TAX RATE LIMITATIONS . . . A school district is authorized to levy M&O taxes subject to approval of a proposition submitted to district voters under Section 45.003(d) of the Texas Education Code, as amended. The maximum M&O tax rate that may be levied by a district cannot exceed the voted maximum rate or the maximum rate described in the next succeeding paragraph. The maximum voted M&O tax rate for the District is $1.50 per $100 of assessed valuation as approved by the voters at an election held on March 5, 2005, under Chapter 45, Texas Education Code.

The maximum tax rate per $100 of assessed valuation that may be adopted by the District may not exceed the lesser of (A) $1.50 and (B) the sum of (1) the rate of $0.17, and (2) the product of the "State Compression Percentage" multiplied by $1.50. The State Compression Percentage has been set, and will remain, at 66.67% for fiscal years 2007–08 through 2012–13. The State Compression Percentage is set by legislative appropriation for each State fiscal biennium or, in the absence of legislative appropriation, by the Commissioner. For a more detailed description of the State Compression Percentage, see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - Local Funding for School Districts." Furthermore, a school district cannot annually increase its tax rate in excess of the district's "rollback tax rate" without submitting such tax rate to a referendum election and a majority of the voters voting at such election approving the adopted rate. See "TAX INFORMATION - Public Hearing and Rollback Tax Rate."

A school district is also authorized to issue bonds and levy taxes for payment of bonds subject to voter approval of one or more propositions submitted to the voters under Section 45.003(b)(1), Texas Education Code, as amended, which provides a tax unlimited as to rate or amount for the support of school district bonded indebtedness (see "THE BONDS - Security and Source of Payment").

Chapter 45 of the Texas Education Code, as amended, requires a district to demonstrate to the Texas Attorney General that it has the prospective ability to pay debt service on a proposed issue of bonds, together with debt service on other outstanding "new debt" of the district, from a tax levied at a rate of $0.50 per $100 of assessed valuation before bonds may be issued. In demonstrating the ability to pay debt service at a rate of $0.50, a district may take into account State allotments to the district which effectively reduces the district's local share of debt service. Once the prospective ability to pay such tax has been shown and the bonds are issued, a district may levy an unlimited tax to pay debt service. Taxes levied to pay debt service on bonds approved by district voters at an election held on or before April 1, 1991, and issued before September 1, 1992 (or debt issued to refund such bonds), are not subject to the foregoing threshold tax rate test. In addition, taxes levied to pay refunding bonds issued pursuant to Chapter 1207, Texas Government Code, as amended, are not subject to the $0.50 tax rate test; however, taxes levied to pay debt service on such bonds are included in the calculation of the $0.50 tax rate test as applied to subsequent issues of "new debt." The Bonds are issued as refunding bonds issued pursuant to Chapter 1207, Texas Government Code, as amended, and are not subject to the $0.50 threshold tax rate test. Under current law, a district may demonstrate its ability to comply with the $0.50 threshold tax rate test by applying the $0.50 tax rate to an amount equal to 90% of projected future taxable value of property in the district, as certified by a registered professional appraiser, anticipated for the earlier of the tax year five years after the current tax year or the tax year in which the final payment for the bonds is due. However, if a district uses projected future taxable values to meet the $0.50 threshold tax rate test and subsequently imposes a tax at a rate greater than $0.50 per $100 of valuation to pay for bonds subject to the test, then for subsequent bond issues, the Attorney General must find that the district has the projected ability to pay principal and interest on the proposed bonds and all previously issued bonds subject to the $0.50 threshold tax rate test from a tax rate of $0.45 per $100 of valuation. The District has not used projected property values to satisfy this threshold test.

PUBLIC HEARING AND ROLLBACK TAX RATE. . . In setting its annual tax rate, the governing body of a school district generally cannot adopt a tax rate exceeding the district's "rollback tax rate" without approval by a majority of the voters voting at an election approving the higher rate. The tax rate consists of two components: (1) a rate for funding of maintenance and operation expenditures and (2) a rate for debt service. The rollback tax rate for a school district is the lesser of (A) the sum of (1) the product of the district's "State Compression Percentage" for that year multiplied by $1.50, (2) the rate of $0.04, (3) any rate increase above the rollback tax rate in prior years that were approved by voters, and (4) the district's current debt rate, or (B) the sum of (1) the district's effective maintenance and operations tax rate, (2) the product of the district's State Compression Percentage for that year multiplied by $0.06; and (3) the district's current debt rate (see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - Local Funding for School Districts" for a description of the "State Compression Percentage"). If for the preceding tax year a district adopted an M&O tax rate that was less than its effective M&O tax rate for that preceding tax year, the district's rollback tax for the current year is calculated as if the district had adopted an M&O tax rate for the preceding tax year equal to its effective M&O tax rate for that preceding tax year.

The "effective maintenance and operations tax rate" for a school district is the tax rate that, applied to the current tax values, would provide local maintenance and operating funds, when added to State funds to be distributed to the district pursuant to Chapter 42 of the Texas Education Code for the school year beginning in the current tax year, in the same amount as would have been available to the district in the preceding year if the funding elements of wealth equalization and State funding for the current year had been in effect for the preceding year.

Section 26.05 of the Property Tax Code provides that the governing body of a taxing unit is required to adopt the annual tax rate for the unit before the later of September 30 or the 60th day after the date the certified appraisal roll is received by the taxing unit, and a failure to adopt a tax rate by such required date will result in the tax rate for the taxing unit for the tax year to be the lower of the effective tax rate calculated for that tax year or the tax rate adopted by the taxing unit for the preceding tax year. Before adopting its annual tax rate, a public meeting must be held for the purpose of adopting a budget for the succeeding year. A notice of public meeting to discuss budget and proposed tax rate must be published in the time, format and manner prescribed in Section 44.004 of the Texas Education Code. Section 44.004(e) of the Texas Education Code provides that a person who owns taxable property in a school district is entitled to an injunction restraining the collection of taxes by the district if the district has not complied with such notice requirements or the language and format requirements of such notice as set forth in Section 44.004(b), (c) and (d) and if such failure to comply was not in good faith. Section 44.004(e) further provides the action to enjoin the collection of taxes must be filed before the date the district delivers substantially all of its tax bills. A district may adopt its budget after adopting a tax rate for the tax year in which the fiscal year covered by the budget begins if the district elects to adopt its tax rate before receiving the certified appraisal roll. A district that adopts a tax rate before adopting its budget must hold a public hearing on the proposed tax rate followed by another public hearing on the proposed budget rather than holding a single hearing on the two items.

PROPERTY ASSESSMENT AND TAX PAYMENT . . . Property within the District is generally assessed as of January 1 of each year. Business inventory may, at the option of the taxpayer, be assessed as of September 1. Effective January 1, 2012, oil and gas reserves are assessed on the basis of a valuation process which uses pricing information contained in the most recently published Early Release Overview of the Annual Energy Outlook published by the United States Energy Information Administration, as well as appraisal formulas developed by the State Comptroller of Public Accounts. 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 installment 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:

Month	Cumulative Penalty[(a)]	Cumulative Interest[(a)]	Total
February	6%	1%	7%
March	7	2	9
April	8	3	11
May	9	4	13
June	10	5	15
July	12[(a)]	6	18

(a) After July, the penalty remains at 12%, and interest accrues at a rate of one percent (1%) for each month or portion of a month the tax remains unpaid. A delinquent tax continues to accrue interest as long as the tax remains unpaid, regardless of whether a judgment for the delinquent tax has been rendered. The purpose of imposing such interest penalty is to compensate the taxing unit for revenue lost because of the delinquency. In addition, if an account is delinquent in July, an attorney's collection fee of up to 20% may be added to the total tax penalty and interest charge.

Taxes levied by the District are a personal obligation of the owner of the property. On January 1 of each year, a tax lien attaches to property to secure the payment of all taxes, penalties and interest ultimately imposed for the year on the property. The lien exists in favor of the State and each taxing unit, including the District, having the power to tax the property. The District's tax lien is on a parity with tax liens of all other such taxing units. A tax lien on real property has priority over the claim of most creditors and other holders of liens on the property encumbered by the tax lien, whether or not the debt or lien existed before the attachment of the tax lien. Personal property under certain circumstances is subject to seizure and sale for the payment of delinquent taxes, penalty and interest. At any time after taxes on property become delinquent, the District may file suit to foreclose the lien securing payment of the tax, to enforce personal liability for the tax, or both. In filing a suit to foreclose a tax lien on real property, the District must join other taxing units that have claims for delinquent taxes against all or part of the same property. The ability of the District to collect delinquent taxes by foreclosure may be adversely affected by the amount of taxes owed to other taxing units, adverse market conditions, taxpayer redemption rights, or bankruptcy proceedings which restrain the collection of a taxpayer's debt. **Federal bankruptcy law provides that an automatic stay of actions 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.

DISTRICT APPLICATION OF TAX CODE . . . The District grants the state-mandated exemption to the market value of the residence homestead of $15,000; the disabled and persons over 65 years of age or older are also granted the state-mandated exemption to the market value of the residence of $10,000.

The District also grants an additional local-option basis exemption of $10,000 to the market value of the residence homestead of persons over 65 years of age or older (but not the disabled).

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

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

The District does not tax nonbusiness personal property; and Tarrant County collects taxes for the District.

The District does permit split payments of taxes and discounts for early payment of taxes are not allowed, although permitted on a local-option basis by State law.

The District does not tax freeport property.

The District does tax goods-in-transit.

TAX ABATEMENT POLICY . . . The District has established a tax abatement program but does not participate in any tax abatements and current policy is that the District will not do so under existing state funding laws.

TAX INCREMENT FINANCE ZONES . . . The District participates in one tax increment financing ("TIF") at the present time. This participation is limited to the maintenance and operations (M&O) taxes and does not include interest and sinking fund (I&S) taxes. As a result, TIF participation has not affected the amount of taxes necessary to pay debt on bonded debt. For tax year 2012, the incremental value of the TIF is $149,554,655.

TABLE 1 - VALUATION, EXEMPTIONS AND TAX SUPPORTED DEBT

2012/13 Market Valuation Established by Tarrant Appraisal District (excluding totally exempt property)		$ 12,212,069,577
Less Exemptions/Reductions at 100% Market Value		
State Mandated General Homestead Exemptions	$ 549,910,442	
State Mandated Over 65 Exemptions	46,169,805	
State Mandated Disability Exemptions	4,362,000	
Local Option Over 65 Homestead Exemptions	45,787,650	
Disabled Veterans Exemptions	27,179,210	
Freeport Exemptions	7,920,469	
Pollution Control Loss	295,252	
Agricultural Deferrals	179,580,289	
Foreign Trade Zone	179,525,149	
Community Housing Development Exemption	166,600	
Solar/Wind Exemptions	1	
Prorated Absolute Exemptions	152,749	$ 1,041,049,616
2012/13 Taxable Assessed Valuation		$ 11,171,019,961 (1)
Debt Payable from Ad Valorem Taxes (as of 03/28/13)		
Outstanding Unlimited Tax Bonds (2)	$ 607,357,009	
The Bonds (3)	84,789,983	
Total Debt Payable from Ad Valorem Taxes (as of 03/28/13)		$ 692,146,991
Ratio Tax Supported Debt to Taxable Assessed Valuation		6.20%

Current Estimated District Population - 159,813
Per Capita Taxable Assessed Valuation - $69,901
Per Capita General Obligation Debt - $4,331

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(1) Exemptions do not include the values on which property taxes are frozen for the Age 65 and Disabled taxpayer exemptions. Also excludes the incremental value of the TIF of $149,554,655.
(2) The amounts of outstanding tax-supported debt shown in the table above include the principal amount of current interest bonds and capital appreciation bonds as of the issuance date thereof. The District has bonds outstanding that were issued in part as capital appreciation bonds. Excludes the Refunded Bonds.
(3) Preliminary, subject to change.

TABLE 2 - TAXABLE ASSESSED VALUATIONS BY CATEGORY

	Taxable Appraised Value for Fiscal Year Ended August 31,					
	2013		2012		2011	
Category	Amount	% of Total	Amount	% of Total	Amount	% of Total
Real, Residential, Single-Family	$ 9,256,742,628	75.80%	$ 9,178,255,191	75.17%	$ 8,967,360,450	75.41%
Real, Residential, Multi-Family	442,846,879	3.63%	424,941,331	3.48%	358,240,889	3.01%
Real, Vacant Lots/Tracts	252,408,129	2.07%	272,091,517	2.23%	257,016,374	2.16%
Real, Acreage (Land Only)	176,493,446	1.45%	193,881,489	1.59%	213,666,648	1.80%
Real, Farm and Ranch Improvements	1,179,000	0.01%	1,355,400	0.01%	1,288,770	0.01%
Real, Commercial and Industrial	1,316,985,755	10.78%	1,282,855,311	10.51%	1,174,936,658	9.88%
Real, Minerals, Oil and Gas	15,692,930	0.13%	33,945,660	0.28%	28,833,830	0.24%
Real and Tangible Personal, Utilities	117,974,041	0.97%	127,933,891	1.05%	115,274,477	0.97%
Tangible Personal, Commercial & Industrial	487,144,039	3.99%	512,842,081	4.20%	553,182,025	4.65%
Tangible Personal, Other	18,666,705	0.15%	17,652,004	0.14%	18,296,496	0.15%
Real & Special, Inventory	125,936,025	1.03%	164,406,445	1.35%	202,946,696	1.71%
Total Appraised Value Before Exemptions	$12,212,069,577	100.00%	$12,210,160,320	100.00%	$ 11,891,043,313	100.00%
Less: Total Exemptions/Reductions	(1,041,049,616)		(1,009,522,197)		(1,053,034,313)	
Taxable Assessed Value	$11,171,019,961		$11,200,638,123		$ 10,838,009,000	

	Taxable Appraised Value for Fiscal Year Ended August 31,			
	2010		2009	
Category	Amount	% of Total	Amount	% of Total
Real, Residential, Single-Family	$ 8,446,270,360	74.28%	$ 8,244,435,673	75.06%
Real, Residential, Multi-Family	337,814,108	2.97%	300,856,689	2.74%
Real, Vacant Lots/Tracts	274,664,055	2.42%	254,721,835	2.32%
Real, Acreage (Land Only)	218,257,917	1.92%	249,398,782	2.27%
Real, Farm and Ranch Improvements	1,348,591	0.01%	1,051,510	0.01%
Real, Business	1,296,637,601	11.40%	1,185,306,274	10.79%
Real, Minerals, Oil and Gas	14,544,320	0.13%	13,543,900	0.12%
Real and Tangible Personal, Utilities	122,545,784	1.08%	134,051,815	1.22%
Tangible Personal, Commercial & Industrial	415,033,580	3.65%	310,323,883	2.83%
Tangible Personal, Other	20,470,154	0.18%	19,907,910	0.18%
Real & Special, Inventory	223,005,591	1.96%	270,428,184	2.46%
Total Appraised Value Before Exemptions	$11,370,592,061	100.00%	$10,984,026,455	100.00%
Less: Total Exemptions/Reductions	(851,606,467)		(771,482,494)	
Taxable Assessed Value	$10,518,985,594		$10,212,543,961	

Valuations shown are certified taxable assessed values reported by the Appraisal District to the State Comptroller of Public Accounts. Certified values are subject to change throughout the year as contested values are resolved and the Appraisal District updates records. Valuations shown do not exclude the values on which property taxes are frozen for the Age 65 and Disabled taxpayer exemptions.

TABLE 3 - VALUATION AND TAX SUPPORTED DEBT HISTORY

Fiscal Year Ended 8/31	Estimated Population[1]	Taxable Assessed Valuation[2]	Taxable Assessed Valuation Per Capita	Tax Debt Outstanding at End of Fiscal Year[3]	Ratio of Tax Debt to Taxable Assessed Valuation	Tax Debt Per Capita
2009	132,430	$ 10,212,543,961	$ 77,117	$735,369,467	7.20%	5,553
2010	132,705	10,518,985,594	79,266	725,718,459	6.90%	5,469
2011	136,038	10,838,009,000	79,669	712,856,753	6.58%	5,240
2012	154,320	11,200,638,123	72,581	700,087,011	6.25%	4,537
2013	159,500	11,171,019,961	70,038	684,454,009 [4]	6.13% [4]	4,291 [4]

(1) Source: District Officials.
(2) As reported by the Appraisal District on the District's annual State Property Tax Reports and subject to change during the ensuing year.
(3) The amounts of outstanding tax-supported debt shown in the table above include the principal amount of current interest bonds and capital appreciation bonds as of the issuance date thereof and exclude the accreted value of such outstanding capital appreciation bonds.
(4) Projected, includes the Bonds but excludes the Refunded Bonds. Preliminary, subject to change.

TABLE 4 - TAX RATE, LEVY AND COLLECTION HISTORY

Fiscal Year Ended 8/31	Tax Rate	Local Maintenance	Interest and Sinking Fund	Tax Levy	% Current Collections	% Total Collections
2009	$ 1.41690	$ 1.04000	$ 0.37690	$ 147,374,611	99.06%	99.85%
2010	1.48630	1.04000	0.44630	162,025,597	98.93%	99.49%
2011	1.53060	1.04000	0.49060	163,551,452	100.22%	101.02%
2012	1.54000	1.04000	0.50000	170,135,313	99.41%	100.73%
2013	1.54000	1.04000	0.50000	173,581,611	62.60% [1]	62.96% [1]

(1) Collections as of December 31, 2012.

TABLE 5 - TEN LARGEST TAXPAYERS

Name of Taxpayer	Nature of Property	2012/13 Taxable Assessed Valuation	% of Total Taxable Assessed Valuation
FMR Texas Ltd Partnership	Financial Services	$ 144,263,970	1.29%
Kroger Co.	Grocery Store	99,954,435	0.89%
Wal-Mart Real Estate Business Trust	Retail	63,402,694	0.57%
Alliance Town Center I LP	Retail	40,436,320	0.36%
Oncor Electric Delivery Co. LLC	Electric Utility	38,503,668	0.34%
Watercolor Partners LP	Real Estate	33,000,000	0.30%
Capri W DTC LP	Land/Improvements	28,500,000	0.26%
Inland Western Watauga	Land/Improvements	27,739,600	0.25%
Hillwood Monterra LP	Land/Improvements	27,428,467	0.25%
SW Fossil Creek Apartment LP	Apartments	27,294,000	0.24%
		$ 530,523,154	4.75%

TABLE 6 - ESTIMATED OVERLAPPING DEBT

Expenditures of the various taxing entities within the territory of the District are paid out of ad valorem taxes levied by such entities on properties within the District. Such entities are independent of the District and may incur borrowings to finance their expenditures. This statement of direct and estimated overlapping ad valorem tax debt ("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 District, the District 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 Tax Debt since the date hereof, and such entities may have programs requiring the issuance of substantial amounts of additional Tax Debt, the amount of which cannot be determined. The following table reflects the estimated share of overlapping Tax Debt of the District.

Taxing Jurisdiction	2012/13 Taxable Assessed Value	2012/13 Tax Rate	Total Tax Supported Debt Projected As Of 3/28/2013	Estimated % Applicable	District's Overlapping Tax Supported Debt Projected As Of 3/28/2013
Keller ISD	$ 11,171,019,961	$ 1.54000	$ 692,146,991 (1)	100.00%	$ 692,146,991 (1)
City of Colleyville	3,778,035,705	0.35590	14,740,000	9.06%	1,335,444
City of Fort Worth	41,750,494,877	0.85500	646,390,000	10.09%	65,220,751
City of Haltom City	1,554,478,270	0.65170	60,405,000	4.49%	2,712,185
City of Hurst	2,135,476,788	0.60850	69,605,000	1.34%	932,707
City of Keller	4,109,746,614	0.44220	102,713,546	97.96%	100,618,190
City of North Richland Hills	3,710,700,861	0.61000	100,240,000	11.87%	11,898,488
City of Southlake	5,634,924,196	0.46200	156,395,000	4.99%	7,804,111
City of Watauga	945,615,206	0.59120	28,440,000	38.95%	11,077,380
Town of Westlake	857,926,594	0.15680	22,227,000	53.94%	11,989,244
Tarrant County	124,676,098,060	0.26400	335,050,000	9.10%	30,489,550
Tarrant County Hospital District	124,838,781,318	0.22790	22,705,000	9.10%	2,066,155
Tarrant County Jr. College District	125,092,633,012	0.14897	26,285,000	9.10%	2,391,935
Total Direct and Overlapping Tax Supported Debt					$ 940,683,130
Ratio of Direct and Overlapping Tax Supported Debt to Taxable Assessed Valuation					8.42%
Per Capita Overlapping Tax Supported Debt					$ 5,886.15

(1) Projected, includes the Bonds and excludes the Refunded Bonds. Does not include interest accreted on outstanding capital appreciation bonds. Preliminary, subject to change.

DEBT INFORMATION

TABLE 7 - PRO-FORMA TAX SUPPORTED DEBT SERVICE REQUIREMENTS

FYE 8/31	Outstanding Debt (1) Principal	Outstanding Debt (1) Interest	Outstanding Debt (1) Total	The Bonds (2) Principal	The Bonds (2) Interest	The Bonds (2) Total	Total Debt Service Requirements	% of Principal Retired
2013	$ 14,508,841	$ 39,571,802	$ 54,080,643	$ 1,124,141	$ 1,785,760	$ 2,909,901	$ 56,990,544	2.23%
2014	23,634,768	31,930,102	55,564,870	-	3,070,950	3,070,950	58,635,820	5.61%
2015	15,475,068	36,846,520	52,321,589	-	3,070,950	3,070,950	55,392,539	7.82%
2016	11,082,087	37,876,039	48,958,126	1,492,113	4,653,837	6,145,950	55,104,076	9.62%
2017	13,582,171	35,341,049	48,923,220	1,538,728	5,422,222	6,960,950	55,884,170	11.78%
2018	17,714,817	31,708,359	49,423,176	3,935,000	3,070,950	7,005,950	56,429,126	14.87%
2019	15,522,529	35,050,591	50,573,120	3,475,000	2,952,900	6,427,900	57,001,020	17.58%
2020	20,237,656	30,587,098	50,824,754	3,900,000	2,848,650	6,748,650	57,573,404	21.03%
2021	21,464,071	29,828,961	51,293,032	4,135,000	2,731,650	6,866,650	58,159,682	24.69%
2022	29,270,000	22,268,075	51,538,075	4,595,000	2,607,600	7,202,600	58,740,675	29.52%
2023	30,955,000	20,845,239	51,800,239	5,110,000	2,423,800	7,533,800	59,334,039	34.67%
2024	27,730,000	19,338,595	47,068,595	10,720,000	2,219,400	12,939,400	60,007,995	40.17%
2025	29,355,000	17,975,734	47,330,734	11,495,000	1,790,600	13,285,600	60,616,334	46.00%
2026	40,585,000	16,522,982	57,107,982	2,700,000	1,330,800	4,030,800	61,138,782	52.18%
2027	38,885,000	14,631,904	53,516,904	7,065,000	1,222,800	8,287,800	61,804,704	58.75%
2028	41,025,000	12,758,916	53,783,916	7,700,000	940,200	8,640,200	62,424,116	65.71%
2029	43,310,000	10,831,093	54,141,093	7,750,000	632,200	8,382,200	62,523,293	73.00%
2030	45,355,000	8,793,731	54,148,731	8,055,000	322,200	8,377,200	62,525,931	80.63%
2031	52,400,000	6,487,762	58,887,762				58,887,762	88.12%
2032	39,570,000	3,958,106	43,528,106				43,528,106	93.77%
2033	13,765,000	2,004,181	15,769,181				15,769,181	95.73%
2034	14,525,000	1,243,413	15,768,413				15,768,413	97.81%
2035	15,345,000	421,988	15,766,988				15,766,988	100.00%
	$ 615,297,009	$ 466,822,241	$1,082,119,250	$ 84,789,983	$ 43,097,468	$ 127,887,451	$1,210,006,700	

(1) "Outstanding Debt" does not include the Refunded Bonds.
(2) Preliminary, subject to change. Interest calculated at a rate of 3.83% for purposes of illustration only.

TABLE 8 - INTEREST AND SINKING FUND BUDGET PROJECTION (1)

Estimated Tax Supported Debt Service Requirements, Fiscal Year Ending 8/31/13		$ 56,990,544
Interest and Sinking Fund Balance - 8/31/12	$ 3,892,876	
Projected Interest and Sinking Fund Tax Levy Collections	55,494,208	
Interest Income	50,000	
Delinquent Taxes, Penalty and Interest	550,000	
Estimated Existing Debt Allotment	10,000	
Estimated Instructional Facilities Allotment	45,000	$ 60,042,084
Estimated Interest and Sinking Fund Balance, 8/31/13		$ 3,051,540

(1) Preliminary, subject to change.

TABLE 9 - AUTHORIZED BUT UNISSUED UNLIMITED TAX BONDS

The District does not have any authorized but unissued unlimited tax bonds.

ANTICIPATED ISSUANCE OF ADDITIONAL UNLIMITED TAX DEBT . . . The District does not anticipate the issuance of additional unlimited tax bonds within the next 12 months.

TABLE 10 - OTHER OBLIGATIONS

On January 28, 2011, the District entered into an agreement with Dell Marketing L.P. for managed technology services. The contract was entered into for a period of five years beginning January 28, 2011 and ending January 28, 2016, with the option to renew for five additional years. The remaining financial commitment at August 31, 2011 under this agreement was $738,175. The financial commitment for each of the four remaining years under the agreement is $1,771,620.

PENSION FUND . . . Pension funds for employees of Texas school districts, and any employee in public education in Texas, are administered by the Teacher Retirement System of Texas (the "System"). The individual employees contribute a fixed amount of their salary to the System, currently 6.4%, and the State of Texas contributes funds to the System based on statutory required minimum salary for certified personnel, except any District personnel paid by Federally funded programs. (For more detailed information concerning the retirement plan, see Appendix B, "Excerpts from the District's Annual Financial Report" - Note #7.)

OTHER POST-EMPLOYMENT BENEFITS . . . In addition to its participation in the System, the District contributes to the Texas Public School Retired Employees Group Insurance Program (the "TRS-Care Retired Plan"), a cost-sharing multiple-employer defined benefit post-employment health care plan. The TRS-Care Retired Plan provides health care coverage for certain persons (and their dependents) who retired under the Teacher Retirement System of Texas. Contribution requirements are not actuarially determined but are legally established each biennium by the Texas Legislature. For the years ended August 31, 2010, 2011 and 2012 the State's contributions to TRS-Care were $1,538,996, $1,573,382 and $565,367, respectively, the active member contributions were $1,002,801, $1,002,711 and $958,628, respectively and the District's contributions were $899,202, $945,042 and $811,154, respectively which equaled the required contributions for those years. Upon an employee's retirement, the District is no longer obligated to make contributions to the TRS-Care Retired Plan on behalf of such retired employee. For more detailed information concerning the District's funding policy and contributions in connection with the TRS-Care Retired Plan, see Appendix B, "Excerpts from the District's Annual Financial Report" - Note #7.

As a result of its participation in the System and the TRS-Care Retired Plan, and having no other post-employment benefit plans, the District has no obligations for other post-employment benefits within the meaning of Governmental Accounting Standards Board Statement 45.

OTHER BENEFITS

COMPENSATED ABSENCES…The District pays certain employees for unused accumulated sick leave upon termination or retirement. The District's liability as of August 31, 2012, was $704,357. For more detailed information concerning the District's compensated absence benefits, see Appendix B, "Excerpts from the District's Annual Financial Report" - Note #1.I. and Note #3.

SELF INSURANCE…The District provides health care benefits to its employees through a self-insurance plan implemented in December 2002 and provides workers' compensation benefits through a self-insurance plan implemented in January 1994. For more detailed information concerning the District's self-insurance plans, see Appendix B, "Excerpts from the District's Annual Financial Report" - Note #8.

FINANCIAL INFORMATION

TABLE 11 - SCHEDULE OF CHANGES IN NET ASSETS

	Fiscal Year Ended August 31,				
	2012	2011	2010	2009	2008
Program Revenues:					
Charges for Services	$ 18,068,929	$ 18,942,250	$ 17,627,529	$ 16,658,169	$ 15,888,800
Operating Grants & Contributions	24,161,384	31,969,236	22,629,116	13,532,702	14,532,569
General Revenues					
Property Taxes	170,418,927	164,484,171	162,550,338	148,035,177	129,419,121
Grants (State Aid and Not Restricted)	88,208,113	92,872,674	78,839,121	78,938,143	75,667,541
Investment Earnings	436,411	364,742	583,181	4,110,151	10,047,879
Other	4,400,916	686,139	6,393,170	4,897,151	4,247,899
Total Revenues	$ 305,694,680	$ 309,319,212	$ 288,622,455	$ 266,171,493	$ 249,803,809
Expenses:					
Instruction	$ 149,547,022	$ 159,641,776	$ 160,197,180	$ 147,615,180	$ 130,853,347
Instructional Resources & Media Services	3,506,194	3,743,225	3,261,124	4,548,868	3,791,403
Curriculum & Staff Development	2,754,701	2,889,302	3,497,953	3,490,394	3,245,795
Instructional Leadership	2,091,486	2,269,740	2,310,199	2,459,408	2,392,807
School Leadership	14,317,804	14,478,924	13,594,932	13,325,500	12,661,163
Guidance, Social Work, Health, Transportation	10,056,213	10,101,315	9,129,293	8,822,213	7,815,695
Health & Social Work Services	3,255,217	2,738,173	2,515,357	2,394,623	2,151,943
Student (Pupil) Transportation	5,448,661	6,808,740	6,222,185	6,035,224	5,105,905
Food Services	12,085,660	10,974,335	10,538,803	10,407,692	9,713,959
Co-curricular/Extracurricular Activities	7,985,415	8,771,031	8,057,423	7,298,740	6,643,550
General Administration	8,082,486	5,584,569	5,837,704	6,271,204	4,988,376
Plant Maintenance & Operations	18,625,453	14,671,718	21,065,268	18,653,300	22,487,313
Security & Monitoring Services	1,299,191	1,675,711	1,468,225	1,154,381	756,555
Data Processing Services	5,227,588	4,380,257	3,379,340	3,639,516	4,053,626
Community Services	1,541,352	1,075,017	1,086,051	801,894	472,403
Debt Service-Interest on Long-Term Debt & Fees	33,103,972	41,249,450	39,427,642	34,538,165	32,158,191
Facilities Acquisition & Construction	0	0	0	0	3,466,383
Shared Services Agreement	3,410,020	3,329,680	3,945,201	3,811,277	0
Juvenile Justice Alternative Education Program	2,375	0	0	5,500	0
Payments to Tax Increment Fund	1,732,427	1,750,904	1,925,666	1,831,416	1,097,395
Total Expenses	$ 284,073,237	$ 296,133,867	$ 297,459,546	$ 277,104,495	$ 253,855,809
Increase (Decrease) in Net Assets	$ 21,621,443	$ 13,185,345	$ (8,837,091)	$ (10,933,002)	$ (4,052,000)
Beginning Net Assets	(7,633,788)	(20,819,133)	(11,982,042)	(1,049,040)	3,002,960
Ending Net Assets (1)	$ 13,987,655	$ (7,633,788)	$ (20,819,133)	$ (11,982,042)	$ (1,049,040)

(1) The negative net assets for fiscal years ending 2008-2011 is primarily due to the relationship between the annual depreciation of the District's capital assets and the effect of the principal amortization of the District's outstanding bonds issued to finance such capital assets.

TABLE 11-A - SCHEDULE OF GENERAL FUND REVENUES AND EXPENDITURE HISTORY

	Fiscal Years Ended August 31,				
	2012	2011	2010	2009	2008
Revenues:					
Local and Intermediate Sources	$122,477,457	$115,342,108	$117,182,293	$111,660,630	$104,365,640
State Sources	94,683,993	101,741,928	86,473,461	84,944,885	82,621,118
Federal Sources	346,711	223,961	238,831	244,835	33,815
Total Revenues	$217,508,161	$217,307,997	$203,894,585	$196,850,350	$187,020,573
Expenditures:					
Instruction and Instructional-Related Services	$128,110,017	$130,303,887	$126,233,969	$128,826,007	$120,108,216
Instructional and School Leadership	14,224,237	15,194,047	14,698,464	14,733,059	13,809,592
Support Services - Student (Pupil)	20,983,761	23,962,105	22,102,622	21,195,358	19,525,015
Administrative Support Services	5,019,367	5,382,277	5,168,217	5,607,324	5,006,260
Support Services - Nonstudent Based	23,305,999	24,399,596	21,732,670	21,348,641	27,126,523
Ancillary Services	562,344	700,459	740,922	666,164	469,717
Debt Service	0	0	0	0	0
Capital Outlay	1,316,799	472,775	1,525,798	125,546	239,748
Intergovernmental Charges	5,144,822	5,080,584	5,870,867	5,648,193	1,097,395
Total Expenditures	$198,667,346	$205,495,730	$198,073,529	$198,150,292	$187,382,466
Other Resources and (Uses)	$ 0	$ 0	$ 0	$ 0	$ 490,727
Excess (Deficiency) of Revenues and Other Resources Over Expenditures and Other Uses	$ 18,840,815	$ 11,812,267	$ 5,821,056	$ (1,299,942)	$ 128,834
Beginning Fund Balance on September 1	$ 64,139,134	$ 52,326,867	$ 46,505,811	$ 47,805,753	$ 47,676,919
Ending Fund Balance on August 31	$ 82,979,949	$ 64,139,134	$ 52,326,867	$ 46,505,811	$ 47,805,753

The District adopted a deficit budget of $12.1 million for fiscal year 2012-13. The deficit budget was anticipated as a part of the District's overall plan to address the reduction in State funding for fiscal years 2011-12 and 2012-13 (see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - The School Finance System as Applied to the District"). The District's policy is to maintain a general fund balance of at least 20% of annual operating expenditures.

FINANCIAL POLICIES

Summary of Significant Accounting Policies . . . The District is a public educational agency operating under the applicable laws and regulations of the State of Texas. It is governed by a seven member Board of Trustees (the "Board") elected by registered voters of the District. The District prepares its general purpose financial statements in conformity with generally accepted accounting principles promulgated by the Government Accounting Standards Board ("GASB") and other authoritative sources identified in *Statement on Auditing Standards No. 69* of the American Institute of Certified Public Accountants; and it complies with the requirements of the appropriate version of Texas Education Agency's *Financial Accountability System Resource Guide* (the "Resource Guide") and the requirements of contracts and grants of agencies from which it receives funds.

The Board is elected by the public and it has the authority to make decisions, appoint administrators and managers, and significantly influence operations. It also has the primary accountability for fiscal matters. Therefore, the District is a financial reporting entity as defined by the Governmental Accounting Standards Board ("GASB") in its Statement No. 14, "The Financial Reporting Entity." There are no component units included within the reporting entity.

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

Governmental fund financial statements use the current financial resources measurement focus and the modified accrual basis of accounting. With this measurement focus, only current assets, current liabilities and fund balances are included on the balance sheet. Operating statements of these funds present net increases and decreases in current assets (i.e., revenues and other financing sources and expenditures and other financing uses).

The modified accrual basis of accounting recognizes revenues in the accounting period in which they become both measurable and available, and it recognizes expenditures in the accounting period in which the fund liability is incurred, if measurable, except for unmatured interest and principal on long-term debt, which is recognized when due. The expenditures related to certain compensated absences and claims and judgments are recognized when the obligations are expected to be liquidated with expendable available financial resources. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the District considers all revenues available if they are collectible within 60 days after year end.

Revenues from local sources consist primarily of property taxes. Property tax revenues and revenues received from the State are recognized under the susceptible to accrual concept. Miscellaneous revenues are recorded as revenue when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned, since they are both measurable and available.

Fund Accounting

The District reports the following major governmental funds:

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

The Debt Service Fund accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

The Capital Projects Fund accounts for proceeds from long-term debt financing and revenues and expenditures related to authorized construction and other capital asset acquisitions.

Budgetary Information . . . The Board of Trustees adopts an "appropriated budget" for the General Fund, Debt Service Fund and the Food Service Fund.

The following procedures are followed in establishing the budgetary data reflected in the general purpose financial statements:

1. Prior to August 20, the District prepares a budget for the next succeeding fiscal year beginning September 1. The operating budget includes proposed expenditures and means of financing them.

2. A meeting of the Board is then called for the purpose of adopting the proposed budget. At least 10 days' public notice of the meeting must be given.

3. Prior to September 1, the budget is legally enacted through passage of a resolution by the Board. Once a budget is approved, it can only be amended at the function and fund level by approval of a majority of the members of the Board. Amendments are presented to the Board at their regular meetings. Each amendment must have Board approval. As required by law, such amendments made before the fact, are reflected in the official minutes of the Board, and are not made after fiscal year-end. Because the District has a policy of careful budgetary control, several amendments were necessary during the year. Significant amendments were made to the following functional areas:

Function	Increase (Decrease)
Instruction	$ 6,083,566
School Leadership	605,464
Guidance and Counseling	548,309
Cocurricular/Extracurricular	484,123
Plant Maintenance and Operations	1,171,246
Data Processing Services	579,864
Facilities Acquisition and Construction	410,500

4. Each budget is controlled by the budget coordinator at the revenue and expenditure function/object level. Budgeted amounts are as amended by the Board. All budget appropriations lapse at year-end.

Encumbrances for goods or purchased services are documented by purchase orders or contracts. Under Texas law, appropriations lapse at August 31, and encumbrances outstanding at that time are to be either canceled or appropriately provided for in the subsequent year's budget.

INVESTMENTS

The District invests its funds in investments authorized by Texas law in accordance with investment policies approved by the Board of Trustees of the District. Both State law and the District's investment policies are subject to change.

LEGAL INVESTMENTS . . . Under Texas law, the District is authorized to invest in (1) obligations of the United States or its agencies and instrumentalities including letters of credit, (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 guaranteed or insured by 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 meeting the requirements of the Texas Public Funds Investment Act (Chapter 2256, Texas Government Code, as amended) (i) that are issued by or through an institution that has its main office or a branch office in Texas and 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 District deposits; or (ii) that are invested by the District through a depository institution that has its main office or a branch office in the State of Texas and otherwise meet the requirements of the Public Funds Investment Act; (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 District, held in the District's name, and deposited at the time the investment is made with the District or with a third party selected and approved by the District and are placed through a primary government securities dealer, as defined by the Federal Reserve, or a financial institution doing business in the State primary government securities dealer or a financial institution doing business in the State; (9) certain bankers' acceptances with the remaining term of 270 days or less, 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 paper with a stated maturity of 270 days or less 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; and (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 this paragraph, 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. If specifically authorized in the authorizing document, bond proceeds may be invested in guaranteed investment contracts that have a defined termination date and are secured by obligations of the United States or its agencies and instrumentalities in an amount at least equal to the amount of bond proceeds invested under such contract, other than the prohibited obligations described in the next succeeding paragraph.

Governmental bodies in the State are authorized to implement 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) of the first paragraph under this subcaption, (b) irrevocable letters of credit issued by a state or national bank that is continuously rated by a nationally recognized investment rating firm not less than "A" or its equivalent, or (c) cash invested in obligations that are described in clauses (1) through (6) and (10) through (12) of the first paragraph under this subcaption, or an authorized investment pool; (ii) securities held as collateral under a loan are pledged to the governmental body, held in the name of the governmental body and deposited at the time the investment is made with the District or a third party designated by the District; (iii) a loan made under the program is placed 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 District 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 District may also contract with an investment management firm registered under the Investment Advisers Act of 1940 (15 U.S.C. Section 80b-1 et seq.) 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 District retains ultimate responsibility as fiduciary of its assets. In order to renew or extend such a contract, the District must do so by order, ordinance, or resolution. The District 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.

As a school district that qualifies as an "issuer" under Chapter 1371, as amended, Texas Government Code, the District is also authorized to purchase, sell, and invest its funds in corporate bonds. Texas law defines "corporate bonds" as senior secured debt obligations issued by a domestic business entity and rated not lower than "AA-" or the equivalent by a nationally recognized investment rating firm. The term does not include a bond that is convertible into stocks or shares in the entity issuing the bond (or an affiliate or subsidy thereof) or any unsecured debt. Corporate bonds must finally mature not later than 3 years from their date of purchase by the school district. A school district may not (1) invest more than 15% of its monthly average fund balance (excluding bond proceeds, reserves, and other funds held for the payment of debt service) in corporate bonds; or (2) invest more than 25% of the funds invested in corporate bonds in any one domestic business entity (including subsidiaries and affiliates thereof). Corporate bonds held by a school district must be sold if they are at any time downgraded below "AA-" (or the equivalent thereof) or, with respect to a corporate bond rated "AA-" (or the equivalent thereof), such corporate bond is placed on negative credit watch. Corporate bonds are not an eligible investment for a public funds investment pool. To invest in corporate bonds, an eligible school district must first (i) amend its investment policy to authorize corporate bonds as an eligible investment, (ii) adopt procedures for monitoring rating changes in corporate bonds and liquidating an investment in corporate bonds, and (iii) identify funds eligible to be invested in corporate bonds. As of the date of this Official Statement, the District has taken no such steps with respect to investment in corporate bonds, nor does it currently intend to do so.

INVESTMENT POLICIES . . . Under Texas law, the District 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 includes a list of authorized investments for District funds, maximum allowable stated maturity of any individual investment, the maximum average dollar-weighted maturity allowed for pooled fund groups, methods to monitor the market price of investments acquired with public funds, a requirement for settlement of all transactions, except investment pool funds and mutual funds, on a delivery versus payment basis, and procedures to monitor rating changes in investments acquired with public funds and the liquidation of such investments consistent with the PFIA. All District funds must be invested consistent with a formally adopted "Investment Strategy Statement" that specifically addresses each funds' 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, District 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 District shall submit an investment report detailing: (1) the investment position of the District, (2) that all investment officers jointly prepared and signed the report, (3) the beginning market value, the ending market value and the fully accrued interest during the reporting period of each pooled fund group, (4) the book value and market value of each separately listed asset at the 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 District funds without express written authority from the Board of Trustees.

ADDITIONAL PROVISIONS . . . Under Texas law, the District is additionally required to: (1) annually review its adopted policies and strategies, (2) adopt a rule, order, ordinance or resolution stating that it has reviewed its investment policy and investment strategies and records any changes made to either its investment policy or investment strategy in the respective rule, order, ordinance or resolution, (3) require any investment officers with personal business relationships or relatives with firms seeking to sell securities to the District to disclose the relationship and file a statement with the Texas Ethics Commission and the Board of Trustees; (4) require the qualified representative of firms offering to engage in an investment transaction with the District to: (a) receive and review the District's investment policy, (b) acknowledge that reasonable controls and procedures have been implemented to preclude investment transactions conducted between the District and the business organization that are not authorized by the District's investment policy (except to the extent that this authorization is dependent on an analysis of the makeup of the District's entire portfolio or requires an interpretation of subjective investment standards), and (c) deliver a written statement in a form acceptable to the District and the business organization attesting to these requirements; (5) perform an annual audit of the management controls on investments and adherence to the District's investment policy; (6) provide specific investment training for the Treasurer, Chief Financial Officer and investment officers; (7) 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 purchase agreement; (8) restrict the investment in no-load mutual funds in the aggregate to no more than 15% of the District's monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service; (9) require local government investment pools to conform to the new disclosure, rating, net asset value, yield calculation, and advisory board requirements, and (10) at least annually review, revise, and adopt a list of qualified brokers that are authorized to engage in investment transactions with the District.

TABLE 12 - CURRENT INVESTMENTS

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

Investment	Percent	Market Value
TexSTAR [(1)]	1.68%	$ 3,623,970
TexPool [(1)]	1.22%	2,636,314
LOGIC	78.58%	169,630,654
Securities	18.52%	39,978,274
	100.00%	$ 215,869,212

(1) A portion of the District's investments are invested in TexSTAR and TexPool, each of which is an investment pool that has an investment objective of achieving and maintaining a stable net asset value of $1.00 per share. Daily investment or redemption of funds is allowed by the participants. TexStar is a local government investment pool for which First Southwest Asset Management, Inc., an affiliate of First Southwest Company, the District's financial advisor, provides customer service and marketing.

TAX MATTERS

OPINION...On the date of initial delivery of the Bonds, McCall, Parkhurst & Horton L.L.P., Dallas, Texas, Bond Counsel to the District, will render its opinion that, in accordance with statutes, regulations, published rulings and court decisions existing on the date thereof ("Existing Law"), (1) interest on the Bonds for federal income tax purposes will be excludable from the "gross income" of the holders thereof and (2) the Bonds will not be treated as "specified private activity bonds" the interest on which would be included as an alternative minimum tax preference item under section 57(a)(5) of the Internal Revenue Code of 1986 (the "Code"). Except as stated above, Bond Counsel will express no opinion as to any other federal, state or local tax consequences of the purchase, ownership or disposition of the Bonds. See "Appendix C - Form of Bond Counsel's Opinion."

In rendering its opinion, Bond Counsel will rely upon (a) certain information and representations of the District, including information and representations contained in the District's federal tax certificate, (b) covenants of the District contained in the Bond documents relating to certain matters, including arbitrage and the use of the proceeds of the Bonds and the Refunded Bonds and the property financed or refinanced therewith, (c) the certificate with respect to arbitrage by the Commissioner of Education regarding the allocation and investment of certain investments in the Permanent School Fund, and (d) the verification report prepared by Grant Thornton LLP. Failure by the District to observe the aforementioned representations or covenants could cause the interest on the Bonds to become taxable retroactively to the date of issuance.

The Code and the regulations promulgated thereunder contain a number of requirements that must be satisfied subsequent to the issuance of the Bonds in order for interest on the Bonds to be, and to remain, excludable from gross income for federal income tax purposes. Failure to comply with such requirements may cause interest on the Bonds to be included in gross income retroactively to the date of issuance of the Bonds. The opinion of Bond Counsel is conditioned on compliance by the Issuer with such requirements, and Bond Counsel has not been retained to monitor compliance with these requirements subsequent to the issuance of the Bonds.

Bond Counsel's opinion represents its legal judgment based upon its review of Existing Law and the reliance on the aforementioned information, representations and covenants. Bond Counsel's opinion is not a guarantee of a result. Existing Law is subject to change by the Congress and to subsequent judicial and administrative interpretation by the courts and the Department of the Treasury. There can be no assurance that Existing Law or the interpretation thereof will not be changed in a manner which would adversely affect the tax treatment of the purchase, ownership or disposition of the Bonds.

A ruling was not sought from the Internal Revenue Service by the Issuer with respect to the Bonds or the property financed or refinanced with proceeds of the Bonds or the Refunded Bonds. No assurances can be given as to whether the Internal Revenue Service will commence an audit of the Bonds. Bond Counsel's opinion is not binding on the Internal Revenue Service. If an Internal Revenue Service audit is commenced, under current procedures the Internal Revenue Service is likely to treat the Issuer as the taxpayer and the Bondholders may have no right to participate in such procedure. No additional interest will be paid upon any determination of taxability.

FEDERAL INCOME TAX ACCOUNTING TREATMENT OF ORIGINAL ISSUE DISCOUNT...The initial public offering price to be paid for one or more maturities of the Bonds may be less than the maturity amount thereof or one or more periods for the payment of interest on the bonds may not be equal to the accrual period or be in excess of one year (the "Original Issue Discount Bonds"). In such event, the difference between (i) the "stated redemption price at maturity" of each Original Issue Discount Bond, and (ii) the initial offering price to the public of such Original Issue Discount Bond would constitute original issue discount. The "stated redemption price at maturity" means the sum of all payments to be made on the bonds less the amount of all periodic interest payments. Periodic interest payments are payments which are made during equal accrual periods (or during any unequal period if it is the initial or final period) and which are made during accrual periods which do not exceed one year.

Under Existing Law, any owner who has purchased such Original Issue Discount Bond in the initial public offering 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 Bond equal to that portion of the amount of such original issue discount allocable to the accrual period. For a discussion of certain collateral federal tax consequences, see the discussion set forth below.

In the event of the redemption, sale or other taxable disposition of such Original Issue Discount Bond prior to stated maturity, however, the amount realized by such owner in excess of the basis of such Original Issue Discount Bond 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 Bond was held by such initial owner) is includable in gross income.

Under Existing Law, the original issue discount on each Original Issue Discount Bond is accrued 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 Bonds 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 Bond 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 (a) 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 (b) the amounts payable as current interest during such accrual period on such Original Issue Discount Bond.

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

COLLATERAL FEDERAL INCOME TAX CONSEQUENCES...The following discussion is a summary of certain collateral federal income tax consequences resulting from the purchase, ownership or disposition of the Bonds. This discussion is based on existing statutes, regulations, published rulings and court decisions, all of which are subject to change or modification, retroactively.

The following discussion is applicable to investors, other than those who are subject to special provisions of the Code, such as financial institutions, property and casualty insurance companies, life insurance companies, individual recipients of Social Security or Railroad Retirement benefits, individuals allowed an earned income credit, certain S corporations with accumulated earnings and profits and excess passive investment income, foreign corporations subject to the branch profits tax and taxpayers who may be deemed to have incurred or continued indebtedness to purchase tax-exempt obligations.

THE DISCUSSION CONTAINED HEREIN MAY NOT BE EXHAUSTIVE. INVESTORS, INCLUDING THOSE WHO ARE SUBJECT TO SPECIAL PROVISIONS OF THE CODE, SHOULD CONSULT THEIR OWN TAX ADVISORS AS TO THE TAX TREATMENT WHICH MAY BE ANTICIPATED TO RESULT FROM THE PURCHASE, OWNERSHIP AND DISPOSITION OF TAX-EXEMPT OBLIGATIONS BEFORE DETERMINING WHETHER TO PURCHASE THE BONDS.

Interest on the Bonds will be includable as an adjustment for "adjusted current earnings" to calculate the alternative minimum tax imposed on corporations by section 55 of the Code.

Under section 6012 of the Code, holders of tax-exempt obligations, such as the Bonds, may be required to disclose interest received or accrued during each taxable year on their returns of federal income taxation.

Section 1276 of the Code provides for ordinary income tax treatment of gain recognized upon the disposition of a tax-exempt obligation, such as the Bonds, if such obligation was acquired at a "market discount" and if the fixed maturity of such obligation is equal to, or exceeds, one year from the date of issue. Such treatment applies to "market discount bonds" to the extent such gain does not exceed the accrued market discount of such bonds; although for this purpose, a de minimis amount of market discount is ignored. A "market discount bond" is one which is acquired by the holder at a purchase price which is less than the stated redemption price at maturity or, in the case of a bond issued at an original issue discount, the "revised issue price" (i.e., the issue price plus accrued original issue discount). The "accrued market discount" is the amount which bears the same ratio to the market discount as the number of days during which the holder holds the obligation bears to the number of days between the acquisition date and the final maturity date.

FUTURE AND PROPOSED LEGISLATION…Tax legislation, administrative actions taken by tax authorities, or court decisions, whether at the Federal or state level, may adversely affect the tax-exempt status of interest on the Bonds under Federal or state law and could affect the market price or marketability of the Bonds. Any such proposal could limit the value of certain deductions and exclusions, including the exclusion for tax-exempt interest. The likelihood of any such proposal being enacted cannot be predicted. Prospective purchasers of the Bonds should consult their own tax advisors regarding the foregoing matters.

STATE, LOCAL AND FOREIGN TAXES...Investors should consult their own tax advisors concerning the tax implications of the purchase, ownership or disposition of the Bonds under applicable state or local laws. Foreign investors should also consult their own tax advisors regarding the tax consequences unique to investors who are not United States persons.

CONTINUING DISCLOSURE INFORMATION

In the Order, the District has made the following agreement for the benefit of the holders and beneficial owners of the Bonds. The District is required to observe the agreement for so long as it remains obligated to advance funds to pay the Bonds. Under the agreement, the District will be obligated to provide certain updated financial information and operating data annually, and timely notice of certain specified events, to the Municipal Securities Rulemaking Board (the "MSRB"). See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" for a description of the TEA's continuing disclosure undertaking to provide certain updated financial information and operating data annually with respect to the Permanent School Fund and the State of Texas, as the case may be, and to provide timely notice of certain specified events related to the guarantee to the MSRB.

ANNUAL REPORTS . . . The District will provide certain updated financial information and operating data to the MSRB annually. The information to be updated includes all quantitative financial information and operating data with respect to the District of the general type included in this Official Statement under Tables numbered 1 through 5 and 7 through 12 and in Appendix B. The District will update and provide this information within six months after the end of each fiscal year ending in and after 2013. The District will provide the updated information to the MSRB in electronic format, which will be available to the public free of charge via the Electronic Municipal Market Access ("EMMA") system at www.emma.msrb.org.

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 District commissions an audit and it is completed by the required time. If audited financial statements are not available by the required time, the District will provide unaudited financial information of the type described in the preceding paragraph by the required time and will provide 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 District may be required to employ from time to time pursuant to State law or regulation.

The District's current fiscal year end is August 31. Accordingly, it must provide updated information by the last day of February in each year following the end of its fiscal year, unless the District changes its fiscal year. If the District changes its fiscal year, it will notify the MSRB of the change.

NOTICE OF CERTAIN EVENTS . . . The District will also provide timely notices of certain events to the MSRB. The District will provide notice of any of the following events with respect to the Bonds 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 status of the Bonds, or other material events affecting the tax status of the Bonds; (7) modifications to rights of holders of the Bonds, if material; (8) Bond calls, if material, and tender offers; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the Bonds, if material; (11) rating changes; (12) bankruptcy, insolvency, receivership, or similar event of the District, which shall occur as described below; (13) the consummation of a merger, consolidation, or acquisition involving the District 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 District will provide timely notice of any failure by the District to provide annual financial information in accordance with their agreement described above under "Annual Reports".

For these purposes, any event described in clause (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 District 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 District, 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 District.

Availability of Information from MSRB . . . The District has agreed to provide the foregoing information only as described above. Investors will be able to access continuing disclosure information filed with the MSRB free of charge at www.emma.msrb.org.

Limitations and Amendments . . . The District has agreed to update information and to provide notices of certain specified events only as described above. The District 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 District makes no representation or warranty concerning such information or concerning its usefulness to a decision to invest in or sell the Bonds at any future date. The District 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 and beneficial owners of the Bonds may seek a writ of mandamus to compel the District to comply with its agreement.

The District may amend its continuing disclosure agreement 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 District, if (1) the agreement, as amended would have permitted an underwriter to purchase or sell the Bonds in the offering made hereby in compliance with the Rule, taking into account any amendments or interpretations of the Rule since such offering as well as such changed circumstances, and (2) either (a) the registered owners of a majority in aggregate principal amount (or any greater amount required by any other provisions of the Order that authorizes such amendment) of the outstanding Bonds consent to such amendment or (b) a person that is unaffiliated with the District (such as nationally recognized bond counsel) determined that such amendment will not materially impair the interest of the registered owners and beneficial owners of the Bonds. The District may also amend or repeal the provisions of this continuing disclosure agreement if the SEC amends or repeals the applicable provisions of the Rule or a court of final jurisdiction enters judgment that such provisions of the Rule 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 Bonds in the primary offering of the Bonds. If the District amends its agreement, it must include with the next financial information and operating data provided in accordance with its agreement described above under "Annual Reports" an explanation, in narrative form, of the reasons for the amendment and of the impact of any change in type of information and data provided.

Compliance with Prior Undertakings... During the last five years, the District has complied in all material respects with all continuing disclosure agreements made by it in accordance with the Rule.

OTHER INFORMATION

Ratings

The presently outstanding tax supported debt of the District is rated "Aa2" by Moody's Investors Service, Inc. ("Moody's") and "AA" by Standard & Poor's Ratings Services, a Standard & Poor's Financial Services LLC business ("S&P") without regard to credit enhancement. The District also has issues outstanding which are rated "Aaa" by Moody's and "AAA" by S&P by virtue of the guarantee of the Permanent School Fund of the State of Texas. Applications for contract ratings on the Bonds have been made to Moody's and S&P. An explanation of the significance of any rating may be obtained from the company furnishing the rating. Each rating reflects only the respective view of such organization and the District makes no representation as to the appropriateness of the rating. There is no assurance that any rating will continue for any given period of time or that it will not be revised downward or withdrawn entirely by such rating company, if in the judgment such company, circumstances so warrant. Any such downward revision or withdrawal of a rating may have an adverse effect on the market price of the Bonds.

Litigation

The District is not a party to any litigation or other proceeding pending or, to its knowledge, threatened, in any court, agency or other administrative body (either state or federal) which, if decided adversely to the District, would have a material adverse effect on the financial condition of the District.

At the time of the initial delivery of the Bonds, the District will provide the Underwriters with a certificate to the effect that no litigation of any nature has been filed or is then pending challenging the issuance of the Bonds or that affects the payment and security of the Bonds or in any other manner questioning the issuance, sale or delivery of the Bonds.

Registration and Qualification of Bonds for Sale

The sale of the Bonds 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 Bonds have not been qualified under the Securities Act of Texas in reliance upon various exemptions contained therein; nor have the Bonds been qualified under the securities acts of any jurisdiction. The District assumes no responsibility for qualification of the Bonds under the securities laws of any jurisdiction in which the Bonds may be sold, assigned, pledged, hypothecated or otherwise transferred. This disclaimer of responsibility for qualification for sale or other disposition of the Bonds 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) provides that the Bonds are negotiable instruments, investment securities governed by Chapter 8, Texas Business and Commerce Code, 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. In addition, various provisions of the Texas Finance Code provide that, subject to a prudent investor standard, the Bonds are legal investments for state banks, savings banks, trust companies with at least $1 million of capital, and savings and loan associations. In accordance with the Public Funds Investment Act, Chapter 2256, Texas Government Code, the Bonds must be rated not less than "A" or its equivalent as to investment quality by a national rating agency in order for most municipalities or other political subdivisions or public agencies of the State of Texas to be authorized to invest in the Bonds, except for purchases for interest and sinking funds of such entities. See "OTHER INFORMATION -- Ratings" herein. Moreover, municipalities or other political subdivisions or public agencies of the State of Texas that have adopted investment policies and guidelines in accordance with the Public Funds Investment Act may have other, more stringent requirements for purchasing securities, including the Bonds. The Bonds 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.

The District has made no investigation of other laws, rules, regulations or investment criteria which might apply to such institutions or entities or which might limit the suitability of the Bonds for any of the foregoing purposes or limit the authority of such institutions or entities to purchase or invest in the Bonds for such purposes. The District has made no review of laws in other states to determine whether the Bonds are legal investments for various institutions in those states.

LEGAL MATTERS

The District will furnish the Underwriters a complete transcript of proceedings had incident to the authorization and issuance of the Bonds, including the unqualified approving legal opinion of the Attorney General of Texas as to the Bonds to the effect that the Bonds are valid and legally binding obligations of the District, and based upon examination of such transcript of proceedings, the approving legal opinion of Bond Counsel to the District to like effect and to the effect that the interest on the Bonds will be excludable from gross income for federal income tax purposes under Section 103(a) of the Code, subject to the matters described under "TAX MATTERS" herein, a form of which opinion is attached to this Official Statement as Appendix C. Though it represents the Financial Advisor and the Underwriters from time to time in matters unrelated to the issuance of the Bonds, Bond Counsel has been engaged by and only represents the District in connection with the issuance of the Bonds. Bond Counsel also advises the TEA in connection with its disclosure obligations under the Federal securities laws, but Bond Counsel has not passed upon any TEA disclosures contained in this Official Statement. The customary closing papers, including a certificate to the effect that no litigation of any nature has been filed or is then pending to restrain the issuance and delivery of the Bonds which would affect the provision made for their payment or security, or in any manner questioning the validity of said Bonds will also be furnished. Bond Counsel was not requested to participate, and did not take part, in the preparation of the Official Statement, and such firm has not assumed any responsibility with respect thereto or undertaken independently to verify any of the information contained therein, except that, in its capacity as Bond Counsel, such firm has reviewed the information under the captions and subcaptions "PLAN OF FINANCING" (excluding the information under the subcaption "Sources and Uses of Proceeds"), "THE BONDS" (excluding the information under the subcaptions "Permanent School Fund Guarantee", "Book-Entry-Only System", "Yield on Premium Capital Appreciation Bonds" and "Bondholders' Remedies"), "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS", "CURRENT PUBLIC SCHOOL FINANCE SYSTEM" (excluding the information under the subcaption "The School Finance System as Applied to the District"), "TAX INFORMATION - Tax Rate Limitations" (first paragraph only), "TAX MATTERS", "CONTINUING DISCLOSURE INFORMATION" (excluding the information under the subcaption "Compliance with Prior Undertakings"), "OTHER INFORMATION - Registration and Qualification of Bonds for Sale", "OTHER INFORMATION - Legal Investments and Eligibility to Secure Public Funds in Texas", and "OTHER INFORMATION - Legal Matters" (excluding the last sentence of the first paragraph thereof) in the Official Statement and such firm is of the opinion that the information relating to the Bonds and the legal issues contained under such captions and subcaptions is an accurate and fair description of the laws and legal issues addressed therein and, with respect to the Bonds, such information conforms to the provisions of the Order. The legal fee to be paid Bond Counsel for services rendered in connection with the issuance of the Bonds is contingent upon the sale and delivery of the Bonds. Certain legal matters will be passed upon for the Underwriters by Fulbright & Jaworski L.L.P., Dallas, Texas, Counsel to the Underwriters, whose legal fees are contingent upon the sale and delivery of the Bonds.

The legal opinions to be delivered concurrently with the delivery of the Bonds 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 that 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.

FINANCIAL ADVISOR

First Southwest Company is employed as Financial Advisor to the District in connection with the issuance of the Bonds. The Financial Advisor's fee for services rendered with respect to the sale of the Bonds is contingent upon the issuance and delivery of the Bonds. First Southwest Company, in its capacity as Financial Advisor, has not verified and 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 Bonds, or the possible impact of any present, pending or future actions taken by any legislative or judicial bodies.

The Financial Advisor to the District 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 District 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.

The ultimate parent of First Southwest Company is Hilltop Holdings Inc. ("Hilltop"). On July 11, 2009, Hilltop extended a $50 million term loan to SWS Group, Inc. ("SWSG"), which is the parent company of Southwest Securities, an investment banking firm that provides financial advisory and underwriting services to municipal issuers and also serves as an underwriter on this transaction. In connection with the term loan, SWSG issued a warrant to Hilltop to purchase 8,695,652 shares of SWSG common stock (the "Warrant"), subject to anti-dilution adjustments, which if fully exercised, would represent approximately a 17% equity interest in SWSG, in addition to any shares of SWSG common stock purchased by Hilltop in open market and block transactions. Additionally, Mr. Gerald J. Ford, the Chairman of the Board of Directors of Hilltop, was appointed as a member of the Board of Directors of SWSG. The specific terms of the loan transaction and Hilltop's beneficial ownership interest in SWSG are summarized in Hilltop's public filings, which may be found at www.sec.gov.

UNDERWRITING

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

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

VERIFICATION OF ARITHMETICAL AND MATHEMATICAL COMPUTATIONS

Grant Thornton LLP, a firm of independent public accountants, will deliver to the District, on or before the settlement date of the Bonds, its verification report indicating that it has verified, in accordance with attestation standards established by the American Institute of Certified Public Accountants, the mathematical accuracy of (a) the mathematical computations of the adequacy of the cash and the maturing principal of and interest on the Federal Securities, to pay, when due, the maturing principal of, interest on and related call premium requirements, if any, of the Refunded Bonds and (b) the mathematical computations of yield used by Bond Counsel to support its opinion that interest on the Bonds will be excluded from gross income for federal income tax purposes.

The verification performed by Grant Thornton LLP will be solely based upon data, information and documents provided to Grant Thornton LLP by First Southwest Company on behalf of the District. Grant Thornton LLP has restricted its procedures to recalculating the computations provided by First Southwest Company on behalf of the District and has not evaluated or examined the assumptions or information used in the computations.

FORWARD-LOOKING STATEMENTS DISCLAIMER

The statements contained in this Official Statement, and in any other information provided by the District, that are not purely historical, are forward-looking statements, including statements regarding the District'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 District on the date hereof, and the District assumes no obligation to update any such forward-looking statements. The District'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 District. 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.

MISCELLANEOUS

The financial data and other information contained herein have been obtained from the District'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 orders contained in this Official Statement are made subject to all of the provisions of such statutes, documents and orders. These summaries do not purport to be complete statements of such provisions and reference is made to such statutes, documents and orders for further information. Reference is made to original documents in all respects.

The Order authorizes the Pricing Officer to approve the form and content of this Official Statement, and any addenda, supplement or amendment thereto, and authorize its use in the reoffering of the Bonds by the Underwriters.

____

Pricing Officer
Keller Independent School District

SCHEDULE I

SCHEDULE OF REFUNDED BONDS*

Keller Independent School District
Unlimited Tax School Building and Refunding Bonds, Series 2005

Original Dated Date	Original Maturity (8/15)	Interest Rates	Principal Amount Outstanding	Principal Amount Refunded	Principal Amount Remaining
June 15, 2005	2014	5.000%	$ 1,795,000	$ 1,465,000	$ 330,000
	2015	5.000%	2,700,000	1,825,000	875,000
	2016	5.000%	2,985,000	2,370,000	615,000
	2017	5.000%	3,875,000	3,160,000	715,000
	2018	5.000%	4,130,000	3,365,000	765,000
	2019	4.000%	3,625,000	2,955,000	670,000
	2020	4.125%	4,165,000	3,395,000	770,000
	2021	4.200%	4,480,000	3,650,000	830,000
	2022	4.250%	5,080,000	4,140,000	940,000
	2023	5.000%	5,705,000	4,650,000	1,055,000
	2024	5.000%	12,620,000	10,285,000	2,335,000
	2025	5.000%	13,675,000	11,145,000	2,530,000
	2026	5.000%	3,920,000	2,450,000	1,470,000
	2027	5.000%	8,380,000	6,830,000	1,550,000
	2028	4.550%	9,230,000	7,520,000	1,710,000
	2029 (1)	5.000%	9,330,000	7,605,000	1,725,000
	2030 (1)	5.000%	9,795,000	7,980,000	1,815,000

The 2014 and 2015 maturities are being defeased to maturity and will be paid on their stated maturity dates.*
The 2016 through 2030 maturities are expected to be redeemed on August 15, 2015.*

(1) Represents mandatory sinking fund redemption amount of term bonds with a stated maturity of August 15, 2030.

* Preliminary, subject to change.

SCHEDULE II

SCHEDULE OF ACCRETED VALUES OF PREMIUM CAPITAL APPRECIATION BONDS*

Accretion Dates	Maturing 8/15/2013	Maturing 8/15/2016	Maturing 8/15/2017
3/28/2013	$	$	$
8/15/2013			
2/15/2014			
8/15/2014			
2/15/2015			
8/15/2015			
2/15/2016			
8/15/2016			
2/15/2017			
8/15/2017			

* Preliminary, subject to change.

APPENDIX A

GENERAL INFORMATION REGARDING THE DISTRICT

THE DISTRICT . . . Keller Independent School District (the "District") is located in the northeast portion of Tarrant County. The northern portion of Fort Worth lies within the boundaries of the District. The commercial, industrial, and residential growth of the District has kept pace with that of the Fort Worth/Dallas area, and has been aided by the District's close proximity to both the Dallas/Fort Worth International Airport and Fort Worth's Alliance Airport.

The District is governed by an elected Board of Trustees (the "Board") comprised of seven members serving three year staggered terms. Elections are held every year in on the first Saturday of May. The Board is charged with policy-making and supervisory functions and delegates administrative responsibilities to a superintendent who is the chief administrative officer of the District. Certain support services are supplied by consultants and advisors.

Modern school facilities provided by the District are capable of housing over 43,755 students from kindergarten through twelfth grade. Enrollment in Keller ISD has doubled during the past 10 years and is expected to plateau in the next 8-10 years at 40,000 students as the area within the District reaches full development.

The physical facilities of the District include:

4	High schools (9-12)
6	Middle schools (7-8)
5	Intermediate schools (5-6)
22	Elementary schools (K-4)
1	Early Learning (Pre-K)
1	Alternative Education (9-12)

Teacher/Student Ratio for 2010/12 is: 1 teacher/17.41 students

All of the buildings are centrally heated and air-conditioned and are under a continuous maintenance program.

For the current school year, the District projects to employ a staff of approximately 3,430 which includes professional staff of approximately 2,356. Projected personnel distribution within the District is as follows:

Total District Personnel	
Administrators	173
Teachers	1,922
Support Personnel-Certified	261
Clerks and Aides	500
Maintenance and Custodians	297
Food Service Workers	256
Other	21
Total	3,430

HISTORICAL ENROLLMENT

Fiscal		Increase/Decrease	
Year	Enrollment	Actual	Percent
1993/94	9,716	625	6.87%
1994/95	10,973	1,257	12.94%
1995/96	11,882	909	8.28%
1996/97	12,572	690	5.81%
1997/98	13,635	1,063	8.46%
1998/99	14,711	1,076	7.89%
1999/00	15,823	1,112	7.56%
2000/01	17,081	1,258	7.95%
2001/02	18,407	1,326	7.76%
2002/03	20,032	1,625	8.83%
2003/04	21,785	1,753	8.75%
2004/05	23,747	1,962	9.01%
2005/06	25,890	2,143	9.02%
2006/07	27,905	2,015	7.78%
2007/08	29,458	1,553	5.57%
2008/09	30,299	841	2.85%
2009/10	31,593	1,294	4.27%
2010/11	32,557	964	3.05%
2011/12 (1)	33,190	633	1.94%
2012/13 (2)	33,367	177	0.53%

(1) As of the end of academic year.
(2) As of October 26, 2012.

PRESENT SCHOOL AVAILABILITY

Name of School	Capacity	Enrollment Average 2010/11 School Year	Enrollment for 2011/12 School Year	Teachers for 2011/12 School Year	Support Personnel [1] 2011/12 School Year	Para-Professional Personnel 2011/12 School Year
Central High	2,940	2,546	2,454	126	12	61
Fossil Ridge High	2,915	2,196	2,166	115	15	56
Keller High	2,947	2,723	2,597	131	11	58
Timber Creek High	2,620	1,557	2,191	106	12	58
Learning Center	100	42	60	16	2	5
Fossil Hill Middle	1,225	885	906	56	5	25
Hillwood Middle	1,350	1,177	1,167	61	5	29
Indian Springs Middle	1,255	907	887	52	7	29
Keller Middle	1,205	827	851	49	4	23
Trinity Springs Middle	1,025	834	968	55	5	25
Timberview Middle	1,445	949	1,038	61	7	27
Bear Creek Intermediate	1,200	824	837	45	5	21
Chisholm Trail Intermediate	1,475	888	943	51	6	27
Parkwood Hill Intermediate	1,500	1,171	1,147	57	6	28
South Keller Intermediate	1,475	858	862	48	6	23
Trinity Meadows Intermediate	1,500	973	1,012	54	8	24
Basswood Elementary	528	364	373	27	6	13
Bette Perot Elementary	836	716	703	42	4	20
Bluebonnet Elementary	902	639	585	37	5	18
Caprock Elementary	770	604	630	44	4	18
Eagle Ridge Elementary	814	726	755	44	6	16
Florence Elementary	748	534	551	35	5	14
Freedom Elementary	748	524	509	32	4	13
Friendship Elementary	814	679	546	36	5	15
Heritage Elementary	726	614	599	38	5	17
Hidden Lakes Elementary	836	698	569	36	7	16
Independence Elementary	858	739	537	33	4	15
Keller Harvel Elementary	858	470	470	30	4	12
Liberty Elementary	638	495	484	31	4	12
Lone Star Elementary	814	735	727	40	4	15
North Riverside Elementary	726	613	568	45	5	16
Park Glen Elementary	726	529	605	35	5	16
Parkview Elementary	836	636	646	46	6	15
Ridgeview Elementary	858	0	434	27	4	11
Shady Grove Elementary	726	533	507	33	8	14
Whitley Road Elementary	682	484	493	33	5	14
Willis Lane Elementary	814	542	551	35	8	17
Woodland Springs Elementary	770	691	595	36	5	16
Early Learning Center	550	635	667	28	16	37
Total	43,755	32,557	33,190	1,906	245	889

(1) Support personnel consists of counselors, diagnosticians, librarians, nurses, physical & occupational therapists, and psychologists.

HISTORICAL EMPLOYMENT DATA (ANNUAL AVERAGE DATA)

	Annual Averages				
	2012 [1]	2011	2010	2009	2008
Tarrant County					
Civilian Labor Force	941,858	934,168	920,160	900,629	880,023
Total Employment	876,309	861,103	844,278	832,041	836,948
Unemployment	65,549	73,065	75,882	68,588	43,075
Percent Unemployment	7.0%	7.8%	8.2%	7.6%	4.9%
State of Texas					
Civilian Labor Force	12,555,694	12,451,504	12,269,727	11,968,199	11,653,877
Total Employment	11,662,069	11,464,525	11,264,748	11,071,106	11,079,931
Unemployment	893,625	986,979	1,004,979	897,093	573,946
Percent Unemployment	7.1%	7.9%	8.2%	7.5%	4.9%

(1) Data shown through November, 2012.

Source: Texas Workforce Commission.

APPENDIX B

EXCERPTS FROM THE

KELLER INDEPENDENT SCHOOL DISTRICT

ANNUAL FINANCIAL REPORT

For the Year Ended August 31, 2012

The information contained in this Appendix consists of excerpts from the Keller Independent School District Annual Financial Report for the Year Ended August 31, 2012, and is not intended to be a complete statement of the District's financial condition. Reference is made to the complete Report for further information.

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Keller Independent School District
Keller, Texas

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Keller Independent School District (the District) as of and for the year ended August 31, 2012, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District'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, each major fund, and the aggregate remaining fund information of the District as of August 31, 2012 and the respective changes in financial position and cash flows, where applicable, thereof 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 18, 2013, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted by the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 12 and 52 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 principally of inquiries of management about the methods of measurement and presentation of the required supplementary information for consistency with management's responses to the inquiries, the basic financial statements and other knowledge we obtained during our audit of the basic financial statements. We do not express and 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 District's financial statements. The accompanying introductory section, combining and individual nonmajor fund financial statements, the required TEA schedules and statistical section on pages 54 through 94 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 individual nonmajor fund financial statements, the required TEA schedules on pages 54 through 66 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 combining and individual nonmajor fund financial statements, the additional financial information on pages 67 through 93 and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the financial statements as a whole. The introductory and statistical sections are presented for the purposes of additional analysis and are not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Weaver and Tidwell, L.L.P.

Fort Worth, Texas
January 18, 2013

Keller Independent School District
Management's Discussion and Analysis
Year Ended August 31, 2012

This section is the Keller Independent School District (District) management discussion and analysis of the annual financial report for the period ending August 31, 2012. It should be read in conjunction with the transmittal letter and the District's financial statements which follow this section.

FINANCIAL HIGHLIGHTS

- The District had approximately $284 million in expenses related to governmental activities, which is a decrease of ($12) million from the prior year; of which $42.2 million of these expenses were offset by program-specific charges for services or grants and contributions. General revenues of $263.4 million partially offset the costs of these programs, resulting in a $21.6 million increase in net assets. Expenses for governmental activities decreased by approximately ($12) million, or (4.07%), from the previous year. This reduction in expenses was due mainly to a series of budget reductions enacted in response to prevailing economic conditions as well as reduced state funding. Expenses for capital projects declined in 2012 as the majority of construction projects were completed.

- General revenues accounted for $263,464,367, or 86.2% of all fiscal year 2012 revenues. Program-specific revenues in the form of charges for services and grants and contributions accounted for $42,230,313 or 13.8% of total fiscal year 2012 revenues. The 2012 charges for services and grants and contributions represent an ($8,681,173) or (17%) decrease from 2011. The reduction in these revenues was due primarily to the loss of stimulus funding as those programs ended.

- At August 31, 2012, the District's assets exceeded its liabilities by $13,987,655 (Net Assets). Unrestricted Net Assets totaled $50,167,324.

- At the close of the fiscal year the combined governmental fund balance was $135,190,813, an increase of $12,111,511 from the prior year. This increase occurred mainly in the General Fund, due mostly to a significant decrease in expenditures and approximately $5 million in additional property tax revenue. The General Fund unassigned fund balance increased by $15,583,536. Assignments of fund balance total $2.2 million and include athletic turf ($440,000), student transportation ($1,025,000), the athletic long term plan ($202,000) and the fine arts long term plan ($566,000). In addition, fund balance equal to 20% of the 2013 general fund expenditure budget has been committed, as per Board policy.

- The District's total long term liabilities decreased by ($24,022,260), or (3.04%), from the previous fiscal year. The key factors in this increase were debt maturities and a bond refunding that occurred on April 15, 2012.

- General Fund expenditures decreased by ($6.8) million or (3.32%) from the prior year. The decrease is mainly due to the budget reductions approved by the Board of Trustees in the 2012 budget. Again, the budget reductions were necessary to offset reduced state funding and lower expected property values due to the prevailing economic conditions. In addition, $8.6 million in federally funded stimulus funds which the district had previously used to offset personnel costs were no longer available. However, the district did receive $4.8 million from the Education Jobs program in 2012 which was used for personnel costs. The expenditures funded by the Education Jobs program are reflected in the Federally Funded Grant Fund, which relieved the general fund of the cost.

OVERVIEW OF THE FINANCIAL STATEMENTS

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

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

The *statement of net assets* presents information on all of the District's assets and liabilities with the difference between the two reported as *net assets*. Over time, increases and decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The *statement of activities* presents information for all of the current year's revenue and expenses regardless of when cash is received or paid. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows for future fiscal periods.

Both of the District's *government-wide financial statements* distinguish the functions of the District as being principally supported by taxes and intergovernmental revenues (*governmental activities*) as opposed to *business-type activities* that are intended to recover all or a significant portion of their costs through user fees and charges.

The government-wide financial statements can be found on pages 13-14 of this report.

Fund Financial Statements- A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related requirements. The *fund financial statements* provide detailed information about the District's most significant funds and not the District as a whole.

All of the funds of the District can be divided into three categories: *governmental funds, proprietary funds,* and *fiduciary funds*.

> ***Governmental fund***- Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus *on near-term inflows and outflows of spendable resources,* as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements. Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.
>
> The basic governmental fund financial statements can be found on pages 15-20 of this report.
>
> ***Proprietary fund***- Proprietary funds offer *short* and *long-term* financial information about the activities the government operates *like businesses*. There are two types of proprietary funds – *enterprise funds* and *internal service funds*. The *enterprise funds* report the same functions presented as *business-type activities* in the *government-wide financial statements*. The district has no enterprise funds. *Internal service funds* are an accounting tool used to accumulate and allocate costs internally among various functions. The District uses *internal service funds* to report activities for its self-funded insurance programs (Workers Compensation and Health Insurance).
>
> The basic proprietary fund financial statements can be found on pages 21-23 of this report.
>
> ***Fiduciary fund***- Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are *not* available to support the District's own programs. The District is the trustee, or fiduciary, for these funds and is responsible for ensuring that the assets reported in these funds are used for their intended purposes.
>
> The basic fiduciary fund financial statement can be found on page 24 of this report.

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

The notes to the financial statements can be found on pages 25-51 of this report.

Other information – In addition to the basic financial statements and accompanying notes, this report also includes certain *required supplementary information* that further explains and supports the financial statements.

Required supplementary information can be found on pages 52-53 of this report.

The combining statements referred to earlier in connection with non-major governmental funds are presented immediately following the required supplementary information.

Combining statements can be found on pages 54-62.

The Texas Education Agency (TEA) requires that certain reports are included in this report.

These statements and schedules can be found on pages 63-66.

Government-wide Financial Statements

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of Keller ISD, assets exceeded liabilities by $13,987,655.

Table A-1

Net Assets

	Governmental Activities		
	2011	2012	Percent Change 2011 to 2012
Current and other assets	$ 157,683,321	$ 158,497,060	0.51%
Capital assets (net)	645,207,590	634,115,342	(1.71%)
Total assets	$ 802,890,911	$ 792,612,402	(1.28%)
Current liabilities	$ 22,569,094	$ 14,691,402	(34.90%)
Long-term liabilities	787,955,605	763,933,345	(3.04%)
Total liabilities	$ 810,524,699	$ 778,624,747	(3.93%)
Net assets:			
Invested in capital assets, net of related debt	$ (38,159,556)	$ (43,992,374)	(15.28%)
Restricted for Food Service	3,573,193	4,604,517	28.86%
Restricted for Debt Service	2,811,717	2,808,188	(0.12%)
Restricted for Employee Health Claims	365,000	400,000	9.58%
Unrestricted Net Assets	23,775,858	50,167,324	111.00%
Total Net Assets	$ (7,633,788)	$ 13,987,655	283.23%

Investment in capital assets (e.g., land, buildings, furniture, and equipment) less any related debt used to acquire those assets that is still outstanding is $(43,992,374). The District uses these capital assets to provide services to students; consequently, these assets are not available for future spending. The increase in Total Net Assets is due primarily to the reduction of long-term debt through annual principal payments and a refunding. Although the District's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

Governmental Activities

Governmental activities increased the District’s net assets by $21,621,443. The total cost of all *governmental activities* this year was $284,073,237. The amount that our taxpayers paid for these activities was $170,418,927 or 59.99%.

Table A-2
Changes in the District's Net Assets

	Governmental Activities		
Revenues:			Percentage Change
Program Revenues:	2011	2012	2011 to 2012
Charges for services	$18,942,250	$18,068,929	(4.61%)
Operating grants & contributions	31,969,236	24,161,384	(24.42%)
General Revenues:			
Property taxes	164,484,171	170,418,927	3.60%
State grants	92,872,674	88,208,113	(5.02%)
Investment earnings	364,742	436,411	19.64%
Other	686,139	4,400,916	541.40%
Total Governmental Revenues	309,319,212	305,694,680	(1.17%)
Expenses:			
Instruction	159,641,776	149,547,022	(6.32%)
Instructional Resources & Media Services	3,743,225	3,506,194	(6.33%)
Curriculum & Instructional Staff Development	2,889,302	2,754,701	(4.65%)
Instructional Leadership	2,269,740	2,091,486	(7.85%)
School Leadership	14,478,924	14,317,804	(1.11%)
Guidance, Counseling & Evaluation Services	10,101,315	10,056,213	(0.44%)
Health and Social Work Services	2,738,173	3,255,217	18.88%
Student (pupil) Transportation	6,808,740	5,448,661	(19.97%)
Food Services	10,974,335	12,085,660	10.12%
Co-Curricular/Extracurricular Activities	8,771,031	7,985,415	(8.95%)
General Administration	5,584,569	8,082,486	44.72%
Plant Maintenance & Operations	14,671,718	18,625,453	26.94%
Security and Monitoring Services	1,675,711	1,299,191	(22.46%)
Data Processing Services	4,380,257	5,227,588	19.34%
Community Services	1,075,017	1,541,352	43.37%
Debt Service-interest on long-term debt	41,249,450	33,103,972	(19.74%)
Shared services agreement	3,329,680	3,410,020	2.41%
Non-operating expenses	1,750,904	1,734,802	(0.91%)
Total Governmental Expenses	296,133,867	284,073,237	(4.07%)
Increase (Decrease) in Net Assets	13,185,345	21,621,443	63.98%
Beginning Net Assets	(20,819,133)	(7,633,788)	63.33%
Ending Net Assets	$(7,633,788)	$13,987,655	283.23%

Property tax revenues are the single largest source of income for the district. Property values increased 3.34% in 2012 from the previous year. Construction of new homes in the District’s 51 square miles is now beginning to moderate after several years of rampant growth. The following graphs depict the District’s sources of revenue for the years 2012 and 2011 as a percentage of total revenues.

Table A-3

Sources of Revenue for Fiscal Year 2012

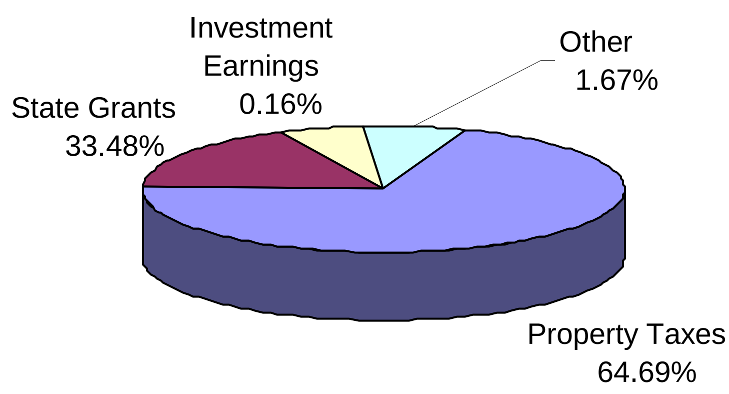

Table A-4

Sources of Revenue for Fiscal Year 2011

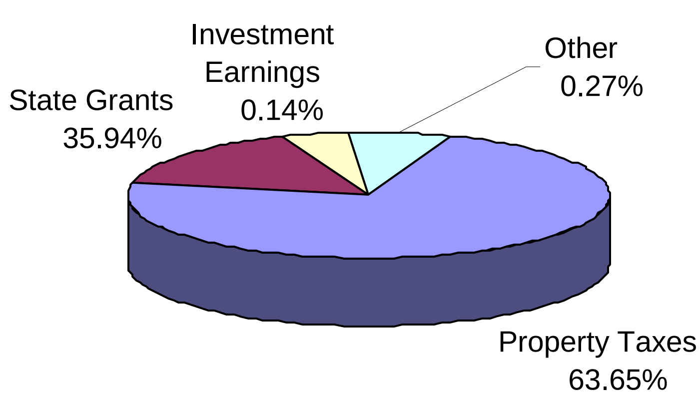

Table A-5 represents the cost of the District's largest programs as well as each program's *net cost* (total cost less fees generated by the activities and intergovernmental aid). The net cost shows the financial burden that was placed on the District's taxpayers by each of these functions. The cost of all *governmental* activities this year was $284,073,237.

Table A-5
Costs of Services

Major Function	Total Cost of Services			Net Cost of Services		
	2011	2012	Percent Change 2011 to 2012	2011	2012	Percent Change 2011 to 2012
Instruction, Curriculum, and Media Services	$166,274,303	$155,807,917	(6.29%)	$137,070,587	$135,607,951	(1.06%)
Instructional and School Leadership	16,748,664	16,409,290	(2.02%)	15,627,665	15,711,846	0.53%
Student Support Services, Child Nutrition, and Co-Curricular Activities	39,393,594	38,831,166	(1.42%)	22,440,460	22,337,267	(0.45%)
General Administration	5,584,569	8,082,486	44.72%	5,187,175	7,793,848	50.25%
Plant Maintenance, Security, and Data Processing	20,727,686	25,152,232	21.34%	19,225,597	23,654,666	23.03%
Community Services	1,075,017	1,541,352	43.37%	271,082	1,392,682	413.74%
Debt Service	41,249,450	33,103,972	(19.74%)	40,610,824	32,051,283	(21.07%)
Shared services agreement	3,329,680	3,410,020	2.41%	3,138,578	3,291,088	4.85%
Non-operating expenses	1,750,904	1,734,802	(0.91%)	1,650,413	2,293	(99.86%)
Total Expenses	$296,133,867	$284,073,237	(4.07%)	$245,222,381	$241,842,924	(1.37%)

Total net expenses decreased (1.37%) in 2012 from the previous year. Net expenses in the General Administration function increased significantly due to a mid-year decision by the Board of Trustees to offset the cost of rising health insurance premiums to the employees by paying the additional cost from the Health Insurance Internal Service fund. The Plant Maintenance, Security and Data Processing function recorded an increase in net expenses of 23.03%, which was due primarily to the addition in 2012 of a contract with Dell Services for managed technology services and to the acquisition of new servers and other technology equipment. Community Services reflected an extremely large percentage increase in net expenses; however, this was the result of the allocation of depreciation expense and of the Internal Service Fund allocation.

Debt Service net expenses decreased by (21.07%) due to the payment of debt and a bond refunding in 2012. The non-operating expenses consist mainly of a payment for the district’s Tax Increment Zone. Since the district is reimbursed for this payment, the net effect to the district is zero. This payment is now reflected differently in Table A-5 to more accurately reflect the inflows and outflows of the function. Thus, for fiscal year 2012 only, the table reflects a large percentage decrease in this function.

FINANCIAL ANALYSIS OF THE DISTRICT'S FUNDS

As noted earlier, the District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements, bond covenants, and segregation for particular purposes.

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

As of the end of the current fiscal year, the District’s governmental funds reported combined ending fund balances of $135,190,813, an increase of $12,111,511. The increase occurred mainly in the general fund, with an increase of $18.8 million. Reasons for this increase are discussed below. The fund balance of the Capital Project funds decreased by ($8.3) million due to construction projects completed during the year. Increases to all other funds were minimal. There were no other decreases of fund balance.

The general fund balance has an unassigned fund balance of $37,287,784. The remainder of fund balance in the general fund and in all other funds is reserved and unavailable for new spending, and has been restricted, committed or assigned as per GASB 54. Non-spendable fund balance consists of inventory ($191,105) and deferred expenditures (519,543). Fund balance is restricted to pay debt service ($3,889,404), for food service ($4,604,517) and for grant funds ($168,943). Commitments of fund balance include $39,757,813 for the capital acquisition program, $3,586,816 for the campus activity fund, and $42,951,888 in the general fund for budgetary contingencies as per Board policy. Fund balance is assigned for repurchase of bus equipment ($1,025,000), for athletic field turf ($440,000), and for the fine arts and athletic long term plans ($768,000).

The general fund is the primary operating fund of the District. At the end of the current fiscal year, unassigned fund balance of the general fund was $37,287,784, while the total fund balance was $82,979,949. As a measure of the general fund's liquidity, it may be useful to compare both unassigned fund balance and total fund balance to the total fund expenditures. Unassigned fund balance represents 18.77% of the total general fund expenditures, while total fund balance represents 41.77% of that same amount. It is important to note that in addition to the unassigned amount of fund balance, KISD Board policy requires that an amount equal to 17-20% of the subsequent year's budget expenditures be committed within fund balance for budgetary contingencies. This amount at 8/31/12 was $42,951,888, and may be used at the discretion of the Board of Trustees.

During the current fiscal year, the fund balance of the District's general fund increased by $18,840,815, compared to an increase in the prior year of $11,812,267. KISD adopted a budget for 2012 that included a general fund surplus, or return to fund balance of $6.6 million. Other key factors for the increase to fund balance in 2012 were the following:

- An additional $4.3 million in property tax revenue was received due to an unexpected change in property values mid-year. Delinquent tax payments, penalties and interest exceeded projections by another $1 million.

- The District was awarded a settlement in a lawsuit over roofing damage from a hail storm. $2.86 million of that settlement was received in the 2012 fiscal year.

- The District also received $1.68 million more than expected in state Foundation and Per Capita revenue. The additional amount consisted of funds resulting from a property value audit, settle-up payments from the state, and adjustments for enrollment fluctuations.

- General fund expenditures declined in 2011-12 because the Board of Trustees, anticipating reduced state funding, adopted a budget for 2012 that included approximately $12 million in budget reductions. When the funding situation later proved not as dire as expected, the Board added back some of the items that had been cut; however, actual expenditures in the General Fund were still $(6.8) million less than the prior year.

General Fund Budgetary Highlights

Over the course of the year, the District revised its budget several times. In accordance with Board Policy CE (Local), the district submits amendments during the course of the budget year to the Board of Trustees for approval. These amendments are presented when a functional category or revenue object is increased.

In addition, at the end of every fiscal year, school districts across the state also make their year-end amended budgets to ensure all functional categories will have favorable balances. If unfavorable functional balances are reported in the audit at the close of the fiscal year, the result is a letter issued by the Texas Education Agency stipulating the legal requirements for budgeting. The District did not exceed the functional budget in any category in the 2011-12 fiscal year.

1. *Variances of original expenditure budget compared to amended budget.* The amended expenditure budget increased $16,552,756 from the original budget. Major budget amendments contributing to this increase include: (1) $6.5 million for TRS on Behalf, (2) $403,125 for a new time clock system, (3) $313,000 for a gifted and talented learning lab, (4) $150,000 to resurface a high school track, (5) $2.3 million for repair of roofs damaged by a severe hail storm, (6) $500,000 for marching band uniforms and athletic uniforms, (7) $1.4 million to offset health insurance premium increases for employees, (8) $450,000 for technology and (9) $610,000 to subsidize the Pay for Ride transportation system

2. *Variances of amended budget to actual expenditures.* For fiscal year 2012, the district received approximately $4.8 million from the Education Jobs Foundation, a federal entity. The funds were budgeted in the general fund. Information received at a later date required that all expenditures for EduJobs be accounted for in a specially identified grant fund. As the grant fund did not require a legally adopted budget, the budget for those expenditures remained in the general fund although the related expenditures can be found in the Federally Funded Grant Fund. As a result, the Instruction function (11) appears to have underspent by $9.79 million, or 7.3% of amended budget.

   In the Facilities Acquisition and Construction function (81), approximately $2.3 million was appropriated mid-year for repairs to various campus roofs that had been damaged in a severe hail storm. The funds were appropriated when the district received $2.8 million as a partial settlement of the insurance claim for the roofs. Although the district anticipated spending the $2.3 million that was appropriated in 2012, the work went more slowly than planned, leaving excess budget in this function. The funds will be re-appropriated in the 2013 fiscal year.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of 2012 the District had invested approximately $634 million in a broad range of capital assets, including land, equipment, and buildings. (See Table A-6) This amount represents a net decrease of ($11.09) million or (1.71) percent from the prior year.

Table A-6
District's Capital Assets

	Governmental Activities		
	2011	2012	Percent Change 2011 to 2012
Land	$34,754,656	$36,685,377	5.55%
Buildings & improvements	733,259,183	735,531,794	0.30%
Furniture & equipment	21,161,075	21,847,082	3.24%
Construction in progress	0	1,913,374	100.00%
Total Assets	789,174,914	795,977,627	0.86%
Less: accumulated depreciation	(143,967,324)	(161,862,285)	(12.42%)
Net Capital Assets	$645,207,590	$634,115,342	(1.71%)

More detailed information about the District's fixed assets is presented in Note 5 in the Notes to the Financial Statements.

Long-term Debt

At the end of August 31, 2012 the District had total bonded debt outstanding of $700,087,012, a decrease of ($12,769,755), or a (1.79%) decrease from the previous year. The District also had accreted interest of $45,363,459, a decrease of ($10,506,103), or a (18.80%) decrease from the previous year.

Table A-7
District's Long-Term Debt

	Governmental Activities		
	2011	2012	Percent Change 2011 to 2012
Bonds and Notes Payable			
General Obligation Bonds	$712,856,767	$700,087,012	(1.79%)
Premium on bonds	28,075,423	26,822,617	(4.46%)
Accreted Interest	55,869,562	45,363,459	(18.80%)
Total Bonds and Notes Payable	796,801,752	772,273,088	(3.07%)
Other Liabilities			
Compensated Absences	682,288	704,357	3.23%
Deferred loss on bond refunding	(9,528,535)	(9,044,100)	5.08%
Total Other Liabilities	(8,846,247)	(8,339,743)	5.72%
Total long-term debt	$787,955,505	$763,933,345	(3.04%)

More detailed information about the District's debt is presented in Note 4 in the Notes to the Financial Statements.

Bond Ratings

The bonds have a primary rating of “AAA” by Moody’s Investors Service, Inc. (“Moody’s”) and “AAA” by Standard & Poor’s Ratings Services, (“S&P”) by virtue of the guarantee of the Permanent School Fund of the State of Texas (“PSF Guarantee”). The underlying or secondary ratings for the District are “Aa2” by Moody’s and “**AA+**” by S&P.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

General fund revenues are budgeted to decrease (5.31%) from 2011-2012 actual revenue. The decrease is primarily attributable to a significant decrease in state funding as well as the end of the funding provided by the Education Jobs Foundation. Changes made to the funding formula in 2006-07 virtually eliminated any increase in school funding for Texas school districts since 2005-06. Although hopes were high that the meeting of the 82nd legislature would bring about positive changes to the funding formula, the State of Texas quickly announced that state revenues were insufficient to maintain the current level of educational funding, much less increase it. The State declared its intention to slash billions from school funding over the biennium.

In the 2012 fiscal year, the district implemented expenditure reductions of approximately $12 million in response to the anticipated state revenue reductions. In combination with the budgeted expenditure reductions, the district received funding for the 2012 year only under the EduJobs program of $4.8 million, which ultimately allowed the district to adopt a budget for 2011-12 with an anticipated surplus to the general fund of $6.9 million.

The budget process for 2012-13 was undertaken with the knowledge that state funding would be reduced even further in this second year of the biennium. However, the surplus to the general fund balance provided for in the 2011-12 budget, along with higher than expected property tax revenues, allowed the district to reinstate many of the budget cuts enacted in the previous year. The Board of Trustees determined that the general fund balance was healthy enough to use a portion of it for reinstatements and additions that were thought to be critical to the mission of the district. The Board decided to add $455,000 to the budget for additional teachers, supplies and equipment for the projected 265 additional students. Some non-discretionary items were identified that were required to be added to the budget, such as increases in property/casualty insurance, increases in utility costs and increases in existing contracts. These costs amounted to a $2.577 addition to the expenditure budget. And finally, $7.785 million was added to the budget for discretionary items, such as a 3% salary increase for staff, a subsidy to the Health Insurance Fund, and various reinstatements.

The final result was that the Board of Trustees adopted a budget for 2012-13 with a deficit of ($12,116,219), to be funded from the general fund balance.

The recognized sign of fiscal health for a school district is an appropriate undesignated, unreserved fund balance for the General Fund (operating fund). The District's current goal is to maintain the fund balance of the General Fund at 17-20% of operating expenses. The value of having an appropriate fund balance level can be expressed as follows:

1. Contingency fund for unexpected costs
2. Cash flow for operational resources at the beginning of the year prior to the tax collection season
3. Viewed as sign of fiscal stability and health by bond rating agencies.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District's Finance Department at 350 Keller Parkway, Keller, Texas 76248, or visit the Keller ISD website at www.kellerisd.net.

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BASIC FINANCIAL STATEMENTS

Exhibit A-1

KELLER INDEPENDENT SCHOOL DISTRICT
STATEMENT OF NET ASSETS
AUGUST 31, 2012

Data Control Codes		Governmental Activities
ASSETS		
1110	Cash and cash equivalents	$ 144,936,766
1110	Restricted cash	400,000
1220	Property taxes receivable (delinquent)	2,736,478
1230	Allowance for uncollectible taxes	(684,119)
1240	Due from other governments	3,167,394
1290	Other receivables	566,751
1300	Inventories, at cost	191,105
1410	Deferred expenses	519,543
1420	Capitalized bond and other debt issuance costs	6,663,142
	Capital Assets	
1510	Land	36,685,377
1520	Buildings, net	585,866,008
1530	Furniture and equipment, net	9,650,583
1580	Construction in progress	1,913,374
1000	Total assets	792,612,402
LIABILITIES		
2110	Accounts payable	5,653,207
2140	Interest payable	1,664,034
2150	Payroll deductions and withholdings payable	624,508
2160	Accrued wages payable	911,963
2180	Due to other governments	2,395
2210	Accrued expenses	728,157
2300	Unearned revenues	5,107,138
	Noncurrent liabilities	
2501	Due within one year	20,236,799
2502	Due in more than one year	743,696,546
2000	Total liabilities	778,624,747
NET ASSETS		
3200	Investment in capital assets, net of related debt	(43,992,374)
3840	Restricted for food service	4,604,517
3850	Restricted for debt service	2,808,188
3490	Restricted for employee health claims	400,000
3900	Unrestricted net assets	50,167,324
3000	Total net assets	$ 13,987,655

The Notes to the Financial Statements are an integral part of this statement.

KELLER INDEPENDENT SCHOOL DISTRICT
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED AUGUST 31, 2012

Data Control Codes		Expenses	Program Revenues: Charges for Services	Program Revenues: Operating Grants & Contributions	Net (Expense) Revenue and Changes in Net Assets: Governmental Activities
Primary Government					
	GOVERNMENTAL ACTIVITIES				
0011	Instruction	$ 149,547,022	$ 4,795,456	$ 13,844,668	$ (130,906,898)
0012	Instructional resources and media services	3,506,194	108,282	1,016,715	(2,381,197)
0013	Curriculum and instructional staff development	2,754,701	73,913	360,932	(2,319,856)
0021	Instructional leadership	2,091,486	64,515	135,057	(1,891,914)
0023	School leadership	14,317,804	414,131	83,741	(13,819,932)
0031	Guidance, counseling, and evaluation services	10,056,213	335,308	1,849,672	(7,871,233)
0032	Social services	156,066	5,153	276	(150,637)
0033	Health services	3,099,151	75,805	9,156	(3,014,190)
0034	Student (pupil) services	5,448,661	182,176	125,804	(5,140,681)
0035	Food services	12,085,660	7,704,516	4,564,258	183,114
0036	Cocurricular/extracurricular activities	7,985,415	839,066	802,709	(6,343,640)
0041	General administration	8,082,486	170,378	118,260	(7,793,848)
0051	Plant maintenance and operations	18,625,453	1,238,443	38,995	(17,348,015)
0052	Security and monitoring services	1,299,191	34,634	25,382	(1,239,175)
0053	Data processing services	5,227,588	151,902	8,210	(5,067,476)
0061	Community services	1,541,352	29,857	118,813	(1,392,682)
0072	Debt service - interest on long term debt	33,103,972	-	1,052,689	(32,051,283)
0093	Shared services agreement	3,410,020	112,888	6,044	(3,291,088)
0095	Payments to Juvenile Justice Alternative Education Program	2,375	79	3	(2,293)
0097	Payments to tax increment fund	1,732,427	1,732,427	-	-
[TP]	TOTAL PRIMARY GOVERNMENT	$ 284,073,237	$ 18,068,929	$ 24,161,384	(241,842,924)

Data Control Codes	General Revenues	
	Taxes	
MT	Property taxes, levied for general purposes	114,660,445
DT	Property taxes, levied for debt service	55,758,482
SF	State grants, unrestricted	88,208,113
IE	Investment earnings	436,411
MI	Miscellaneous local and intermediate	4,400,916
TR	Total general revenues	263,464,367
CN	Change in net assets	21,621,443
NB	Net assets -- beginning	(7,633,788)
NE	Net assets -- ending	$ 13,987,655

The Notes to the Financial Statements are an integral part of this statement.

KELLER INDEPENDENT SCHOOL DISTRICT
BALANCE SHEET
GOVERNMENTAL FUNDS
AUGUST 31, 2012

Data Control Codes		10 General Fund	20 Federally Funded Grant Fund
	ASSETS		
1110	Cash and temporary investments	87,159,741	$ 4,974,984
1220	Property taxes - delinquent	1,964,017	-
1230	Allowance for uncollectible taxes	(491,004)	-
1240	Due from other governments	60,205	3,057,189
1260	Due from other funds	2,926,838	-
1290	Other receivables	286,962	261,279
1300	Inventories, at cost	191,105	-
1410	Deferred expenditures	316,172	159,647
1000	Total assets	$ 92,414,036	$ 8,453,099
	LIABILITIES and FUND BALANCES		
	Liabilities		
2110	Accounts payable	2,528,367	375,846
2150	Payroll deduction and withholdings payable	624,508	-
2160	Accrued wages payable	799,514	112,055
2170	Due to other funds	463,150	2,854,437
2180	Due to other governments	40	-
2210	Accrued expenditures	68,633	13,025
2300	Deferred revenue	4,949,875	333,572
2000	Total liabilities	9,434,087	3,688,935
	FUND BALANCES		
	Nonspendable		
3410	Investments in inventory	191,105	-
3440	Deferred expenditures	316,172	159,647
	Restricted for		
3420	Retirement of long term debt	-	-
3450	Food service	-	4,604,517
3490	Grant funds	-	-
	Committed for		
3470	Capital acquisition program	-	-
3545	Campus activity fund	-	-
3590	Other purposes	42,951,888	-
	Assigned for		
3590	Other purposes	2,233,000	-
	Unassigned		
3600	Reported in General Fund	37,287,784	-
3000	Total fund balances	82,979,949	4,764,164
4000	Total liabilities and fund balances	$ 92,414,036	$ 8,453,099

The Notes to Financials Statements are
an integral part of this statement.

50 Debt Service Fund	60 Capital Projects Fund	Non-Major Governmental Funds	Total Governmental Funds
4,787,057	40,631,318	$ 3,925,724	$ 141,478,824
772,461	-	-	2,736,478
(193,115)	-	-	(684,119)
-	-	50,000	3,167,394
91,005	-	-	3,017,843
-	-	18,510	566,751
-	-	-	191,105
3,472	-	40,252	519,543
$ 5,460,880	$ 40,631,318	$ 4,034,486	$ 150,993,819
-	408,048	162,060	3,474,321
-	-	-	624,508
-	394	-	911,963
-	4	72,019	3,389,610
-	-	2,355	2,395
-	465,059	2,041	548,758
1,568,004	-	-	6,851,451
1,568,004	873,505	238,475	15,803,006
-	-	-	191,105
3,472	-	40,252	519,543
3,889,404	-	-	3,889,404
-	-	-	4,604,517
-	-	168,943	168,943
-	39,757,813	-	39,757,813
-	-	3,586,816	3,586,816
-	-	-	42,951,888
-	-	-	2,233,000
-	-	-	37,287,784
3,892,876	39,757,813	3,796,011	135,190,813
$ 5,460,880	$ 40,631,318	$ 4,034,486	$ 150,993,819

Exhibit C-2

KELLER INDEPENDENT SCHOOL DISTRICT
RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE STATEMENT OF NET ASSETS
AUGUST 31, 2012

Total fund balances - governmental funds	$ 135,190,813
The District uses internal service funds to charge the costs of certain activities, such as self-insurance, to appropriate functions in other funds. The assets and liabilities of the internal service funds are included in governmental activities in the statement of net assets. The net effect of this consolidation is to increase net assets.	1,871,427
Capital assets used in governmental activities are not financial resources and therefore are not reported in governmental funds.	795,977,627
Accumulated depreciation has not been recorded in the fund financial statements.	(161,862,285)
Bonds payable have not been included in the fund financial statements.	(700,087,012)
Accreted interest on capital appreciation bonds is not capitalized in the fund financial statements.	(45,363,459)
Bond issue costs are not capitalized in the fund financial statements.	6,663,142
Premiums on the issuance of bonds are not capitalized in the fund financial statements.	(26,822,617)
Deferred loss on bond refunding has not been reflected in the fund financial statements.	9,044,100
Revenue from property taxes is reported as deferred revenue in the fund financial statements but is recognized as revenue in the government-wide financial statements.	1,744,310
Accrued liabilities for compensated absences have not been reflected in the fund financial statements.	(704,357)
Interest is accrued on outstanding debt in the government-wide financial statements whereas in the fund financial statements interest expenditures are reported when due.	(1,664,034)
Net assets of governmental activities	$ 13,987,655

KELLER INDEPENDENT SCHOOL DISTRICT
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
YEAR ENDED AUGUST 31, 2012

Data Control Codes		10 General Fund	20 Federally Funded Grant Fund
	REVENUES		
5700	Total local and intermediate sources	122,477,457	7,715,387
5800	State program revenues	94,683,993	742,716
5900	Federal program revenues	346,711	16,087,524
5020	Total revenues	217,508,161	24,545,627
	EXPENDITURES		
	Current		
0011	Instruction	124,322,850	8,628,192
0012	Instructional resources and media services	2,042,530	841,768
0013	Curriculum and instructional staff development	1,744,637	334,379
0021	Instructional leadership	1,749,503	136,734
0023	School leadership	12,474,734	23,821
0031	Guidance, counseling and evaluation services	7,365,218	1,895,903
0032	Social work services	155,656	-
0033	Health services	2,282,194	5,252
0034	Student (pupil) transportation	5,327,277	120,575
0035	Food services	-	11,502,531
0036	Cocurricular/extracurricular activities	5,853,416	-
0041	General administration	5,019,367	-
0051	Facilities maintenance and operations	17,671,549	-
0052	Security and monitoring services	1,046,033	-
0053	Data processing services	4,588,417	-
0061	Community services	562,344	105,632
	Debt Service		
0071	Debt Service - Principal on long term debt	-	-
0072	Debt Service - Interest on long term debt	-	-
0073	Debt Service - Bond issuance cost and fees	-	-
	Capital Outlay		
0081	Facilities acquisition and construction	1,316,799	-
	Intergovernmental		
0093	Shared services agreement	3,410,020	-
0095	Juvenile Justice Alternative Education Program	2,375	-
0097	Payments to tax increment fund	1,732,427	-
6030	Total expenditures	198,667,346	23,594,787
1100	Excess (deficiency) of revenues over (under) expenditures	18,840,815	950,840
	Other Financing Sources (Uses)		
7911	Issuance of bonds	-	-
7915	Transfers in	-	-
7916	Premium or discount on issuance of bonds	-	-
8911	Transfers out	-	-
8949	Payment to refunded bond escrow agent	-	-
	Total other financing sources (uses)	-	-
1200	Net change in fund balance	18,840,815	950,840
0100	Fund balance - September 1 (beginning)	64,139,134	3,813,324
3000	Fund balance - August 31 (ending)	$ 82,979,949	$ 4,764,164

50 Debt Service Fund	60 Capital Project Fund	Non-Major Governmental Funds	Total Governmental Funds
55,909,665	218,079	4,350,492	$ 190,671,080
1,052,689	4,424	2,376,312	98,860,134
-	-	-	16,434,235
56,962,354	222,503	6,726,804	305,965,449
-	78,629	4,449,197	137,478,868
-	-	294,415	3,178,713
-	-	51,546	2,130,562
-	-	-	1,886,237
-	-	56,674	12,555,229
-	-	10,218	9,271,339
-	-	-	155,656
-	-	62	2,287,508
-	-	-	5,447,852
-	-	295	11,502,826
-	-	1,162,061	7,015,477
-	2,373,704	39,049	7,432,120
-	41,395	9,139	17,722,083
-	-	34,507	1,080,540
-	2,236	-	4,590,653
-	-	23,283	691,259
12,694,742	-	-	12,694,742
44,192,957	-	-	44,192,957
87,034	-	-	87,034
-	6,005,221	70,665	7,392,685
-	-	-	3,410,020
-	-	-	2,375
-	-	-	1,732,427
56,974,733	8,501,185	6,201,111	293,939,162
(12,379)	(8,278,682)	525,693	12,026,287
2,710,000	-	-	2,710,000
-	-	-	-
200,974	-	-	200,974
-	-	-	-
(2,825,750)	-	-	(2,825,750)
85,224	-	-	85,224
72,845	(8,278,682)	525,693	12,111,511
3,820,031	48,036,495	3,270,318	123,079,302
$ 3,892,876	$ 39,757,813	$ 3,796,011	$ 135,190,813

KELLER INDEPENDENT SCHOOL DISTRICT
RECONCILIATION OF THE
STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES OF THE GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
YEAR ENDED AUGUST 31, 2012

Total net change in fund balances - governmental funds	$ 12,111,511
The District uses internal service funds to charge the costs of certain activities, such as self-insurance and catering, to appropriate functions in other funds. The net income of internal service funds are reported with governmental activities. The net effect of this consolidation is to increase net assets.	(2,890,520)
Current year capital outlays are expenditures in the fund financial statements, but they are shown as increases in capital assets in the government-wide financial statements. The net effect of removing the 2012 capital outlays is to increase net assets.	6,802,713
Depreciation is not recognized as an expenditure in governmental funds since it does not require the use of current financial resources. The net effect of the current year's depreciation is to decrease net assets.	(17,894,961)
Current year long term debt principal payments are expenditures in the fund financial statements, whereas they are reported as reductions of bonds payable in the government-wide financial statements. The effect of current year principal paid on bonds payable increased net assets.	12,694,855
The current year issuance of bonds are shown as an other resource in the fund financial statements but are shown as an increase in long term debt in the government-wide financial statements.	(2,710,000)
Current year payments to bond refunding escrow agent are shown as other uses in the fund financial statements but are shown as reductions in long term debt and as a deferred loss on bond refunding in the government-wide financial statements.	2,785,000
Current year accretion on capital appreciation bonds is not recorded in the fund financial statements, but is shown as an increase in the accreted interest on the government-wide financial statements.	10,506,103
Bond issuance costs are expended in full when paid on the fund financial statements, whereas they are amortized to expense over the life of the related bonds payable on the government-wide financial statements.	85,225
Current year amortization of bond issue costs is not reflected in the fund financial statements, but is shown as a reduction to the bond issue costs asset in the government-wide financial statements.	(377,257)
Premiums associated with bonds payable are reported as revenue on the fund financial statements when bonds are issued. Amounts are reported net of amortization on the government-wide financial statements.	(160,224)
The current year amortization of the premium on bonds payable is not recorded in the fund financial statements, but is shown as a reduction of the premium in the government-wide financial statements.	1,453,780
Current year amortization of the deferred loss on the issuance of refunding bonds is not reflected in the fund financial statements, but is shown as a reduction of the loss in the government-wide financial statements.	(525,185)
Revenues from property taxes are deferred in the fund financial statements until they are considered available to finance current expenditures, but such revenues are recognized when assessed net of an allowance for uncollectible accounts in the government-wide statements.	(270,768)
Compensated absences are recognized when the related obligation matures and is expected to be liquidated with expendable available financial resources. Therefore additions to the accrual for compensated absences are not reported in the fund financial statements. The net effect of the current year increase in compensated absences was to decrease net assets.	(22,069)
Interest is accrued on outstanding debt in the government-wide financial statements, whereas in the fund financial statements interest expenditures are reported when due.	33,240
Change in Net Assets of Governmental Activities	$ 21,621,443

The Notes to Financial Statements are
an integral part of this statement.

Exhibit D-1

KELLER INDEPENDENT SCHOOL DISTRICT
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
AUGUST 31, 2012

	Governmental Activities - Total Internal Service Funds
ASSETS	
Current assets	
Cash and temporary investments	3,457,942
Due from other funds	372,144
Cash - restricted	400,000
Total assets	4,230,086
LIABILITIES	
Current liabilities	
Accounts payable	2,178,886
Due to other funds	377
Accrued expenses	179,399
Total liabilities	2,358,662
NET ASSETS	
Restricted for employee health claims	400,000
Unrestricted net assets	1,471,427
Total net assets	$ 1,871,427

The Notes to Financial Statements are an integral part of this statement.

Exhibit D-2

KELLER INDEPENDENT SCHOOL DISTRICT
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
YEAR ENDED AUGUST 31, 2012

	Governmental Activities - Internal Service Funds
Operating Revenues	
Local and intermediate sources	15,012,963
Total operating revenues	15,012,963
Operating Expenses	
Payroll costs	142,089
Professional and contracted services	1,865,219
Claim settlement costs	15,906,910
Other operating costs	7,924
Total operating expenses	17,922,142
Operating loss	(2,909,179)
Nonoperating Revenues (Expenses)	
State on-behalf revenue	6,140
Earnings from temporary deposits and investments	12,519
Total nonoperating revenues (expenses)	18,659
Change in net assets	(2,890,520)
Total net assets - September 1 (beginning)	4,761,947
Total net assets - August 31 (ending)	$ 1,871,427

The Notes to Financial Statements are
an integral part of this statement.

KELLER INDEPENDENT SCHOOL DISTRICT
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
YEAR ENDED AUGUST 31, 2012

	Governmental Activities - Internal Service Funds
Cash flows from operating activities	
Cash received from assessments - other funds	$ 15,012,963
Cash payments to employees for services	(142,089)
Cash payments for insurance claims	(17,734,420)
Cash payments for other operating expenses	(7,924)
Net cash used in operating activities	(2,871,470)
Cash flows from investing activities	
Interest and dividends on investments	12,519
Net cash provided by investing activities	12,519
Net change in cash and cash equivalents	(2,858,951)
Cash and cash equivalents at beginning of the year	6,316,893
Cash and cash equivalents at end of the year	$ 3,457,942
Reconciliation of operating loss to net cash used in operating activities	
Operating loss	$ (2,909,179)
Adjustments to reconcile operating loss to net cash used in operating activities	
State on-behalf revenue	6,140
Change in assets and liabilities	
Increase in due from other funds	(290,269)
Increase in restricted cash	(35,000)
Increase in accounts payable	538,173
Increase in due to other funds	377
Decrease in accrued expenditures	(181,712)
Net cash used in operating activities	$ (2,871,470)

The Notes to Financial Statements are an integral part of this statement.

Exhibit E-1

KELLER INDEPENDENT SCHOOL DISTRICT
STATEMENT OF ASSETS AND LIABILITIES - FIDUCIARY FUNDS
AUGUST 31, 2012

	Agency Funds
ASSETS	
Cash and cash equivalents	$ 381,579
Accounts receivable	118
Total assets	$ 381,697
LIABILITIES	
Accounts payable	$ 14,792
Due to other governments	35
Due to student groups	366,870
Total liabilities	$ 381,697

The Notes to Financial Statements are an integral part of this statement.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

The Keller Independent School District (the District) is a public educational agency operating under the applicable laws and regulations of the State of Texas. It is governed by a seven member Board of Trustees (the Board) that is elected by registered voters of the District. The District prepares its basic financial statements in conformity with U.S. Generally Accepted Accounting Principles (GAAP) promulgated by the Governmental Accounting Standards Board (GASB) and other authoritative sources identified in *Statement of Auditing Standards No. 69* of the American Institute of Certified Public Accountants. Additionally, the District complies with the requirements of the appropriate version of the Texas Education Agency (TEA) *Financial Accountability System Resource Guide* (FASRG) and the requirements of contracts and grants of agencies from which it receives funds. The following is a summary of the more significant accounting policies of the District.

A. Reporting Entity

The Board of Trustees is elected by the public and has the authority to make decisions, appoint administrators and managers, and significantly influence operations. It also has the primary accountability for fiscal matters. Therefore, the District is a financial reporting entity as defined by the GASB in its *Statement No. 14, The Financial Reporting Entity,* as amended by GASB in its *Statement No. 39, Determining Whether Certain Organizations are Component Units*. There are no component units included within the reporting entity and the District is not included in any other governmental reporting entity.

B. Government-Wide and Fund Financial Statements

The Statement of Net Assets and the Statement of Activities are government-wide financial statements. They report information on all of the District's non-fiduciary activities with most of the interfund activities removed. Governmental activities include programs supported primarily by taxes, state foundation funds, grants and other intergovernmental revenues.

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

Interfund activities between governmental funds and between governmental and proprietary funds appear as due to/due from on the Governmental Fund Balance Sheet and Proprietary Fund Statement of Net Assets and as other resources and other uses on the governmental fund Statement of Revenues, Expenditures and Changes in Fund Balance and on the Proprietary fund Statement of Revenues, Expenses, and Changes in Net Assets. All interfund transactions between governmental funds are eliminated on the government-wide statements as prescribed by GASB Statement No. 34.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

B. Government-Wide and Fund Financial Statements – Continued

The fund financial statements provide reports on the financial condition and results of operations for three fund categories - governmental, proprietary, and fiduciary. Since the resources in the fiduciary funds cannot be used for District operations, they are not included in the government-wide statements. The emphasis of fund financial statements is on major governmental funds, each displayed in a separate column. All remaining governmental funds are aggregated and reported as non-major funds.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All other revenues and expenses are non-operating.

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

Measurement focus is the accounting convention, which determines when revenues and expenditures are recognized in the accounts and reported in the financial statements.

Basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of measurements made, regardless of the measurement focus applied.

The government-wide financial statements use the economic resources measurement focus and the accrual basis of accounting, as do the Proprietary Fund and Fiduciary Fund financial statements (with the exception of Agency Funds which are custodial in nature thus do not have a measurement focus). Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements use the current financial resources measurement focus and the modified accrual basis of accounting. With this measurement focus, only current assets, current liabilities and fund balances are included on the balance sheet. Operating statements of these funds present net increases and decreases in current assets (i.e., revenues and other financing sources and expenditures and other financing uses).

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

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

The modified accrual basis of accounting recognizes revenues in the accounting period in which they become both measurable and available, and it recognizes expenditures in the accounting period in which the fund liability is incurred, if measurable, except for unmatured interest and principal on long-term debt, which is recognized when due. The expenditures related to certain compensated absences and claims and judgments are recognized when the obligations are expected to be liquidated with expendable available financial resources. The District considers all revenues available if they are collectible within 60 days after year end.

Revenues from local sources consist primarily of property taxes. Property tax revenues and revenues received from the State are recognized under the susceptible-to-accrual concept. Miscellaneous revenues are recorded as revenue when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned, since they are both measurable and available.

Grant funds are considered to be earned to the extent of expenditures made under the provisions of the grant. Accordingly, when such funds are received, they are recorded as deferred revenues until related and authorized expenditures have been made. If balances have not been expended by the end of the project period, grantors sometimes require the District to refund all or part of the unused amounts.

The Proprietary Fund and Fiduciary Fund are accounted for on a flow of economic resources measurement focus and utilize the accrual basis of accounting, except for Agency Finds, which are custodial in nature and therefore do not have a measurement focus. This basis of accounting recognizes revenues in the accounting period in which they are earned and become measurable and expenses in the accounting period in which they are incurred and become measurable.

The District applies all GASB pronouncements as well as the Financial Accounting Standards Board pronouncements issued on or before November 30, 1989, unless these pronouncements conflict or contradict GASB pronouncements. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the fund Statement of Net Assets. Net assets are segregated into invested in capital assets net of related debt, restricted net assets, and unrestricted net assets.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

D. Fund Accounting

The District's accounting system is organized and operated on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures. District resources are allocated to and accounted for in individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled.

The District reports the following major governmental funds:

The General Fund – The general fund is the District's primary operating fund. It accounts for all financial resources except those required to be accounted for in another fund. Major program revenues include local property taxes, state funding under the Foundation School Program, and interest earnings. Expenditures include all costs associated with the daily operations of the District except for specific programs funded by the federal or state government, food service, debt service, and capital projects.

Federally Funded Grant Funds – All funds which receive Federal financial assistance are accounted for in this fund. Some State financial assistance is included in this major fund as well. Sometimes unused balances must be returned to the grantor at the close of specified project periods. Also included in this fund is the Child Nutrition Fund, which is partially funded by state and local revenue.

Debt Service Funds – The debt service fund is utilized to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest, and related costs arising from general obligation bonds.

Capital Projects Funds – The capital project fund is utilized to account for financial resources to be used for the acquisition or construction of major capital facilities. Such resources are derived from proceeds of General Obligation Bonds and interest earned on such monies and local sources designated for such purposes.

Proprietary Funds:

Internal Service Funds – Revenues and expenses related to services provided to organizations inside the District on a cost reimbursement basis are accounted for in an internal service fund. The District's Internal Service Fund is a Worker’s Compensation and Health Insurance fund.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

D. Fund Accounting – Continued

Fiduciary Funds:

Agency Funds – The District accounts for resources held for others in a custodial capacity in agency funds. The District's Agency Funds are Student Activity funds and Employee Activity funds.

Additionally, the District reports the following nonmajor fund types:

Governmental Funds:

Special Revenue Funds – The District accounts for resources restricted to, or assigned for, specific purposes by the District or local grantor. Sometimes unused balances must be returned to the grantor at the close of specified project periods.

E. Budgets and Budgetary Accounting

The District facilitates budgeting and budgetary control by preparing annual budgets for the General Fund, Child Nutrition Program Fund and Debt Service Fund and appropriately amending the budgets as circumstances dictate; the annual budgets as amended are an integral part of the accounting system, providing appropriate budgetary control over revenues, expenditures and transfers through comparison of actual data and encumbrances to budgetary data.

The Superintendent of Schools is designated as the budget officer of the District and is responsible for preparing, or causing to be prepared, a budget for the next succeeding fiscal year.

The budget is required to be prepared no later than August 20 at a meeting of the Board of Trustees called for the purpose of adopting such budget after ten days public notice of the meeting has been given.

The Board of Trustees may approve amendments to the budget, which are required when a change is made to any one of the functional expenditure categories or revenue object accounts defined by the TEA. Such amendments must be reflected in the official minutes of the Board, and may not, by law, occur after August 31. Therefore, the legal level of budgetary control is at the function level within each budgeted fund. Management may transfer appropriations between objects, sub-objects, organizations, programs, and projects without approval from the Board of Trustees, as long as appropriations are not increased at the function level.

TEA requires the budgets to be filed with the TEA through regular submissions to the Public Education Information Management System (PEIMS). The budget should not be exceeded in any functional expenditure category under TEA requirements. The final amended versions of these budgets are used in this report.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

E. Budgets and Budgetary Accounting – Continued

Unused appropriations lapse at the end of each fiscal year; however, the District increases the subsequent year appropriations by an amount equal to outstanding encumbrances.

Budgets for the General, Child Nutrition and Debt Service Funds are adopted on a basis consistent with U.S. generally accepted accounting principles (GAAP).

F. Cash and Cash Equivalents

The District's cash is comprised of demand accounts and imprest funds. All daily receipts are deposited to the demand accounts until the funds are invested under the terms of the District's depository contract. The District considers cash equivalents to be all highly liquid investments with initial maturities of ninety days or less from the date of purchase.

G. Temporary Investments

In accordance with GASB Statement No. 31, the District's general policy is to report money market investments and short-term participating interest-earning investment contracts at amortized cost and to report nonparticipating interest-earning investment contracts using a cost-based measure. However, if the fair value of an investment is significantly affected by the impairment of the credit standing of the issuer or by other factors, it is reported at fair value. All other investments are reported at fair value unless a legal contract exists which guarantees a higher value. The term "short-term" refers to investments which have a remaining term of one year or less at the time of purchase. The term "nonparticipating" means that the investment's value does not vary with market interest rate changes.

H. Inventory

Inventories on the balance sheet consist of material and supplies and are recorded at first-in, first-out (FIFO) cost. Inventories are recorded as expenditures when consumed. In the governmental funds, a non spendable fund balance indicates that these funds are unavailable as current expendable financial resources.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

I. Compensated Absences

Any District employee who is professionally certified and has at least five years of service to the District is paid for all local sick days upon termination of employment with the District. Local sick leave days are earned at a rate of five days per year. The leave days shall accrue with no limit. A resigning employee shall receive $35 per day, if he or she completes their contract. A retiring employee shall receive $35 per day at the time of retirement provided he or she qualifies for retirement benefits from the Teacher Retirement System of Texas.

The accrual for accumulated unpaid sick leave benefits has been recorded in the government-wide financial statements.

J. Account Code Reporting

In accordance with the Texas Education Code, the District has adopted and installed an accounting system which meets at least the minimum requirements prescribed by the State Board of Education and approved by the State Auditor. Specifically, the District's accounting system uses codes and the code structure prescribed by the TEA in the Resource Guide. Mandatory codes are recorded in the order provided in that section.

K. Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

The amount of state foundation revenue a school district earns for a year can and does vary until the time when final values for each of the factors in the formula becomes available. Availability can be as late as midway into the next fiscal year. It is at least reasonably possible that the foundation revenue estimate as of August 31, 2012 will change.

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

L. Property Taxes

Property taxes are levied by October 1 on the assessed value listed as of January 1 for all real and business personal property located in the District in conformity with Subtitle E, Texas Property Tax Code. Taxes are due on receipt of the tax bill and are delinquent if not paid before February 1 of the year following the year in which imposed. On January 31 of each year, a tax lien attaches to property to secure the payment of all taxes, penalties, and interest ultimately imposed. Property tax revenues are considered available (1) when they become due or past due and receivable within the current period and (2) when they are expected to be collected during a 60-day period after the close of the school fiscal year.

Delinquent taxes are prorated between maintenance and debt service based on rates adopted for the year of the levy. Allowances for uncollectible taxes within the General and Debt Service Funds are based upon historical experience in collecting property taxes. The District is prohibited from writing off real property taxes without specific statutory authority from the Texas Legislature.

The District expects to receive all significant receivables within one year of August 31, 2012.

M. Capital Assets

Capital assets, which include land, buildings and furniture and equipment, are reported in the government-wide financial statements. Capital assets are defined by the District as assets with an initial, individual cost of more than $5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Buildings and furniture and equipment of the District are depreciated using the straight line method over the following estimated useful lives:

Assets	Years
Buildings	50
Building Improvements	5-25
Vehicles	5-10
Office equipment	3-20
Computer equipment	5

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

N. Long-Term Debt

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, 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 straight line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognized 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.

O. Interfund Transactions

During the course of normal operations, it is necessary for the District to enter into transactions among its various funds. These transactions consist of one or more of the following types:

- Reimbursements to a fund, which are generally reflected through the allocation of pooled cash accounts, for expenditures or expenses initially made from it that are properly applicable to another fund. All interfund receivable / payable balances at August 31, 2012 were the result of these types of reimbursements and are expected to be repaid within one year.
- Transfers of equity balances from one fund to another.
- Transfers in and out, as appropriate, which are shown as other financing sources or uses in the fund financial statements.
- All other outstanding balances between funds are reported as "due to/from other funds" in the fund financial statements.

P. Restricted Resources

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

Q. Prepaid (Deferred) Expenditures

Deferred expenditures indicate payments made by the District in the current year to provide services occurring in the subsequent fiscal year. The District uses the consumption approach when recording prepaid expenditures. The consumption approach provides for the initial reporting of the item as an asset while recognition of the expenditure is deferred until the period that the item is actually used or "consumed".

KELLER INDEPENDENT SCHOOL DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS

NOTE 2. BONDED DEBT PAYABLE

Bonded debt payable as of August 31, 2012 is as follows:

Description	Interest Rate Payable	Amount of Original Issue	Amount Outstanding 9/1/2011	Issued Current Year	Refunded Current Year	Retired Current Year	Amount Outstanding 8/31/2012
Refunding and School Building Bonds Series 1992 & 1992A Final maturity 2013	5.625-6.25	$ 29,245,000	$ 341,747	$ -	$ -	$ 178,083	$ 163,664
Refunding and School Building Bonds Series 1993 & 1993A Final maturity 2014	3.50-6.25	31,065,000	315,000	-	-	-	315,000
Unlimited Tax School Building and Refunding Bonds Series 1996A Final maturity 2021	3.60-5.90	59,539,931	14,519,482	-	-	654,836	13,864,646
Unlimited Tax School Building and Refunding Bonds Series 1997A Final maturity 2027	3.85-6.00	29,698,013	4,019,995	-	-	-	4,019,995
Unlimited Tax School Building and Refunding Bonds Series 1998 Final maturity 2030	4.20-5.00	90,610,038	350,767	-	-	350,767	-
Unlimited Tax School Building and Refunding Bonds Series 1999 Final maturity 2031	4.00-4.90	30,190,000	215,002	-	-	85,000	130,002
Unlimited Tax School Building and Refunding Bonds Series 2001 Final maturity 2022	5.25-5.5	117,068,480	6,919,108	-	2,785,000	2,697,585	1,436,523
Unlimited Tax Refunding Bonds Series 2002 Final maturity 2013	3.00-4.20	7,184,997	585,000	-	-	270,000	315,000
Unlimited Tax Refunding Bonds Series 2005 Final maturity 2030	4.75-5.00	98,339,961	92,454,961	-	-	790,000	91,664,961

KELLER INDEPENDENT SCHOOL DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS

NOTE 2. BONDED DEBT PAYABLE – CONTINUED

Description	Interest Rate Payable	Amount of Original Issue	Amount Outstanding 9/1/2011	Issued Current Year	Refunded Current Year	Retired Current Year	Amount Outstanding 8/31/2012
Unlimited Tax Building and Refunding Bonds Series 2005A Final maturity 2025	4.00-5.00	117,165,000	114,790,000	-	-	2,245,000	112,545,000
Unlimited Tax School Refunding Bonds Series 2006 Final maturity 2029	4.00-5.00	89,844,973	88,379,973	-	-	330,000	88,049,973
Unlimited Tax School Refunding Bonds Series 2006A Final maturity 2029	4.00-4.60	64,749,980	63,943,761	-	-	8,016	63,935,745
Unlimited Tax School Refunding Bonds Series 2007 Final maturity 2028	4.00-5.00	136,470,000	134,560,000	-	-	1,090,000	133,470,000
Unlimited Tax School Building Bonds Series 2009 Final maturity 2035	4.39-5.00	142,299,951	140,969,951	-	-	3,375,000	137,594,951
Unlimited Tax Refunding Bonds Series 2009 Final maturity 2023	3.00-4.625	11,199,999	10,590,000	-	-	230,000	10,360,000
Unlimited Tax Refunding Bonds Series 2009A Final maturity 2031	3.50-4.50	22,419,992	22,372,022	-	-	5,470	22,366,552
Unlimited Tax Refunding Bonds Series 2010 Final maturity 2030	2.00-4.125	8,389,999	8,159,998	-	-	319,998	7,840,000
Unlimited Tax Refunding Bonds Series 2011 Final maturity 2028	2.00-4.00	9,370,000	9,370,000	-	-	65,000	9,305,000
Unlimited Tax Refunding Bonds Series 2012A Final maturity 2031	3.50	-	-	2,710,000	-	-	2,710,000
Total bonded debt payable			$ 712,856,767	$ 2,710,000	$ 2,785,000	$ 12,694,755	$ 700,087,012

NOTE 2. BONDED DEBT PAYABLE – CONTINUED

The debt service requirements on the above bonds are as follows:

Due Fiscal Year Ending August 31	Principal	Interest	Total
2013	$ 14,508,840	$ 43,673,339	$ 58,182,179
2014	25,099,769	36,009,854	61,109,623
2015	17,300,068	40,853,025	58,153,093
2016	13,777,089	41,496,290	55,273,379
2017	16,712,170	39,121,303	55,833,473
2018-2022	121,559,076	166,102,367	287,661,443
2023-2027	202,730,000	99,887,799	302,617,799
2028-2032	244,765,000	44,862,225	289,627,225
2033-2036	43,635,000	3,669,581	47,304,581
	$ 700,087,012	$ 515,675,783	$ 1,215,762,795

Bonded debt payable is collateralized by revenue from the District's tax collections.

On April 15, 2012, the District issued $2,710,000 in unlimited tax refunding bonds, with interest rates of 3.50% to advance refund $2,785,000 of series 2001 Bonds with original maturities between 2007 and 2031 and interest rates between 5.25% and 5.50%. The refunding was undertaken to reduce the District’s total debt service payments over the next 20 years by approximately $1,110,228 and to obtain an economic gain (difference between the present value of the debt service payments on the old and new debt) of approximately $834,014.

NOTE 3. ACCUMULATED UNPAID SICK LEAVE BENEFITS

Professional certified employees who have completed five years of continuous service in the District and who leave the system shall be paid for each day of unused accumulated sick leave. A summary of changes in the accumulated sick leave follows:

Balance, September 1, 2011	$ 682,288
New entrants and salary increments	35,842
Payments to participants	(13,773)
Balance, August 31, 2012	$ 704,357

NOTE 4. CHANGES IN LONG-TERM LIABILITIES

Long-term activity for the year ended August 31, 2012 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental activities					
Bonds and notes payable					
General obligation bonds	$ 712,856,767	$ 2,710,000	$ 15,479,755	$ 700,087,012	$ 14,508,840
Accreted interest	55,869,562	4,575,648	15,081,751	45,363,459	4,736,280
Premium on bonds	28,075,423	200,974	1,453,780	26,822,617	1,453,776
Deferred loss on bond refunding	(9,528,535)	(40,750)	(525,185)	(9,044,100)	(525,185)
Compensated absences	682,288	35,842	13,773	704,357	63,088
Total governmental activities long-term liabilities	$ 787,955,505	$ 7,481,714	$31,503,874	$ 763,933,345	$ 20,236,799

The General Fund has been used to liquidate the liability for compensated absences.

KELLER INDEPENDENT SCHOOL DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS

NOTE 5. CAPITAL ASSET ACTIVITY

Capital asset activity for the District for the year ended August 31, 2012 was as follows:

Primary Government:

	Balance 9/1/2011	Additions (Transfers)	Deletions	Balance 8/31/2012
Capital assets, not being depreciated				
Land	$ 34,754,656	$ 1,930,721	$ -	$ 36,685,377
Construction in progress	-	1,913,374	-	1,913,374
Total capital assets, not being depreciated	34,754,656	3,844,095	-	38,598,751
Capital assets, being depreciated				
Buildings and improvements	733,259,183	2,272,611	-	735,531,794
Furniture and equipment	21,161,075	686,007	-	21,847,082
Total capital assets, being depreciated	754,420,258	2,958,618	-	757,378,876
Less accumulated depreciation on				
Buildings and improvements	134,216,912	15,448,874	-	149,665,786
Furniture and equipment	9,750,412	2,446,087	-	12,196,499
Accumulated depreciation	143,967,324	17,894,961	-	161,862,285
Total capital assets, being depreciated, net	610,452,934	(14,936,343)	-	595,516,591
Governmental activities capital assets, net	$ 645,207,590	$(11,092,248)	$ -	$ 634,115,342

NOTE 5. CAPITAL ASSET ACTIVITY – CONTINUED

Depreciation expense of the governmental activities was charged to functions/programs as follows:

Instruction	$ 11,685,238
Instructional resources and media services	193,870
Curriculum and staff development	184,278
Instructional leadership	77,064
School leadership	1,338,178
Guidance, counseling and evaluation services	687,661
Social services	116
Health services	366,864
Student (pupil) transportation	809
Food services	295,231
Co-curricular/extracurricular activities	607,211
General administration	232,998
Plant maintenance and operations	982,411
Security and monitoring services	198,427
Data processing services	650,451
Community services	394,154
Total depreciation expense	$ 17,894,961

NOTE 6. DEPOSITS AND INVESTMENTS

The District'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 its agent bank, approved pledged securities in an amount sufficient to protect District 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 Public Funds Investment Act (Government Code Chapter 2256) contains specific provisions in the areas of investment practices, management reports and establishment of appropriate policies. Among other things, it requires the District to adopt, implement, and publicize an investment policy. That policy must address the following areas: (1) safety of principal and liquidity, (2) portfolio diversification, (3) allowable investments, (4) acceptable risk levels, (5) expected rates of return, (6) maximum allowable stated maturity of portfolio investments, (7) maximum average dollar-weighted maturity, allowed based on the stated maturity date for the portfolio, (8) investment staff quality and capabilities, (9) and bid solicitation preferences for certificates of deposit. Statutes and the District's investment policy authorized the District to invest in the following investments as summarized in the table on the following page:

NOTE 6. DEPOSITS AND INVESTMENTS – CONTINUED

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio	Maximum Investment in One Issuer
U.S. Treasury obligations	10 years	none	none
U.S. Agency obligations	10 years	none	none
State of Texas securities	10 years	none	none
Collateralized mortgage obligations	10 years	none	none
Certificates of deposit	none	none	none
Repurchase agreements	90 days	none	none
Securities lending program	1 year	none	none
Banker's acceptance	270 days	none	none
Commercial paper	270 days	none	none
No-load mutual funds	2 years	15%	none
Guaranteed investment contracts	5 years	none	none
Public funds investment pool	n/a	none	none

The Act also requires the District to have independent auditors perform test procedures related to investment practices as provided by the Act. The District is in substantial compliance with the requirements of the Act and with local policies.

Cash and investments as of August 31, 2012 are classified in the accompanying financial statements as follows:

Primary government	$ 144,936,767
Fiduciary funds	381,579
	$ 145,318,346

Cash and investments as of August 31, 2012 consist of the following:

Deposits with financial institutions	$ (1,113,050)
Investments	146,431,395
	$ 145,318,345

Disclosures relating to interest rate risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the District manages its exposure to interest rate risk is by investing mainly in investment pools which purchase a combination of shorter term investments with an average maturity of less than 60 days thus reducing the interest rate risk. The District monitors the interest rate risk inherent in its portfolio by measuring the weighted average maturity of its portfolio. The District has no formal policy related to interest rate risk.

NOTE 6. DEPOSITS AND INVESTMENTS – CONTINUED

As of August 31, 2012, the District had the following investments, classified as cash and investments and restrict cash in the financial statements:

Investment Type	Amount	Weighted Average Maturity	Minimum Legal Rating	Rating as of August 31, 2012
TexPool	$ 2,634,926	43 days	AAA	AAAm
TexSTAR	3,621,946	49 days	AAA	AAAm
LOGIC	140,174,523	47 days	AAA	AAAm
	$ 146,431,395			

As of August 31, 2012 the District did not invest in any securities which are highly sensitive to interest rate fluctuations.

Disclosures Relating to Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented above is the minimum rating required by (where applicable) the Public Funds Investment Act, the District's investment policy, or debt agreements, and the actual rating as of year end for each investment type.

Concentration of Credit Risk

The investment policy of the District contains no limitations on the amount that can be invested in any one issuer. As of August 31, 2012, other than external investment pools, the District did not have 5% or more of its investment with one issuer.

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The Public Funds Investment Act and the District's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, other than the following provision for deposits: The Public Funds Investment Act requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The fair value of the pledged securities in the collateral pool must equal at least the bank balance less the FDIC insurance at all times.

NOTE 6. DEPOSITS AND INVESTMENTS – CONTINUED

At August 31, 2012, the District deposits with financial institutions were fully covered by federal depository insurance.

In addition, the following is disclosed regarding coverage of combined balances on the date of the highest deposit:

A. Depository: Bank of America
B. Security pledged as of the date of the highest combined balance on deposit was $0.
C. Largest cash, savings and time deposit combined account balance amounted to $8,846,746 and occurred during the month of November 2011.
D. Total amount of FDIC coverage at the time of largest combined balance was $8,846,746, which was 100% of the account balance.

Investment in State Investment Pools

The District is a voluntary participant in various investment pools. These pools included the following: TexPool, TexSTAR and LOGIC.

The State Comptroller of Public Accounts exercises responsibility over TexPool. Oversight includes the ability to significantly influence operations, designation of management, and accountability for fiscal matters. Additionally, the State Comptroller has established an advisory board composed of both participants in TexPool and other persons who do not have a business relationship with TexPool. TexPool operates in a manner consistent with the SEC's Rule2a7 of the Investment Company Act of 1940. TexPool uses amortized cost rather than market value to report net assets to compute share prices. Accordingly, the fair value of the position in TexPool is the same as the value of TexPool shares.

TexSTAR is a local government investment pool created under the Interlocal Cooperation Act specifically tailored to meet Texas state and local government investment objectives of preservation of principal, daily liquidity, and competitive yield. TexSTAR is administered by First Southwest Asset Management, Inc. and JPMorgan Chase. Together these organizations bring to the TexSTAR program the power partnership of two leaders in financial services with a proven track record in local government investment pool management. The fair value of the position in TexSTAR is the same as the value of TexSTAR shares.

LOGIC is governed by a 6-member board and is an AAA rated investment program tailored to the investment needs of local governments within the state of Texas. LOGIC assists governments across Texas make the most of taxpayer dollars. Local officials can improve the return on their invested balances by pooling their money with other entities to achieve economies of scale in a conservative fund in full compliance with the Texas Public Funds Investment Act. The fair value of the position in LOGIC is the same as the value of LOGIC shares.

NOTE 7. RETIREMENT PLAN

Plan Description. The District contributes to the Teacher Retirement System of Texas (TRS), a cost-sharing multiple employer defined benefit pension plan. TRS administers retirement and disability annuities, and death and survivor benefits to employees and beneficiaries of employees of the public school systems of Texas. It operates primarily under the provisions of the Texas Constitution, Article XVI, Sec. 67 and Texas Government Code, Title 8, Subtitle C. TRS also administers proportional retirement benefits and service credit transfer under Texas Government Code, Title 8, Chapters 803 and 805, respectively. TRS issues a publicly available financial report that includes financial statements and required supplementary information for the defined benefit pension plan. That report may be obtained by writing to the TRS Communications Department, 1000 Red River Street, Austin, Texas 78701-2698, by calling the TRS Communications Department at 1-800-223-8778, or by downloading the report from the TRS Internet website, www.trs.state.tx.us, under the TRS Publications heading.

Funding Policy. State law provides a state contribution rate of 6.0 for fiscal year 2012, and 6.644% for fiscal years 2011 and 2010. The member contribution rate was 6.4% for fiscal years 2010, 2011 and 2012. In certain instances, the reporting district is required to make all or a portion of the state's 6.0% contribution. Contribution requirements are not actuarially determined but are legally established each biennium pursuant to the following state funding policy: (1) the state constitution requires the legislature to establish a member contribution rate of not less than 6.0% of the member's annual compensation and a state contribution rate of not less than 6.0% and not more than 10.0% of the aggregate annual compensation of all members of the system during that fiscal year; (2) a state statute prohibits benefit improvements or contribution reductions if, as a result of the particular action, the time required to amortize TRS's unfunded actuarial liabilities would be increased to a period that exceeds 31 years or, if the amortization period already exceeds 31 years, the period would be increased by such action. State contributions to TRS made on behalf of the District's employees and reflected in the District's financial statements as both revenue and expenditures for the years ended August 31, 2010, 2011 and 2012 were $7,631,542, $8,422,215 and $5,778,008 respectively. The District paid additional state contributions for the years ended August 31, 2010, 2011 and 2012 in the amount of $2,233,855, $1,579,393, and $2,485,324 respectively, on a portion of the employees' salaries that exceeded the statutory minimum.

Retiree Health Plan

Plan Description. Keller Independent School District contributes to the Texas Public School Retired Employees Group Insurance Program (TRS-Care), a cost-sharing multiple-employer defined benefit postemployment health care plan administered by the Teacher Retirement System of Texas. TRS-Care Retired Plan provides health care coverage for certain persons (and their dependents) who retired under the Teacher Retirement System of Texas. he statutory authority for the program is Texas Insurance Code, Chapter 1575. Section 1575.052 grants the TRS Board of Trustees the authority to establish and amend basic and optional group insurance coverage for participants. The TRS issues a publicly available financial report that includes financial statements and required supplementary information for TRS-Care. This report may be obtained by visiting the TRS website at www.trs.state.tx.us, or by writing to the Communications Department of the Teacher Retirement System of Texas at 1000 Red River Street, Austin, Texas 78701, or by calling 800-223-8778.

NOTE 7. RETIREMENT PLAN – CONTINUED

Retiree Health Plan – Continued

Funding Policy. Contribution requirements are not actuarially determined but are legally established each biennium by the Texas Legislature. Texas Insurance Code, Sections 1575.202, 203, and 204 establish state, active employee, and public school contributions respectively. The state of Texas and active public school employee contribution rates were 1.0% and 0.65% of the public school payroll, respectively, with school districts contributing a percentage of payroll set at 0.55% for fiscal year 2012. Per Texas Insurance Code, Chapter 1575, the public school contribution may not be less than 0.25% or greater than 0.75% of the salary of each active employee of the public school. For the years ended August 31, 2010, 2011 and 2012 the State's contributions to TRS-Care were $1,538,996, $1,573,382 and $565,367, respectively, the active member contributions were $1,002,801, $1,002,711 and $958,628, respectively and the District's contributions were $899,202, $945,042 and $811,154, respectively which equaled the required contributions for those years.

Prescription Drug Coverage. The Medicare Prescription Drug, Improvement, and Modernization act of 2003 established prescription drug coverage for Medicare beneficiaries known as Medicare Part D. Under Medicare Part D, TRS-Care retiree drug subsidy payments from the federal government to offset certain prescription drug expenditures for eligible TRS-Care participants. For the years ended August 31, 2010, 2011 and 2012, the subsidy payments received by TRS-Care on behalf of the District were $376,861, $373,501 and $390,107, respectively. These payments are recorded as equal revenues and expenditures in the governmental funds financial statements.

Early Retiree Reinsurance program (ERRP) The ERRP, implement in 2012, is a provision of the Patient Protection and Affordable Care Act (PPACA) and provides reimbursement to plan sponsors for a portion of the cost of providing health benefits to retirees between the ages of 55-64 and their covered dependents regardless of age. An "early retiree" is defined as a plan participant aged 55-64 who is not eligible for Medicare and is not covered by an active employee of the plan sponsor. This temporary program is available to help employers continue to provide coverage to early retirees. ERRP reimbursement is available on a first come, first served basis for qualified employers that apply and become certified for the program. TRS has been certified for this program and has received funds from the ERRP program. Total amount received by TRS Care on behalf of the District was $386,916.

NOTE 8. RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters for which the District carries commercial insurance.

NOTE 8. RISK MANAGEMENT – CONTINUED

Effective January 1994, the District discontinued its participation in the Texas Association of School Boards (TASB) workers' compensation risk pool and established a self-insurance plan for workers' compensation benefits for employees. The Districts' retention of risk is $350,000 per occurrence with an aggregate stop-loss limit of $1,000,000 over a three year period. The District's aggregate attachment point was $3,313,892. Claims incurred by the employees of the District are handled by a third party administrator who is responsible for estimating losses to be incurred by the District and ultimately paid to the claimant.

Effective December 2002, the District established a self-funded health insurance plan. The District and employees share the cost of employee coverage. Employees, at their option, can authorize payroll withholdings to pay contributions or premiums for dependents. The plan is authorized by Article 3.51-2, Texas Insurance Code and is documented by a contractual agreement. The District's retention of risk is $400,000 per employee with an aggregate stop-loss limit of approximately $2,000,000 at August 31, 2012. The District's aggregate attachment point was $17,825,044.

Settled claims have not exceeded the aggregate coverage in any of the past three fiscal years. Insurance coverage has not been reduced for the year from the prior year. Accrued claims payable of $2,168,219 as of August 31, 2012, includes provisions for claims reported but not paid and claims incurred but not reported. The provision for reported claims is determined by estimating the amount that will ultimately be paid each claimant and is calculated and provided by the District's third party administrator. The District estimates the provision for claims incurred but not yet reported. Accrued claims payable have not been discounted to their present value as the District expects such claims to be paid within the following fiscal year. The District believes that any discount of the claims payable would not be material to the overall financial statements.

Changes in the fund's claims liability amount for the year ended August 31, 2012 and 2011 are as follows:

	2012	2011
Liability, beginning of year	$ 1,639,923	$ 1,309,438
Current year claims and changes in estimates	12,901,963	12,695,065
Claim payments	(12,373,667)	(12,364,580)
Liability, end of year	$ 2,168,219	$ 1,639,923

NOTE 9. LITIGATION

The District is a party to various legal actions, none of which is believed by the administration or its legal counsel to have a material effect on the financial condition of the District. Accordingly, no provision for losses has been recorded in the accompanying basic financial statements for such contingencies.

NOTE 10. COMMITMENTS

In a prior year, the District entered into an agreement with Stock Transportation, Inc. (now Durham School Services, LP) for the outsourcing of student transportation, whereby the District sold its existing fleet of school buses to Stock Transportation for a price of $1,021,000 and Stock Transportation agreed to lease the District's transportation facilities for $1 per annum for the term of the agreement.

The initial agreement was renewed for a period of five years beginning August 1, 2004 and ending July 31, 2009, with the option to renew for two additional years. That option was exercised for the year 2009-2010 and on August 1, 2010 a new agreement was entered into for the period of August 1, 2010 through July 31, 2014.

As of August 31, 2012, the District has entered into long-term construction projects with an aggregate unexpended balance of $1,354,130.

The District has also entered into operating leases for office equipment which expire in September 2017. There were no expenditures under these leases for the year ended August 31, 2012. The District's financial commitment under these leases for the fiscal year ending August 31, 2013 is $605,579. The financial commitment for each of the four remaining years under the agreement is $606,061.

On January 28, 2011, the District entered into an agreement with Dell Marketing L.P. for managed technology services. The contract was entered into for a period of five years beginning January 28, 2011 and ending January 28, 2016, with the option to renew for five additional years. The remaining financial commitment at August 31, 2012 under this agreement was $611,532. The financial commitment for each of the three remaining years under the agreement is $1,834,596.

NOTE 11. DUE FROM STATE AGENCIES

The District participates in a variety of federal and state programs from which it receives grants to partially or fully finance certain activities. In addition, the District receives entitlements from the State through the School Foundation and Per Capita Programs. Amounts due from federal and state governments as of August 31, 2012, are summarized below. All federal grants shown below are passed through the TEA and are reported on the combined financial statements as Due from Other Governments.

Fund	Entitlements	Federal Grants	Total
General	$ 60,205	$ -	$ 60,205
Nonmajor governmental funds	50,000	-	50,000
Federally funded grants	-	3,057,189	3,057,189
Total	$ 110,205	$ 3,057,189	$ 3,167,394

NOTE 12. DEFERRED REVENUE

Deferred revenue at August 31, 2012 consisted of the following:

	General Fund	Federally Funded Grant Fund	Debt Service Fund	Total
Net tax revenue	$ 963,746	$ -	$ 483,476	$ 1,447,222
Funds received in advance of expenditures or service	3,986,129	333,572	1,084,528	5,404,229
Total	$ 4,949,875	$ 333,572	$ 1,568,004	$ 6,851,451

NOTE 13. INTERFUND BALANCES AND ACTIVITIES

Interfund balances at August 31, 2012 consisted of the following individual fund balances:

Due To Fund	Due From Fund	Amount	Purpose
General Fund	Non-Major Governmental Fund	$ 72,019	Reimbursement of expenditures
Debt Service Fund	General Fund	91,005	Reimbursement of revenue
Internal Service Fund	General Fund	372,144	Reclassification of revenue
General Fund	Internal Service Fund	377	Reclassification of revenue
General Fund	Federall Funded Grant Fund	2,854,438	Reimbursement of expenditures
General Fund	Capital Projects Fund	4	Reimbursement of revenue
		$ 3,389,987	

All amounts due are scheduled to be repaid within one year.

NOTE 14. RECONCILIATION TO BASIC FINANCIAL STATEMENTS

The following is a reconciliation of expenditures of federal awards per Exhibit K-1 to amounts reported on Exhibit C-3.

Total expenditures of federal awards per K-1	$ 16,087,524
School Health and Related Services (SHARS)	161,365
E-rate revenue reported in general fund	185,346
Total reported on and reconciled to exhibit C-3	$ 16,434,235

NOTE 15. INTERFUND TRANSFERS

All interfund transfers between various funds are approved supplements to the operations of those funds. There were no Individual fund operating transfers for fiscal year 2012.

NOTE 16. OTHER RECEIVABLES

Other receivables recorded in the fund level financial statements consisted of the following at August 31, 2012:

	General Fund	Federally Funded Grants	Non-Major Governmental Funds	Total
Services rendered	$ 101,616	$ 261,279	$ 18,510	$ 381,405
E-rate receivable	185,346	-	-	185,346
Total	$ 286,962	$ 261,279	$ 18,510	$ 566,751

NOTE 17. CLASSIFICATION OF FUND BALANCE

Fund Balance Classifications

In accordance with Governmental Accounting Standards Board Statement 54, Fund Balance Reporting and Governmental Fund Type Definitions, the District classifies governmental fund balances effective with its financial statements for the year ended August 31, 2011, and thereafter, as follows:

1. Nonspendable Fund Balance – includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual requirements. Examples include inventories, long-term receivables, endowment principal, and/or prepaid items.

NOTE 17. CLASSIFICATION OF FUND BALANCE – CONTINUED

Fund Balance Classifications – Continued

2. Spendable Fund Balance

   a. Restricted Fund Balance – includes amounts that can be spent only for the specific purposes as imposed by law, or imposed by creditors, grantors, contributors, or other governments' laws and regulations. Examples include federal and state grant programs, retirement of long-term debt, and construction.

      i. The proceeds of specific revenue sources which are restricted to expenditures for specified purposes as designated by grantors, contributors, or governmental entities over state or local program grants.
      ii. The aggregate fund balance in the debt service fund is legally restricted for payment of bonded indebtedness and is not available for other purposes until all bonded indebtedness is liquidated.

   b. Committed Fund Balance – includes amounts that can be used only for the specific purposes as determined by the governing body by formal action recorded in the minutes of the governing body. Commitments may be changed or lifted only by the governing body taking the same formal action that imposed the constraint originally. Examples include, but specifically not limited to, Board action regarding construction, claims, and judgments, retirement of loans/notes payable, capital expenditures, and self-insurance. The District's Board must take action to commit funds, modify a commitment or rescind a commitment for a specific purpose prior to the end of the fiscal year, but the amount of the commitment may be determined after the end of the fiscal year.

      i. The fund balance of the capital projects fund reflects an amount committed for construction and major renovation projects, and it usually represents unexpended proceeds from the sale of school building bonds, which primarily have restricted uses.
      ii. Campus activity funds are considered committed by the governing body through adoption of board policy pertaining to the usage of these funds.
      iii. The District's Board of Trustees voted to commit fund balance equal to 20% of the 2012 general fund expenditure budget for budgetary contingencies.

   c. Assigned Fund Balance – comprises amounts intended to be used by the District for specific purposes. Pursuant to GASB 54, this intent can be expressed by an official or body to which the governing body delegates that authority. That authority has not been delegated to any official or body. The Board of Trustees is the only governing body that can assign fund balance for specific purposes by formal action recorded in the official minutes. Examples take on the similar appearance as those enumerated for committed fund balance, but may also include the appropriation of existing fund balance to eliminate a deficit in next year's budget.

NOTE 17. CLASSIFICATION OF FUND BALANCE – CONTINUED

Fund Balance Classifications – Continued

Assigned for:	
Student transportation	$ 1,025,000
Athletic field, turf, track, other	440,000
Fine arts - ten year plan	566,000
Athletic - ten year plan	202,000
Total	$ 2,233,000

Unassigned Fund Balance – is the residual classification of the General Fund and includes all amounts not contained in other classifications. Only the general fund will have unassigned amounts. If other governmental funds incur expenditures for specified purposes that exceed the amounts restricted, committed, or assigned to those purposes, it may be necessary to report a negative unassigned fund balance.

NOTE 18. INSTRUCTIONAL MATERIALS ALLOTMENT

In May 2011, Senate Rule 6, repealed the technology allotment used by Texas schools and created an Instructional Materials Allotment (IMA) for the purchase of instructional materials, technology equipment, and technology related services. Under the IMA instructional material purchases must be made through TEA's online registration system. Instructional materials acquired through the IMA totaling $2,261,278 are recorded as revenues and expenditures in the State Instructional Materials Fund.

Ownership of textbooks previously purchased by the state and utilized by the District was transferred to the District. The majority of these textbooks were sold or otherwise disposed of in accordance with TEA guidelines. At August 31, 2012, the remainder of the textbooks, in possession of the District, have minimal value and are not otherwise reflected elsewhere in these statements.

NOTE 19. NEW ACCOUNTING PRONOUNCEMENTS

The GASB issued Statement No. 64, Accounting and Financial Reporting for Derivative Instruments, which was effective for periods beginning after June 15, 2011. The Statement clarifies the existing requirements for the termination of hedge accounting. This statement applies to all state and government entities and amends Statement 53, paragraphs 22d and 82. The District has no derivative instruments. In the future if there is a situation that applies to this Statement, the District will account for it appropriately.

NOTE 19. NEW ACCOUNTING PRONOUNCEMENTS – CONTINUED

The GASB issued Statement No. 63, Accounting and Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position, which will be effective in the fiscal year ending after December 15, 2011. The Statement will improve financial reporting by standardizing the presentation of deferred outflows of resources and deferred inflows of resources and their effects on a government's net position. It alleviates uncertainty about reporting those financial statement elements by providing guidance where none previously existed. The District will evaluate the impact of the standard on its Financial Statements and will take the necessary steps to implement it.

The GASB issued Statement No. 60, Accounting and Financial Reporting for Service Concession Arrangements, which will be effective for periods beginning after December 15, 2011. The objective of this Statement is to improve financial reporting by addressing issues related to service concession arrangements, which are a type of public-private or public-public partnership. The District will evaluate the impact of the standard on its Financial Statements and will take the necessary steps to implement it.

APPENDIX C

FORM OF BOND COUNSEL'S OPINION

Proposed Form of Opinion of Bond Counsel

An opinion in substantially the following form will be delivered by McCall, Parkhurst & Horton L.L.P., Bond Counsel, upon the delivery of the Bonds, assuming no material changes in facts or law.

LAW OFFICES

McCALL, PARKHURST & HORTON L.L.P.

600 CONGRESS AVENUE	717 NORTH HARWOOD	700 N. ST. MARY'S STREET
Suite 1800	Suite 900	Suite 1525
AUSTIN, TEXAS 78701-3248	**DALLAS, TEXAS 75201-6587**	**SAN ANTONIO, TEXAS 78205-3503**
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KELLER INDEPENDENT SCHOOL DISTRICT
UNLIMITED TAX REFUNDING BONDS,
SERIES 2013, DATED MARCH 1, 2013,
IN THE AGGREGATE PRINCIPAL AMOUNT OF $___________

AS BOND COUNSEL FOR THE ISSUER (the "Issuer") of the Bonds described above (the "Bonds"), we have examined into the legality and validity of the Bonds, which mature in principal amounts and bear interest from the dates specified in the text of the Bonds, until maturity or redemption, at the rates and payable on the dates as stated in the text of the Bonds, with the Bonds being subject to redemption prior to maturity, all in accordance with the terms and conditions stated in the text of the Bonds.

WE HAVE EXAMINED the Constitution and laws of the State of Texas, certified copies of the proceedings of the Issuer and other documents authorizing and relating to the issuance of said Bonds, including two of the executed Bonds (Bond Numbers R-1 and CR-1).

BASED ON SAID EXAMINATION, IT IS OUR OPINION that said Bonds have been authorized, issued and duly delivered in accordance with law; and that except as may be limited by governmental immunity, bankruptcy, insolvency, reorganization, moratorium liquidation and other similar laws now or hereafter enacted relating to creditor's rights generally or by principles of equity which permit the exercise of judicial discretion, the Bonds constitute valid and legally binding obligations of the Issuer; and that ad valorem taxes sufficient to provide for the payment of the interest on and principal of said Bonds have been levied and pledged for such purpose, without legal limit as to rate or amount.

IN EXPRESSING SUCH OPINION, we have considered the effect of the November 22, 2005 decision by the Texas Supreme Court in *West Orange-Cove Consolidated Independent School District, et al. v. Neeley, et al.*, upholding, in part, a lower court judgment concluding that the local ad valorem maintenance and operation tax authorized under the school finance system then in effect had become a State property tax in violation of article VIII, section 1-e of the Texas Constitution, in that school districts did not have meaningful discretion in levying the tax. The Court's opinion further noted that the court "...remain convinced...that defects in the structure of the public school finance system expose the system to constitutional challenge. . . . [Such challenges] will repeat until the system is overhauled." Subsequent to such decision, legislation was enacted by the Texas Legislature to address the constitutional issues raised in the court's ruling. Reference is made to the Official Statement for the Bonds for a further description of the rulings and the legislation enacted by the Texas Legislature.

IT IS FURTHER OUR OPINION, except as discussed below, that the interest on the Bonds is excludable from the gross income of the owners thereof for federal income tax purposes under the statutes, regulations, published rulings and court decisions existing on the date of this opinion. We are further of the opinion that the Bonds are not "specified private activity bonds" and that, accordingly, interest on the Bonds will not be included as an individual or corporate alternative minimum tax preference item under Section 57(a)(5) of the Internal Revenue Code of 1986 (the "Code"). In expressing the aforementioned opinions, we have relied on, and assume compliance by the Issuer with, certain covenants regarding the use and investment of the proceeds of the Bonds and the use of the property financed therewith, the report of Grant Thornton LLP and the certificate with respect to arbitrage by the Commissioner of Education regarding the allocation and investment of certain investments in the Permanent School Fund. We call your attention to the fact that if such representations are determined to be inaccurate or upon failure by the Issuer to comply with such covenants, interest on the Bonds may become includable in gross income retroactively to the date of issuance of the Bonds.

EXCEPT AS STATED ABOVE, we express no opinion as to any other federal, state or local tax consequences of acquiring, carrying, owning or disposing of the Bonds.

WE CALL YOUR ATTENTION TO THE FACT that the interest on tax-exempt obligations, such as the Bonds is included in a corporation's alternative minimum taxable income for purposes of determining the alternative minimum tax imposed on corporations by Section 55 of the Code.

WE EXPRESS NO OPINION as to any insurance policies issued with respect to the payments due for the principal of and interest on the Bonds, nor as to any such insurance policies issued in the future.

OUR SOLE ENGAGEMENT in connection with the issuance of the Bonds is as Bond Counsel for the Issuer, and, in that capacity, we have been engaged by the Issuer for the sole purpose of rendering an opinion with respect to the legality and validity of the Bonds under the Constitution and laws of the State of Texas, and with respect to the exclusion from gross income of the interest on the Bonds for federal income tax purposes, and for no other reason or purpose. The foregoing opinions represent our legal judgment based upon a review of existing legal authorities that we deem relevant to render such opinions and are not a guarantee of a result. We have not been requested to investigate or verify, and have not independently investigated or verified any records, data, or other material relating to the financial condition or capabilities of the Issuer, or the disclosure thereof in connection with the sale of the Bonds, and have not assumed any responsibility with respect thereto. We express no opinion and make no comment with respect to the marketability of the Bonds and have relied solely on certificates executed by officials of the Issuer as to the current outstanding indebtedness of, and assessed valuation of taxable property within the Issuer. Our role in connection with the Issuer's Official Statement prepared for use in connection with the sale of the Bonds has been limited as described therein.

OUR OPINIONS 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 our opinions to reflect any facts or circumstances that may thereafter come to our attention or to reflect any changes in any law that may thereafter occur or become effective. Moreover, our opinions are not a guarantee of a result and are not binding on the Internal Revenue Service (the "Service"). Rather, our 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 Bonds. If an audit is commenced, in accordance with its current published procedures the Service is likely to treat the Issuer as the taxpayer. We observe that the Issuer has covenanted not to take any action, or omit to take any action within its control, that if taken or omitted, respectively, might result in the treatment of interest on the Bonds as includable in gross income for federal income tax purposes.

Respectfully,

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