OFFICIAL STATEMENT

Dated April 12, 2013

Rating:
S&P: "AA-"
(See "OTHER INFORMATION - RATING" herein)

NEW ISSUE – Book-Entry-Only

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.

$7,280,000
CITY OF SAN MARCOS, TEXAS
(Hays, Caldwell and Guadalupe Counties)
GENERAL OBLIGATION REFUNDING BONDS, SERIES 2013

Dated Date: April 1, 2013 **Due: August 15, as shown on the inside cover page**
Interest Accrues from the Date of Initial Delivery

PAYMENT TERMS . . . Interest on the $7,280,000 City of San Marcos, Texas General Obligation Refunding Bonds, Series 2013 (the "Bonds") will accrue from the date of initial delivery, will be payable on August 15 and February 15 of each year commencing August 15, 2013, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The definitive Bonds will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company, New York, New York ("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 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 OBLIGATIONS – BOOK-ENTRY-ONLY SYSTEM"). The initial Paying Agent/Registrar is Regions Bank, Houston, Texas (see "THE OBLIGATIONS – PAYING AGENT/REGISTRAR").

AUTHORITY FOR ISSUANCE . . . The Bonds are being issued pursuant to the Constitution and general laws of the State of Texas including particularly Chapters 1207 and 1371, Texas Government Code, as amended, an ordinance authorizing the issuance of the Bonds adopted by the City Council of the City on April 2, 2013 and a pricing certificate executed by the pricing officer as designated in the ordinance (collectively, the "Bond Ordinance"). The Bonds are direct obligations of the City payable from the levy and collection of a direct and continuing ad valorem tax levied, within the limits prescribed by law, on all taxable property within the City as provided in the Bond Ordinance) (see "THE OBLIGATIONS – AUTHORITY FOR ISSUANCE" and "THE OBLIGATIONS – SECURITY AND SOURCE OF PAYMENT").

PURPOSE . . . Proceeds from the sale of the Bonds will be used to (i) refund certain outstanding obligations of the City as shown on SCHEDULE I hereto (the "Tax Exempt Refunded Obligations") to achieve a debt service savings; and (ii) pay the costs of issuing the Bonds (see "PLAN OF FINANCING").

CUSIP PREFIX: 798764
MATURITY SCHEDULE
See Inside Front Cover

REDEMPTION . . . The City reserves the right, at its option, to redeem Bonds having stated maturities on and after August 15, 2024, in whole or from time to time in part in principal amounts of $5,000 or any integral multiple thereof, on August 15, 2023, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption (see "THE OBLIGATIONS – OPTIONAL REDEMPTION"). Additionally, Term Bonds maturing on August 15, 2022 are subject to mandatory sinking fund redemption (see "THE OBLIGATIONS – MANDATORY SINKING FUND REDEMPTION").

LEGALITY . . . The Bonds are offered by the City subject to prior sale, when, as and if issued by the City and accepted by the Underwriters, subject, among other things, to the approval of the Initial Bond by the Attorney General of the State of Texas and the approval of certain legal matters by McCall, Parkhurst & Horton L.L.P., Bond Counsel, Austin, Texas. Certain legal matters will be passed upon for the Underwriters by their counsel, Andrews Kurth LLP, Austin, Texas.

DELIVERY . . . Delivery of the Bonds is expected through the facilities of DTC on May 21, 2013.

STEPHENS INC.
COMERICA SECURITIES

SAMCO CAPITAL MARKETS, INC.
BOSC, INC.
A subsidiary of BOK Financial Corporation

MATURITY SCHEDULE

Maturity (August 15)	Amount	Rate	Initial Yield		CUSIP Numbers[1]
2013	$ 105,000	1.000%	0.300%		7987643B0
2014	1,390,000	1.500%	0.400%		7987643C8
2015	90,000	2.000%	0.610%		7987643D6
2016	85,000	2.000%	0.790%		7987643E4
2017	45,000	2.000%	0.980%		7987643F1
2018	40,000	3.000%	1.220%		7987643G9
***	***	***			***
2023	50,000	3.000%	2.460%		7987643J3
2024	50,000	3.000%	2.690%	(2)	7987643K0
***	***	***	***		***
2030	2,980,000	5.000%	3.090%	(2)	7987643L8
2031	2,260,000	5.000%	3.140%	(2)	7987643M6

$185,000 3.000% Term Bonds due August 15, 2022, Priced at 105.620% to Yield 2.320% – 7987643H7[1]

(Interest Accrues from the Date of Initial Delivery)

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(1) CUSIP is a registered trademark of the American Bankers Association. CUSIP data herein 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. CUSIP numbers are included herein solely for the convenience of the owners of the Bonds. Neither the City, the Financial Advisor nor the Underwriters during pricing shall be responsible for the selection or correctness of the CUSIP numbers shown herein.

(2) Yield calculated based on the assumption that the Bonds denoted and sold at a premium will be redeemed on August 15, 2023, the first optional call date for such Bonds, at a redemption price of par, plus accrued interest to the redemption date.

SEPARATE ISSUES . . . The Bonds are being offered by the City concurrently with the "City of San Marcos, Texas, General Obligation Refunding Bonds, Taxable Series 2013" (the "Taxable Bonds") and the "City of San Marcos, Texas, Combination Tax and Revenue Certificates of Obligation, Series 2013" (the "Certificates"), under a common Official Statement, and such Bonds, Taxable Bonds and Certificates are hereinafter sometimes referred to collectively as the "Obligations." The Bonds, the Taxable Bonds and the Certificates are separate and distinct securities offerings being issued and sold independently except for the common Official Statement, and, while the Obligations share certain common attributes, each issue is separate from the other and should be reviewed and analyzed independently, including the type of obligation being offered, its terms for payment, the security for its payment, the rights of the holders, and other features.

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OFFICIAL STATEMENT

Dated April 12, 2013

Rating:
S&P: "AA-"
(See "OTHER INFORMATION - RATING" herein)

NEW ISSUE – Book-Entry-Only

The Taxable Bonds are not obligations described in Section 103(a) of the Internal Revenue Code of 1986. See "TAX MATTERS" herein.

$11,980,000
CITY OF SAN MARCOS, TEXAS
(Hays, Caldwell and Guadalupe Counties)
GENERAL OBLIGATION REFUNDING BONDS, TAXABLE SERIES 2013

Dated Date: April 1, 2013 **Due: August 15, as shown on the inside cover page**
Interest Accrues from the Date of Initial Delivery

PAYMENT TERMS . . . Interest on the $11,980,000 City of San Marcos, Texas General Obligation Refunding Bonds, Taxable Series 2013 (the "Taxable Bonds") will accrue from the date of initial delivery, will be payable on August 15 and February 15 of each year commencing August 15, 2013, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The definitive Taxable Bonds will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company, New York, New York ("DTC") pursuant to the book-entry-only system described herein. Beneficial ownership of the Taxable Bonds may be acquired in denominations of $5,000 or integral multiples thereof. **No physical delivery of the Taxable Bonds will be made to the beneficial owners thereof.** Principal of, premium, if any, and interest on the Taxable 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 Taxable Bonds (see "THE OBLIGATIONS – BOOK-ENTRY-ONLY SYSTEM"). The initial Paying Agent/Registrar is Regions Bank, Houston, Texas (see "THE OBLIGATIONS – PAYING AGENT/REGISTRAR").

AUTHORITY FOR ISSUANCE . . . The Taxable Bonds are being issued pursuant to the Constitution and general laws of the State of Texas including particularly Chapters 1207 and 1371, Texas Government Code, as amended, an ordinance authorizing the issuance of the Taxable Bonds adopted by the City Council of the City on April 2, 2013 and a pricing certificate executed by the pricing officer as designated in the ordinance (collectively, the "Taxable Bond Ordinance"). The Taxable Bonds are direct obligations of the City payable from the levy and collection of a direct and continuing ad valorem tax levied, within the limits prescribed by law, on all taxable property within the City as provided in the Taxable Bond Ordinance) (see "THE OBLIGATIONS – AUTHORITY FOR ISSUANCE" and "THE OBLIGATIONS – SECURITY AND SOURCE OF PAYMENT").

PURPOSE . . . Proceeds from the sale of the Taxable Bonds will be used to (i) refund certain outstanding obligations of the City as shown on SCHEDULE II hereto (the "Taxable Refunded Obligations") to achieve a debt service savings; and (ii) pay the costs of issuing the Taxable Bonds (see "PLAN OF FINANCING").

CUSIP PREFIX: 798764
MATURITY SCHEDULE
See Page 4

REDEMPTION . . . The Taxable Bonds are not subject to optional redemption prior to their stated maturities (see "THE OBLIGATIONS – OPTIONAL REDEMPTION").

LEGALITY . . . The Taxable Bonds are offered by the City subject to prior sale, when, as and if issued by the City and accepted by the Underwriters, subject, among other things, to the approval of the Initial Taxable Bond by the Attorney General of the State of Texas and the approval of certain legal matters by McCall, Parkhurst & Horton L.L.P., Bond Counsel, Austin, Texas. Certain legal matters will be passed upon for the Underwriters by their counsel, Andrews Kurth LLP, Austin, Texas.

DELIVERY . . . Delivery of the Taxable Bonds is expected through the facilities of DTC on May 21, 2013.

STEPHENS INC.
COMERICA SECURITIES

SAMCO CAPITAL MARKETS, INC.
BOSC, INC.
A subsidiary of BOK Financial Corporation

MATURITY SCHEDULE

Maturity (August 15)	Amount	Rate	Initial Yield	CUSIP Numbers[(1)]
2013	$ 110,000	0.480%	0.480%	7987644E3
2014	195,000	0.630%	0.630%	7987644F0
2015	1,045,000	0.780%	0.780%	7987644G8
2016	1,060,000	1.047%	1.047%	7987644H6
2017	1,070,000	1.278%	1.278%	7987644J2
2018	2,770,000	1.578%	1.578%	7987644K9
2019	2,830,000	1.886%	1.886%	7987644L7
2020	2,900,000	2.036%	2.036%	7987644M5

(Interest Accrues from the Date of Initial Delivery)

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Separate Issues . . . The Taxable Bonds are being offered by the City concurrently with the "City of San Marcos, Texas, General Obligation Refunding Bonds, Series 2013" (the "Bonds") and the "City of San Marcos, Texas, Combination Tax and Revenue Certificates of Obligation, Series 2013" (the "Certificates"), under a common Official Statement, and such Bonds, Taxable Bonds and Certificates are hereinafter sometimes referred to collectively as the "Obligations." The Bonds, the Taxable Bonds and the Certificates are separate and distinct securities offerings being issued and sold independently except for the common Official Statement, and, while the Obligations share certain common attributes, each issue is separate from the other and should be reviewed and analyzed independently, including the type of obligation being offered, its terms for payment, the security for its payment, the rights of the holders, and other features.

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OFFICIAL STATEMENT

Dated April 12, 2013

Rating:
S&P: "AA-"
(See "OTHER INFORMATION - RATING" herein)

NEW ISSUE – Book-Entry-Only

In the opinion of Bond Counsel, interest on the Certificates 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.

$11,870,000
CITY OF SAN MARCOS, TEXAS
(Hays, Caldwell and Guadalupe Counties)
COMBINATION TAX AND REVENUE CERTIFICATES OF OBLIGATION, SERIES 2013

Dated Date: April 1, 2013 **Due: August 15, as shown on the next page**
Interest Accrues from the Date of Initial Delivery

PAYMENT TERMS . . . Interest on the $11,870,000 City of San Marcos, Texas Combination Tax and Revenue Certificates of Obligation, Series 2013 (the "Certificates") will accrue from the date of initial delivery, will be payable on February 15 and August 15 of each year commencing February 15, 2014, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The definitive Certificates will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company, New York, New York ("DTC") pursuant to the book-entry-only system described herein. Beneficial ownership of the Certificates may be acquired in denominations of $5,000 or integral multiples thereof. **No physical delivery of the Certificates will be made to the beneficial owners thereof.** Principal of, premium, if any, and interest on the Certificates will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Certificates (see "THE OBLIGATIONS – BOOK-ENTRY-ONLY SYSTEM"). The initial Paying Agent/Registrar is Regions Bank, Houston, Texas (see "THE OBLIGATIONS – PAYING AGENT/REGISTRAR").

AUTHORITY FOR ISSUANCE . . . The Certificates are issued pursuant to the Constitution and general laws of the State of Texas (the "State"), particularly Subchapter C of Chapter 271, Texas Local Government Code, as amended (the "Certificate of Obligation Act of 1971"), Chapters 1371 and 1502, Texas Government Code, as amended, an ordinance authorizing the issuance of the Certificates adopted by the City Council of the City on April 2, 2013 and a pricing certificate executed by the pricing officer as designated in the ordinance (collectively, the "Certificate Ordinance"). The Certificates constitute direct obligations of the City of San Marcos, Texas (the "City"), payable from a continuing ad valorem tax levied on all taxable property within the City, within the limits prescribed by law, and a limited pledge of the surplus revenues of the City's waterworks and sewer system (not to exceed $1,000) as provided in the Certificate Ordinance (see "THE OBLIGATIONS – AUTHORITY FOR ISSUANCE" and "THE OBLIGATIONS – SECURITY AND SOURCE OF PAYMENT").

PURPOSE . . . Proceeds from the sale of the Certificates will be used for (i) constructing, improving and extending the City's water and wastewater system; (ii) improving and upgrading the City airport including reconditioning the runway and acquisition of land; (iii) designing and improving the existing City animal shelter; (iv) acquisition and installation of energy efficiency improvements for City facilities; (v) constructing and improving the City's drainage facilities; (vi) constructing and improving the City's electric system including replacement and upgrade of substation power transformer T-1; (vii) upgrading technology for City facilities; (viii) engineering, architecture and other related costs for future capital improvement planning; (ix) acquisition of public safety equipment and fire trucks; (x) constructing, improving, extending, expanding, upgrading and developing City streets, bridges, sidewalks, intersections and related traffic improvements including purchasing any necessary rights-of-way, equipment, pedestrian and bike routes, traffic signalization, updating traffic master plan and implementing railroad quiet zones; (xi) acquiring property for transit stop; and (xii) the payment of professional services in connection therewith including legal, fiscal and engineering fees and the costs of issuing the Certificates.

CUSIP PREFIX: 798764
MATURITY SCHEDULE
See Page 6

REDEMPTION . . . The City reserves the right, at its option, to redeem Certificates having stated maturities on and after August 15, 2023, in whole or from time to time in part in principal amounts of $5,000 or any integral multiple thereof, on August 15, 2022, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption (see "THE OBLIGATIONS – OPTIONAL REDEMPTION"). Additionally, Term Certificates maturing on August 15 in the years 2030 and 2033 are subject to mandatory sinking fund redemption (see "THE OBLIGATIONS – MANDATORY SINKING FUND REDEMPTION").

LEGALITY . . . The Certificates are offered by the City subject to prior sale, when, as and if issued by the City and accepted by the Underwriters, subject, among other things, to the approval of the Initial Certificate by the Attorney General of the State of Texas and the approval of certain legal matters by McCall, Parkhurst & Horton L.L.P., Bond Counsel, Austin, Texas. Certain legal matters will be passed upon for the Underwriters by their counsel, Andrews Kurth LLP, Austin, Texas.

DELIVERY . . . Delivery of the Certificates is expected through the facilities of DTC on May 21, 2013.

STEPHENS INC.
COMERICA SECURITIES

SAMCO CAPITAL MARKETS, INC.
BOSC, INC.
A subsidiary of BOK Financial Corporation

MATURITY SCHEDULE

Maturity (August 15)	Amount	Rate	Initial Yield		CUSIP Numbers[1]
2015	$ 435,000	2.000%	0.610%		7987643N4
2016	455,000	2.000%	0.790%		7987643P9
2017	480,000	2.000%	0.980%		7987643Q7
2018	495,000	3.000%	1.220%		7987643R5
2019	525,000	3.000%	1.470%		7987643S3
2020	540,000	3.000%	1.730%		7987643T1
2021	555,000	3.000%	1.990%		7987643U8
2022	570,000	3.000%	2.270%		7987643V6
2023	590,000	3.000%	2.460%	(2)	7987643W4
2024	605,000	4.000%	2.640%	(2)	7987643X2
2025	635,000	4.000%	2.820%	(2)	7987643Y0
2026	650,000	4.000%	3.010%	(2)	7987643Z7
2027	685,000	4.000%	3.120%	(2)	7987644A1
2028	710,000	4.000%	3.210%	(2)	7987644B9

$1,500,000 3.375% Term Certificates due August 15, 2030, Priced at 98.516% to Yield 3.490% – 7987644C7[1]
$2,440,000 3.500% Term Certificates due August 15, 2033, Priced at 98.003% to Yield 3.640% – 7987644D5[1]

(Interest Accrues from the Date of Initial Delivery)

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(2) Yield calculated based on the assumption that the Bonds denoted and sold at a premium will be redeemed on August 15, 2022, the first optional call date for such Bonds, at a redemption price of par, plus accrued interest to the redemption date.

SEPARATE ISSUES . . . The Certificates are being offered by the City concurrently with the "City of San Marcos, Texas, General Obligation Refunding Bonds, Series 2013" (the "Bonds") and the "City of San Marcos, Texas, General Obligation Refunding Bonds, Taxable Series 2013" (the "Taxable Bonds") under a common Official Statement, and such Certificates, Taxable Bonds and Bonds are hereinafter sometimes referred to collectively as the "Obligations." The Certificates, the Taxable Bonds and the Bonds are separate and distinct securities offerings being issued and sold independently except for the common Official Statement, and, while the Obligations share certain common attributes, each issue is separate from the other and should be reviewed and analyzed independently, including the type of obligation being offered, its terms for payment, the security for its payment, the rights of the holders, and other features.

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No dealer, broker, salesman or other person has been authorized by the City 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 City or the Financial Advisor. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy Obligations in any jurisdiction in which, or to any person to whom, it is unlawful to make such offer or solicitation.

The information set forth or included in this Official Statement has been provided by the City or obtained from other sources believed by the City to be reliable. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale hereunder shall create any implication that there has been no change in the financial condition or operations of the City described herein since the date hereof. This Official Statement contains, in part, estimates and matters of opinion that are not intended as statements of fact, and no representation or warranty is made as to the correctness of such estimates and opinions or that they will be realized.

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

THE OBLIGATIONS ARE EXEMPT FROM REGISTRATION WITH THE SECURITIES AND EXCHANGE COMMISSION AND CONSEQUENTLY HAVE NOT BEEN REGISTERED THEREWITH. THE REGISTRATION, QUALIFICATION, OR EXEMPTION OF THE OBLIGATIONS IN ACCORDANCE WITH APPLICABLE SECURITIES LAW PROVISIONS OF THE JURISDICTION IN WHICH THESE SECURITIES HAVE BEEN REGISTERED, OR EXEMPTED SHOULD NOT BE REGARDED AS A RECOMMENDATION THEREOF.

THE PRICES AND OTHER TERMS RESPECTING THE OFFERING AND SALE OF THE OBLIGATIONS MAY BE CHANGED FROM TIME TO TIME BY THE UNDERWRITERS AFTER THE OBLIGATIONS ARE RELEASED FOR SALE, AND THE OBLIGATIONS MAY BE OFFERED AND SOLD AT PRICES OTHER THAN THE INITIAL OFFERING PRICES, INCLUDING SALES TO DEALERS WHO MAY SELL THE OBLIGATIONS INTO INVESTMENT ACCOUNTS.

THE UNDERWRITERS HAVE PROVIDED THE FOLLOWING SENTENCE FOR INCLUSION IN THIS OFFICIAL STATEMENT. THE UNDERWRITERS HAVE REVIEWED THE INFORMATION IN THIS OFFICIAL STATEMENT PURSUANT TO THEIR RESPECTIVE RESPONSIBILITIES TO INVESTORS UNDER THE FEDERAL SECURITIES LAWS, BUT THE UNDERWRITERS DO NOT GUARANTEE THE ACCURACY OF OR COMPLETENESS OF SUCH INFORMATION.

NONE OF THE CITY, ITS FINANCIAL ADVISOR, OR 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.

TABLE OF CONTENTS

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

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 Obligations 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 OBLIGATIONS

THE OBLIGATIONS........................... The Bonds are issued as $7,280,000 General Obligation Refunding Bonds, Series 2013. The Bonds are issued as serial Bonds maturing on August 15 in the years 2013 through 2018 and 2023 through 2024 and 2030 through 2031 and as Term Bonds maturing August 15, 2022.

The Taxable Bonds are issued as $11,980,000 General Obligation Refunding Bonds, Taxable Series 2013. The Taxable Bonds are issued as serial Bonds maturing on August 15 in the years 2013 through 2020, inclusive.

The Certificates are issued as $11,870,000 Combination Tax and Revenue Certificates of Obligation, Series 2013. The Certificates are issued as serial Certificates maturing on August 15 in the years 2015 through 2028 and as Term Certificates maturing on August 15 in the years 2030 and 2033.

PAYMENT OF INTEREST .... Interest on the Bonds and the Taxable Bonds accrues from the date of initial delivery and is payable on August 15, 2013, and each February 15 and August 15 thereafter until maturity or prior redemption.

Interest on the Certificates accrues from the date of initial delivery and is payable on February 15, 2014, and each August 15 and February 15 thereafter until maturity or prior redemption (see "THE OBLIGATIONS – DESCRIPTION OF THE OBLIGATIONS" and "THE OBLIGATIONS – OPTIONAL REDEMPTION").

AUTHORITY FOR ISSUANCE .... The Bonds are being issued pursuant to the Constitution and general laws of the State of Texas (the "State") including particularly Chapters 1207 and 1371, Texas Government Code, as amended, an ordinance authorizing the issuance of the Bonds adopted by the City Council of the City on April 2, 2013 and a pricing certificate executed by the pricing officer as designated in the ordinance (collectively, the "Bond Ordinance").

The Taxable Bonds are being issued pursuant to the Constitution and general laws of the State of Texas including particularly Chapters 1207 and 1371, Texas Government Code, as amended, an ordinance authorizing the issuance of the Taxable Bonds adopted by the City Council of the City on April 2, 2013 and a pricing certificate executed by the pricing officer as designated in the ordinance (collectively, the "Taxable Bond Ordinance").

The Certificates are issued pursuant to the Constitution and general laws of the State, particularly Subchapter C of Chapter 271, Texas Local Government Code, as amended (the "Certificate of Obligation Act of 1971"), and Chapters 1371 and 1502, Texas Government Code, as amended, the City's Home Rule Charter and an ordinance authorizing the issuance of the Certificates adopted by the City Council of the City on April 2, 2013 and a pricing certificate executed by the pricing officer as designated in the ordinance (collectively, the "Certificate Ordinance") (see "THE OBLIGATIONS – AUTHORITY FOR ISSUANCE").

SECURITY.. The Obligations constitute direct obligations of the City, payable from the levy and collection of a direct and continuing ad valorem tax levied, within the limits prescribed by law, on all taxable property located within the City as provided in the respective ordinance authorizing the issuance of the Obligations (the "Bond Ordinance," the "Taxable Bond Ordinance" or the "Certificate Ordinance", as applicable and collectively, the "Ordinances"). The Certificates are additionally secured by a limited pledge of surplus net revenues of the City's Waterworks and Waste Water System (not to exceed $1,000) as provided in the Certificate Ordinance (see "THE OBLIGATIONS – SECURITY AND SOURCE OF PAYMENT").

REDEMPTION .... The City reserves the right, at its option, to redeem the Bonds having stated maturities on and after August 15, 2024, in whole or from time to time in part in principal amounts of

$5,000 or any integral multiple thereof on August 15, 2023, or any date thereafter, at par value thereof plus accrued interest to the date of redemption.

The City reserves the right, at its option, to redeem the Certificates having stated maturities on and after August 15, 2023, in whole or from time to time in part in principal amounts of $5,000 or any integral multiple thereof, on August 15, 2022, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption.

The Taxable Bonds are not subject to redemption prior to their stated maturities (see "THE OBLIGATIONS – OPTIONAL REDEMPTION").

Additionally, Term Bonds maturing on August 15, 2022 and Term Certificates maturing on August 15 in the years 2030 and 2033 are subject to mandatory sinking fund redemption (see "THE OBLIGATIONS – MANDATORY SINKING FUND REDEMPTION").

TAX EXEMPTION.............................. In the opinion of Bond Counsel, the interest on the Bonds and Certificates 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 the caption "TAX MATTERS" herein including the alternative minimum tax on corporations.

The Taxable Bonds are not obligations described in Section 103(a) of the Internal Revenue Code of 1986.

USE OF PROCEEDS .... Proceeds from the sale of the Bonds will be used to (i) refund certain outstanding obligations of the City as shown on SCHEDULE I hereto (the "Tax Exempt Refunded Obligations") to achieve a debt service savings; and (ii) pay the costs of issuing the Bonds.

Proceeds from the sale of the Taxable Bonds will be used to (i) refund certain outstanding obligations of the City as shown on SCHEDULE II hereto (the "Taxable Refunded Obligations") to achieve a debt service savings; and (ii) pay the costs of issuing the Taxable Bonds.

Proceeds from the sale of the Certificates will be used for (i) constructing, improving and extending the City's water and wastewater system; (ii) improving and upgrading the City airport including reconditioning the runway and acquisition of land; (iii) designing and improving the existing City animal shelter; (iv) acquisition and installation of energy efficiency improvements for City facilities; (v) constructing and improving the City's drainage facilities; (vi) constructing and improving the City's electric system including replacement and upgrade of substation power transformer T-1; (vii) upgrading technology for City facilities; (viii) engineering, architecture and other related costs for future capital improvement planning; (ix) acquisition of public safety equipment and fire trucks; (x) constructing, improving, extending, expanding, upgrading and developing City streets, bridges, sidewalks, intersections and related traffic improvements including purchasing any necessary rights-of-way, equipment, pedestrian and bike routes, traffic signalization, updating traffic master plan and implementing railroad quiet zones; (xi) acquiring property for transit stop; and (xii) the payment of professional services in connection therewith including legal, fiscal and engineering fees and the costs of issuing the Certificates (see "PLAN OF FINANCING").

GENERAL

THE CITY.. The City of San Marcos, Texas (the "City"), is a political subdivision located in Hays, Caldwell and Guadalupe Counties operating as a home-rule city under the laws of the State and a home-rule charter, initially approved by the voters in 1967 and last amended on November 2, 2010. The City operates under the City Council/Manager form of government where the Mayor is elected for a term of two years and two (of six) Councilmembers are elected each year to serve a three-year term. The City Council formulates operating policy for the City while the City Manager is the chief administrative officer. The City is approximately 27.79 square miles in area (see "APPENDIX A – GENERAL INFORMATION REGARDING THE CITY").

RATING.. The Obligations have been rated "AA-" by Standard and Poor's Ratings Services, A Standard & Poor's Financial Services LLC business ("S&P"). The outstanding general obligation debt of the City is rated "Aa2" by Moody's Investors Service ("Moody's"). The City has not applied to Moody's for a rating on the Obligations. The City also has various issues outstanding which are rated based on insurance provided by various commercial insurance companies (see "OTHER INFORMATION – RATING").

BOOK-ENTRY-ONLY SYSTEM........... The definitive Obligations 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 Obligations may be acquired in denominations of $5,000 or integral multiples thereof. No physical delivery of the Obligations will be made to the beneficial owners thereof. Principal of, premium, if any, and interest on the Obligations 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 Obligations (see "THE OBLIGATIONS – BOOK-ENTRY-ONLY SYSTEM").

PAYMENT RECORD........................... The City has never defaulted in the payment of its debt.

SELECTED FINANCIAL INFORMATION

Fiscal Year Ended 9/30	Estimated Population [1]	Taxable Assessed Valuation	Taxable Assessed Valuation Per Capita	Funded Debt Outstanding at End of Year [2]	Ratio of Funded Debt to Taxable Assessed Valuation	Funded Debt Per Capita	% Total Collections to Date
2009	50,913	$ 2,623,365,186	$ 51,526	$ 77,960,000	2.97%	$ 1,531	100.70%
2010	53,913 [3]	2,504,035,456	46,446	86,585,000	3.46%	1,606	100.55%
2011	47,505	2,452,170,753	51,619	74,615,000	3.04%	1,571	100.85%
2012	53,065	2,699,706,853	50,875	71,980,000	2.67%	1,356	100.14%
2013	53,065	2,840,899,896	53,536	72,515,000 [4]	2.55%	1,367	96.90% [5]

(1) Source: the City.
(2) Excludes self-supporting debt. See "Table 1 – Valuation, Exemption and General Obligation Debt, footnote 3."
(3) The 2010 Census Number was 44,894. The City is challenging this number.
(4) Projected; includes the Obligations and excludes the Tax-Exempt Refunded Obligations and the Taxable Refunded Obligations.
(5) As of March 15, 2013.

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CITY OFFICIALS, STAFF AND CONSULTANTS

ELECTED OFFICIALS

City Council	Length of Service	Term Expires
Daniel Guerrero Mayor	2½ Years	November 2015
Kim Porterfield Councilmember, District 1	5½ Years	November 2013
Jude Prather Councilmember, District 2	2½ Years	November 2013
John Thomaides Councilmember, District 3	1½ Years	November 2014
Wayne Becak Councilmember, District 4	1½ Years	November 2014
Ryan Thomason Councilmember, District 5	3½ Years	November 2015
Shane Scott Councilmember, District 6	2½ Years	November 2015

SELECTED ADMINISTRATIVE STAFF

Name	Position
Jim Nuse	City Manager
Collette Jamison	Assistant City Manager
Steve Parker	Assistant City Manager/Director of Finance
Heather Hurlbert	Assistant Director of Finance
Jamie Lee Pettijohn	City Clerk
Michael Cosentino	City Attorney

CONSULTANTS AND ADVISORS

Auditors .... Pattillo, Brown & Hill, L.L.P.
Waco, Texas

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

Financial Advisor.. Specialized Public Finance Inc.
Austin, Texas

For additional information regarding the City, please contact:

Mr. Steve Parker
Assistant City Manager/ Director of Finance
City of San Marcos, Texas
630 East Hopkins
San Marcos, Texas 78666
512/393-8170
512/392-4612 Fax

or

Mr. Dan Wegmiller
Managing Director
Specialized Public Finance Inc.
7000 N. MoPac Expressway, Suite 410
Austin, Texas 78731
512/275-7300
512/275-7305 Fax

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OFFICIAL STATEMENT
RELATING TO

$7,280,000
CITY OF SAN MARCOS, TEXAS
GENERAL OBLIGATION REFUNDING
BONDS, SERIES 2013

$11,980,000
CITY OF SAN MARCOS, TEXAS
GENERAL OBLIGATION REFUNDING
BONDS, TAXABLE SERIES 2013

$11,870,000
CITY OF SAN MARCOS, TEXAS
COMBINATION TAX AND REVENUE
CERTIFICATES OF OBLIGATION, SERIES 2013

INTRODUCTION

This Official Statement, which includes the Appendices hereto, provides certain information regarding the issuance of $7,280,000 City of San Marcos, Texas General Obligation Refunding Bonds, Series 2013 (the "Bonds"), the $11,980,000 City of San Marcos, Texas General Obligation Refunding Bonds, Taxable Series 2013 (the "Taxable Bonds") and $11,870,000 City of San Marcos, Texas Combination Tax and Revenue Certificates of Obligation, Series 2013 (the "Certificates") (collectively, the "Obligations"). Capitalized terms used in this Official Statement have the same meanings assigned to such terms in the respective ordinance (the "Bond Ordinance", the "Taxable Bond Ordinance" or the "Certificate Ordinance", as applicable and collectively, the "Ordinances"), except as otherwise indicated herein.

There follows in this Official Statement descriptions of the Obligations and certain information regarding the City and its finances. All descriptions of documents contained herein are only summaries and are qualified in their entirety by reference to each such document. Copies of such documents may be obtained from the City's Financial Advisor, Specialized Public Finance Inc., Austin, Texas, by electronic mail or upon payment of reasonable copying, handling, and delivery charges.

This Official Statement speaks only as to its date, and the information contained herein is subject to change. A copy of the Final Official Statement pertaining to the Obligations will be submitted to the Municipal Securities Rulemaking Board through its Electronic Municipal Market Access ("EMMA") system. See "CONTINUING DISCLOSURE OF INFORMATION" herein for a description of the City's undertaking to provide certain information on a continuing basis.

DESCRIPTION OF THE CITY . . . The City is a political subdivision located in Hays, Caldwell and Guadalupe Counties in the State of Texas (the "State"), duly organized and existing under the laws of the State, including the City's Home Rule Charter initially adopted by the voters in 1967, last amended on November 2, 2010. The City was incorporated in 1877. The City operates as a home-rule city under the Council/Manager form of government with a City Council comprised of the Mayor and six Councilmembers. The term of office of the Mayor is two years and the term of office of each Councilmember is three years, with staggered terms so that two members are elected to a regular term each year. The City Manager is the chief administrative officer for the City. Some of the services that the City provides are: public safety (police and fire protection), highways and streets, electric, water and sanitary wastewater utilities, health and social services, culture-recreation, public transportation, public improvements, planning and zoning, and general administrative services. The City is approximately 27.79 square miles in area. For more information regarding the City, see "APPENDIX A – GENERAL INFORMATION REGARDING THE CITY."

PLAN OF FINANCING

PURPOSE . . . Proceeds from the sale of the Bonds will be used to (i) refund certain outstanding obligations of the City as shown on SCHEDULE I hereto (the "Tax-Exempt Refunded Obligations") to achieve a debt service savings; and (ii) pay the costs of issuing the Bonds.

Proceeds from the sale of the Taxable Bonds will be used to (i) refund certain outstanding obligations of the City as shown on SCHEDULE II hereto (the "Taxable Refunded Obligations") to achieve a debt service savings; and (ii) pay the costs of issuing the Taxable Bonds.

Proceeds from the sale of the Certificates will be used for (i) constructing, improving and extending the City's water and wastewater system; (ii) improving and upgrading the City airport including reconditioning the runway and acquisition of land; (iii) designing and improving the existing City animal shelter; (iv) acquisition and installation of energy efficiency improvements for City facilities; (v) constructing and improving the City's drainage facilities; (vi) constructing and improving the City's electric system including replacement and upgrade of substation power transformer T-1; (vii) upgrading technology for City facilities; (viii) engineering, architecture and other related costs for future capital improvement planning; (ix) acquisition of public safety equipment and fire trucks; (x) constructing, improving, extending, expanding, upgrading and developing City streets, bridges, sidewalks, intersections and related traffic improvements including purchasing any necessary rights-of-way, equipment, pedestrian and bike routes, traffic signalization, updating traffic master plan and implementing railroad quiet zones; (xi) acquiring property for transit stop; and (xii) the payment of professional services in connection therewith including legal, fiscal and engineering fees and the costs of issuing the Certificates.

REFUNDED OBLIGATIONS . . . The principal of and interest due on the Tax-Exempt Refunded Obligations and the Taxable Refunded Obligations (collectively, the “Refunded Obligations”) are to be paid on the scheduled interest payment dates, maturity dates and the respective redemption dates of such Refunded Obligations, as applicable, from funds and direct obligations of the United States of America to be deposited pursuant to a certain escrow agreement (the “Escrow Agreement”) between the City and Regions Bank, Houston, Texas (the “Escrow Agent”). The Bond Ordinance and the Taxable Bond Ordinance provide that from the proceeds of the sale of the Bonds and the Taxable Bonds received from the Underwriters the City will deposit with the Escrow Agent cash and direct obligations of the United States in amounts sufficient to accomplish the discharge and final payment of the Refunded Obligations on their respective maturity dates and redemption dates, as applicable (see “SCHEDULE I – SCHEDULE OF TAX-EXEMPT REFUNDED OBLIGATIONS” and “SCHEDULE II – SCHEDULE OF TAXABLE REFUNDED OBLIGATIONS”).

Grant Thornton LLP, Certified Public Accountants, will verify the mathematical accuracy of schedules provided by the Financial Advisor at the time of delivery of the Bonds and the Taxable Bonds to the Underwriters and that the Federal Securities will mature at such times and yield interest in amounts, together with uninvested funds, if any, in the Escrow Fund, sufficient to pay the principal of and interest on the Refunded Obligations as the same shall become due by reason of stated maturity or earlier redemption. Such funds will be held by the Escrow Agent in a special escrow account (the “Escrow Fund”). Under the Escrow Agreement, the Escrow Fund is irrevocably pledged to the payment of the principal of and interest on the Refunded Obligations. Such maturing principal of and interest on the Federal Securities will not be available to pay principal of or interest on the Bonds and the Taxable Bonds.

Simultaneously with the issuance of the Bonds and the Taxable Bonds, the City will give irrevocable instructions to provide notice to the owners of the Refunded Obligations that the Refunded Obligations will be redeemed prior to their stated maturity on the first optional redemption date, on which date money will be made available to redeem the Refunded Obligations from money held under the Escrow Agreement.

By the deposit of the Federal Securities and cash with the Escrow Agent pursuant to the Escrow Agreement, the City will have entered into firm banking and financial arrangements for the discharge, defeasance and fund payment of the Refunded Obligations pursuant to the terms of the ordinances authorizing the issuance of such Refunded Obligations and in accordance with State law, including Chapter 1207, Texas Government Code, as amended. Bond Counsel will render an opinion to the effect that, in reliance upon the report of Grant Thornton LLP and as a result of such defeasance, the Refunded Obligations will be deemed to be no longer outstanding except for the purpose of being paid from funds provided therefor by, and secured solely by and payable solely from, the Escrow Agreement.

The City has covenanted 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 Obligations, 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.

SOURCES AND USES OF PROCEEDS . . . The proceeds from the sale of the Bonds, the Taxable Bonds and the Certificates will be applied approximately as follows:

Sources:	Bonds	Taxable Bonds	Certificates
Principal	$ 7,280,000.00	$ 11,980,000.00	$ 11,870,000.00
Net Premium	906,007.65	0.00	493,318.60
Total Sources	$ 8,186,007.65	$ 11,980,000.00	$ 12,363,318.60
Uses:			
Deposit to Escrow Fund	$ 8,053,384.03	$ 11,801,901.27	$ 0.00
Deposit to Project Fund	0.00	0.00	12,186,500.00
Deposit to Debt Service Fund	292.15	595.63	4,638.38
Underwriters’ Discount	47,331.47	73,603.10	79,780.22
Costs of Issuance	85,000.00	103,900.00	92,400.00
Total Uses	$ 8,186,007.65	$ 11,980,000.00	$ 12,363,318.60

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THE OBLIGATIONS

DESCRIPTION OF THE OBLIGATIONS . . . The Obligations are dated April 1, 2013 and mature on August 15 in each of the years and in the amounts shown on page 2, 4 and 6 hereof. Interest on the Bonds and the Taxable Bonds will accrue from the date of initial delivery, will be computed on the basis of a 360-day year consisting of twelve 30-day months, and will be payable on August 15 and February 15, commencing on August 15, 2013. Interest on the Certificates will accrue from the date of initial delivery, will be computed on the basis of a 360-day year consisting of twelve 30-day months, and will be payable on February 15 and August 15, commencing on February 15, 2014. The definitive Obligations will be issued only in fully registered form in any integral multiple of $5,000 for any one maturity and will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company, New York, New York ("DTC") pursuant to the book-entry-only system described herein. **No physical delivery of the Obligations will be made to the owners thereof.** Principal of, premium, if any, and interest on the Obligations 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 Obligations. See "Book-Entry-Only System" herein.

AUTHORITY FOR ISSUANCE . . . The Bonds are being issued pursuant to the Constitution and general laws of the State including particularly Chapters 1207 and 1371, Texas Government Code, as amended, an ordinance authorizing the issuance of the Bonds adopted by the City Council of the City on April 2, 2013, and a pricing certificate executed by the pricing officer as designated in the Ordinance (collectively, the "Bond Ordinance").

The Taxable Bonds are being issued pursuant to the Constitution and general laws of the State including particularly Chapters 1207 and 1371, Texas Government Code, as amended, and an ordinance authorizing the issuance of the Taxable Bonds adopted by the City Council of the City on April 2, 2013, and a pricing certificate executed by the pricing officer as designated in the Ordinance (collectively, the "Taxable Bond Ordinance").

The Certificates are being issued pursuant to the Constitution and general laws of the State, particularly Subchapter C of Chapter 271, Texas Local Government Code, as amended, and Chapters 1371 and 1502, Texas Government Code, as amended, the City Home Rule Charter and an ordinance approved by the City Council authorizing the issuance of the Certificates adopted by the City Council of the City on April 2, 2013, and a pricing certificate executed by the pricing officer as designated in the Ordinance (collectively, the "Certificate Ordinance")..

SECURITY AND SOURCE OF PAYMENT . . . All taxable property within the City is subject to a continuing direct annual ad valorem tax levied by the City, within the limits prescribed by law, sufficient to provide for the payment of principal of and interest on the Obligations as provided in the Ordinances. The Certificates are additionally secured by a limited pledge of surplus net revenues of the City's Waterworks and Waste Water System (not to exceed $1,000).

TAX RATE LIMITATION . . . All taxable property within the City is subject to the assessment, levy and collection by the City of a continuing, direct annual ad valorem tax sufficient to provide for the payment of principal of and interest on all ad valorem tax debt within the limits prescribed by law. Article XI, Section 5, of the Texas Constitution limits the maximum ad valorem tax rate for home-rule cities to $2.50 per $100 taxable assessed valuation for all purposes. The Home Rule Charter of the City adopts the constitutionally authorized maximum tax rate of $2.50 per $100 taxable assessed valuation. Administratively, the Texas Attorney General's office will permit allocation of $1.50 of the $2.50 maximum tax rate for ad valorem tax debt.

OPTIONAL REDEMPTION . . . The city reserves the right, at its option, to redeem the Bonds having stated maturities on and after August 15, 2024, in whole or from time to time in part in principal amounts of $5,000 or any integral multiple thereof, on August 15, 2023, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption.

The City reserves the right, at its option, to redeem the Certificates having stated maturities on and after August 15, 2023, in whole or from time to time in part in principal amounts of $5,000 or any integral multiple thereof, on August 15, 2022, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption. If less than all of the Bonds and Certificates are to be redeemed, the City may select the maturities to be redeemed. If less than all the Bonds and Certificates of any maturity are to be redeemed, the Paying Agent/Registrar (or DTC while the Bonds and Certificates are in book-entry-only form) shall determine by lot the Bonds and Certificates or portions thereof, within such maturity to be redeemed. If any Bond or Certificate (or any portion of the principal sum thereof) shall have been called for redemption and notice of such redemption shall have been given, such Bond or Certificate (or the principal amount thereof to be redeemed) shall become due and payable on such redemption date and interest thereon shall cease to accrue from and after the redemption date, provided funds for the payment of the redemption price and accrued interest thereon are held by the Paying Agent/Registrar on the redemption date.

The Taxable Bonds are not subject to optional redemption prior to their stated maturities.

MANDATORY SINKING FUND REDEMPTION . . . The Bonds maturing on August 15, 2022 (the “Term Bonds”) are subject to mandatory sinking fund redemption by lot or other customary random method prior to maturity at the redemption price of par and accrued interest to the date of redemption on the respective dates and in principal amounts as follows:

Term Bonds Due August 15, 2022	
Redemption Date	Principal Amount
August 15, 2019	$ 45,000
August 15, 2020	45,000
August 15, 2021	45,000
August 15, 2022*	50,000

*Stated Maturity.

The Certificates maturing on August 15 in the years 2030 and 2033 (the “Term Certificates”) are subject to mandatory sinking fund redemption by lot or other customary random method prior to maturity at the redemption price of par and accrued interest to the date of redemption on the respective dates and in principal amounts as follows:

Term Certificates Due August 15, 2030		Term Certificates Due August 15, 2033	
Redemption Date	Principal Amount	Redemption Date	Principal Amount
August 15, 2029	$ 735,000	August 15, 2031	$ 785,000
August 15, 2030*	765,000	August 15, 2032	815,000
		August 15, 2033*	840,000

*Stated Maturity.

The principal amount of the Bonds and Certificates required to be redeemed pursuant to the operation of the mandatory sinking fund redemption provisions shall be reduced, at the option of the City, by the principal amount of any Bonds or Certificates of the stated maturity which, at least 50 days prior to a mandatory redemption date (1) shall have been acquired by the City at a price not exceeding the principal amount of such Bonds or Certificates plus accrued interest to the date of purchase thereof, and delivered to the Paying Agent/Registrar for cancellation, (2) shall have been purchased and cancelled by the Paying Agent/Registrar at the request of the City with monies in the Debt Service Fund at a price not exceeding the principal amount of the Bonds or Certificates plus accrued interest to the date of purchase thereof, or (3) shall have been redeemed pursuant to the optional redemption provisions and not theretofore credited against a mandatory sinking fund redemption requirement.

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

The Paying Agent/Registrar and the City, so long as a book-entry-only system is used for the Bonds or Certificates will send any notice of redemption, notice of proposed amendment to the respective Ordinance or other notices with respect to the Bonds or Certificates 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 Bond or Certificate called for redemption or any other action premised or any such notice.

Redemption of portions of the Bonds or Certificates by the City will reduce the outstanding principal amount of such Bonds or Certificates held by DTC. In such event, DTC may implement, through its book-entry-only system, a redemption of such Bond or Certificate 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 Bond or Certificate from the beneficial owners. Any such selection of Bonds or Certificates to be redeemed will not be governed by the respective Ordinance and will not be conducted by the City or the Paying Agent/Registrar. Neither the City 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 Certificates or the providing of notice to DTC participants, indirect participants, or beneficial owners of the selection of portions of the Bonds or Certificates for redemption. See “Book-Entry-Only System” herein.

With respect to any optional redemption of the Bonds or Certificates, unless certain prerequisites to such redemption required by the respective Ordinance have been met and money sufficient to pay the principal of an premium, if any, and interest on the Bonds or Certificates to be redeemed will have been received by the Paying Agent/Registrar prior to the giving of such notice of redemption, such notice will state that said redemption may, at the option of the City, be 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 City will not redeem such Bonds or Certificates, and the Paying Agent/Registrar will give notice in the manner in which the notice of redemption was given, to the effect that the Bonds or Certificates have not been redeemed.

DTC REDEMPTION PROVISIONS . . . The Paying Agent/Registrar and the City so long as a book-entry-only system is used for the Obligations, will send any notice of redemption, notice of proposed amendment to the Ordinance or other notices with respect to the Obligations to DTC. Any failure by DTC to advise any DTC Participant, or of any Direct Participant or Indirect Participant to notify the beneficial owner, shall not affect the validity of the redemption of the bonds called for redemption or any other action premised on any such notice. Redemption of portions of the Obligations by the City will reduce the outstanding principal amount of such Obligations held by DTC. In such event, DTC may implement, through its book-entry-only system, a redemption of such Obligations held for the account of DTC Participants in accordance with its rules or other agreements with DTC Participants and then Direct Participants and Indirect Participants may implement a redemption of such Obligations and such redemption will not be conducted by the City or the Paying/Agent Registrar. Neither the City nor the Paying Agent/Registrar will have any responsibility to DTC Participants, Indirect Participants or persons for whom DTC Participants, or beneficial owners of the selection of portions of the Obligations for redemption.

DEFEASANCE . . . *General.* The Ordinances provide for the defeasance of the Obligations and the termination of the pledge of taxes and revenues with respect to the Certificates and all other general covenants in the Ordinances under certain circumstances. Any Obligation and the interest thereon shall be deemed to be paid, retired and no longer outstanding ("Defeased Obligation") within the meaning of the Ordinances, except to the extent provided below for the Paying Agent/Registrar to continue payments and for the City to retain the right to call Defeased Obligations to be paid at maturity, when the payment of all principal and interest payable with respect to such Defeased Obligations to the due date or dates thereof (whether such due date or dates be by reason of maturity, upon redemption, or otherwise) either (1) shall have been made or caused to be made in accordance with the terms thereof (including the giving of any required notice of redemption) or (2) shall have been provided for on or before such due date by irrevocably depositing with or making available to the Paying Agent/Registrar or a commercial bank or trust company for such payment (a) lawful money of the United States of America sufficient to make such payment, (b) Defeasance Securities (defined below) that mature as to principal and interest in such amounts and at such times as will ensure the availability, without reinvestment, of sufficient money to provide for such payment and when proper arrangements have been made by the City with the Paying Agent/Registrar for the payment of its services until after all Defeased Obligations shall have become due and payable or (c) any combination of (a) and (b). At such time as a Obligation shall be deemed to be a Defeased Obligation, such Obligation and the interest thereon shall no longer be secured by, payable from, or entitled to the benefits of, the ad valorem taxes, or revenues with respect to the Certificates, levied and pledged as provided in the Ordinance, and such principal and interest shall be payable solely from such money or Defeasance Securities.

The deposit under clause (2) above shall be deemed a payment of an Obligation when proper notice of redemption of such Obligations shall have been given, in accordance with the Ordinances. Any money so deposited with the Paying Agent/Registrar or a commercial bank or trust company may at the discretion of the City also be invested in Defeasance Securities, as hereinafter defined, maturing in the amounts and at the times as set forth in the Ordinances, and all income from such Defeasance Securities received by the Paying Agent/Registrar or a commercial bank or trust company that is not required for the payment of the Obligations and interest thereon, with respect to which such money has been so deposited, shall be remitted to the City.

All money or Defeasance Securities set aside and held in trust pursuant to the provisions of the Ordinances for the payment of principal of the Obligations and premium, if any, and interest thereon, shall be applied to and used solely for the payment of the particular Obligations and premium, if any, and interest thereon, with respect to which such money or Defeasance Securities have been so set aside in trust. Until all Defeased Obligations shall have become due and payable, the Paying Agent/Registrar or a commercial bank or trust company shall perform the services of Paying Agent/Registrar for such Defeased Obligations the same as if they had not been defeased, and the City shall make proper arrangements to provide and pay for such services as required by the Ordinances.

If money or Defeasance Securities have been deposited or set aside with the Paying Agent/Registrar or a commercial bank or trust company for the payment of Obligations and such Obligations shall not have in fact been actually paid in full, no amendment of the defeasance provisions of the Ordinance shall be made without the consent of the registered owner of each Obligation affected thereby.

*Retention of Right*s. To the extent that, upon the defeasance of any Defeased Obligations to be paid at its maturity, the City retains the right under State law to later call any Defeased Obligations which is subject to redemption (i.e. the Obligations) in accordance with the provisions of the Ordinances, the City may call such Defeased Obligations for redemption upon complying with the provisions of State law and upon the satisfaction of the provisions set forth above regarding such Defeased Obligations as though it was being defeased at the time of the exercise of the option to redeem the Defeased Obligations and the effect of the redemption is taken into account in determining the sufficiency of the provisions made for the payment of the Defeased Obligations.

*Investment*s. Any escrow agreement or other instrument entered into between the City and the Paying Agent/Registrar or a commercial bank or trust company pursuant to which money and/or Defeasance Securities are held by the Paying

Agent/Registrar or a commercial bank or trust company for the payment of Defeased Obligations may contain provisions permitting the investment or reinvestment of such moneys in Defeasance Securities or the substitution of other Defeasance Securities upon the satisfaction of certain requirements. All income from such Defeasance Securities received by the Paying Agent/Registrar or a commercial bank or trust company which is not required for the payment of the Obligations and interest thereon, with respect to which such money has been so deposited, will be remitted to the City.

For the purposes of these provisions, "Defeasance Securities" means (i) Federal Securities, (ii) 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 the City Council adopts or approves proceedings authorizing the issuance of refunding bonds or otherwise provide for the funding of an escrow to effect the defeasance of the Obligations are rated as to investment quality by a nationally recognized investment rating firm not less than "AAA" or its equivalent, (iii) noncallable obligations of a state or an agency or a county, municipality, or other political subdivision of a state that have been refunded and that, on the date the City Council adopts or approves proceedings authorizing the issuance of refunding bonds or otherwise provide for the funding of an escrow to effect the defeasance of the Obligations, are rated as to investment quality by a nationally recognized investment rating firm no less than "AAA" or its equivalent and (iv) any other then authorized securities or obligations under applicable state law that may be used to defease obligations such as the Obligations. For the purposes of these provisions, "Federal Securities" means direct, noncallable obligations of the United States of America, including obligations that are unconditionally guaranteed by the United States of America (including Interest Strips of the Resolution Funding Corporation).

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 Ordinances do not contractually limit such investments, registered owners may 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 as Defeasance Securities or those for any other Defeasance Security will be maintained at any particular rating category.

BOOK-ENTRY-ONLY SYSTEM . . . This section describes how ownership of the Obligations is to be transferred and how the principal of, premium, if any, and interest on the Obligations are to be paid to and credited by DTC while the Obligations are registered in its nominee's name. The information in this section concerning DTC and the Book-Entry-Only System has been provided by DTC for use in disclosure documents such as this Official Statement. The City believes the source of such information to be reliable, but takes no responsibility for the accuracy or completeness thereof.

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

DTC will act as securities depository for the Obligations. The Obligations will be issued as fully-registered Obligations 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 Obligation certificate will be issued for each maturity of the Obligations, each in the aggregate principal amount 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 Obligations under the DTC system must be made by or through Direct Participants, which will receive a credit for the Obligations on DTC's records. The ownership interest of each actual purchaser of each Obligation ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from

DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Obligations 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 Obligations, except in the event that use of the book-entry system for the Obligations is discontinued.

To facilitate subsequent transfers, all Obligations 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 Obligations 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 Obligations; DTC's records reflect only the identity of the Direct Participants to whose accounts such Obligations 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 Obligations may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Obligations, such as redemptions, tenders, defaults, and proposed amendments to the Obligation documents. For example, Beneficial Owners of Obligations may wish to ascertain that the nominee holding the Obligations 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 Obligations 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 Obligations unless authorized by a Direct Participant in accordance with DTC's MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the City as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Obligations are credited on the record date (identified in a listing attached to the Omnibus Proxy).

All payments on the Obligations will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or the Paying Agent/Registrar, 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 Obligations 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 City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or 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 Obligations at any time by giving reasonable notice to the City or the Paying Agent/Registrar. Under such circumstances, in the event that a successor depository is not obtained, Obligation certificates are required to be printed and delivered.

The City may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, Obligation 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 City believes to be reliable, but neither the City nor the Underwriters take any responsibility for the accuracy thereof.

USE OF CERTAIN TERMS IN OTHER SECTIONS OF THIS OFFICIAL STATEMENT . . . In reading this Official Statement it should be understood that while the Obligations are in the book-entry-only system, references in other sections of this Official Statement to registered owners should be read to include the person for which the Participant acquires an interest in the Obligations, but (i) all rights of ownership must be exercised through DTC and the book-entry-only system, and (ii) except as described above, notices that are to be given to registered owners under the Ordinance will be given only to DTC.

Information concerning DTC and the book-entry-only system has been obtained from DTC and is not guaranteed as to accuracy or completeness by, and is not to be construed as a representation by the City, the Financial Advisor, or the Underwriters.

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

TRANSFER, EXCHANGE AND REGISTRATION . . . In the event the book-entry-only system should be discontinued, the Obligations may be transferred and exchanged on the registration books of the Paying Agent/Registrar only upon presentation and surrender to the Paying Agent/Registrar and such transfer or exchange shall be without expense or service charge to the registered owner, except for any tax or other governmental charges required to be paid with respect to such registration, exchange and transfer.

Obligations may be assigned by the execution of an assignment form on the respective Obligations or by other instrument of transfer and assignment acceptable to the Paying Agent/Registrar. New Obligations will be delivered by the Paying Agent/Registrar, in lieu of the Obligations 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 Obligations issued in an exchange or transfer of Obligations 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 Obligations 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 Obligations registered and delivered in an exchange or transfer shall be in any integral multiple of $5,000 for any one maturity and for a like aggregate principal amount as the Obligations surrendered for exchange or transfer. See “Book-Entry-Only System” herein for a description of the system to be utilized initially in regard to ownership and transferability of the Obligations. Neither the City nor the Paying Agent/Registrar shall be required to transfer or exchange any Obligation 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 any Obligations.

RECORD DATE FOR INTEREST PAYMENT. . . The record date (“Record Date”) for the interest payable on the Obligations 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 City. Notice of the Special Record Date and of the scheduled payment date of the past due interest (“Special Payment Date”, which shall be 15 days after the Special Record Date) shall be sent at least five business days prior to the Special Record Date by United States mail, first-class postage prepaid, to the address of each Holder of an Obligation 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.

OBLIGATIONHOLDERS’ REMEDIES . . . The Ordinances establish specific events of default with respect to the Obligations. If the City defaults in the payment of the principal of or interest on the Obligations when due, or the City defaults in the observance or performance of any of the covenants, conditions, or obligations of the City, the failure to perform which materially, adversely affects the rights of the owners, including but not limited to, their prospect or ability to be repaid in accordance with the Ordinances, and the continuation thereof for a period of 60 days after notice of such default is given by any owner to the City, the Ordinances provide that any registered owner is entitled to seek a writ of mandamus from a court of proper jurisdiction requiring the City to make such payment or observe and perform such covenants, obligations, or conditions. The issuance of a writ of mandamus may be sought if there is no other available remedy at law to compel performance of the Obligations or the Ordinances and the City’s obligations are not uncertain or disputed. The remedy 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 Obligations in the event of default and, consequently, the remedy of mandamus may have to be relied upon from year to year. The Ordinances do not provide for the appointment of a trustee to represent the interest of the bondholders upon any failure of the City to perform in accordance with the terms of the Ordinances, 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*, 49 Tex. Sup. Ct. J. 819 (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 City’s sovereign immunity from a suit for money damages, bondholders may not be able to bring such a suit against the City for breach of the Obligations or covenants in the Ordinances. Even if a judgment against the City could be obtained, it could not be enforced by direct levy and execution against the City’s property. Further, the registered owners cannot themselves foreclose on property within the City or sell property within the City to enforce the tax lien on taxable property to pay the principal of and interest on the Obligations. Furthermore, the City 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 City avail itself of Chapter 9 protection from creditors, the ability to enforce would be subject to the approval of the Bankruptcy Court (which could require that the action be heard in Bankruptcy Court instead of 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 Obligations are qualified with respect to the customary rights of debtors relative to their creditors.

AMENDMENTS TO THE ORDINANCES . . . In the Ordinances, the City has reserved the right to amend the Ordinances without the consent of any owners for the purpose of amending or supplementing such Ordinances to (1) cure any ambiguity, defect or omission therein that does not materially adversely affect the interests of the owners, (2) grant additional rights or security for the benefit of the owners, (3) add events of default as shall not be inconsistent with the provisions of the Ordinances that do not materially adversely affect the interests of the owners, (4) qualify the Ordinances under the Trust Indenture Act of 1939, as amended, or corresponding provisions of federal laws from time to time in effect, or (5) make such other provisions in regard to matters or questions arising under the Ordinances that are not inconsistent with the provisions thereof and which, in the opinion of Bond Counsel for the City, do not materially adversely affect the interest of the owners.

The Ordinances further provide that the owners of the Obligations aggregating in principal amount 51% of the outstanding Obligations shall have the right from time to time to approve any amendment not described above to the Ordinances if it is deemed necessary or desirable by the City; provided, however, that without the consent of 100% of the owners in original principal amount of the then outstanding Obligations no amendment may be made of the purpose of: (1) making any change in the maturity of any of the outstanding Obligations; (2) reducing the rate of interest borne by any of the outstanding Obligations; (3) reducing the amount of the principal of, or redemption premium, if any, payable on any outstanding Obligations; (4) modifying the terms of payment of principal or of interest or redemption premium on outstanding Obligations, or imposing any condition with respect to such payment; or (5) changing the minimum percentage of principal amount of the Obligations necessary for consent to such amendment. Reference is made to the Ordinances for further provisions relating to the amendment thereof.

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TAX INFORMATION

AD VALOREM TAX LAW . . . The appraisal of property within the City is the responsibility of the Hays Central Appraisal District, the Guadalupe Central Appraisal District and the Caldwell Central Appraisal District (collectively, the "Appraisal District"). Excluding agricultural and open-space land, which may be taxed on the basis of productive capacity, the Appraisal District is required under the State's 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 market value of property, different methods of appraisal may be used, including the cost method of appraisal, the income method of appraisal and market data comparison method of appraisal, and the method considered most appropriate by the chief appraiser is to be used.

State law 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 not to exceed the lesser of (1) the property's market value in the most recent tax year in which the market value was determined by the appraisal 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 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 three 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 City may require annual review at its own expense, and is entitled to challenge the determination of appraised value of property within the City by petition filed with the Appraisal Review Board.

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

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

Under Article VIII, Section 1-b, and State law, the governing body of a political subdivision, at its option, may grant, or upon presentation of a petition must call an election on whether to grant: (1) an exemption of not less than $3,000 of the market value of the residence homestead of persons 65 years of age or older and the disabled from all ad valorem taxes thereafter levied by the political subdivision; and (2) an exemption of up to 20% of the market value of residence homesteads, with the minimum exemption under this provision being $5,000. The surviving spouse of an individual who qualifies for the foregoing exemption 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 taxpayer qualified if (i) the taxpayer died in a year in which the taxpayer qualified for the exemption, (ii) the surviving spouse was at least 55 years of age at the time of the death of the taxpayer and (iii) the property was the residence homestead of the surviving spouse when the taxpayer died and remains the residence homestead of the surviving spouse.

In addition, cities are authorized to refrain from increasing the total ad valorem tax (except for increases attributable to certain improvements) on the residence homestead of the disabled or persons 65 years of age or older and their spouses above the amount of tax imposed in the later of (1) the year such residence qualified for an exemption based upon the disability or age of the owner or (2) the year the city chooses to establish the above-referenced limitation. On the receipt of a petition signed by five percent of the registered voters of the City, the City must call an election to determine by majority vote whether to establish such a tax limitation. Such freeze on ad valorem taxes is transferable to a different residence homestead and to a surviving spouse living in such homestead who is disabled or is at least 55 years of age. If improvements (other than maintenance or repairs) are made to the property, the value of the improvements is taxed at the then current tax rate, and the total amount of taxes imposed is increased to reflect the new improvements with the new amount of taxes then serving as the ceiling on taxes for the following years. Once established, the tax rate limitation may not be repealed or rescinded.

State law and Article VIII, Section 2, 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 and a disabled veteran who receives 100% disability compensation from the United States Department of Veterans Affairs or its successor due to a service-connected disability and a rating of 100% disabled or of individual un-employability is entitled to an exemption from taxation of the total appraised value of the veteran's residence homestead; additionally, effective January 1, 2012, subject to certain conditions, the surviving spouse of a disabled veteran who is entitled to an exemption for the full value of the veteran's residence homestead is also entitled to an exemption from taxation of the total appraised value of the same property to which the disabled veteran's exemption applied.

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 certificate of the contract by which the debt was created.

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

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

Article VIII, Section 1-j of the Texas Constitution provides for an exemption from ad valorem taxation for "freeport property," which is defined as goods detained in the State for 175 days or less for the purpose of assembly, storage, manufacturing, processing or fabrication. Taxing units that took action prior to April 1, 1990 may continue to tax freeport property and decisions to continue to tax freeport property may be reversed in the future. However, decisions to exempt freeport property are not subject to reversal. In addition, effective for tax years 2008 and thereafter, Article VIII, Section 1-n of the Texas Constitution provides for an exemption from taxation for "goods-in-transit," which are defined as personal property acquired or imported into the State and transported to another location inside or outside the state within 175 days of the date the property was acquired or imported into the State. 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. After holding a public hearing, a taxing unit may take action by January 1 of the year preceding a tax year to tax goods-in-transit during the following tax year. A taxpayer may obtain only a freeport exemption or a goods-in-transit exemption for items of personal property.

The City may create one or more Tax Increment Financing Districts ("TIFD") within the City for the purpose of financing the costs of specific public improvements with a TIFD. The City and other taxing units levying taxes on property in a TIFD may agree to contribute all or part of the taxes collected on the increased value of property within the TIFD over its base value. The "base value" is the value of all property in the district in the year the TIFD is established. Taxes received on the base value continue as revenue to the taxing entities general fund. Taxes received on the increment, or value in excess of the base value, are deposited into a special TIFD fund for financing of public projects within the TIFD and are not available for general City use.

The City may also enter into tax abatement agreements with companies to encourage economic development. In a tax abatement agreement, the City agrees to not levy a tax on all or a portion of the new value added by a development for a period of up to ten years if the developer must meet certain requirements regarding investment value, job creation, local and minority/women owned business contracting, etc.

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

EFFECTIVE TAX RATE AND ROLLBACK TAX RATE . . . By the later of September 30 of each year or the 60th day after the date the certified appraisal roll is received by the City, the City is required to adopt a tax rate per $100 of each year taxable value for the current year. If the City does not adopt a tax rate by such required date, the tax rate for that tax year is the lower of the effective tax rate calculated for that tax year or the tax rate adopted by the City for the preceding tax year. The tax rate consists of two components: (1) a rate for funding of maintenance and operation expenditures, and (2) a rate for debt service.

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

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

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

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

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

PROPERTY ASSESSMENT AND TAX PAYMENT . . . Property within the City is generally assessed as of January 1 of each year. Business inventory may, at the option of the taxpayer, be assessed as of September 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 before February 1 of each year and the final installment due before August 1.

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

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

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

CITY APPLICATION OF TAX CODE . . . The City grants an exemption to the market value of the residence homestead of persons who are 65 years of age or older or who are disabled of $25,000.

The City has granted an additional exemption of up to 20% of the market value of residence homesteads.

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

The City has not established a freeze on the taxes on residence homesteads of persons who are 65 years of age or older or who are disabled, as may be done on a local option basis.

The City does not tax nonbusiness vehicles and Hays County collects taxes for the City.

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

The City does not tax freeport property, and the City has not taken action to tax goods-in-transit.

The City does collect the additional one-half cent sales tax for property tax reduction.

The City has adopted a tax abatement policy. The City currently has abatements in effect for various taxable properties that are subject to tax abatement pursuant to existing tax abatement agreements. The final year of the tax abatements offered under such existing agreements vary with the latest expiration date for such agreements occurring in 2015.

TAX INCREMENT FINANCING ZONES . . . In May of 2005, the City Council created Tax Increment Reinvestment Zone No. 2 ("TIRZ No. 2") to provide funding for costs related to the construction of the Yarrington Road railroad overpass in connection with the development of the Blanco Vista Subdivision. The City and Hays County (the "County") are both participants in TIRZ No. 2. The City and the County have agreed to pay $7.1 million of the cost of construction of the overpass.

In March of 2006, the City Council created Tax Increment Reinvestment Zone No. 3 ("TIRZ No. 3") to provide funding for costs related to the construction of a hotel and conference center that the City developed with John Q. Hammons Hotels & Resorts, LLC ("Hammons"). The City agreed to pay 70% of the conference center's construction cost. TIRZ No. 3 was established with an original term of 25 years (expiring on September 30, 2030). The City and the County are both participants in TIRZ No. 3. The City has provided approximately $2 million of additional assistance to Hammons pursuant to a Chapter 380 Economic Development Grant and Loan Agreement for site acquisition for the hotel and conference center. In addition, the City issued approximately $23 million of its combination tax and revenue certificates of obligation to finance costs related to the construction of the conference center.

In November 2011, the City created Tax Increment Reinvestment Zone No. 4 ("TIRZ No. 4") to provide funding to reimburse Carma Paso Robles LLC for costs related to certain public infrastructure for the Paso Robles development. TIRZ No. 4 has a 30 year term with the City contributing 40% of the tax increment collected within the boundaries of TIRZ No. 4.

In December 2011, the City created the Tax Increment Reinvestment Zone No. 5 ("TIRZ No. 5") to provide funding for certain eligible costs incurred in the 244 acre downtown core. TIRZ No. 5 has an initial term of 5 years with the City contributing 70% of the tax increment collected within the boundaries of TIRZ No. 5.

TABLE 1 – VALUATION, EXEMPTIONS AND GENERAL OBLIGATION DEBT

2012/13 Market Valuation Established by Hays, Guadalupe and Caldwell Central Appraisal Districts		
(excluding totally exempt property)		$ 3,052,395,598
Less Exemptions/Reductions at 100% Market Value:		211,495,702
2012/13 Taxable Assessed Valuation		$ 2,840,899,896
City Funded Debt Payable from Ad Valorem Taxes (as of 3-1-13)	$ 207,370,000 (1)	
The Bonds	7,280,000	
The Taxable Bonds	11,980,000	
The Certificates	11,870,000	
Total Debt Payable from Ad Valorem Taxes		$ 219,240,000
Less: Self-Supporting Debt		161,120,000 (2)
Net Debt Payable from Ad Valorem Taxes		$ 58,120,000
Interest and Sinking Fund (as of 3-1-13)		$ 10,973,198
Ratio Tax Supported Debt to Taxable Assessed Valuation		2.05%

2013 Estimated Population - 53,065

Per Capita Taxable Assessed Valuation - $53,536

Per Capita Net General Obligation Debt Payable from Ad Valorem Taxes - $1,095

(1) Excludes Refunded Obligations.

(2) The amounts shown represent (i) 87.31% of the City of San Marcos, Texas Pass-Through Toll Revenue and Limited Tax Bonds, Series 2008 (the "Toll Revenue Bonds"), which are currently outstanding in the aggregate principal amount of $35,880,000 and are secured by amounts received pursuant to a Pass-Through Toll Agreement with the Texas Department of Transportation (the "Department"), which payments are subject to annual appropriation by the Department, and (ii) portions of the City's following ad valorem tax debt: Combination Tax and Revenue Certificates of Obligation, Series 2004, Series 2007, Series 2007A, Series 2007B, Series 2008, Series 2009, Tax and Revenue Refunding Bonds, Series 2009, Certificates of Obligation Series 2009 and Series 2010, General Obligation Refunding Bonds, Series 2010, General Obligation Refunding Bonds Series 2011, and the General Obligation Refunding Bonds, Series 2012, the Taxable Bonds, the Certificates and the Bonds (collectively, "Self-Supporting Debt") that the City intends to pay using revenue derived from enterprise funds or other special sources of governmental funds. There is no guarantee that discretionary payments in respect to Self-Supporting Debt derived from such enterprise fund and other special governmental funds will be made in the future. If (a) payments are not received from the Department, (b) payments in respect of Self-Supporting Debt are not made from sources described, or (c) payments from such sources are not sufficient, the City is obligated to provide funding for any shortfall through the levy of ad valorem taxes.

TABLE 2 – VALUATION AND GENERAL OBLIGATION DEBT HISTORY

Fiscal Year Ended 9/30	Estimated Population [1]	Taxable Assessed Valuation	Taxable Assessed Valuation Per Capita	Funded Debt Outstanding at End of Year[2]	Ratio of Funded Debt to Taxable Assessed Valuation	Funded Debt Per Capita
2009	50,913	$ 2,623,365,186	$ 51,526	$ 77,960,000	2.97%	$ 1,531
2010	53,913 [3]	2,504,035,456	46,446	86,585,000	3.46%	1,606
2011	47,505	2,452,170,753	51,619	74,615,000	3.04%	1,571
2012	53,065	2,699,706,853	50,875	71,980,000	2.67%	1,356
2013	53,065	2,840,899,896	53,536	72,515,000 [4]	2.55%	1,367

(1) Source: The City.
(2) Excludes self-supporting debt. See "Table 1 – Valuation, Exemptions and General Obligation Debt, footnote 2."
(3) 2010 Census Number was 44,984. The City is challenging this number.
(4) Projected; includes the Obligations and excludes the Refunded Obligations.

TABLE 3 – TAX RATE, LEVY AND COLLECTION HISTORY

Fiscal Year Ended 9/30	Tax Rate	General Fund	Interest and Sinking Fund	Tax Levy	% Current Collections	% Total Collections to Date
2009	$ 0.5302	$ 0.2006	$ 0.3296	$ 12,147,748	98.49%	100.70%
2010	0.5302	0.2102	0.3200	14,099,916	98.63%	100.55%
2011	0.5302	0.2102	0.3200	13,970,763	98.85%	100.85%
2012	0.5302	0.2332	0.2970	14,366,519	96.47%	100.14%
2013	0.5302	0.2651	0.2651	15,074,322	96.10% [1]	96.90% [1]

(1) As of March 15, 2013.

TABLE 4 – TEN LARGEST TAXPAYERS

Name of Taxpayer	2012 Taxable Assessed Valuation	% of Total Taxable Assessed Valuation
Hays Energy Limited Partnership	$ 195,078,720	6.87%
H.E. Butt Warehouse	106,978,973	3.77%
San Marcos Factory Stores, Ltd.	42,736,053	1.50%
Tanger Properties, LP	42,264,170	1.49%
Prime Outlets at San Marcos II LLC	35,102,300	1.24%
Copper Beech Townhome Communities	25,960,360	0.91%
Goodrich Corp.	25,138,938	0.88%
H.E. Butt Grocery Company	23,301,786	0.82%
JQH-San Marcos Development LLC	22,870,720	0.81%
Cabana Beach Apartments	22,496,600	0.79%
	$ 541,928,620	19.08%

GENERAL OBLIGATION DEBT LIMITATION . . . The City of San Marcos has no legal debt limit established by its Home Rule Charter or ordinances. For a description of limitations on the City's maximum ad valorem tax rate, see "THE OBLIGATIONS – TAX RATE LIMITATION."

TABLE 5 - ESTIMATED OVERLAPPING DEBT

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

Taxing Jurisdiction	Total Tax Supported Debt	Estimated % Applicable	City's Overlapping Tax Supported Debt as of 3-1-13
Caldwell County	$ 11,945,000	0.71%	$ 84,810
Hays County	282,824,998	21.68%	61,316,460
Guadalupe County	14,440,000	0.02%	2,888
Hays CISD	293,130,000	3.82%	11,197,566
San Marcos CISD	112,154,959	94.76%	106,278,039
City of San Marcos	58,120,000 (1)	100.00%	58,120,000
Total Direct and Overlapping Tax Supported Debt			$ 236,999,762
Ratio of Direct and Overlapping Tax Supported Debt to Taxable Assessed Valuation			8.34%
Per Capita Overlapping Tax Supported Debt			$ 4,466

(1) Includes the Obligations. Excludes the Refunded Obligations and self-supporting debt. See "Table 1 – Valuation, Exemptions and General Obligation Debt, footnote 2."

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DEBT INFORMATION

TABLE 6 – AD VALOREM TAX DEBT SERVICE REQUIREMENTS

Fiscal Year Ending 9/30	Outstanding Ad Valorem Tax Debt [1] Principal	Outstanding Ad Valorem Tax Debt [1] Interest	The Bonds[2] Principal	The Bonds[2] Interest	The Taxable Bonds[3] Principal	The Taxable Bonds[3] Interest	The Certificates[4] Principal	The Certificates[4] Interest	Less: Build America Bond Subsidy[5]	Less: System-Supported Debt Service	Total Tax-Supported Debt Service
2013	$ 9,890,000	$ 9,031,476	$ 105,000	$ 69,545	$ 110,000	$ 44,522	$ -	$ -	$ 365,426	$ 11,050,858	$ 7,834,259
2014	10,795,000	8,534,108	1,390,000	297,000	195,000	190,281	-	484,793	361,731	12,198,322	9,326,128
2015	12,020,000	8,148,242	90,000	276,150	1,045,000	189,052	435,000	393,075	356,999	14,588,048	7,651,472
2016	12,965,000	7,734,628	85,000	274,350	1,060,000	180,901	455,000	384,375	351,303	15,172,914	7,615,037
2017	13,435,000	7,297,341	45,000	272,650	1,070,000	169,803	480,000	375,275	344,749	15,246,983	7,553,337
2018	12,450,000	6,762,438	40,000	271,750	2,770,000	156,128	495,000	365,675	337,338	15,556,774	7,416,879
2019	12,370,000	6,268,765	45,000	270,550	2,830,000	112,418	525,000	350,825	329,204	15,569,686	6,873,668
2020	12,940,000	5,785,599	45,000	269,200	2,900,000	59,044	540,000	335,075	320,248	15,586,662	6,967,008
2021	12,580,000	5,257,851	45,000	267,850	-	-	555,000	318,875	309,542	12,714,013	6,001,021
2022	13,105,000	4,718,194	50,000	266,500	-	-	570,000	302,225	287,181	12,704,267	6,020,471
2023	12,930,000	4,159,475	50,000	265,000	-	-	590,000	285,125	263,428	12,135,411	5,880,761
2024	12,525,000	3,553,804	50,000	263,500	-	-	605,000	267,425	239,037	11,721,767	5,303,925
2025	11,255,000	2,958,674	-	262,000	-	-	635,000	243,225	213,892	10,097,017	5,042,990
2026	10,910,000	2,429,010	-	262,000	-	-	650,000	217,843	187,983	9,764,495	4,516,375
2027	10,420,000	1,890,181	-	262,000	-	-	685,000	191,825	158,973	9,685,874	3,604,159
2028	9,215,000	1,365,536	-	262,000	-	-	710,000	164,425	129,331	8,832,662	2,754,968
2029	9,045,000	895,789	-	262,000	-	-	735,000	136,025	95,679	8,832,697	2,145,438
2030	5,335,000	432,077	2,980,000	262,000	-	-	765,000	111,219	60,868	8,654,501	1,169,927
2031	2,235,000	145,056	2,260,000	113,000	-	-	785,000	85,400	-	5,063,931	559,525
2032	1,615,000	39,681	-	-	-	-	815,000	57,925	-	2,270,631	256,975
2033	-	-	-	-	-	-	840,000	29,400	-	615,825	253,575
	$ 208,035,000	$ 87,407,925	$ 7,280,000	$ 4,749,045	$ 11,980,000	$ 1,102,149	$ 11,870,000	$ 5,100,029	$ 4,712,912	$ 228,063,338	$ 104,747,899

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(1) Excludes the Refunded Obligations and includes self-supporting ad valorem tax debt.
(2) Interest calculated at a true interest cost of 3.64%.
(3) Interest calculated at a true interest cost of 1.85%.
(4) Interest calculated at a true interest cost of 3.13%.
(5) Represents Build America Bonds subsidy payments expected to be received on Taxable Series 2010 Certificates of Obligation. Payment is not guaranteed. See “SEQUESTRATION OF BUILD AMERICA BOND DIRECT SUBSIDY PAYMENTS.”

ANTICIPATED ISSUANCE OF GENERAL OBLIGATION DEBT . . . The City does not anticipate the issuance of any additional tax supported debt over the next 6 months.

TABLE 7 – AUTHORIZED BUT UNISSUED DEBT . . . The City does not have any authorized but unissued bonds remaining. The City may incur non-voted debts payable from or secured by its collection of taxes and other sources of revenue, including tax notes, certificates of obligation, public property finance contractual obligations, and leases for various purposes.

OTHER DEBT OBLIGATIONS . . . See "APPENDIX B – EXCERPTS FROM THE CITY'S ANNUAL FINANCIAL REPORT."

PENSION FUND . . . The City provides pension benefits for all of its full-time employees through the Texas Municipal Retirement System ("TMRS"), a State-wide administered pension plan. The City makes annual contributions to the plan equal to the amounts accrued for pension expense. (For more detailed information concerning the retirement plan, see "APPENDIX B – EXCERPTS FROM THE CITY'S ANNUAL FINANCIAL REPORT".)

OTHER POST-EMPLOYMENT BENEFITS . . . In addition to the pension benefits described above, the City provides certain other post-retirement benefits to retired employees and their dependents that fall within the scope of Governmental Accounting Standards Board's Statement of General Accounting Standards no. 45 ("GASB 45"), Accounting by Employer for Other Post-Employment Benefits ("OPEB"). GASB 45, which sets forth standards for the measurement, recognition, and display of post-employment benefits other than pensions (such as health and life insurance for current and future retirees), applies to the City and required implementation by the City for the fiscal year that began October 1, 2008. GASB 45 requires the City to: (i) measure the cost of benefits, and recognize other post-employment benefits expense, on the accrual basis of accounting over the working lifetime of the employees; (ii) provide information about the actuarial liabilities for promised benefits associated with past services and whether, or to what extent, the future costs of those benefits have been funded; and provide information useful in assessing potential demands on the employer's future cash flows. The employer's contributions to OPEB costs that are less than an actuarially determined annual required contribution will result in a net OPEB cost, which under GASB 45 must be recorded as a liability in the employer's financial statements.

Based on an actuarial valuation report obtained by the City (the "GASB 45 Report"), the City's annual OPEB cost was calculated based on the City's annual required contribution (ARC), in accordance with the parameters of GASB 45. The ARC represents a level of accrual that is projected to recognize the normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The GASB 45 Report was performed for the fiscal year beginning October 1, 2008, as required by GASB. The City's annual OPEB cost for the fiscal year ending September 30, 2011, as indicated in the GASB 45 Report, was as follows:

Annual required contribution	$338,359
Interest on OPEB obligation	27,399
Adjustment to ARC	(25,385)
Annual OPEB cost (expense) end of year	340,373
Net estimated employer contributions	(315,131)
Increase in net OPEB obligation	25,242
Net OPEB obligation – as of beginning of the year	60,8865
Net OPEB obligation (asset)– as of end of year	$ 634,107

Under GASB 45 reporting parameters, the GASB 45 Report indicated that City's retiree health care plan is 0% funded with an estimated actuarial accrued liability exceeding actuarial assets by $3,420,429 at September 30, 2011.

Based on the GASB 45 Report, the City is considering strategies to manage the impact of the required future liability reporting. The magnitude of OPEBs depends on a variety of factors, including whether the City elects to use "pay-as-you-go" funding to partially fund the costs or to fully fund the costs. (For more detailed information concerning the City's implementation of GASB 45, see "APPENDIX B – EXCERPTS FROM THE CITY'S ANNUAL FINANCIAL REPORT".)

FINANCIAL ADMINISTRATION . . . The financial administration of the City is vested in the Department of Finance. The Department of Finance operates under the Director of Finance, who is appointed by the City Manager. Required activities of the Department of Finance are control, custody and disbursement of City funds, assessment and collection of taxes and issuance of licenses. Other activities of the Department of Finance include utility billing and collections, internal service fund operation, annual budget preparation and interim and annual financial reports.

FINANCIAL POLICIES

Basis of Accounting . . . All governmental funds and agency funds are accounted for using the modified accrual basis of accounting. Under the modified accrual basis, revenues are recognized when they become measurable and available as net current assets. Expenditures are generally recognized under the modified accrual basis of accounting when the related fund liability is incurred. The exception to this general rule is that principal and interest on general long-term debt is recognized when due.

The more significant revenues which are treated as susceptible to accrual under the modified accrual basis are property taxes, intergovernmental revenues, charges for services, and interest. Other revenue sources are not considered measurable and available, and are not treated as susceptible to accrual.

All proprietary funds and the pension trust fund are accounted for using the accrual basis of accounting. Their revenues are recognized when they are earned and their expenses are recognized when they are incurred.

General Fund Balance . . . The City policy is to maintain surplus and unencumbered funds equal to 25% of expenditures in the General Fund.

Use of Bond proceeds, Grants, etc. . . . The City's policy is to use bond proceeds, grants or other non-recurring revenues for capital expenditures only. Such revenues are never to be used to fund City operations.

Budgetary Procedures . . . The City's Home Rule Charter establishes the fiscal year as the twelve-month period beginning October 1. The departments submit to the City Manager a budget of estimated expenditures for the ensuing fiscal year by the first of July. The City Manager subsequently submits a budget of estimated expenditures and revenues to the City Council by August 15. The City Council then holds a public hearing on the budget. The Council then makes any changes in the budget as it deems advisable and adopts a budget prior to September 20.

Fund Investments . . . The City's investment policy parallels State law which governs investment of public funds. The City generally restricts investments to direct obligations of the United States Government and to insured or collateralized bank certificates of deposits. The City's investment portfolio does not invest in derivative securities. See "INVESTMENTS."

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FINANCIAL INFORMATION

TABLE 8 – GENERAL FUND REVENUES AND EXPENDITURE HISTORY

	Fiscal Year Ending September 30,				
	2012	2011	2010	2009	2008
Revenues:					
Taxes	$ 28,606,490	$ 26,808,963	$ 25,410,877	$ 23,854,020	$ 30,426,277
Licenses and Permits	1,039,855	994,123	821,853	847,678	813,976
Fines and Forfeitures	1,531,308	1,537,951	1,721,581	1,631,490	1,409,343
Charges for Services	5,139,612	5,021,489	4,954,980	4,978,075	4,941,970
Intergovernmental	188,265	182,525	182,825	180,153	174,330
Interest on investments	48,956	48,096	83,606	360,235	409,357
Miscellneous	962,903	844,032	1,900,866	1,380,362	562,202
Total Revenues	$ 37,517,389	$ 35,437,179	$ 35,076,588	$ 33,232,013	$ 38,737,455
Expenditures:					
General Government	$ 15,033,754	$ 14,890,128	$ 13,471,704	$ 14,839,502	$ 14,387,576
Public Safety	19,694,976	19,758,262	18,361,837	16,760,120	15,537,036
Community service	6,132,981	5,975,860	5,537,376	5,382,048	4,980,871
Capital Outlay	-	16,958	-	-	881,499
Debt Service	-	-	-	14,395	59,881
Total Expenses	$ 40,861,711	$ 40,641,208	$ 37,370,917	$ 36,996,065	$ 35,846,863
Excess (Deficiency) of Revenues over Expenditures	$ (3,344,322)	$ (5,204,029)	$ (2,294,329)	$ (3,764,052)	$ 2,890,592
Operating Transfers In	$ 6,454,760	$ 7,628,731	$ 5,684,618	$ 5,765,729	$ 121,798
Capital related debt issued	-	20,791	-	48,039	-
Sale of Capital Assets	23,728	-	36,394	-	-
Operating Transfers Out	(2,013,105)	(2,021,352)	(2,951,983)	(2,754,041)	(4,132,970)
Net Increase (Decrease)	$ 4,465,383	$ 424,141	$ 474,700	$ (704,325)	$ (1,120,580)
Fund Equity at Beginning of Year	13,803,824	13,376,970	12,902,270	13,606,595	14,727,175
Adjustments to Fund Balance	-	2,713	-	-	-
Fund Equity at End of Year	$ 14,924,885	$ 13,803,824	$ 13,376,970	$ 12,902,270	$ 13,606,595

Source: City's audited financial statements.

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TABLE 9 – MUNICIPAL SALES TAX HISTORY

The City has adopted the Municipal Sales and Use Tax Act, Chapter 321, Texas Tax Code, which grants the City the power to impose and levy a 1.0% Local Sales and Use Tax within the City; the proceeds are credited to the General Fund and are not pledged to the payment of the Bonds. Collections and enforcements are effected through the offices of the Comptroller of Public Accounts of the State of Texas, which remits the proceeds of the tax, after deduction of a 2% service fee, to the City monthly.

In addition, the Tax Code provides certain cities and counties the option of assessing a maximum one-half percent (1/2%) sales tax on retail sales of taxable items for the purpose of reducing its ad valorem taxes, if approved by a majority of the voters in a local option election. If the additional tax is approved and levied, the ad valorem property tax levy must be reduced by the estimated amount of the sales tax revenues to be generated in the current year.

Subject to the approval of a majority of the voters in a local option election, state law also provides certain cities the option of assessing a sales and use tax for a variety of other purposes, including economic and industrial development, municipal street maintenance and repair, and sports and community venues.

State law limits the maximum aggregate sales and use tax rate in any area to 8¼%. Accordingly, the collection of local sales and use taxes in the area of the City (including sales and use taxes levied by the City) is limited to no more than 2% (when combined with the State sales and use tax rate of 6¼%).

In addition to the one percent (1%) local sales and use tax referred to above, voters in the City have approved the imposition of an additional one-half percent (½%) sales and use tax for property tax reduction. The following table sets forth the City's historical collections of sales and uses taxes.

Fiscal Year Ended 9/30	Total Collected	% of Ad Valorem Tax Levy	Equivalent of Ad Valorem Tax Rate	Per Capita
2009	$ 18,043,157	148.53%	$ 0.6878	$ 354.39
2010	18,398,707	130.49%	0.7348	387.30
2011	19,854,399	142.11%	0.8097	374.15
2012	20,979,803	146.03%	0.7385	395.36
2013	9,873,965 (1)	65.50%	0.3476	186.07

Source: Texas State Comptroller's Office.
(1) Partial collections through February 28, 2013.

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INVESTMENTS

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

INVESTMENT AUTHORITY AND INVESTMENT PRACTICES OF THE CITY . . . Under Texas law, the City 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 is 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 (i) meeting the requirements of the Texas Public Funds Investment Act (Chapter 2256, Texas Government Code) that are issued by or through an institution that either has its main office or a branch 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 City deposits or,(ii) where (a) the funds are invested by the City through (I) a broker that has its main office or a branch office in the State of Texas and is selected from a list adopted by the City as required by law or (II) a depository institution that has its main office or a branch office in the State of Texas that is selected by the City; (iii) the broker or the depository institution selected by the City arranges for the deposit of the funds in certificates of deposit in one or more federally insured depository institutions, wherever located, for the account of the City; (iv) the full amount of the principal and accrued interest of each of the certificates of deposit is insured by the United States or an instrumentality of the United States, and (v) the City appoints the depository institution selected under (ii) above, an entity as described by Section 2257.041(d) of the Texas Government Code, or a clearing broker-dealer registered with the Securities and Exchange Commission and operating pursuant to Securities and Exchange Commission Rule 15c3-3 (17 C.F.R. Section 240.15c3-3) as custodian for the City with respect to the certificates of deposit issued for the account of the City; (8) fully collateralized repurchase agreements that have a defined termination date, are secured by a combination of cash and obligations described in clause (1),require the securities being purchased by the City or cash held by the City to be pledged to the City, held in the City=s name, and deposited at the time the investment is made with the City or with a third party selected and approved by the City, and are placed through a primary government securities dealer, as defined by the Federal Reserve, or a financial institution doing business in the State; (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 the 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. In addition, bond proceeds may be invested in guaranteed investment contracts that have a defined termination date and are secured by obligations, including letters of credit, 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 below.

A political subdivision such as the City may enter into securities lending programs if (i) the securities loaned under the program are 100% collateralized, a loan made under the program allows for termination at any time and a loan made under the program is either secured by (a) obligations that are described in clauses (1) through (6) above, (b) irrevocable letters of credit issued by a state or national bank that is continuously rated by a nationally recognized investment rating firm at not less than A or its equivalent or (c) cash invested in obligations described in clauses (1) through (6) above, clauses (10) through (12) above, or an authorized investment pool; (ii) securities held as collateral under a loan are pledged to the City, held in the City's name and deposited at the time the investment is made with the City or a third party designated by the City; (iii) a loan made under the program 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 City may invest in such obligations directly or through government investment pools that invest solely in such obligations provided that the pools are rated no lower than "AAA" or "AAAm" or an equivalent by at least one nationally recognized rating service. The City may also contract with an investment management firm registered under the Investment Advisers Act of 1940 (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 City retains ultimate responsibility as fiduciary of its assets. In order to renew or extend such a contract, the City must do so by order, ordinance, or resolution.

The City is specifically prohibited from investing in: (1) obligations whose payment represents the coupon payments on the outstanding principal balance of the underlying mortgage-backed security collateral and pays no principal; (2) obligations whose payment represents the principal stream of cash flow from the underlying mortgage-backed security and bears no interest; (3)

collateralized mortgage obligations that have a stated final maturity of greater than 10 years; and (4) collateralized mortgage obligations the interest rate of which is determined by an index that adjusts opposite to the changes in a market index.

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

Under Texas law, the City's 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 City's investment officers must submit an investment report to the City Council detailing: (1) the investment position of the City, (2) that all investment officers jointly prepared and signed the report, (3) the beginning market value, and any additions and changes to market value and the ending value of each pooled fund group, (4) the book value and market value of each separately listed asset at the beginning and end of the reporting period, (5) the maturity date of each separately invested asset, (6) the account or fund or pooled fund group for which each individual investment was acquired, and (7) the compliance of the investment portfolio as it relates to: (a) adopted investment strategies and (b) Texas law. No person may invest City funds without express written authority from the City Council.

Under Texas law, the City is additionally required to: (1) annually review its adopted policies and strategies, (2) require any investment officers with personal business relationships or family relationships with firms seeking to sell securities to the City to disclose the relationship and file a statement with the Texas Ethics Commission and the City, (3) require the registered principal of firms seeking to sell securities to the City to: (a) receive and review the City's investment policy, (b) acknowledge that reasonable controls and procedures have been implemented to preclude imprudent investment activities, and (c) deliver a written statement attesting to these requirements; (4) in conjunction with its annual financial audit, perform a compliance audit of the management controls on investments and adherence to the City's investment policy, (5) restrict reverse repurchase agreements to not more than 90 days and restrict the investment of reverse repurchase agreement funds to no greater than the term of the reverse repurchase agreement, (6) restrict the investment in non-money market mutual funds in the aggregate to no more than 15% of the City's monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service, (7) require local government investment pools to conform to the new disclosure, rating, net asset value, yield calculation, and advisory board requirements and (8) provide specific investment training for the Treasurer, the chief financial officer (if not the Treasurer) and the investment officer.

TABLE 10 – CURRENT INVESTMENTS . . . The City is authorized to invest in certificates of deposit, direct obligations of the United States government, United States government agency securities, fully collateralized direct repurchase agreements, no-load money market funds whose portfolio meet the City's investment requirements, and in qualified local government investment pools as approved by the City Council.

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

Investments	Market Value	% of Total
TexasTerm Daily	$ 410,384	0.27%
Federal Agency Coupon Securities	32,747,328	21.47%
Municipal Bonds	26,699,425	17.50%
TexSTAR	8,570,187	5.62%
Lone Star Pool	1,001,439	0.66%
Certificates of Deposit	5,000,000	3.28%
Wells Fargo	77,601,962	50.87%
TexPool	506,733	0.33%
	$ 152,537,458	100.00%

As of such date, 100% of the City's investment portfolio will mature within one year. The market value of the investment portfolio was approximately 100% of its purchase price.

TAX MATTERS

THE FOLLOWING DISCUSSION, WHICH WAS WRITTEN TO SUPPORT THE PROMOTION OR MARKETING OF THE SALE OF THE OBLIGATIONS, IS NOT INTENDED OR WRITTEN TO BE USED, AND CANNOT BE USED BY ANY TAXPAYER, TO AVOID PENALTIES THAT MIGHT BE IMPOSED ON THE TAXPAYER IN CONNECTION WITH THE MATTERS DISCUSSED THEREIN. INVESTORS SHOULD CONSULT THEIR OWN TAX ADVISORS CONCERNING THE TAX IMPLICATIONS OF THE PURCHASE, OWNERSHIP OR DISPOSITION OF THE OBLIGATIONS UNDER APPLICABLE STATE OR LOCAL LAWS, OR ANY OTHER TAX CONSEQUENCE.

Certain Federal Income Tax Considerations

General. The following discussion is a summary of certain expected material federal income tax consequences of the purchase, ownership and disposition of the Obligations and is based on the Internal Revenue Code of 1986, as amended (the "*Code*"), the regulations promulgated thereunder, published rulings and pronouncements of the Internal Revenue Service ("*IRS*") and court decisions currently in effect. There can be no assurance that the IRS will not take a contrary view, and no ruling from the IRS, has been, or is expected to be, sought on the issues discussed herein. Any subsequent changes or interpretations may apply retroactively and could affect the opinion and summary of federal income tax consequences discussed herein.

The following discussion is not a complete analysis or description of all potential U.S. federal tax considerations that may be relevant to, or of the actual tax effect that any of the matters described herein will have on, particular holders of the Obligations and does not address U.S. federal gift or estate tax or (as otherwise stated herein) the alternative minimum tax, state, local or other tax consequences. This summary does not address special classes of taxpayers (such as partnerships, or other pass-thru entities treated as a partnerships for U.S. federal income tax purposes, S corporations, mutual funds, insurance companies, financial institutions, small business investment companies, regulated investment companies, real estate investment trusts, grantor trusts, former citizens of the U.S., broker-dealers, traders in securities and tax-exempt organizations, individual recipients of Social Security or Railroad Retirement benefits, taxpayers who may be subject to or personal holding company provisions of the Code) that are subject to special treatment under U.S. federal income tax laws, or persons that hold Obligations as a hedge against, or that are hedged against, currency risk or that are part of hedge, straddle, conversion or other integrated transaction, or persons whose functional currency is not the "U.S. dollar". This summary is further limited to investors who will hold the Obligations as "capital assets" (generally, property held for investment) within the meaning of Section 1221 of the Code. This discussion is based on existing statutes, regulations, published rulings and court decisions, all of which are subject to change or modification, retroactively.

As used herein, the term "U.S. Holder" means a beneficial owner of an Obligation who or which is: (i) an individual citizen or resident of the United States, (ii) a corporation or partnership created or organized under the laws of the United States or any political subdivision thereof or therein, (iii) an estate, the income of which is subject to U.S. federal income tax regardless of the source; or (iv) a trust, if (a) a court within the U.S. is able to exercise primary supervision over the administration of the trust and one or more U.S. persons have the authority to control all substantial decisions of the trust, or (b) the trust validly elects to be treated as a U.S. person for U.S. federal income tax purposes. As used herein, the term "Non-U.S. Holder" means a beneficial owner of an Obligation that is not a U.S. Holder.

THIS SUMMARY IS INCLUDED HEREIN FOR GENERAL INFORMATION ONLY AND DOES NOT DISCUSS ALL ASPECTS OF THE U.S. FEDERAL INCOME TAXATION THAT MAY BE RELEVANT TO A PARTICULAR HOLDER OF THE OBLIGATIONS IN LIGHT OF THE HOLDER'S PARTICULAR CIRCUMSTANCES AND INCOME TAX SITUATION. PROSPECTIVE HOLDERS OF THE OBLIGATIONS SHOULD CONSULT THEIR OWN TAX ADVISORS AS TO THE TAX TREATMENT WHICH MAY BE ANTICIPATED TO RESULT FROM THE PURCHASE, OWNERSHIP AND DISPOSITION OF THE OBLIGATIONS BEFORE DETERMINING WHETHER TO PURCHASE THE OBLIGATIONS.

FOREIGN INVESTORS SHOULD ALSO CONSULT THEIR OWN TAX ADVISORS REGARDING THE TAX CONSEQUENCES UNIQUE TO NON-U.S. HOLDERS.

Information Reporting and Backup Withholding. Subject to certain exceptions, information reports describing interest income, including original issue discount, with respect to the Obligations will be sent to each registered holder and to the IRS. Payments of interest and principal may be subject to backup withholding under Section 3406 of the Code if a recipient of the payments fails to furnish to the payor such owner's social security number or other taxpayer identification number ("*TIN*"), furnishes an incorrect TIN, or otherwise fails to establish an exemption from the backup withholding tax. Any amounts so withheld would be allowed as a credit against the recipient's federal income tax. Special rules apply to partnerships, estates and trusts, and in certain circumstances, and in respect of Non-U.S. Holders, certifications as to foreign status and other matters may be required to be provided by partners and beneficiaries thereof.

The Bonds and the Certificates

Opinion. On the date of initial delivery of the Bonds and Certificates, McCall, Parkhurst & Horton L.L.P., Bond Counsel to the City, will render its opinions that, in accordance with statutes, regulations, published rulings and court decisions existing on the date thereof ("*Existing Law*") (1) for federal income tax purposes, interest on the Bonds and Certificates will be excludable from the "gross income" of the holders thereof and (2) the Bonds and Certificates 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 Code. Except as stated above, Bond Counsel to the City will express no opinion as to any other federal, state or local tax consequences of the purchase, ownership or disposition of the Bonds and Certificates. See **"**APPENDIX C – FORMS OF BOND COUNSEL'S OPINIONS."

In rendering their opinion, Bond Counsel to the City will rely upon (a) certain information and representations of the City, including information and representations contained in the City's federal tax certificate related to the Bonds and Certificates, and (b) covenants of the City contained in the Bond and Certificate documents relating to certain matters, including arbitrage and the use of the proceeds of the Bonds and Certificates and the property financed or refinanced therewith. Failure by the City to observe the aforementioned representations or covenants could cause the interest on the Bonds and Certificates 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 and Certificates in order for interest on the Bonds and Certificates 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 and Certificates to be included in gross income retroactively to the date of issuance of the Bonds and Certificates. The opinions of Bond Counsel to the City is conditioned on compliance by the City with such requirements, and Bond Counsel to the City has not been retained to monitor compliance with these requirements subsequent to the issuance of the Bonds and Certificates.

Bond Counsel's opinions regarding the Bonds and the Certificates represent its legal judgment based upon its review of Existing Law and the reliance on the aforementioned information, representations and covenants. Bond Counsel's opinion related to the Bonds and Certificates 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 and the Certificates.

A ruling was not sought from the IRS by the City with respect to the Bonds and Certificates or property financed or refinanced with the proceeds of the Bonds and Certificates. No assurances can be given as to whether or not the IRS will commence an audit of the Bonds and Certificates, or as to whether the IRS would agree with the opinions of Bond Counsel. If an audit is commenced, under current procedures the IRS is likely to treat the City as the taxpayer and the holders 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 and Certificates may be less than the principal amount thereof or one or more periods for the payment of interest on the Bonds and Certificates 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 and Certificates 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 U.S. Holder who has purchased a Bond or Certificate as an Original Issue Discount Bond or Certificate 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 or Certificate 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 discussion set forth below. In the event of the redemption, sale or other taxable disposition of such Original Issue Discount Bond or Certificate prior to stated maturity, however, the amount realized by such U.S. Holder in excess of the basis of such Original Issue Discount Bond or Certificate in the hands of such U.S. Holder (adjusted upward by the portion of the original issue discount allocable to the period for which such Original Issue Discount Bond or Certificate was held by such initial owner) is includable in gross income.

Under Existing Law, the original issue discount on each Original Issue Discount Bond or Certificate is accrued daily to the stated maturity thereof (in amounts calculated as described below for each accrual period and ratably within each such accrual period) and the accrued amount is added to an initial owner's basis for such Original Issue Discount Bond or Certificate for purposes of determining the amount of gain or loss recognized by such owner upon the redemption, sale or other disposition thereof. The amount to be added to basis for each accrual period is equal to (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 or Certificate.

All U.S. Holders of Original Issue Discount Bonds or Certificates 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 or Certificates and with respect to the federal, state, local and foreign tax consequences of the purchase, ownership, redemption, sale or other disposition of such Original Issue Discount Bonds or Certificates.

Collateral Federal Income Tax Consequences. Interest on the Bonds and Certificates will be includable as an adjustment for "adjusted current earnings" to calculate the alternative maximum tax imposed on corporations by Section 55 of the Code.

Under section 6012 of the Code, U.S. Holders of tax-exempt obligations, such as the Bonds and Certificates, 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 and Certificates, 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 and Certificates under Federal or state law and could affect the market price or marketability of the Bonds and Certificates. 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.

Taxable Bonds

Certain U.S. Federal Income Tax Consequences to U.S. Holders. Periodic Interest Payments and Original Issue Discount. The Taxable Bonds are not obligations described in Section 103(a) of the Code. Accordingly, the stated interest paid on the Taxable Bonds or original issue discount, if any, accruing on the Taxable Bonds will be includable in "gross income" within the meaning of Section 61 of the Code of each owner thereof and be subject to federal income taxation when received or accrued, depending upon the tax accounting method applicable to such owner.

Disposition of Taxable Bonds. An owner will recognize gain or loss on the redemption, sale, exchange or other disposition of a Bond equal to the difference between the redemption or sale price (exclusive of any amount paid for accrued interest) and the owner's tax basis in the Taxable Bonds. Generally, a U.S. Holder's tax basis in the Taxable Bonds will be the owner's initial cost, increased by income reported by such U.S. Holder, including original issue discount and market discount income, and reduced, but not below zero, by any amortized premium. Any gain or loss generally will be a capital gain or loss and either will be long-term or short-term depending on whether the Taxable Bond has been held for more than one year.

Defeasance of the Taxable Bonds. Defeasance of any Taxable Bond may result in a reissuance thereof, for U.S. federal income tax purposes, in which event a U.S. Holder will recognize taxable gain or loss as described above.

State, Local and Other Tax Consequences. Investors should consult their own tax advisors concerning the tax implications of holding and disposing of the Taxable Bonds under applicable state or local laws, or any other tax consequence, including the application of gift and estate taxes. Effective for tax years beginning after December 31, 2012, pursuant to the Health Care and Education Reconciliation Act of 2010, which was intended to help finance the cost of healthcare reform, certain individuals, estates or trusts may be subject to a 3.8% surtax on all or a portion of the taxable interest that is paid on the Taxable Bonds. PROSPECTIVE PURCHASERS OF THE TAXABLE BONDS SHOULD CONSULT THEIR OWN TAX ADVISORS REGARDING THE FOREGOING MATTERS.

Certain U.S. Federal Income Tax Consequences to Non-U.S. Holders. A Non-U.S. Holder that is not subject to U.S. federal income tax as a result of any direct or indirect connection to the U.S. in addition to its ownership of a Taxable Bond, will not be subject to U.S. federal income or withholding tax in respect of such Taxable Bond, provided that such Non-U.S. Holder complies, to the extent necessary, with identification requirements including delivery of a signed statement under penalties of perjury, certifying that such Non-U.S. Holder is not a U.S. person and providing the name and address of such Non-U.S. Holder. Absent such exemption, payments of interest, including any amounts paid or accrued in respect of accrued original issue discount, may be subject to withholding taxes, subject to reduction under any applicable tax treaty. Non-U.S. Holders are urged to consult their own tax advisors regarding the ownership, sale or other disposition of a Taxable Bond.

The foregoing rules will not apply to exempt a U.S. shareholder of a controlled foreign corporation from taxation on the U.S. shareholder's allocable portion of the interest income received by the controlled foreign corporation.

CONTINUING DISCLOSURE OF INFORMATION

In the Ordinances, the City has made the following agreement for the benefit of the holders and beneficial owners of the Obligations. The City is required to observe the agreement for so long as it remains obligated to advance funds to pay the Obligations. Under the agreement, the City will be obligated to provide certain updated financial information and operating data annually, and timely notice of specified events, to the Municipal Securities Rulemaking Board ("MSRB").

ANNUAL REPORTS . . . The City 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 City of the general type included in this Official Statement under Tables numbered 1 through 4 and 6 through 10 and in APPENDIX B. The City will update and provide this information within six months after the end of each fiscal year ending in or after 2013. The City will provide the updated information to the MSRB in an electronic format.

The City may provide updated information in full text or may incorporate by reference certain other publicly available documents, as permitted by SEC Rule 15c2-12 (the "Rule"). The updated information will include audited financial statements, if the City commissions an audit and it is completed by the required time. If audited financial statements are not available by the required time, the City will provide unaudited financial statements by the required time and audited financial statements when and if such audited financial statements become available. Any such financial statements will be prepared in accordance with the accounting principles described in APPENDIX B or such other accounting principles as the City may be required to employ from time to time pursuant to state law or regulation.

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

NOTICE OF CERTAIN EVENTS . . . The City will provide notice to the MSRB of any of the following events with respect to the Obligations, if such event is material within the meaning of the federal securities laws: (1) non-payment related defaults; (2) modifications to rights of bondholders; (3) Bond calls; (4) release, substitution, or sale of property securing repayment of the Obligations; (5) the consummation of a merger, consolidation, or acquisition involving an obligated person or the sale of all or substantially all of the assets of the obligated person, other than in the ordinary course of business, the entry into 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; and (6) appointment of a successor or additional trustee or the change of name of a trustee.

The City will also provide notice to the MSRB of any of the following events with respect to the Obligations without regard to whether such event is considered material within the meaning of the federal securities laws: (1) principal and interest payment delinquencies; (2) unscheduled draws on debt service reserves reflecting financial difficulties; (3) unscheduled draws on credit enhancements reflecting financial difficulties; (4) substitution of credit or liquidity providers, or their failure to perform; (5) adverse tax opinions or the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB) or other material notices or determinations with respect to the tax-exempt status of the bonds, or other events affecting the tax-exempt status of the Obligations; (6) tender offers; (7) defeasances; (8) rating changes; and (9) bankruptcy, insolvency, receivership or similar event of the City (which is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent, or similar officer for the City in a proceeding under the United States Bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the City, or if such jurisdiction has been assumed by leaving the existing governing body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement, or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets of the City).

The City will provide notice of the aforementioned events to the MSRB in a timely manner (but not in excess of ten business days after the occurrence of the event). The City will also provide timely notice of any failure by the City to provide annual financial information in accordance with their agreement described above under "- Annual Reports."

AVAILABILITY OF INFORMATION FROM MSRB . . . The City has agreed to provide the foregoing information only to the MSRB. All documents provided by the City to the MSRB described above under "Annual Reports" and "Notice of Certain Events" will be in an electronic format and accompanied by identifying information as prescribed by the MSRB. This information will be available free of charge from the MSRB via its EMMA system at www.emma.msrb.org.

The address of the MSRB is 1900 Duke Street, Suite 600, Alexandria VA 22314, and its telephone number is (703) 797-6600.

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

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

If the City so amends the agreement, it has agreed to include with the next financial information and operating data provided in accordance with its agreement described above under "Annual Reports" an explanation, in narrative form, of the reasons for the amendment and of the impact of any change in the type of financial information and operating data so provided.

COMPLIANCE WITH PRIOR AGREEMENTS . . . During the past five years the City has complied in all material respects with its continuing disclosure agreements entered into pursuant to the Rule, except as follows: (i) due to administrative oversight, the City filed certain annual reports for its Water and Waste Water debt and its Electric Revenue debt late for fiscal year ending 2007-2011 and (ii) due to administrative oversight the City filed its 2008 audit late. All required information has since been filed including a notice of late filing. In addition, the City has implemented measures to ensure all required information will be filed in a timely manner going forward.

OTHER INFORMATION

RATING . . . The Obligations have been rated "AA-" by Standard and Poor's Ratings Services, a Standard & Poor's Financial Services LLC business ("S&P"). The outstanding debt of the City is rated "Aa2" by Moody's Investors Service ("Moody's"). The City has not applied to Moody's for a rating on the Obligations. The City also has various issues outstanding which are rated based on insurance provided by various commercial insurance companies. An explanation of the significance of such rating may be obtained from the company furnishing the rating. The rating reflects only the respective view of such organization and the City makes no representation as to the appropriateness of the rating. There is no assurance that such rating will continue for any given period of time or that it will not be revised downward or withdrawn entirely by one or more of such rating company, if in the judgment of such company, circumstances so warrant. Any such downward revision or withdrawal of any of such rating may have an adverse effect on the market price of the Obligations.

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

REGISTRATION AND QUALIFICATION OF OBLIGATIONS FOR SALE . . . The sale of the Obligations 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 Obligations have not been qualified under the Securities Act of Texas in reliance upon various exemptions contained therein; nor have the Obligations been qualified under the securities acts of any jurisdiction. The City assumes no responsibility for qualification of the Obligations under the securities laws of any jurisdiction in which the Obligations may be sold, assigned, pledged, hypothecated or otherwise transferred. This disclaimer of responsibility for qualification for sale or other disposition of the Obligations 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 . . . Under the Texas Public Security Procedures Act, Chapter 1201, Texas Government Code, as amended, the Obligations (1) are negotiable instruments, (2) are investment securities to which Chapter 8 of the Texas Uniform Commercial Code applies, and (3) are legal and authorized investments for (a) an insurance company, (b) a fiduciary or trustee, or (c) a sinking fund of a municipality or other political subdivision or public agency of the State of Texas. The Obligations are eligible to secure deposits of any public funds of the State, its agencies and political subdivisions, and are legal security for those deposits to the extent of their market value. For political subdivisions in Texas which have adopted investment policies and guidelines in accordance with the Public Funds Investment Act, Chapter 2256, Texas Government Code, as amended, the Obligations may have to be assigned a rating of at least "A" or its equivalent as to investment quality by a national rating agency before such obligations are eligible investments for sinking funds and other public funds. See "OTHER INFORMATION – RATING" herein. In addition, various provisions of the Texas Finance Code provide that, subject to a prudent investor standard, the Obligations are legal investments for state banks, savings banks, trust companies with at least $1 million of capital, and savings and loan associations. No review has been made of the laws in other states to determine whether the Obligations are legal investments for various institutions in those states.

The City 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 Obligations for any of the foregoing purposes or limit the authority of such institutions or entities to purchase or invest in the Obligations for such purposes. The City has made no review of laws in other states to determine whether the Obligations are legal investments for various institutions in those states.

SEQUESTRATION OF BUILD AMERICA BOND DIRECT SUBSIDY PAYMENTS . . . On September 14, 2012, the United States Office of Management and Budget ("OMB") delivered a report to Congress (the "OMB Report") that provided estimates of cuts to federal programs that are necessary to reduce spending to levels under the congressionally-mandated sequestration process of the Budget Control Act of 2011. Unless Congress took action during calendar year 2012, the first cuts required under sequestration were to be ordered by the President on January 2, 2013 (the "Sequester Cuts"), for federal fiscal year ending September 30, 2013 ("FFY 2013"). The Sequester Cuts identified in the OMB Report include cuts to the subsidy payments to be made by the federal government to issuers of "direct-pay" tax credit bonds, such as Build America Bonds ("BABs"). Congress could also rescind or alter the Sequester Cuts after they are ordered to take effect by the President. On January 2, 2013, the President signed into law the American Taxpayer Relief Act of 2012 ("ATRA") which delayed implementation of the Sequester Cuts until March 1, 2013. On March 1, 2013 the Sequester Cuts went into effect and on March 4, 2013 the Tax-Exempt Bond Office of the IRS issued guidance providing that federal payments to issuers of direct-pay tax credit bonds (such as the BABs) will be reduced by 8.7% for the remainder of FFY 2013 unless intervening Congressional action is taken.

The City issued $21,880,000 of its Combination Tax and Revenue Certificates of Obligation, Taxable Series 2010 (Build America Bonds – Direct Subsidy) (the "Series 2010 Bonds"), as taxable BABs and elected to receive a subsidy payment from the United States Treasury equal to 35% of the amount of each interest payment on the Series 2010 Bonds. With the Sequester Cuts in effect for FFY 2013, the City estimates that it will receive a range of approximately $19,368 to $27,772 (a range of 5.3% to 7.6%) less in direct subsidy payments than it otherwise expected to receive during FFY 2013 on the Series 2010 Bonds. The City is obligated to make payments of principal and interest on its obligations without regard to the receipt of any federal subsidy payments. At this time, the City can make no representation as to whether the Sequester Cuts will remain in effect or the amount of such reduction in the federal subsidy that would otherwise be payable to the City during FFY 2013 or any impact on future years.

LEGAL MATTERS . . . The delivery of the Obligations is subject to the approval of the Attorney General of Texas to the effect that the Obligations are valid and legally binding obligations of the City payable from the proceeds of an annual ad valorem tax levied, within the limits prescribed by law, upon all taxable property in the City and the approving legal opinion of McCall, Parkhurst & Horton L.L.P., Austin, Texas, Bond Counsel, to like effect and to the effect that the interest on the Obligations 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, including the alternative minimum tax on corporations. The proposed forms of Bond Counsel's opinions are attached hereto as APPENDIX C. In connection with the issuance of the Obligations, Bond Counsel was engaged by, and only represents, the City. Except as noted below, Bond Counsel was not requested to participate, and did not take part, in the preparation of this Official Statement and such firm has not assumed any responsibility with respect thereto or undertaken independently to verify any of the information contained herein, except in its capacity as Bond Counsel, such firm has reviewed the information appearing under captions "PLAN OF FINANCING" (except under the subcaption "Sources and Uses of Proceeds"), "THE OBLIGATIONS" (except under the subcaptions "BOOK-ENTRY-ONLY SYSTEM" and "BONDHOLDERS' REMEDIES"), "TAX MATTERS", "OTHER INFORMATION – REGISTRATION AND QUALIFICATION OF OBLIGATIONS FOR SALE", "OTHER INFORMATION – LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS," "OTHER INFORMATION – LEGAL MATTERS" (except for the last sentence of the first paragraph thereof) and "CONTINUING DISCLOSURE OF INFORMATION" (except under subcaption "COMPLIANCE WITH PRIOR UNDERTAKINGS") and such firm is of the opinion that the information relating to the Obligations and legal matters 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 Obligations, such information conforms to the Ordinances. The legal fee to be paid Bond Counsel for services rendered in connection with the issuance of the Obligations is contingent upon the sale and delivery of the Obligations. The legal opinions of Bond Counsel will accompany the Obligations deposited with DTC or will be printed on the definitive Obligations in the event of the discontinuance of the Book-Entry-Only System. Certain legal matters will be passed upon for the Underwriters by their counsel, Andrews Kurth LLP, Austin, Texas.

The various legal opinions to be delivered concurrently with the delivery of the Obligations 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 . . . Specialized Public Finance Inc. is employed as Financial Advisor to the City in connection with the issuance of the Obligations. The Financial Advisor's fee for services rendered with respect to the sale of the Obligations is contingent upon the issuance and delivery of the Obligations. Specialized Public Finance Inc., 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 Obligations, or the possible impact of any present, pending or future actions taken by any legislative or judicial bodies.

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

VERIFICATION OF ARITHMETICAL AND MATHEMATICAL COMPUTATIONS . . . Grant Thornton LLP, a firm of independent certified public accountants, upon delivery of the Obligations, will deliver to the City its report indicating that they have examined the mathematical accuracy of computations prepared by Specialized Public Finance Inc. relating to (a) the sufficiency of the anticipated receipts from the escrowed securities and cash deposited into the Escrow Fund to pay the Refunded Obligations and (b) the yields on the Bonds and the Taxable Bonds.

The report of Grant Thornton LLP will include the statement that the scope of their engagement was limited to verifying the mathematical accuracy of the computations contained in such schedules provided to them and that they have no obligation to update their report because of events occurring, or data or information coming to their attention, subsequent to the date of their report.

FORWARD-LOOKING STATEMENTS . . . The statements contained in this Official Statement, and in any other information provided by the City, that are not purely historical, are forward-looking statements, including statements regarding the City's expectations, hopes, intentions, or strategies regarding the future.

Readers should not place undue reliance on forward-looking statements. All forward-looking statements included in this Official Statement are based on information available to the City on the date hereof, and the City assumes no obligation to update any such forward-looking statements.

The forward-looking statements 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, therefore, there can be no assurance that the forward-looking statements included in this Official Statement would prove to be accurate.

UNDERWRITING . . . The Underwriters have agreed, subject to certain conditions, to purchase the Bonds from the City, at a price equal to the initial offering prices to the public, as shown on page 2 of this Official Statement, less an underwriting discount of $47,331.47 for the Bonds. 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 agreed, subject to certain conditions, to purchase the Taxable Bonds from the City, at a price equal to the initial offering prices to the public, as shown on page 4 of this Official Statement, less an underwriting discount of $73,603.10 for the Taxable Bonds. The Underwriters will be obligated to purchase all of the Taxable Bonds if any Taxable Bonds are purchased. The Taxable Bonds to be offered to the public may be offered and sold to certain dealers (including the Underwriters and other dealers depositing Taxable Bonds into investment trusts) at prices lower than the public offering prices of such Taxable Bonds, and such public offering prices may be changed, from time to time, by the Underwriters.

The Underwriters have agreed, subject to certain conditions, to purchase the Certificates from the City, at a price equal to the initial offering prices to the public, as shown on page 6 of this Official Statement, less an underwriting discount of $79,780.22 for the Certificates. The Underwriters will be obligated to purchase all of the Certificates if any Certificates are purchased. The Certificates to be offered to the public may be offered and sold to certain dealers (including the Underwriters and other dealers depositing Certificates into investment trusts) at prices lower than the public offering prices of such Certificates, and such public offering prices may be changed, from time to time, by the Underwriters.

One of the Underwriters is BOSC, Inc., which is not a bank, and the Bonds are not deposits of any bank and are not insured by the Federal Deposit Insurance Corporation.

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

Reference is made to original documents in all respects. The Ordinance authorizing the issuance of the Obligations will also approve the form and content of this Official Statement, and any addenda, supplement or amendment thereto, and authorize its further use in the reoffering of the Obligations by the Underwriters.

CERTIFICATION AS TO OFFICIAL STATEMENT . . . The City, acting by and through its City Council in its official capacity hereby certifies, as of the date hereof, that to the best of its knowledge and belief, the information, statements and descriptions pertaining to the City and its affairs herein contain no untrue statements of a material fact and do not omit to state any material fact necessary to make the statements herein, in light of the circumstances under which they were made, not misleading. The information, description and statements concerning entities other than the City, including particularly other governmental entities, have been obtained from sources believed to be reliable, but the City has made no independent investigation or verification of such matters and makes no representation as to the accuracy or completeness thereof. Except as set forth in "CONTINUING DISCLOSURE OF INFORMATION" herein, the City has no obligation to disclose any changes in the affairs of the City and other matters described in this Official Statement subsequent to the "end of the underwriting period" which shall end when the City delivers the Obligations to the Underwriters at closing, unless extended by the Underwriters. All information with respect to the resale of the Obligations subsequent to the "end of the underwriting period" is the responsibility of the Underwriters.

This Official Statement will be approved by the City Council of the City for distribution in accordance with the provisions of the Securities and Exchange Commission's rule codified at 17 C.F.R. Section 240.15c2-12, as amended.

/s/ DANIEL GUERRERO
Mayor
City of San Marcos, Texas

ATTEST:

/s/ JAMIE LEE PETTIJOHN
City Clerk
City of San Marcos, Texas

SCHEDULE I

SCHEDULE OF TAX-EXEMPT REFUNDED OBLIGATIONS

Pass-Through Toll Revenue and
Limited Tax Bonds, Series 2008

Amount	Maturity	Coupon
$ 3,180,000	8/15/2030 (1)	5.125%
2,475,000	8/15/2031 (1)	5.125%
$ 5,655,000		

Redemption Date: 8/15/2014
Redemption Price: 100%

Water & Wastewater System Revenue
Refunding & Improvement Bonds, Series 2004A

Amount	Maturity	Coupon
$ 1,355,000	8/15/2014	3.750%
85,000	8/15/2015	5.000%
85,000	8/15/2016	5.000%
45,000	8/15/2017	4.100%
45,000	8/15/2018	4.150%
50,000	8/15/2019	4.250%
50,000	8/15/2020	4.300%
50,000	8/15/2021 (2)	5.000%
55,000	8/15/2022 (2)	5.000%
55,000	8/15/2023	5.000%
60,000	8/15/2024	5.000%
$ 1,935,000		

Redemption Date: 8/15/2013
Redemption Price: 100%

(1) Term Bonds maturing on August 15, 2031.
(2) Term Bonds maturing on August 15, 2022.

SCHEDULE II

SCHEDULE OF TAXABLE REFUNDED OBLIGATIONS

Waterworks & Wastewater System
Revenue Refunding Bonds, Series 2005

Amount	Maturity	Coupon
$ 850,000	8/15/2015	3.700%
885,000	8/15/2016	3.800%
920,000	8/15/2017	4.000%
2,645,000	8/15/2018	5.000%
2,790,000	8/15/2019	5.000%
2,950,000	8/15/2020	5.000%
$ 11,040,000		

Redemption Date: 8/15/2014
Redemption Price: 100%

APPENDIX A

GENERAL INFORMATION REGARDING THE CITY

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THE CITY

LOCATION AND POPULATION . . . The City of San Marcos, Texas (the "City") is the county seat and principal commercial, educational and recreational center of Hays County located in the center of the State of Texas in the Austin-San Marcos statistical metropolitan area, approximately midway between the metropolitan areas of San Antonio and Austin. The City is located on Interstate Highway 35, U.S. 81, State Highways 80, 142, 21, 123 and Ranch Road 12 and encompasses an area of approximately 27.79 square miles (18,430 acres).

Historical Population

Year	Population
2010 Census	44,894 (1)
2000 Census	34,733
1990 Census	28,743
1980 Census	23,420
1970 Census	18,860

(1) The City is challenging this number.

LABOR MARKET PROFILE . . . The most recent civilian labor force estimates for the City of San Marcos and for the State of Texas are as follows:

City of San Marcos

	February 2013	February 2012
Total Civilian Labor Force	26,246	25,596
Total Employment	25,002	24,202
Total Unemployment	1,244	1,394
Percent Unemployed	4.7%	5.4%

State of Texas

	February 2013	February 2012
Total Civilian Labor Force	12,662,626	12,520,764
Total Employment	11,845,578	11,613,053
Total Unemployment	817,048	907,711
Percent Unemployed	6.5%	7.2%

Source: Texas Workforce Commission.

MUNICIPAL GOVERNMENT . . . The City has a City Council/Manager form of government with an elected council of six members and an elected mayor. The police department is composed of 94 commissioned police officers. The fire department has 54 commissioned firefighting personnel and 15 reserve firefighters. There are 4 fire stations.

In 1983, the San Marcos City Council adopted the San Marcos Master Plan. That document represents the goals and objectives of the citizens of San Marcos. The policies in the Master Plan are used by the City to effectively guide and coordinate the development of the San Marcos community and to guide public officials in the development of annual capital improvement programs. The Master Plan encourages the public agencies to coordinate their services in an efficient and economic manner and guide private development to those areas most suitable in order to coordinate both public and private development efforts. The Master Plan is updated every three years.

TRANSPORTATION . . . The City is traversed by Interstate Highway 35 (North and South System) and is 20 miles from Interstate 10 (East and West System). Also, connecting the City to the State are State Highways 21, 80, 123, 142 and Ranch Road 12.

Missouri Pacific, Amtrak and Missouri-Kansas-Texas have daily freight trains through the City.

San Marcos Municipal Airport is able to accommodate most kinds of aircraft. Charter plane service is available. Austin Municipal International Airport, located 28 miles north of San Marcos, has commercial airline service with all major carriers. San Antonio International Airport, located 45 miles to the south, also has ten different commercial airlines servicing the area.

Local bus service is available daily from Greyhound Trailways.

Trolley services are available with daily service.

BUSINESS AND INDUSTRY

Employer	2012 Employees
Texas State University	3,036
Prime Outlets at San Marcos	2,100
Tanger Factory Outlet Center	1,540
San Marcos CISD	1,200
Hays County	813
Central Texas Medical Center	800
Hunter Industries Manufacturing	650
HEB Distribution Center	650
Gary Job Corps	560
City of San Marcos	550

Source: City's audited financial statements.

EDUCATIONAL FACILITIES . . . Texas State University-San Marcos, a full 4 year multi-purpose university, is located on a hill overlooking the City of San Marcos. It is easily identified by the castle-like structure of Old Main which was the first building constructed when the University, then a college, began operation in 1902. It became a University on May 15, 1969, and now has an enrollment of approximately 30,816 students.

The San Marcos Consolidated Independent School District operates a highly accredited campus, including a preschool, 6 elementary schools (grades K-5), 2 junior high schools (grades 6-8), and 1 senior high school (grades 9-12).

The San Marcos Baptist Academy and the Brown School are 2 private educational institutions within the City. Also located in the City is Gary Job Corps, a federal training center which provides technical training.

LIBRARY . . . The City operates a 27,000 square foot public library with over 140,000 volumes, an adult education program, computer lab and audit and video media. Texas State University-San Marcos Library has over 1,231,626 cataloged holdings, tutorial programs, computer lab and audit and video media.

RECREATION . . . Within the City, there are numerous public parks of various sizes, consisting of baseball fields, an Olympic size swimming pool, lighted tennis courts and various picnic facilities. There is also a private country club with a restaurant, swimming pool, tennis courts, and an 18-hole golf course which is open to the public.

APPENDIX B

EXCERPTS FROM THE
CITY OF SAN MARCOS, TEXAS
ANNUAL FINANCIAL REPORT
For the Year Ended September 30, 2012

The information contained in this APPENDIX consists of excerpts from the City of San Marcos, Texas Annual Financial Report for the Year Ended September 30, 2012, and is not intended to be a complete statement of the City's financial condition. Reference is made to the complete Report for further information.

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

INDEPENDENT AUDITORS' REPORT

The Honorable Mayor
and Members of City Council
City of San Marcos, Texas

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of San Marcos, Texas (the "City"), as of and for the year ended September 30, 2012, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information, and the respective budgetary comparison for the General Fund of the City, as of September 30, 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 March 1, 2013, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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.

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AFFILIATE OFFICES: BROWNSVILLE, TX (956) 544-7778 ■ HILLSBORO, TX (254) 582-2583
TEMPLE, TX (254) 791-3460 ■ ALBUQUERQUE, NM (505) 266-5904

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and analysis on pages 3 through 12 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's financial statements as a whole. The introductory section, combining and individual nonmajor fund financial statements and budgetary schedules, and statistical section, are presented for purposes of additional analysis and are not a required part of the financial statements. The combining and individual nonmajor fund financial statements and budgetary schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The introductory and statistical sections have 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.

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

March 1, 2013

MANAGEMENT'S DISCUSSION AND ANALYSIS

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MANAGEMENT'S DISCUSSION AND ANALYSIS

SEPTEMBER 30, 2012

As management of the City of San Marcos, we offer readers of the City of San Marcos' financial statements this narrative overview and analysis of the financial activities for the City of San Marcos for the fiscal year ended September 30, 2012. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal, which can be found on pages iii – x of this report.

FINANCIAL HIGHLIGHTS

- The assets of the City of San Marcos exceeded its liabilities at the close of the fiscal year ending September 30, 2012, by $240 million (net assets). Of this amount, $59.3 million (unrestricted net assets) may be used to meet the government's ongoing obligations to citizens and creditors.

- As of September 30, 2012, the City of San Marcos' governmental funds reported combined ending fund balances of $64.9 million, a decrease of $(1.0) million in comparison with the prior fiscal year.

- At the end of the current fiscal year, unassigned fund balance for the General Fund was $14 million, or 33% of total General Fund expenditures.

- The City's total debt decreased by $5.4 million during the current fiscal year. The City issued $33.6 million in General Obligation Refunding Bonds and $8.1 in Revenue Bonds.

OVERVIEW OF THE FINANCIAL STATEMENTS

The discussion and analysis serves as an introduction to the City of San Marcos' basic financial statements. The City of San Marcos' basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. The comprehensive annual financial report (CAFR) also contains other supplementary information in addition to the basic statements themselves.

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

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

The *statement of activities* presents information showing how the City's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but not used vacation leave).

The *statement of net assets* and the *statement of activities* are prepared utilizing the accrual basis of accounting.

In the *statement of net assets* and the *statement of activities*, the City's operations are divided into two kinds of activities:

- Governmental Activities – Most of the City's basic services are reported here, including the police, fire, libraries, planning and development, transportation, parks and recreation, and general administration. Property tax, sales tax and franchise fee revenues finance most of these activities.

- Business-type Activities – The City charges a fee to customers to help cover all or most of the cost of certain services it provides. The City's Electric, Water and Wastewater, Airport, Drainage and Waste Collection Funds are reported here.

The government-wide financial statements can be found on pages 13 – 15 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 City of San Marcos, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The fund financial statements provide detailed information about the most significant funds – not the City as a whole. Some funds are required to be established by state law and by bond covenants. However, the City establishes many other funds to help it control and manage money for particular purposes or to show that it is meeting legal responsibilities for using certain taxes, grants and other money. The City's two kinds of funds – governmental and proprietary – utilize different accounting approaches.

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

Because the focus of governmental funds are more narrow 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. The relationships or differences between governmental activities (reported in the *statement of net assets* and the *statement of activities*) and governmental funds is detailed in a reconciliation following the fund financial statements.

The City of San Marcos maintains 20 individual governmental funds. Information is presented separately in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures, and changes in fund balances for the General Fund, Capital Projects Fund, and Debt Service Fund, all of which are considered to be major funds. Data from the other 17 governmental funds are combined into a single, aggregated nonmajor fund presentation. Individual fund data for each of these nonmajor governmental funds is provided in the form of combining statements elsewhere in the CAFR

The basic governmental fund financial statements can be found on pages 16 – 20 of this report.

Proprietary funds. The City charges customers for certain services it provides. These services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the *statement of net assets* and the *statement of activities*.

The City of San Marcos maintains five individual enterprise funds: Electric, Water and Wastewater, Airport, Drainage, and Waste Collection. The fund financial statements provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Electric, Water and Wastewater, and Stormwater Drainage Funds, all of which are considered to be major funds of the City. Data from the other two enterprise funds are combined into a single, aggregated nonmajor fund presentation. Individual fund data for each of these nonmajor enterprise funds is provided in the form of combining statements elsewhere in the CAFR.

The basic proprietary funds financial statements can be found on pages 21 – 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 – 54 of this report.

Other Information. In addition to the basic financial statements and accompanying notes, this report presents the combining statements referred to earlier in connection with nonmajor governmental and enterprise funds, comparative information for the General Fund and budgetary information to demonstrate the City's budgetary compliance. Combining and individual fund statements and schedules can be found on pages 55 – 86 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

The City's combined net assets were $240.2 million as of September 30, 2012. Analyzing the net assets and net expenses of governmental and business-type activities separately, the business-type activities net assets are $127.9 million. This analysis focuses on the net assets (Table 1) and changes in net assets of the City's governmental and business-type activities (Table 2).

By far, the largest portion of the City's net assets (67%) reflects its investment in capital assets (e.g., land, buildings, machinery, and equipment), less any related debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The remaining balance of unrestricted net assets ($59.3 million) may be used to meet the government's ongoing obligations to citizens and creditors.

At the end of the current fiscal year, the City of San Marcos is able to report positive balances in all three categories of net assets, both for the government as a whole, as well as for its separate governmental and business-type activities. The same situation held true for the prior fiscal year

TABLE 1

CITY OF SAN MARCOS' NET ASSETS

	Governmental Activities		Business-type Activities		Totals	
	2012	2011	2012	2011	2012	2011
Current and other assets	$ 79,496,756	$ 82,605,912	$ 100,063,095	$ 98,007,233	$ 179,559,851	$ 180,613,145
Capital assets	182,327,643	176,108,824	169,561,856	164,989,010	351,889,499	341,097,834
Total assets	261,824,399	258,714,736	269,624,951	262,996,243	531,449,350	521,710,979
Long-term liabilities outstanding	137,671,110	143,129,795	129,761,798	129,152,626	267,432,908	272,282,421
Other liabilities	11,856,100	12,556,695	11,996,473	10,621,478	23,852,573	23,178,173
Total liabilities	149,527,210	155,686,490	141,758,271	139,774,104	291,285,481	295,460,594
Net assets:						
Invested in capital assets, net of related debt	82,639,548	74,247,634	77,417,956	76,737,408	160,057,504	150,985,042
Restricted	20,848,878	9,972,700	-	-	20,848,878	9,972,700
Unrestricted	8,808,763	18,807,912	50,448,724	46,484,731	59,257,487	65,292,643
Total net assets	$ 112,297,189	$ 103,028,246	$ 127,866,680	$ 123,222,139	$ 240,163,869	$ 226,250,385

Governmental activities. The City's governmental revenues increased when compared to the prior year by 20.2% or $9,386,378. This increase is due to several factors including increases in sales tax revenue of $1.2 million and a $7.1 million increase in capital grants and contributions, primarily due to the timing of the TxDOT pass-thru toll reimbursement on the Wonder World Drive project.

The most significant governmental expense for the City was in providing for public safety, which incurred expenses of $19.4 million. The public safety expense increase was primarily due to the funding of the second year of the meet and confirm contract entered into in 2010 and routine step increases.

Business-type activities. Revenues of the City's business-type activities were $89.7 million for the fiscal year ending September 30, 2012. Expenses for the City's business-type activities were $78.7 million for the year, resulting in a net increase in net assets of $11.0 million. The net revenues are the result of several factors, including the following:

- The City's Water and Wastewater System recorded charges for services of $28.1 million, which exceeded expenses of $27.9 million. The most significant expenses of the Water and Wastewater Fund $7.4 million for contracted services for the operation of the surface water treatment plant, and $3.3 million in salaries and benefits.

- The City's Electric distribution system recorded charges for services of $51.8 million, which exceeded expenses $45.6 million. The most significant expense of the Electric Fund was $36.5 million for the purchase of power.

- The increase in net assets from business-type activities was primarily due to increased revenue from water, sewer, and electric sales due to the unseasonably hot and dry spring and summer weather. Capital contributions of water and sewer infrastructure as new construction activity continues in the City.

Governmental and business-type activities increased the City's net assets (Table 2) by $13.9 million.

TABLE 2

CITY OF SAN MARCOS' CHANGES IN NET ASSETS

	Governmental Activities		Business-type Activities		Totals	
	2012	2011	2012	2011	2012	2011
Revenues:						
Program revenues:						
Charges for services	$ 3,698,461	$ 3,576,394	$ 85,356,174	$ 79,715,074	$ 89,054,635	$ 83,291,468
Operating grants and contributions	3,250,996	2,619,600	-	-	3,250,996	2,619,600
Capital grants and contributions	8,244,456	1,149,409	1,274,418	1,085,830	9,518,874	2,235,239
General revenues:						
Property taxes, levied for general purposes	6,411,156	5,839,764	-	-	6,411,156	5,839,764
Property taxes, levied for debt service	8,036,946	8,396,878	-	-	8,036,946	8,396,878
Sales taxes	21,079,582	19,854,399	-	-	21,079,582	19,854,399
Franchise taxes	1,436,152	1,447,569	-	-	1,436,152	1,447,569
Hotel/motel taxes	2,510,750	2,296,276	-	-	2,510,750	2,296,276
Investment earnings	261,704	319,091	303,932	376,915	565,636	696,006
Other	1,428,050	959,702	2,780,304	2,029,511	4,208,354	2,989,213
Total revenues	56,358,253	46,459,082	89,714,828	83,207,330	146,073,081	129,666,412
Expenses:						
General government	17,452,471	15,419,706	-	-	17,452,471	15,419,706
Public safety	19,367,969	18,040,389	-	-	19,367,969	18,040,389
Community service	10,399,904	10,092,399	-	-	10,399,904	10,092,399
Interest and fiscal charges	6,255,072	6,412,611	-	-	6,255,072	6,412,611
Electric	-	-	45,590,881	43,413,456	45,590,881	43,413,456
Water and sewer	-	-	27,890,126	26,701,908	27,890,126	26,701,908
Airport	-	-	601,781	710,558	601,781	710,558
Drainage	-	-	2,491,018	1,897,978	2,491,018	1,897,978
Waste collection	-	-	2,110,375	1,773,160	2,110,375	1,773,160
Total expenses	53,475,416	49,965,105	78,684,181	74,497,060	132,159,597	124,462,165
Increases in net assets before transfers	2,882,837	(3,506,023)	11,030,647	8,710,270	13,913,484	5,204,247
Transfers	6,386,106	6,290,865	(6,386,106)	(6,290,865)	-	-
Increase in net assets	9,268,943	2,784,842	4,644,541	2,419,405	13,913,484	5,204,247
Net assets, beginning	103,028,246	100,243,404	123,222,139	120,802,734	226,250,385	221,046,138
Net assets, ending	$ 112,297,189	$ 103,028,246	$ 127,866,680	$ 123,222,139	$ 240,163,869	$ 226,250,385

FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

As noted earlier, the City of San Marcos uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

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

As of the end of the current fiscal year, the City of San Marcos' governmental funds reported combined fund balances of $64.9 million, a decrease of $(1.0) million in comparison with the prior year. Approximately 21.1% of this total amount constitutes unassigned fund balance, which is available for use within the City's fund designation and fiscal policies. The remainder of fund balance is restricted to indicate that it is not available for new spending because it has already been committed 1) to liquidate contracts and purchase prepaid expenses of the prior period, 2) to pay debt service, 3) for capital projects, 4) to generate income to pay for the perpetual care of the municipal cemetery, 5) to be used for general government, or 6) to be used for community services.

The General Fund is the main operating fund of the City of San Marcos. At the end of the current fiscal year, unassigned fund balance of the General Fund was $13.6 million, while total fund balance reached $14.9 million. As a measure of the General Fund's liquidity, it may be useful to compare both unassigned fund balance and total fund balance to total fund expenditures. Unassigned fund balance represents 33.2% of total General Fund expenditures.

In the General Fund, the City budgeted for a fund balance decrease in the current year of $(867,532). It is one of the City's financial policies to maintain fund balance in the General Fund equal to 90 days' expenditures and when those balances exceed the 90-day target to transfer the excess to Capital Project Funds to fund pay-as-you-go capital expenditures. Even though use of fund balance was budgeted, $1,121,061 was added to fund balance at year-end. This is primarily attributable to sales tax revenue coming in $1.2 million above budget and actual expenditures being less than originally budgeted. The Debt Service Fund Balance increased by $3.3 million from 2011 to 2012. This fund balance increase was primarily due to the timing of the TxDot Pass-through Toll revenue. Increases in the General Fund, Debt Service, and other governmental fund balances off set by the decrease in Capital Projects Funds of $5.8 Million due to progress on construction contributed to the net change in fund balances of $971,800.

TABLE 3

GOVERNMENTAL TAX REVENUES

	2012	2011	Increase (Decrease)
Property	$ 14,514,084	$ 14,260,359	$ 253,725
Sales	21,079,582	19,854,399	1,225,183
Franchise	1,282,507	1,184,223	98,284
Hotel/motel	2,510,750	2,296,276	214,474
Mixed drink	243,974	263,346	(19,372)
	$ 39,630,897	$ 37,858,603	$ 1,772,294

Other factors concerning the finances of governmental funds have already been addressed in the discussion of the City's governmental activities in the government-wide financial statements.

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

Unrestricted net assets of Water and Wastewater Fund at the end of the year amounted to $35.1 million, and those for the Electric Fund amounted to $11.4 million. Other factors concerning the finances of these two funds have already been discussed in the discussion of the City of San Marcos' business-type activities in the government-wide financial statements.

GENERAL FUND BUDGETARY HIGHLIGHTS

For FY2012, actual expenditures on a budgetary basis were $40.9 million compared to the budget amount of $41.6 million. The $0.8 million positive variance was due to savings achieved through salary vacancy savings and conservative spending.

For FY2012, actual revenues on a budgetary basis were $37.5 million as compared to the budget amount of $36.8 million. The majority of the $696,000 variance was due to sales tax revenue collections above budgeted amounts.

The City of San Marcos has a General Fund balance of $14.9 million as of the fiscal year-end, compared to the budgeted fund balance of $12.9 million. The variance in fund balance is primarily due to cost containment measures implemented by management and conservative budgetary practices and increased sales tax revenue.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets. At the end of the fiscal year 2012, the City had $496.8 million invested in a broad range of capital assets, including police and fire equipment, buildings, park facilities, roads, bridges, and water and wastewater lines. (See Table 4 below.) For more detailed information on capital assets, please refer to the accompanying notes 38 – 39.

TABLE 4

CITY OF SAN MARCOS' CAPITAL ASSETS AT YEAR-END (Net of Accumulated Depreciation)

	Governmental Activities		Business-type Activities		Totals	
	2012	2011	2012	2011	2012	2011
Land	$ 7,286,864	$ 7,224,964	$ 1,446,029	$ 1,446,029	$ 8,732,893	$ 8,670,993
Buildings	36,544,215	36,544,215	6,369,767	6,369,767	42,913,982	42,913,982
Improvements other than buildings	50,088,473	49,931,357	168,701,317	165,019,670	218,789,790	214,951,027
Equipment	22,018,760	22,255,300	8,686,069	8,418,119	30,704,829	30,673,419
Construction in progress	94,867,389	86,332,855	72,117,636	62,287,907	166,985,025	148,620,762
Infrastructure	28,656,436	25,361,436	-	-	28,656,436	25,361,436
Total capital assets	$ 239,462,137	$ 227,650,127	$ 257,320,818	$ 243,541,492	$ 496,782,955	$ 471,191,619

Long-term debt. At year-end, the City had $259.2 million in General Obligation Bonds, Combination Tax and Revenue Certificates of Obligations and Revenue Bonds outstanding as compared to $264.7 million at the end of the prior fiscal year, a decrease of (2.1%). For more detailed information on long term debt, please refer to the accompanying notes on pages 41 – 45.

TABLE 5

CITY OF SAN MARCOS' OUTSTANDING DEBT AT YEAR-END

	Governmental Activities		Business-type Activities		Totals	
	2012	2011	2012	2011	2012	2011
General obligation bonds	$ 30,355,000	$ 26,980,000	$ -	$ -	$ 30,355,000	$ 26,980,000
Certificates of obligation	99,130,000	109,235,000	-	-	99,130,000	109,235,000
Revenue bonds	-	-	129,750,000	128,450,000	129,750,000	128,450,000
	$ 129,485,000	$ 136,215,000	$ 129,750,000	$ 128,450,000	$ 259,235,000	$ 264,665,000

During this fiscal year, General Obligation Refunding totaling $33.6 were issued to refund some previous debt issues.

The City has maintained its AA- rating from Standard & Poor's Corporation, and its A1 rating from Moody's Investor Services on its tax supported debt. The City is permitted by Article XI, Section 5, of the State of Texas Constitution to levy taxes up to $2.50 per $100 assessed valuation for general governmental services including the payment of principal and interest on general obligation long-term debt. The current ratio of net tax-supported debt to assessed value of all taxable property is 2.85%.

The City sponsors an employee benefit plan that provides partially self-insured medical and self-insured dental coverage to employees and voluntary coverage to their participating dependents. The plan is designed to provide a specified level of coverage, with excess insurance coverage provided by specific and aggregate reinsurance. The City's maximum medical claim exposure is limited to $100,000 in claims per covered person and a dental benefit of $1,250 per covered person per year. Aggregate coverage based on a monthly enrollment limits the medical claims exposure. Claim liability was $1,059,950 at September 30, 2012, compared to $897,277 at September 30, 2011.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City's elected and appointed officials considered many factors when setting the fiscal year 2013 budget, tax rates, and fees that will be charged. In January 2011, the San Marcos City Council held a Visioning Workshop to explore important policy issues facing the City. At that meeting, five primary strategic initiatives were developed that will guide staff during the upcoming years. These initiatives include:

- Sound Finances
- Customer Friendly Processes
- Big Picture Infrastructure
- San Marcos River Protection, Recreation and Maintenance
- Community Wellness/Encourage the Middle Class

These strategic initiatives were used as the basis for setting and adopting the operating budget for fiscal year 2013. The total FY2013 combined budget appropriation is $160.9 million. This represents an increase of $11.3 million or 7.5% over the FY2012 budget. The increase in the annual budget is attributed to several facts including:

- Addition of the Transit Fund which is funded through Federal Transit Revenue received by the City for the operation of a transit system.

- Addition of personnel and increased routine maintenance to Parks, Facilities, IT, and Streets in the General Fund

- Transfer of fund balances in excess of 25% in the Water/Wastewater and Electric Fund to Capital Reserves

- Increase in the Cost of Power in the Electric Fund

The General Fund's largest single revenue source is sales taxes. The City collects a 1.5-cent sales tax on all taxable goods in the City. Sales tax revenue for FY2013 is budgeted at $21.1 million.

The property tax rate for FY2012 is $0.5302 per $100 valuation. Of this tax rate, 50.0% or $0.2651 is used for operations and maintenance activities and 50.0% is used for debt service. The operations and maintenance portion of property tax revenue for FY2013 is estimated to be $7.6 million.

The largest revenue source for the Water and Wastewater Fund is water sales, at $14.3 million. The base rate for FY2013 is $20.14 for the first 2,000 gallons for a 5/8" – 3/4" meter in the city limits. This rate increases as the meter size increases and/or if the meter is located outside of the city limits. This rate was increased 3.0% for FY2013 in accordance with the two year ordinance adopted in FY2012. The second largest revenue source for the Water and Wastewater Fund is wastewater charges, at $13.1 million. The base rate for FY2013 is $23.56 for the first 2,000 gallons. This rate was increased 2.5% for FY2013 in accordance with the two year ordinance adopted in FY2012.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Finance Department, at the City of San Marcos, 630 E. Hopkins, San Marcos, TX 78666.

BASIC
FINANCIAL STATEMENTS

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CITY OF SAN MARCOS, TEXAS

STATEMENT OF NET ASSETS

SEPTEMBER 30, 2012

	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and equivalents	$ 14,620,736	$ 39,062,952	$ 53,683,688
Investments	55,341,315	47,982,955	103,324,270
Receivables (net of allowance for uncollectible):			
Accounts	1,660,501	10,032,907	11,693,408
Taxes	3,854,823	-	3,854,823
Other	27,827	-	27,827
Due from other governments	1,469,910	12,142	1,482,052
Internal balances	40,049	(40,049)	-
Inventories	280,804	1,097,881	1,378,685
Prepaid items	115,679	1,443	117,122
Deferred charges	2,085,112	1,912,864	3,997,976
Capital assets:			
Land	7,286,864	1,446,029	8,732,893
Construction in progress	94,867,389	72,117,636	166,985,025
Buildings	36,544,215	6,369,767	42,913,982
Improvements other than buildings	50,088,473	168,701,317	218,789,790
Equipment	22,018,760	8,686,069	30,704,829
Infrastructure	28,656,436	-	28,656,436
Less: accumulated depreciation	(57,134,494)	(87,758,962)	(144,893,456)
Total capital assets	182,327,643	169,561,856	351,889,499
Total assets	261,824,399	269,624,951	531,449,350
LIABILITIES			
Accounts payable	4,587,773	7,060,667	11,648,440
Accrued liabilities	2,489,463	421,258	2,910,721
Unearned revenues	4,003,867	560,146	4,564,013
Customer deposits	17,736	3,044,574	3,062,310
Accrued interest payable	757,261	909,828	1,667,089
Noncurrent liabilities:			
Due within one year	7,520,601	7,838,405	15,359,006
Due in more than one year	130,150,509	121,923,393	252,073,902
Total liabilities	149,527,210	141,758,271	291,285,481
NET ASSETS			
Invested in capital assets, net of related debt	82,639,548	77,417,956	160,057,504
Restricted for:			
Capital projects	7,398,250	-	7,398,250
Grant requirements	79,808	-	79,808
Public safety	364,383	-	364,383
Debt service	10,484,328	-	10,484,328
Future convention center	1,482,309	-	1,482,309
Park and cemetery trust:			
Nonexpendable	1,039,800	-	1,039,800
Unrestricted	8,808,763	50,448,724	59,257,487
Total net assets	$ 112,297,189	$ 127,866,680	$ 240,163,869

The accompanying notes are an integral part of these financial statements.

CITY OF SAN MARCOS, TEXAS

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED SEPTEMBER 30, 2012

		Program Revenue		
Functions/Programs	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
Primary government				
Governmental activities:				
General government	$ 17,452,471	$ 1,246,616	$ 994,794	$ 7,861,248
Public safety	19,367,969	1,682,378	713,809	-
Community service	10,399,904	769,467	1,542,393	383,208
Interest on long-term debt	6,255,072	-	-	-
Total governmental activities	53,475,416	3,698,461	3,250,996	8,244,456
Business-type activities:				
Electric	45,590,881	51,783,661	-	-
Water and wastewater	27,890,126	28,139,268	-	1,274,418
Airport	601,781	580,554	-	-
Drainage	2,491,018	2,553,844	-	-
Waste collection	2,110,375	2,298,847	-	-
Total business-type activities	78,684,181	85,356,174	-	1,274,418
Total primary government	$ 132,159,597	$ 89,054,635	$ 3,250,996	$ 9,518,874

General revenues:
Taxes:
Property taxes, levied for general purposes
Property taxes, levied for debt service
Sales
Franchise taxes
Hotel/motel
Other
Investment earnings
Miscellaneous
Transfers
Total general revenues and transfers

Change in net assets

Net assets - beginning

Net assets - ending

The accompanying notes are an integral part of these financial statements.

Net (Expense) Revenue and Changes in Net Assets		
Primary Government		
Governmental Activities	Business-type Activities	Total
$(7,349,813)	$ -	$(7,349,813)
(16,971,782)	-	(16,971,782)
(7,704,836)	-	(7,704,836)
(6,255,072)	-	(6,255,072)
(38,281,503)	-	(38,281,503)
-	6,192,780	6,192,780
-	1,523,560	1,523,560
-	(21,227)	(21,227)
-	62,826	62,826
-	188,472	188,472
-	7,946,411	7,946,411
(38,281,503)	7,946,411	(30,335,092)
6,411,156	-	6,411,156
8,036,946	-	8,036,946
21,079,582	-	21,079,582
1,436,152	-	1,436,152
2,510,750	-	2,510,750
90,329	-	90,329
261,704	303,932	565,636
1,337,721	2,780,304	4,118,025
6,386,106	(6,386,106)	-
47,550,446	(3,301,870)	44,248,576
9,268,943	4,644,541	13,913,484
103,028,246	123,222,139	226,250,385
$ 112,297,189	$ 127,866,680	$ 240,163,869

CITY OF SAN MARCOS, TEXAS

BALANCE SHEET

GOVERNMENTAL FUNDS

SEPTEMBER 30, 2012

	General	Capital Projects	Debt Service	Other Governmental	Total
ASSETS					
Cash and cash equivalents	$ -	$ 9,689,622	$ 475,693	$ 2,414,952	$ 12,580,267
Investments	16,239,826	27,330,332	8,751,969	3,019,188	55,341,315
Receivables (net of allowance for uncollectibles):					
Accounts	1,545,617	15,759	-	31,082	1,592,458
Taxes	2,666,606	-	504,646	683,571	3,854,823
Loans	-	-	-	27,827	27,827
Due from other funds	1,396,558	1,477,737	1,441,928	545,104	4,861,327
Due from other governments	-	-	-	1,469,910	1,469,910
Inventories	280,804	-	-	-	280,804
Prepaid items	104,694	155	-	10,830	115,679
Total assets	$ 22,234,105	$ 38,513,605	$ 11,174,236	$ 8,202,464	$ 80,124,410
LIABILITIES AND FUND BALANCES					
Liabilities:					
Accounts payable	$ 1,395,186	$ 1,613,507	$ 233	$ 489,810	$ 3,498,736
Accrued liabilities	1,761,835	56,491	-	43,769	1,862,095
Deferred revenue	1,697,209	-	488,868	2,899,829	5,085,906
Customer deposits	15,605	-	-	2,131	17,736
Due to other funds	2,439,385	405,972	200,807	1,673,684	4,719,848
Total liabilities	7,309,220	2,075,970	689,908	5,109,223	15,184,321
Fund balances:					
Nonspendable for:					
Inventories	280,804	-	-	-	280,804
Prepaid items	104,694	155	-	10,830	115,679
Restricted for:					
Public safety	-	-	-	339,639	339,639
Community services	-	-	-	1,586,861	1,586,861
Cemetery memorial	-	-	-	1,039,800	1,039,800
Capital projects	980,103	36,437,480	-	-	37,417,583
Debt service	-	-	10,484,328	-	10,484,328
Unassigned	13,559,284	-	-	116,111	13,675,395
Total fund balances	14,924,885	36,437,635	10,484,328	3,093,241	64,940,089
Total liabilities and fund balances	$ 22,234,105	$ 38,513,605	$ 11,174,236	$ 8,202,464	$ 80,124,410

The accompanying notes are an integral part of these financial statements.

CITY OF SAN MARCOS, TEXAS

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE STATEMENT OF NET ASSETS

SEPTEMBER 30, 2012

Total fund balance, governmental funds	$ 64,940,089
Amounts reported for governmental activities in the Statement of Net Assets are different because:	
Capital assets used in governmental activities are not current financial resources and therefore are not reported in this fund financial statement, but are reported in the governmental activities of the Statement of Net Assets.	182,211,743
Certain other long-term assets are not available to pay current period expenditures and therefore are not reported in this fund financial statement, but are reported in the governmental activities of the Statement of Net Assets.	1,149,355
The assets and liabilities of certain internal service funds are not included in the fund financial statement, but are included in the governmental activities of the Statement of Net Assets.	850,729
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.	(136,854,727)
Net Assets of Governmental Activities in the Statement of Net Assets	$ 112,297,189

The accompanying notes are an integral part of these financial statements.

CITY OF SAN MARCOS, TEXAS

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

GOVERNMENTAL FUNDS

FOR THE YEAR ENDED SEPTEMBER 30, 2012

	General	Capital Projects	Debt Service	Other Governmental	Total
REVENUES					
Taxes	$ 28,606,490	$ -	$ 8,072,954	$ 2,951,453	$ 39,630,897
Licenses and permits	1,039,855	-	-	-	1,039,855
Fees and penalties	1,531,308	-	-	206,834	1,738,142
Charges for services	5,139,612	-	-	95,940	5,235,552
Intergovernmental	188,265	89,897	6,060,000	5,105,066	11,443,228
Interest on investments	48,956	191,247	4,630	16,871	261,704
Contributions and donations	-	30,000	-	-	30,000
Miscellaneous	962,903	261,012	145,070	58,598	1,427,583
Total revenues	37,517,389	572,156	14,282,654	8,434,762	60,806,961
EXPENDITURES					
Current:					
General government	15,033,754	1,209,752	-	351,652	16,595,158
Public safety	19,694,976	-	-	832,518	20,527,494
Community service	6,132,981	-	-	3,172,413	9,305,394
Capital outlay	-	6,642,703	-	2,582,991	9,225,694
Debt service:					
Principal	-	-	6,620,000	-	6,620,000
Interest and fiscal charges	-	-	6,074,720	-	6,074,720
Bond issuance costs	-	-	77,783	-	77,783
Total expenditures	40,861,711	7,852,455	12,772,503	6,939,574	68,426,243
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(3,344,322)	(7,280,299)	1,510,151	1,495,188	(7,619,282)
OTHER FINANCING SOURCES (USES)					
Transfers in	6,454,760	1,513,776	1,759,536	79,662	9,807,734
Transfers out	(2,013,105)	(51,100)	-	(1,210,505)	(3,274,710)
Insurance recoveries	-	11,517	-	-	11,517
Sale of capital assets	23,728	-	-	-	23,728
Capital related debt issued	-	-	5,520,000	-	5,520,000
Payment to refunded bond escrow agent	-	-	(6,016,992)	-	(6,016,992)
Premium on debt issued	-	-	576,210	-	576,210
Total other financing sources and uses	4,465,383	1,474,193	1,838,754	(1,130,843)	6,647,487
NET CHANGE IN FUND BALANCES	1,121,061	(5,806,106)	3,348,905	364,345	(971,795)
FUND BALANCES, BEGINNING	13,803,824	42,243,741	7,135,423	2,728,896	65,911,884
FUND BALANCES, ENDING	$ 14,924,885	$ 36,437,635	$ 10,484,328	$ 3,093,241	$ 64,940,089

The accompanying notes are an integral part of these financial statements.

CITY OF SAN MARCOS, TEXAS

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

FOR THE YEAR ENDED SEPTEMBER 30, 2012

Net change in fund balances - total governmental funds:	$(971,795)
Amounts reported for Governmental Activities in the Statement of Activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.	6,212,663
Governmental funds report the entire net sales price (proceeds) from sale of an asset as revenue because it provides current financial resources. In contrast, the Statement of Activities reports only the gain on the sale of the assets. Thus, the change in net assets differs from the change in fund balance by the cost of the asset sold.	(109,744)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	(66,563)
The issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets.	6,041,303
Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.	(621,847)
Internal service funds are used by management to charge the costs of certain activities, such as fleet maintenance and information technology, to individual funds. The net revenue (expense) of certain internal service funds is reported with governmental activities.	(1,215,074)
Change in net assets of governmental activities	$ 9,268,943

The accompanying notes are an integral part of these financial statements.

CITY OF SAN MARCOS, TEXAS

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL

GENERAL FUND

FOR THE YEAR ENDED SEPTEMBER 30, 2012

	Budgeted Amounts			Variance with Final Budget - Positive
	Original	Final	Actual Amounts	(Negative)
REVENUES				
Taxes	$ 27,701,546	$ 27,701,546	$ 28,606,490	$ 904,944
Licenses and permits	907,255	907,255	1,039,855	132,600
Fines and penalties	1,689,782	1,689,782	1,531,308	(158,474)
Charges for services	5,163,525	5,163,525	5,139,612	(23,913)
Intergovernmental	212,652	212,652	188,265	(24,387)
Interest on investments	61,000	61,000	48,956	(12,044)
Miscellaneous	1,085,680	1,085,680	962,903	(122,777)
Total revenues	36,821,440	36,821,440	37,517,389	695,949
EXPENDITURES				
Current:				
General government	16,839,807	15,602,924	15,033,754	569,170
Public safety	19,652,205	19,821,427	19,694,976	126,451
Community service	6,179,498	6,204,667	6,132,981	71,686
Debt service:				
Principal	29,180	-	-	-
Total expenditures	42,700,690	41,629,018	40,861,711	767,307
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(5,879,250)	(4,807,578)	(3,344,322)	1,463,256
OTHER FINANCING SOURCES (USES)				
Transfers in	5,716,197	5,836,215	6,454,760	618,545
Transfers out	(894,923)	(2,044,169)	(2,013,105)	31,064
Sale of capital assets	148,000	148,000	23,728	(124,272)
Total other financing sources and uses	4,969,274	3,940,046	4,465,383	525,337
NET CHANGE IN FUND BALANCES	(909,976)	(867,532)	1,121,061	1,988,593
FUND BALANCES, BEGINNING	13,803,824	13,803,824	13,803,824	-
FUND BALANCES, ENDING	$ 12,893,848	$ 12,936,292	$ 14,924,885	$ 1,988,593

The accompanying notes are an integral part of these financial statements.

CITY OF SAN MARCOS, TEXAS

STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
SEPTEMBER 30, 2012

	Business-type Activities - Enterprise Funds					Governmental Activities-
	Electric	Water and Wastewater	Stormwater Drainage	Other Enterprise	Total	Internal Service
ASSETS						
Current assets:						
Cash and cash equivalents	$ 9,889,665	$ 25,760,892	$ 2,134,609	$ 1,277,786	$ 39,062,952	$ 2,040,469
Investments	10,011,897	29,152,712	8,818,346	-	47,982,955	-
Accounts receivable, net	5,791,269	3,546,061	316,624	378,953	10,032,907	727
Due from other funds	99,842	338,567	95,706	51,798	585,913	156,710
Due from other governments	-	-	-	12,142	12,142	-
Inventories	601,986	495,895	-	-	1,097,881	-
Prepaid items	1,133	155	155	-	1,443	-
Total current assets	26,395,792	59,294,282	11,365,440	1,720,679	98,776,193	2,197,906
Non-current assets:						
Deferred charges	151,478	1,489,857	271,529	-	1,912,864	-
Capital assets:						
Land	31,695	1,313,997	-	100,337	1,446,029	-
Buildings	472,092	1,557,930	-	4,339,745	6,369,767	-
Improvements other than buildings	15,356,214	137,558,671	7,570,165	8,216,267	168,701,317	-
Furnishings and equipment	2,837,130	5,425,813	403,663	19,463	8,686,069	-
Construction in progress	21,483,903	43,150,792	6,338,963	1,143,978	72,117,636	-
Less accumulated depreciation	(14,329,304)	(62,323,147)	(1,830,332)	(9,276,179)	(87,758,962)	-
Total capital assets	25,851,730	126,684,056	12,482,459	4,543,611	169,561,856	-
Total non-current assets	26,003,208	128,173,913	12,753,988	4,543,611	171,474,720	-
Total assets	$ 52,399,000	$ 187,468,195	$ 24,119,428	$ 6,264,290	$ 270,250,913	$ 2,197,906
LIABILITIES						
Current liabilities:						
Accounts payable	3,740,252	2,446,604	656,444	217,367	7,060,667	29,087
Accrued liabilities	215,594	191,183	4,290	10,191	421,258	-
Due to other funds	386,370	275,881	14,088	60,845	737,184	146,918
Deferred revenue	-	560,146	-	-	560,146	-
Claims payable	-	-	-	-	-	1,059,950
Customer deposits	2,276,271	632,333	1,179	134,791	3,044,574	-
Accrued interest payable	162,814	638,616	108,398	-	909,828	-
Compensated absences	112,787	111,446	7,078	-	231,311	-
Current maturities of long-term debt	1,173,519	5,624,396	809,179	-	7,607,094	-
Total current liabilities	8,067,607	10,480,605	1,600,656	423,194	20,572,062	1,235,955
Non-current liabilities:						
Compensated absences	27,551	27,236	1,730	-	56,517	-
Long-term debt	14,515,278	90,453,945	16,886,031	11,622	121,866,876	-
Total non-current liabilities	14,542,829	90,481,181	16,887,761	11,622	121,923,393	-
Total liabilities	22,610,436	100,961,786	18,488,417	434,816	142,495,455	1,235,955
NET ASSETS						
Invested in capital assets, net of related debt	18,361,769	51,446,509	3,066,067	4,543,611	77,417,956	-
Unrestricted	11,426,795	35,059,900	2,564,944	1,285,863	50,337,502	961,951
Total net assets	$ 29,788,564	$ 86,506,409	$ 5,631,011	$ 5,829,474	127,755,458	$ 961,951
The assets and liabilities of certain internal service funds are not included in the fund financial statement, but are included in the business-type activities of the statement of net assets.					111,222	
Total net assets per government-wide financial statements					$ 127,866,680	

The accompanying notes are an integral part of these financial statements.

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CITY OF SAN MARCOS, TEXAS

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2012

	Business-type Activities - Enterprise Funds					Governmental Activities
	Electric	Water and Wastewater	Stormwater Drainage	Other Enterprise	Total	Internal Service
OPERATING REVENUES						
Charges for services	$ 49,843,421	$ 28,095,240	$ 2,553,844	$ 2,560,157	$ 83,052,662	$ -
Intergovernmental	1,940,240	44,028	-	319,244	2,303,512	-
Employer contributions	-	-	-	-	-	2,892,053
Employee contributions	-	-	-	-	-	914,530
Retiree contributions	-	-	-	-	-	171,699
Pharmacy rebates	-	-	-	-	-	17,844
Total operating revenues	51,783,661	28,139,268	2,553,844	2,879,401	85,356,174	3,996,126
OPERATING EXPENSES						
Purchased power	36,529,320	-	-	-	36,529,320	-
Personnel services	3,339,658	3,337,286	285,148	37,321	6,999,413	-
Contracted services	1,224,275	7,418,125	669,818	2,373,801	11,686,019	-
Materials and supplies	1,163,504	891,174	20,624	17,069	2,092,371	-
Indirect costs	973,651	3,105,034	130,917	-	4,209,602	-
Claims	-	-	-	-	-	4,533,042
Other charges	1,005,811	590,834	7,021	24,785	1,628,451	657,057
Depreciation	660,543	7,974,161	526,374	255,089	9,416,167	-
Total operating expenses	44,896,762	23,316,614	1,639,902	2,708,065	72,561,343	5,190,099
OPERATING INCOME	6,886,899	4,822,654	913,942	171,336	12,794,831	(1,193,973)
NON-OPERATING REVENUES (EXPENSES)						
Investment earnings	65,824	208,272	29,836	-	303,932	7,131
Interest and fiscal charges	(625,349)	(4,531,444)	(847,359)	-	(6,004,152)	-
Other	248,588	2,423,687	46,676	61,353	2,780,304	-
Total non-operating revenue (expenses	(310,937)	(1,899,485)	(770,847)	61,353	(2,919,916)	7,131
INCOME BEFORE TRANSFERS	6,575,962	2,923,169	143,095	232,689	9,874,915	(1,186,842)
Capital contributions	-	1,274,418	-	-	1,274,418	-
Transfers in	-	-	-	170,636	170,636	-
Transfers out	(4,194,426)	(2,362,316)	-	-	(6,556,742)	(146,918)
CHANGE IN NET ASSETS	2,381,536	1,835,271	143,095	403,325	4,763,227	(1,333,760)
TOTAL NET ASSETS, BEGINNING	27,407,028	84,671,138	5,487,916	5,426,149	122,992,231	2,295,711
TOTAL NET ASSETS, ENDING	$ 29,788,564	$ 86,506,409	$ 5,631,011	$ 5,829,474	127,755,458	$ 961,951
Change in net assets, per above					4,763,227	
Internal service funds are used by management to charge the costs of certain activities to individual funds. The net revenue (expense) of certain internal service funds is reported with Business Activities.					(118,686)	
Change in business-type activities in net assets per government-wide financial statements					$ 4,644,541	

The accompanying notes are an integral part of these financial statements.

CITY OF SAN MARCOS, TEXAS

STATEMENT OF CASH FLOWS

PROPRIETARY FUNDS

YEAR ENDED SEPTEMBER 30, 2012

	Business-type Activities - Enterprise Funds					Governmental Activities -
	Electric	Water and Wastewater	Stormwater Drainage	Other Funds	Totals	Internal Service Fund
CASH FLOWS FROM OPERATING ACTIVITIES						
Cash received from customers	$ 52,934,268	$ 28,088,258	$ 2,517,678	$ 2,779,965	$ 86,320,169	$ 3,995,399
Cash paid to suppliers for goods and services	(40,661,174)	(10,391,646)	(663,366)	(2,420,308)	(54,136,494)	(6,461,769)
Cash paid to employees for services	(3,322,519)	(3,258,151)	(285,509)	2,009	(6,864,170)	-
Net cash provided (used) by operating activities	8,950,575	14,438,461	1,568,803	361,666	25,319,505	(2,466,370)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES						
Cash received from miscellaneous items	248,588	2,423,687	46,676	-	2,718,951	-
Transfers from other funds	-	-	-	170,636	170,636	-
Transfers to other funds	(4,194,426)	(2,362,316)	-	-	(6,556,742)	-
Net cash provided (used) by noncapital financing activities	(3,945,838)	61,371	46,676	170,636	(3,667,155)	-
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES						
Proceeds from capital debt	8,090,000	31,500	4,696	-	8,126,196	-
Capital contributions	-	1,274,418	-	-	1,274,418	-
Principal paid on debt	(1,035,000)	(5,655,000)	(775,000)	-	(7,465,000)	-
Interest and fiscal charges paid on debt	(591,951)	(4,474,252)	(841,749)	-	(5,907,952)	-
Acquisition of capital assets	(2,433,043)	(10,253,967)	(1,378,447)	(67,935)	(14,133,392)	-
Net cash provided (used) by capital and related financing activities	4,030,006	(19,077,301)	(2,990,500)	(67,935)	(18,105,730)	-
CASH FLOWS FROM INVESTING ACTIVITIES						
Sale of investment securities	(1,410,450)	30,130,089	1,283,101	-	30,002,740	3,095,985
Interest received	65,824	208,272	29,836	61,353	365,285	7,131
Net cash provided (used) by investing activities	(1,344,626)	30,338,361	1,312,937	61,353	30,368,025	3,103,116
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	7,690,117	25,760,892	(62,084)	525,720	33,914,645	636,746
CASH AND CASH EQUIVALENTS, BEGINNING	2,199,548	-	2,196,693	752,066	5,148,307	1,403,723
CASH AND CASH EQUIVALENTS, ENDING	$ 9,889,665	$ 25,760,892	$ 2,134,609	$ 1,277,786	$ 39,062,952	$ 2,040,469

(continued)

CITY OF SAN MARCOS, TEXAS

STATEMENT OF CASH FLOWS

PROPRIETARY FUNDS
(Continued)
YEAR ENDED SEPTEMBER 30, 2012

	Business-type Activities - Enterprise Funds					Governmental Activities - Internal Service Fund
	Electric	Water and Wastewater	Stormwater Drainage	Other Funds	Totals	
Reconciliation of operating income to net cash provided by operating activities:						
Operating income (loss)	$ 6,886,899	$ 4,822,654	$ 913,942	$ 171,336	$ 12,794,831	$(1,193,973)
Adjustments to reconcile operating income to net cash provided by operating activities:						
Depreciation	660,543	7,974,161	526,374	255,089	9,416,167	-
Changes in assets and liabilities:						
Decrease (increase) in assets:						
Accounts receivable	972,055	(29,618)	(36,421)	(56,075)	849,941	(727)
Due from other funds	511,205	446,748	(64,284)	2,533	896,202	187,297
Due from other governments	-	-	-	(8,623)	(8,623)	-
Inventories	(40,558)	(99,003)	-	-	(139,561)	-
Prepaid items	17,589	1,845	(155)	-	19,279	-
Increase (decrease) in liabilities:						
Accounts payable	(593,728)	845,257	220,497	17,173	489,199	16,649
Accrued liabilities	23,062	57,392	(594)	2,009	81,869	-
Due to other funds	277,939	(456,050)	7,065	(13,949)	(184,995)	(1,638,289)
Deferred revenue	-	560,146	-	(21,921)	538,225	-
Claims payable	-	-	-	-	-	162,673
Net pension obligation	60,552	261,123	1,798	2,007	325,480	-
OPEB libility	2,388	53,455	93	-	55,936	-
Compensated absences	(5,923)	21,743	233	-	16,053	-
Customer deposits	178,552	(21,392)	255	12,087	169,502	-
Net cash provided (used) by operations	$ 8,950,575	$ 14,438,461	$ 1,568,803	$ 361,666	$ 25,319,505	$(2,466,370)

The accompanying notes are an integral part of these financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The City of San Marcos, Texas (the City) was incorporated July 11, 1877, while the City's Home Rule Charter was adopted by election in 1967. The City operates under a Council-Manager form of government and provides the following services as authorized by its charter: public safety (police and fire), highways and streets, sanitation, health and social services, culture-recreation, public improvements, planning and zoning, general and administrative, electric, water and wastewater services.

The accompanying financial statements comply with the provisions of the GASB Statement No. 14 and 39, "The Financial Reporting Entity," in that the financial statements include all organizations, activities, functions and component units for which the City (the "primary government") is financially accountable. Financial accountability is defined as the appointment of a voting majority of a legally separate organization's governing body and either (1) the City's ability to impose its will over the organization, or (2) the potential that the organization will provide a financial benefit to or impose a financial burden on the City. There are no component units which satisfy requirements for blending within the City's financial statements or for discrete presentation.

B. Government-wide and Fund Financial Statements

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

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

Separate financial statements are provided for governmental and proprietary funds. Major individual governmental funds and major individual Enterprise Funds are reported as separate columns in the fund financial statements.

(continued)

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

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

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting.* Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be *available* when it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenue to be available if collected within 30 days of the end of the current fiscal period. Property taxes availability period is considered to be 60 days. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

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

The City reports the following major governmental funds:

The ***General Fund*** is the City'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 ***Capital Projects Fund*** accounts for the acquisition of fixed assets or construction of major capital projects not being financed by other funds.

The ***Debt Service Fund*** accounts for the accumulation of resources for the payment of general long-term principal, interest, and related costs.

(continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

The City reports the following major proprietary funds:

The ***Electric Fund*** accounts for the activities necessary for the provision of electric services.

The ***Water and Wastewater Fund*** accounts for the activities necessary for the provision of water and sewer services.

The ***Stormwater Drainage Fund*** was created to address the need for improvements in drainage channels throughout the City. The fund obtains revenue through the assessment of a monthly drainage utility fee to both residential and commercial customers.

Additionally, the City reports the following fund type:

Internal Service Fund accounts for benefits provided to other departments or agencies of the City on a cost-reimbursement basis.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the *option* of following subsequent private-sector guidance for their business-type activities and Enterprise Funds, subject to this same limitation. The City has elected not to follow subsequent private-sector guidance.

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

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

(continued)

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

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

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

D. Assets, Liabilities and Net Assets or Equity

Deposits and Investments

The City's cash and cash equivalents are considered to be cash on hand, certificates of deposit, investment securities with a maturity of three months or less from the date of purchase.

Statutes authorize the City to invest in obligations of U. S. Treasury or its agencies and instrumentalities, obligations of the state or its agencies, other investments guaranteed by the U. S. Treasury or the State of Texas, or investments rated by a national rating company at "A" or better. The City is also authorized to invest in fully collateralized repurchase agreements, local government investment pools, and in certificates of deposit issued by banks domiciled in Texas that are FDIC insured or have securities (of aforementioned quality) pledged to secure these deposits. The investment of idle funds has been restricted to U. S. Government Treasury and agency securities and time deposits with the City's depository banks.

Investments for the City are reported at fair value. The State Treasurer's Investment Pool operates in accordance with appropriate state laws and regulations. The reported value of the pool is the same as the fair value of the pool shares.

Receivables and Payables

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

All trade and property tax receivables are shown net of an allowance for uncollectibles. Trade accounts receivable in excess of 180 days comprise the trade accounts receivable allowance for uncollectibles. The property tax receivable allowance is equal to 15 percent of outstanding property taxes at September 30, 2012.

(continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Assets, Liabilities and Net Assets or Equity (Continued)

Receivables and Payables (Continued)

Property taxes are levied on October 1 and attach as an enforceable lien on property as of January 1. Statements are mailed on October 1, or as soon thereafter as possible, and are due upon receipt. All unpaid taxes become delinquent if not paid before February 1 of the following year.

Inventories and Prepaid Items

Inventory is valued at cost using the average cost method of accounting. Inventory in the General Fund consists of expendable supplies held for consumption. The cost of inventory is recorded as an expenditure at the time individual inventory items are consumed (consumption method). Inventory reported in the General Fund is offset by a fund balance reserve which indicates that it does not represent "available spendable resources" even though it is a component of net current assets. Inventory in the Water and Wastewater and Electric Funds consists of parts and maintenance items.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

Capital Assets

Capital assets, which include property, plant, equipment and infrastructure assets (e.g. roads, bridges, sidewalks and similar items) are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. The City defines capital assets as assets with an initial, individual cost of more than $5,000 and an estimated useful life in excess of one year. 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.

Property, plant and equipment is depreciated using the straight-line method over the following useful lives:

Assets	Years
Buildings	20-50
Improvements	10-40
Equipment	5-10
Infrastructure (streets and drainage)	35-125

(continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Assets, Liabilities and Net Assets or Equity (Continued)

Compensated Absences

It is the City's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. A liability for these amounts is reported in the applicable governmental funds and business-type funds as it is due to the employees at the time of resignation and retirement. The liability is recorded as follows: All employees are entitled to be paid up to 30 days (90 days with 20 years of continuous service) of accumulated vacation; in addition Civil Service-Police are entitled to be paid up to 90 days of sick and Civil Service-Fire is entitled to 90 days of sick at 1,080 hours for 12-hour days.

Long-term Obligations

In the government-wide financial statements and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net 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 recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Fund Balance Classification

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

- Nonspendable: This classification includes amounts that cannot be spent because they are either (a) not in spendable form or (b) are legally or contractually required to be maintained intact. Nonspendable items are not expected to be converted to cash or are not expected to be converted to cash within the next year.

(continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. <u>Assets, Liabilities and Net Assets or Equity</u> (Continued)

Fund Balance Classification (Continued)

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

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

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowing used for the acquisition, construction or improvements of those assets, and adding back unspent proceeds. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislations adopted by the City or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

(continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Assets, Liabilities and Net Assets or Equity (Continued)

Estimates

The preparation of financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual amounts could differ from those estimates.

Comparative Data/Reclassifications

Comparative total data for the prior year have been presented in order to provide an understanding of the changes in the financial position and operations. Also, certain amounts presented in the prior year have been reclassified in order to be consistent with the current year's presentation.

2. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

Explanation of Certain Differences Between the Governmental Fund Balance Sheet and the Government-wide Statement of Net Assets

The governmental fund balance sheet includes a reconciliation between *fund balance – total governmental funds* and *net assets – governmental activities* as reported in the government-wide statement of net assets. One element of that reconciliation explains, "Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds." The details of this $(136,854,727) difference are as follows:

General obligation bonds	$(129,485,000)
Discounts on bonds	553,412
Premiums on bonds	(1,484,522)
Accrued interest payable	(757,261)
Compensated absences	(5,064,209)
Deferred charge for bond issuance costs	2,085,112
Deferred loss on refunding	1,336,050
Retainage payable	(511,468)
TMRS Net pension obligation	(3,000,415)
OPEB Net pension obligation	(526,426)
Net adjustment to reduce *fund balance - total governmental funds* to arrive at *net assets - governmental activities*	$(136,854,727)

(continued)

2. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS (Continued)

Explanation of Certain Differences Between the Governmental Fund Statement of Revenue, Expenditures and Changes in Fund Balances and the Government-wide Statement of Activities

The governmental fund statement of revenue, expenditures and changes in fund balances includes a reconciliation between *net changes in fund balances – total governmental fund* and *changes in net assets of governmental activities* as reported in the government-wide statement of activities. One element of that reconciliation explains, "Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense." The details of this $6,212,663 difference are as follows:

Capital outlay	$ 12,447,411
Depreciation expense	(6,234,748)
Net adjustment to increase *net changes in fund balances - total governmental funds* to arrive at *changes in net assets of governmental activities*	$ 6,212,663

Another element of that reconciliation states, "Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds." The details of this $(66,563) difference are as follows:

Property taxes	$(65,982)
Court fines	(581)
Net adjustment to increase *net changes in fund balances - total governmental funds* to arrive at *changes in net assets of governmental activities*	$(66,563)

Another element of that reconciliation states, "The issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets." The details of this $6,041,303 difference are as follows:

(continued)

2. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS (Continued)

Explanation of Certain Differences Between the Governmental Fund Statement of Revenue, Expenditures and Changes in Fund Balances and the Government-wide Statement of Activities (Continued)

Debt issued or incurred:	
Issuance of general obligation bonds	$(5,520,000)
Deferred charge for bond issuance costs	73,427
Premium on bond issuance	(576,210)
TMRS Net pension obligation	(552,488)
OPEB Net pension obligation	(20,418)
Principal repayments:	
General obligation bonds refunded	5,630,000
Deferred loss on refunding	485,525
Discount on refunding	(98,533)
General obligation debt	6,620,000
Net adjustment to decrease *net changes in fund balances - total governmental funds* to arrive at *changes in net assets of governmental activities*	$ 6,041,303

Another element of that reconciliation states, "Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds." The details of this $(621,847) difference are as follows:

Compensated absences	$(445,851)
Accrued interest	5,625
Amortization of deferred charge on refunding	(122,351)
Amortization of issuance costs	(118,281)
Amortization of bond discounts	(38,024)
Amortization of bond premiums	97,035
Net adjustment to decrease *net changes in fund balances - total governmental funds* to arrive at *changes in net assets of governmental activities*	$(621,847)

3. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary Information

The City Charter prescribes certain requirements for adoption of an annual operating budget by the City Council. The Council must have a public hearing on the budget and may not adopt the budget until after 14 days after the hearing. The budget is to be adopted at least 15 days before the beginning of the fiscal year to which it applies.

The amounts of proposed expenditures become appropriated to the objects and purposes named in the budget upon the effective date after adoption. The total estimated expenditures of the General Fund shall not exceed the total estimated resources of the fund (prospective income plus cash on hand).

(continued)

3. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY (Continued)

Budgetary Information (Continued)

The City budget may be amended and appropriations may be altered in cases of public necessity, as declared by the City Council. The City Manager has the ability to reallocate funds from one line item to another within the various budget categories within departments in the same fund (i.e., personnel services, other charges, contracted services, etc.), but City Council approval is required for budget adjustments between funds.

The budget ordinance states that expenditures should not exceed the budget in the various departments (administration, personnel, finance, etc.) within an individual fund. The City's appropriation ordinance approves items as detailed in the approved budget. Budgeted amounts reported are based on the budget ordinance originally adopted and as amended by the City Council throughout the year.

Formal budgetary accounting is employed for all funds of the City, excluding Grants and Special Entitlements, Public Education, PARD Recreation Programs, Library Memorial, Parks and Recreation, Capital Projects and the Cemetery Perpetual Permanent Fund. Annual operating budgets are prepared and presented for the General Fund, Debt Service Fund, and all other Special Revenue Funds. All annual appropriations lapse at fiscal year-end.

Budgets for the Governmental Fund Types are prepared and adopted on the GAAP basis. Budgets for expenses used for managerial control have been prepared for the Enterprise Funds on a non-GAAP basis, which excludes depreciation, but includes capital outlay and total debt service.

The City Council made several supplemental budgetary appropriations throughout the year. The supplemental budgetary appropriations were not considered material.

4. DETAILED NOTES ON ALL FUNDS

Deposits and Investments

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 City 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 investments, (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, and (9) bid solicitation preferences for certificates of deposit. Statutes authorize the City to invest in (1) obligations of the U. S. Treasury, certain U. S. agencies, and the State of Texas, (2) certificates of deposit, (3) certain municipal securities, (4) money market savings accounts, (5) repurchase agreements, (6) bankers acceptances, (7) Mutual Funds, (8) investment pools, (9) guaranteed investment contracts, and (10) common trust funds. The Act also requires the City to have independent auditors perform test procedures related to investment practices as provided by the Act. The City is in substantial compliance with the requirements of the Act and with local parties.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Deposits and Investments (Continued)

In compliance with the Public Funds Investment Act, the City has adopted a deposit and investment policy. That policy does address the following risks:

1. Custodial Credit Risk – Deposits: In the case of deposits, this is the risk that, in the event of a bank failure, the government's deposits may not be returned to it. State statutes require that all deposits in financial institutions be fully collateralized by U. S. Government Obligations or its agencies and instrumentalities or direct obligations of Texas or its agencies and instrumentalities that have a fair value of not less than the principal amount of deposits. As of September 30, 2012, the City's bank balance was fully collateralized with securities held by independent third party financial institutions.

2. Credit Risk: It is the City's policy to limit investments to investment types with an investment quality rating no lower than AAA (regular funds) and A (reserved funds) or an equivalent rating by at least one nationally recognized rating service or no lower than investment grade by at least one nationally recognized rating service with a weighted average maturity no greater than 360 days for regular fund and 18 months for reserved funds. The City's investment pool was rated AAAm by Standard & Poor's Investors Services.

3. Interest Rate Risk: In accordance with the City's investment policy, the City manages its exposure to declines in fair values by limiting the weighted average maturity of its investment portfolio to 360 days or less for regular funds and 18 months for reserved funds, dependent on market conditions.

4. Concentration of Credit Risk: The government's investment policy states the maximum percentage allowed for each different investment instrument that can be used to make up the portfolio.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Deposits and Investments (Continued)

The City's investments at September 30, 2012, are shown below:

	Fair Value	Rating	Rating Agency	Weighted Average Maturity (Days)
TexStar	$ 8,566,508	AAAm	Standard & Poor's	49
TexPool	506,531	AAAm	Standard & Poor's	41
TexasTERM	410,252	AAAf	Standard & Poor's	39.4
Lonestar	1,001,061	AAA	Standard & Poor's	45
Wellsfargo	86,873,189	AA-	Standard & Poor's	1
FNMA	6,759,942	AA+	Standard & Poor's	985
FHLB	10,004,100	AA+	Standard & Poor's	688
FHLMC	3,004,551	AA+	Standard & Poor's	844
Binghamton NY BOFA	5,013,600	A+	Standard & Poor's	123
Citizens Property Ins Corp FL	5,067,250	A+	Standard & Poor's	243
Nassau County NY BOFA	5,042,290	A+	Standard & Poor's	205
Oyster Bay NY BOFA	7,141,750	A+	Standard & Poor's	312
Freddie Mac	13,013,631	AA+	Standard & Poor's	586
Total Fair Value	$ 152,404,655			
Portfolio Weighted Average Maturity (Days)				192.92

Receivables

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

	General	Other Governmental	Capital Projects	Debt Service	Electric	Water/ Wastewater	Stormwater Drainage	Nonmajor Enterprise	Internal Service	Total
Receivables:										
Taxes	$ 2,708,793	$ -	$ -	$ 547,041	$ -	$ -	$ -	$ -	$ -	$ 3,255,834
Accounts	1,545,617	714,653	15,759	-	6,456,952	3,930,390	359,319	456,367	727	13,479,784
Due from governments	-	1,469,910	-	-	-	-	-	12,142	-	1,482,052
Loans	-	27,827	-	-	-	-	-	-	-	27,827
Gross receivables	4,254,410	2,212,390	15,759	547,041	6,456,952	3,930,390	359,319	468,509	727	18,245,497
Less: allowance for uncollectibles	(42,187)	-	-	(42,395)	(665,683)	(384,329)	(42,695)	(77,414)	-	(1,254,703)
Net total receivables	$ 4,212,223	$ 2,212,390	$ 15,759	$ 504,646	$ 5,791,269	$ 3,546,061	$ 316,624	$ 391,095	$ 727	$ 16,990,794

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

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Receivables (Continued)

	Unavailable	Unearned
Delinquent property taxes receivable (General fund)	$ 593,171	$ -
Activity Center (General fund)	123,935	-
Grant drawdown (General fund)	980,103	-
Delinquent property taxes receivable (Debt service)	488,868	-
Hotel occupancy (Nonmajor governmental)	-	32
Grant drawdowns (Nonmajor governmental)	-	2,899,797
Developer fees (Major enterprise - water and wastewater)	-	560,146
Total Deferred/Unearned Revenue for Governmental Funds	$ 2,186,077	$ 3,459,975

Capital Assets

Capital asset activity for the year ended September 30, 2012, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Government activities:				
Capital assets, not being depreciated:				
Land	$ 7,224,964	$ 171,643	$(109,743)	$ 7,286,864
Construction in progress	86,332,855	8,678,716	(144,182)	94,867,389
Total assets not being depreciated	93,557,819	8,850,359	(253,925)	102,154,253
Capital assets, being depreciated:				
Buildings	36,544,215	-	-	36,544,215
Machinery and equipment	22,255,300	396,734	(633,274)	22,018,760
Improvements other than buildings	49,931,357	165,403	(8,287)	50,088,473
Infrastructure	25,361,436	3,295,000	-	28,656,436
Total capital assets being depreciated	134,092,308	3,857,137	(641,561)	137,307,884
Less accumulated depreciation:				
Buildings	(6,086,093)	(752,842)	-	(6,838,935)
Machinery and equipment	(16,898,138)	(1,285,616)	633,274	(17,550,480)
Improvements other than buildings	(20,414,945)	(3,143,327)	8,287	(23,549,985)
Infrastructure	(8,142,127)	(1,052,967)	-	(9,195,094)
Total accumulated depreciation	(51,541,303)	(6,234,752)	641,561	(57,134,494)
Total capital assets being depreciated, net	82,551,005	(2,377,615)	-	80,173,390
Governmental activities capital assets, net	$ 176,108,824	$ 6,472,744	$(253,925)	$ 182,327,643

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Capital Assets (Continued)

	Beginning Balance	Increases	Decreases	Ending Balance
Business-type activities:				
Capital assets, not being depreciated:				
Land	$ 1,446,029	$ -	$ -	$ 1,446,029
Construction in progress	62,287,907	13,529,562	(3,699,833)	72,117,636
Total assets not being depreciated	63,733,936	13,529,562	(3,699,833)	73,563,665
Capital assets, being depreciated:				
Buildings	6,369,767	-	-	6,369,767
Machinery and equipment	8,418,119	459,449	(191,499)	8,686,069
Improvements other than buildings	165,019,670	3,699,833	(18,186)	168,701,317
Total capital assets being depreciated	179,807,556	4,159,282	(209,685)	183,757,153
Less accumulated depreciation:				
Buildings	(3,297,249)	(120,973)	-	(3,418,222)
Machinery and equipment	(5,680,509)	(483,630)	191,499	(5,972,640)
Improvements other than buildings	(69,574,724)	(8,811,562)	18,186	(78,368,100)
Total accumulated depreciation	(78,552,482)	(9,416,165)	209,685	(87,758,962)
Total capital assets being depreciated, net	101,255,074	(5,256,883)	-	95,998,191
Business-type activities capital assets, net	$ 164,989,010	$ 8,272,679	$(3,699,833)	$ 169,561,856

Depreciation expense was charged to functions/programs of the primary government as follows:

Governmental activities:	
General government	$ 4,496,837
Public safety	1,091,124
Community services	646,791
Total depreciation expense - governmental activities	$ 6,234,752
Business-type activities:	
Electric	$ 660,543
Water and wastewater	7,974,159
Airport	255,089
Stormwater drainage	526,374
Total depreciation expense - business-type activities	$ 9,416,165

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Interfund Receivables, Payables and Transfers

The composition of interfund balances as of September 30, 2012, is as follows:

Due to/from other funds:

Receivable Fund	Payable Fund	Amount
General	Capital projects	$ 28,051
	Nonmajor governmental	532,653
	Internal service	146,918
	Water and wastewater	312,868
	Electric	385,248
	Stormwater drainage	17
	Nonmajor enterprise	60,845
Capital projects	General	1,093,480
	Nonmajor governmental	283,679
	Water and wastewater	33,055
	Stormwater drainage	11,808
Debt service	General	585,471
	Nonmajor governmental	856,457
Nonmajor governmental	General	301,600
	Debt service	119,456
	Capital projects	122,252
	Nonmajor governmental	895
	Electric	901
Electric	General	90,781
	Debt service	9,061
Water and wastewater	General	92,723
	Capital projects	175,766
	Debt service	67,594
	Electric	221
	Stormwater drainage	2,263
Stormwater drainage	General	27,678
	Capital projects	29,903
	Debt service	4,696
Nonmajor enterprise	General	1,798
	Capital projects	50,000
Internal service - insurance	General	156,710

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Interfund Receivables, Payables and Transfers (Continued)

Due to/from other funds (Continued)

Balances resulted from the time lag between the dates that 1) interfund goods and services are provided or reimbursable expenditures occur, 2) transactions are recorded in the accounting system, and 3) payments between funds are made.

Interfund transfers

	Transfers In					
	General	Capital Projects	Debt Service	Nonmajor Governmental	Nonmajor Enterprise	Total
Transfers Out:						
General	$ -	$ 1,263,776	$ 549,031	$ 79,662	$ 120,636	$ 2,013,105
Capital projects	1,100	-	-	-	50,000	51,100
Nonmajor governmental	-	-	1,210,505	-	-	1,210,505
Internal service	146,918	-	-	-	-	146,918
Electric	4,094,426	100,000	-	-	-	4,194,426
Water and wastewater	2,212,316	150,000	-	-	-	2,362,316
Total	$ 6,454,760	$ 1,513,776	$ 1,759,536	$ 79,662	$ 170,636	$ 9,978,370

Transfers are used to 1) move revenues from the fund that statute or budget requires to collect them to the fund that statute or budget requires to expend them, 2) move receipts restricted to debt service from the funds collecting the receipts to the Debt Service Fund as debt service payments become due, and 3) use unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

Capital Lease

The City has one capital lease for caterpillar generators and trailers that they entered into in FY 11 in their water and sewer fund. These leases meet the criteria of a capital lease as defined by Statement of Financial Accounting Standards No. 13, *"Accounting for Leases."*

The following is a schedule of the future minimum lease payments under the capitalized leases together with the present value of the net minimum lease payments at September 30, 2012:

Year Ending September 30, 2013	$ 34,194
Total minimum lease payments	34,194
Less: amount representing interest	426
Present value of minimum lease payments	$ 33,768

(continued)

Long-term Debt

General Obligation Bonds and Combination Tax and Revenue Bonds

The government issues general obligation bonds and combination tax and revenue bonds to provide funds for the acquisition and construction of major capital facilities. These debt issues have been issued for both governmental and business-type activities. These bonds are reported in the proprietary funds if they are expected to be repaid from proprietary fund revenue. The original amount of general obligation and combination tax and revenue bonds issued in prior years was $264,665,000. During the year, the city issued $8,090,000 of Combination Tax and Revenue Certificates of Obligation, Series 2011 with a 2-3% interest rate that mature August 15, 2022 for the Electric fund.

Bond Refunding

On November 15, 2011, the City issued $14,800,000 of General Obligation Refunding Bonds, Series 2011. The net proceeds from the issuance of the bonds were used to purchase U. S. Government Securities and those securities were deposited in an irrevocable trust with an escrow agent to provide future debt service payments. A deposit of $14,772,302 was made to an escrow account to provide the refunding of $9,235,000 of Series 2004A Waterworks and Waste Water System Revenue and Improvement Bonds, and $4,485,000 of Series 2006 Waterworks and Waste Water System Revenue Bonds. As of August 31, 2012, the outstanding balance of these defeased bonds is $9,235,000. The refunded bonds are considered legally defeased and the liability for these bonds has been removed. The reacquisition price exceeded the net carrying amount of the old debt by $1,299,336. The City refunded to reduce its total debt service payments by $957,986 and to obtain an economic gain of $719,095 (present value).

On August 1, the City issued $18,780,000 of General Obligation Refunding Bonds, Series 2012. The net proceeds from the issuance of the bonds were used to purchase U. S. Government Securities and those securities were deposited in an irrevocable trust with an escrow agent to provide future debt service payments. A deposit of $20,486,195 was made to an escrow account to provide the refunding of $3,885,000 of the Series 2004 Combination Tax and Revenue Certificates of Obligations, $4,010,000 of the Series 2005 Combination Tax and Revenue Certificates of Obligations, $4,355,000 of the Series 2004 Waterworks and Waste Water System Revenue Bonds, $2,675,000 of the Series 2005A Waterworks and Waste Water System Revenues Bonds, and $4,370,000 of the Series 2002 Electric Utility System Revenue Refunding Bonds. As of August 31, 2012, the outstanding balance of these defeased bonds is $19,295,000. The reacquisition price exceeded the net carrying amount of the old debt by $1,250,095. The advance refunding was done in order to reduce debt service payments in the short-term. The refunding increased the City's total debt service payments by $1,503,041. The transaction resulted in an economic loss of $1,627,565 (present value).

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt

General Obligation Bonds and Combination Tax and Revenue Bonds (Continued)

General obligation bonds are direct obligations and pledge the full faith and credit of the government. Combination Tax and Revenue bonds constitute direct obligations of the City and are payable from a combination of the levy of ad valorem taxes and a limited pledge of surplus revenues of the City's water and wastewater system. Both bonds generally are issued as 20-year serial bonds with equal amounts of principal maturing each year. Bonds currently outstanding are as follows:

Purpose	Interest Rates	Amount
Governmental activities	3.50 - 4.61%	$ 107,195,000
Governmental activities - refunding	2.00 - 5.375%	22,290,000
Business-type activities	3.50 - 5.00%	85,625,000
Business-type activities- refunding	2.000 - 5.00%	44,125,000
		$ 259,235,000

Annual debt service requirements to maturity for general obligation bonds are as follows:

Year Ending September 30,	Governmental Activities	
	Principal	Interest
2013	$ 6,795,000	$ 5,870,876
2014	7,000,000	5,625,378
2015	6,790,000	5,295,040
2016	7,010,000	5,034,161
2017	7,255,000	4,768,826
2018-2022	36,210,000	19,339,987
2023-2027	35,800,000	10,845,767
2028-2032	22,625,000	2,718,930
Total	$ 129,485,000	$ 59,498,965

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt (Continued)

Revenue Bonds

Annual debt service requirements to maturity for revenue bonds are as follows:

Year Ending September 30,	Business-type Activities Principal	Business-type Activities Interest
2013	$ 7,670,000	$ 5,418,163
2014	7,345,000	5,160,153
2015	7,590,000	4,906,076
2016	7,815,000	4,362,179
2017	8,055,000	4,125,273
2018-2022	40,770,000	15,561,452
2023-2027	36,045,000	8,309,733
2028-2032	11,935,000	1,883,431
2033-2036	2,525,000	335,760
Total	$ 129,750,000	$ 50,062,220

Defeasance of Bonds

In prior years, the City defeased certain bonds by placing the proceeds of refunding bonds in irrevocable trusts to provide for all future debt service payments on the defeased bonds. Accordingly, the trusts' assets and liabilities for the defeased bonds are not included in the City's financial statements. At September 30, 2012, the outstanding balance of the defeased bonds is $52,322,000.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Long-term Debt (Continued)

Changes in Long-term Liabilities

Long-term liability activity for the year ended September 30, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental activities					
General obligation bonds	$ 136,215,000	$ 5,520,000	$(12,250,000)	$ 129,485,000	$ 6,795,000
Discount on bonds	(689,969)	-	136,557	(553,412)	(38,024)
Premium on bonds	1,005,347	605,520	(126,345)	1,484,522	126,345
Deferred amount on refundings	(972,876)	(485,525)	122,351	(1,336,050)	(122,351)
Compensated absences	4,618,358	2,333,023	(1,887,172)	5,064,209	759,631
TMRS Net pension obligation	2,447,927	552,488	-	3,000,415	-
OPEB Net pension obligation	506,008	20,418	-	526,426	-
Governmental activity Long-term liabilities	$ 143,129,795	$ 8,545,924	$(14,004,609)	$ 137,671,110	$ 7,520,601
Business-type activities					
Bonds payable:					
Revenue bonds	$ 128,450,000	$ 36,150,000	$(34,850,000)	$ 129,750,000	$ 7,670,000
Premium on bonds	1,825,864	1,588,850	(466,182)	2,948,532	236,338
Deferred amount on refundings	(1,787,114)	(2,549,431)	618,167	(3,718,378)	(317,105)
Discount on bonds	(282,136)	-	15,907	(266,229)	(15,907)
Capital leases	66,690	-	(32,922)	33,768	33,768
TMRS Net pension obligation	504,689	113,907	-	618,596	-
OPEB Net pension obligation	102,857	4,824	-	107,681	-
Total bonds payable	128,880,850	35,308,150	(34,715,030)	129,473,970	7,607,094
Compensated absences	271,775	410,587	(394,534)	287,828	231,311
Business-type activity Long-term liabilities	$ 129,152,625	$ 35,718,737	$(35,109,564)	$ 129,761,798	$ 7,838,405

For governmental activities, TMRS net pension obligation, OPEB liability, and compensated absences are, and were in prior years, generally liquidated by the General Fund.

Other Information

Benefits Management

The City sponsors an employee benefit plan that provides partially self-insured medical and self-insured dental coverage to employees and voluntary coverage to their participating dependents. The plan is designed to provide a specified level of coverage, with excess insurance coverage provided in both specific and aggregate reinsurance. The City's maximum medical claim exposure for a specific covered person is limited to $100,000 in claims. Each covered person is subject to a maximum lifetime benefit reimbursement of $1,000,000 for medical and a maximum annual benefit on dental of $1,250. Aggregate coverage is purchased for the plan in order to limit the total medical claims exposure.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Other Information (Continued)

Benefits Management (Continued)

The plan includes a pre-existing clause to deter adverse selection into the plan subject to the provisions of the Health Insurance Portability and Accountability Act of 1996. Features of the medical plan include a preferred provider network, specialty networks and a pharmacy benefit which includes a tiered co-pay structure and various techniques to provide incentives to utilize lower cost drugs, over the counter alternatives and to manage utilization based on therapeutic equivalencies. An annual benefit and wellness fair is hosted to increase employee awareness. The City continues to identify and implement features to contain costs and provide a sustainable benefit program. Examples include specialty networks for lab services and specialized provider networks including pharmacy benefits. The plan is funded by contributions from the City and participating employees based on recommendations of maximum plan exposure as calculated by an employee benefits specialty firm. Projected claim costs are based on claims experience, lag studies, industry trends, census and aggregate factors. A liability for claims is established based on estimated incurred but not recorded claims outstanding and anticipated associated insurance and administrative costs. The stop-loss contract establishes the aggregate attachment point based on census and aggregate factors defined in the contract.

A reconciliation of changes in the aggregate liabilities of the prior and current year is presented below:

Year Ended September 30,	Beginning Liability	Current Year Claims and Changes in Estimate	Claim Payments	Ending Liability
2010	$ 842,520	$ 3,741,640	$ 3,590,682	$ 993,478
2011	993,478	3,455,750	3,551,951	897,277
2012	897,277	5,222,174	5,059,501	1,059,950

Risk and Safety Management

The City of San Marcos maintains a risk management program to prevent and mitigate financial loss. Components of the program include the identification of exposure to loss and the selection, implementation and monitoring of risk management techniques. Prevention measures include activities such as training, annual review of assets and exposures, driving and drug testing programs, safety awareness events and the "Safety Coach" Safety Leadership Development Program. Post incident measures designed to mitigate losses include incident investigation and management of all claims through final disposition. A cornerstone of our commitment to managing workers compensation claims is a return to work program. In rating a worker's compensation program, an underwriter begins at 100% which represents an average employer. This is 'modified' based on a specific employer's claims history. During this reporting period the City has achieved a .20% premium modifier. Collectively, risk management programs have resulted in direct savings in excess of a million dollars while improving the health, safety, and well-being of City Employees.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

<u>Other Information</u> (Continued)

Risk and Safety Management (Continued)

The City's Safety Program has been recognized by awards from the Public Risk Management Association (PRIMA) and the National Safety Council (NSC). The City participates in the National Safety Council Annual Awards Program which presents awards for occupational safety and health, safe worker and safe drivers. Eighteen departments were recognized for maintaining a perfect record or a reduction in frequency of lost time injuries.

In October the City held the Annual Benefits and Safety Expo. The event includes over 55 Health and Safety vendors including safety demonstrations. Over 300 employees participate in the Expo.

Contingent Liabilities

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

There are currently several claims and lawsuits pending against the City. It is the opinion of the City Attorney and City Staff that there is no pending litigation against the City that, if decided against the City, would have a material adverse effect upon the operations of the City or that would exceed the contingency amounts set aside for such purpose.

Commitments

The City purchases electric power at wholesale rates from The Lower Colorado River Authority for its own use to resell to customers of its electric distribution system. The initial term of the purchased-power agreement ends in 2016, with successive renewal periods of 10 years.

(continued)

<u>Other Information</u> (Continued)

Estimated costs to complete construction in progress at year-end totals approximately $30,019,333 for governmental capital assets, $20,840,794 for Water and Wastewater, $8,198,836 for Electric, and $8,278,818 for Drainage.

<u>Pension Plans – Primary Government</u>

<u>Defined Benefit Plan – Texas Municipal Retirement System (TMRS)</u>

Plan Description. The City provides pension benefits for all employees working a thousand hours or more annually through a nontraditional, joint contributory, hybrid defined benefit plan in the state-wide Texas Municipal Retirement System (TMRS), an agent multiple-employer public employee retirement system. The plan provisions that have been adopted by the City are within the options available in the governing state statutes of TMRS.

TMRS issues a publicly available comprehensive annual financial report that includes financial statements and required supplementary information (RSI) for TMRS; the report also provides detailed explanations of the contributions, benefits and actuarial methods and assumptions used by the System. This report may be obtained by writing to TMRS, P.O. Box 149153, Austin, TX 78714-9153 or by calling 800-924-8677; in addition, the report is available on TMRS' website at www.TMRS.com.

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

	Plan Year 2010	Plan Year 2011	Plan Year 2012
Deposit rate	7%	7%	7%
Matching ratio (city to employee)	2 to 1	2 to 1	2 to 1
A member is vested after	5 years	5 years	5 years
Service retirement eligibility (expressed as age/years of service)	60/5; 0/20	60/5; 0/20	60/5; 0/20
Updated service credit	100% repeating, transfers	100% repeating, transfers	100% repeating, transfers
Annuity increases (to retirees)	70% of CPI. repeating	70% of CPI. repeating	70% of CPI. repeating

<u>Contributions</u>

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

(continued)

Pension Plans – Primary Government (Continued)

Contributions (Continued)

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

Annual Required Contribution (ARC)	$ 5,380,662
Interest on Net Pension Obligation	221,446
Adjustment to the ARC	(183,552)
Annual Pension Cost	5,418,556
Contributions Made	(4,752,162)
Increase (Decrease) in Net Pension Obligation	666,394
Net Pension Obligation/(Asset), beginning of year	2,952,616
Net Pension Obligation/(Asset), ending of year	$ 3,619,010

Three-Year Trend Information

Accounting Year Ending	Annual Pension Cost (APC)	Actual Contribution Made	Percentage of APC Contributed	Net Pension Obligation
09/30/10	$ 5,277,774	$ 4,130,110	79.00%	$ 1,147,664
09/30/11	5,669,895	4,586,458	80.89%	2,952,616
09/30/12	5,418,556	4,752,162	87.70%	3,619,010

Contributions

The required contribution rates for fiscal year 2012 were determined as part of the December 31, 2009 and 2010 actuarial valuations. Additional information as of the latest actuarial valuation, December 31, 2011, also follows:

Actuarial Valuation Date	12/31/09	12/31/10	12/31/11
Actuarial cost method	Projected Unit Credit	Projected Unit Credit	Projected Unit Credit
Amortization method	Level percent of payroll	Level percent of payroll	Level percent of payroll
GASB 25 equivalent single amortization period	28.2 years; closed period	27.2 years; closed period	27.2 years; closed period
Amortization period for new gains/losses	30 years	30 years	30 years
Asset valuation method	10-year smoothed market	10-year smoothed market	10-year smoothed market
Actuarial Assumptions:			
Investment rate of return*	7.5%	7.0%	7.0%
Projected salary increases*	varies by age and service	varies by age and service	varies by age and service
*Includes Inflation at	3.0%	3.0%	3.0%
Cost-of-living adjustments	2.1%	2.1%	2.1%

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Pension Plans – Primary Government (Continued)

Contributions (Continued)

Funded Status and Funding Progress

The funded status as of December 31, 2011, the most recent actuarial valuation date, is as follows:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability	Percentage Funded	Unfunded Actuarial Accrued Liability	Annual Covered Payroll	Unfunded Actuarial Accrued Liability as a Percentage of Covered Payroll
12/31/2011	$ 97,843,592	$ 131,900,915	74.2%	$ 34,057,323	$ 28,202,003	120.8%

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

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

Other Postemployment Benefits

Post-retirement Health Care Benefits

The City provides certain health care and life insurance benefits through a single employer defined benefit OPEB plan, under City ordinance, for all full time and part-time employees in an eligible class. Retired employees who have satisfied the requirement as defined by the Texas Municipal Retirement System and their dependents who were covered prior to retirement. The requirement as defined by the Texas Municipal Retirement System is any age with 20 years of service or 5 years of service for age 60 and above. Currently, the City has 521 active employees and 38 retirees and beneficiaries eligible to participate in the plan.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

<u>Other Postemployment Benefits</u> (Continued)

Post-retirement Health Care Benefits (Continued)

Retirees pay premiums for coverage in the OPEB programs. The is not a maximum employer paid premium amount (capped benefit). Active employees do not contribute to the retiree health care plan.

Retirees are eligible for medical, dental, prescription and life insurance benefits until death of employee in service. Once death of employee in service, spouse is eligible for dependents through COBRA only.

Retirees are eligible for benefits immediately upon retirement. If retiree opts out of coverage, retiree is not eligible for re-enrollment.

Annual OPEB Cost and Net OPEB Obligation

The City's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The City does not issue separate financial statements for the plan and the City has not established a trust fund to fund the plan. The City's annual OPEB cost for the current year and the related information is listed below:

Annual Required Contribution (ARC)	$ 338,359
Interest on Net Pension Obligation	27,399
Adjustment to the ARC	(25,385)
Annual Pension Cost	340,373
Contributions Made	(315,131)
Increase (Decrease) in Net Pension Obligation	25,242
Net Pension Obligation/(Asset), beginning of year	608,865
Net Pension Obligation/(Asset), ending of year	$ 634,107

Expenses for post-retirement health care benefits are recognized on a pay-as-you-go basis.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Other Postemployment Benefits (Continued)

Annual OPEB Cost and Net OPEB Obligation (Continued)

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the prior three years (4.5% discount rate, and level percent of pay amortization).

Fiscal Year Ended	Annual OPEB Cost	Employer Contribution	Percentage Contributed	Net OPEB Obligation
09/30/10	$ 315,034	$ 137,490	43.7%	$ 436,454
09/30/11	329,540	157,129	47.7%	608,865
09/30/12	340,373	315,131	92.6%	634,107

Funding Status and Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded (AAL) (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
12/31/10	$ -	$ 3,420,429	$ 3,420,429	0%	$ 26,691,575	12.8%

This is the second year of implementation of GASB 45. Accordingly, only one year of funding progress is available. The projection of future payments for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the heath care cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Actuarial Methods and Assumptions

The Projected Unit Credit actuarial cost method is used to calculate the GASB 45 ARC for the City's retiree health care plan. Using the plan benefits, the present health premiums and a set of actuarial assumptions, the anticipated future payments are projected. The projected unit credit method then provides for a systematic recognition of the cost of these anticipated payments. The yearly ARC is computed to cover the cost of benefits being earned by covered members as well as to amortize a portion of the unfunded accrued liability.

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

Other Postemployment Benefits (Continued)

Actuarial Methods and Assumptions (Continued)

Projections of health benefits are based on the plan as understood by the City and include the types of benefits in force at the valuation date and the pattern of sharing benefit costs between the City and the City's employees to that point. Actuarial calculations reflect a long-term perspective and employ methods and assumptions that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets. Significant methods and assumptions were as follows:

Actuarial Methods and Assumptions

Actuarial Valuation Date	12/31/2011
Actuarial Cost Method	Projected Unit Credit
Amortization Method	Level as a percentage of payroll
Remaining Amortization Period	30 years; open
Asset Valuation Method	Market Value
Actuarial Assumptions:	
Investment Rate of Return	4.5%
Payroll Growth Rate	3.0%
General Inflation Rate	3.0%
Health care trend	9% in 2011, declining by 0.5% per year to an ultimate rate of 4.5% in 2020 thereafter

Supplemental Death Benefits Plan (SDBF)

Supplemental Death Benefits Fund

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

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

Contributions

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

(continued)

4. DETAILED NOTES ON ALL FUNDS (Continued)

<u>Supplemental Death Benefits Plan (SDBF)</u> (Continued)

Supplemental Death Benefits Fund (Continued)

<u>Contributions</u> (Continued)

The City's contributions to the TMRS SDBF for the years ended 2012, 2011 and 2010, were $44,833, $54,726, and $49,237, respectively, which equaled the required contributions each year.

Schedule of Contribution Rates
(Retiree-only portion of the rate)

Plan/ Calendar Year	Annual Required Contribution (Rate)	Actual Contribution Made (Rate)	Percentage of ARC Contributed
2008	0.04%	0.04%	100.00%
2009	0.02%	0.02%	100.00%
2010	0.02%	0.02%	100.00%
2011	0.02%	0.02%	100.00%
2012	0.02%	0.02%	100.00%
2013	0.02%	0.02%	100.00%

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APPENDIX C

FORMS OF BOND COUNSEL'S OPINIONS

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[*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*.]

CITY OF SAN MARCOS, TEXAS
GENERAL OBLIGATION REFUNDING BONDS
SERIES 2013
IN THE AGGREGATE PRINCIPAL AMOUNT OF $7,280,000

AS BOND COUNSEL FOR THE CITY OF SAN MARCOS, TEXAS (the "City") in connection with the issuance of the bonds described above (the "Bonds"), we have examined into the legality and validity of the Bonds, which bear interest from the dates specified in the text of the Bonds, until maturity or redemption, at the rates and payable on the dates specified in the text of the Bonds and in the ordinance of the City adopted on April 2, 2013 authorizing the issuance of the Bonds and the Pricing Certificate as defined in, and authorized by, the ordinance (collectively, the "Ordinance").

WE HAVE EXAMINED the applicable and pertinent Constitution and laws of the State of Texas, certified copies of the pertinent proceedings of the City, and other pertinent instruments authorizing and relating to the issuance of said Bonds, including one of the executed Bonds (Bond Number T-1).

BASED ON SAID EXAMINATION, IT IS OUR OPINION that said Bonds have been duly authorized, issued and delivered in accordance with law; and that said Bonds, except as the enforceability thereof may be limited by laws relating to bankruptcy, insolvency, reorganization, moratorium, liquidation and other similar laws now or hereafter enacted related to creditors' rights generally or by general principle of equity which permit the exercise of judicial discretion, the Bonds constitute valid and legally binding obligations of the City, and that ad valorem taxes sufficient to provide for the payment of the interest on and the principal of the Bonds have been levied and pledged for such purpose, within the limit prescribed by law, on taxable property within the City.

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 certain representations, the accuracy of which we have not independently verified, and assume compliance by the City with certain covenants, regarding the use and investment of the proceeds of the Bonds and the use of the property financed and refinanced therewith. In expressing the aforementioned opinions, we have relied on the Verification Report of Grant Thornton, LLP, and assume compliance by the City with certain representations and covenants regarding the use and investment of the proceeds of the Bonds. We call your attention to the fact that if such representations are determined to be inaccurate or upon a failure by the City to comply with such covenants, interest on the Bonds may become includable in gross income retroactively to the date of issuance of the Bonds.

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 result and are not binding on the Internal Revenue Service (the "Service"); rather, such opinions represent our legal judgment based upon our review of existing law and in reliance upon the representations and covenants referenced above that we deem relevant to such opinions. The Service has an ongoing audit program to determine compliance with rules that relate to whether interest on state or local obligations is includable in gross income for federal income tax purposes. No assurance can be given 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 City as the taxpayer. We observe that the City has covenanted not to take any action, or omit to take any action within its control, that if taken or omitted, respectively, may result in the treatment of interest on the Bonds as includable in gross income for federal income tax purposes.

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. In particular, but not by way of limitation, we express no opinion with respect to the federal, state or local tax consequences arising from the enactment of any pending or future legislation.

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 the 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 City, and, in that capacity, we have been engaged by the City 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. 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 City, 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 City as to the current outstanding indebtedness of the City and the assessed valuation of taxable property within the City. Our role in connection with the City's Official Statement prepared for use in connection with the sale of the Bonds has been limited as described therein.

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.

Respectfully,

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[*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*.]

CITY OF SAN MARCOS, TEXAS
GENERAL OBLIGATION REFUNDING BONDS
TAXABLE SERIES 2013
IN THE AGGREGATE PRINCIPAL AMOUNT OF $11,980,000

AS BOND COUNSEL FOR THE CITY OF SAN MARCOS, TEXAS (the "City") in connection with the issuance of the bonds described above (the "Bonds"), we have examined into the legality and validity of the Bonds, which bear interest from the dates specified in the text of the Bonds, until maturity or redemption, at the rates and payable on the dates specified in the text of the Bonds and in the ordinance of the City adopted on April 2, 2013 authorizing the issuance of the Bonds and the Pricing Certificate as defined in, and authorized by, the ordinance (collectively, the "Ordinance").

WE HAVE EXAMINED the applicable and pertinent Constitution and laws of the State of Texas, certified copies of the pertinent proceedings of the City, and other pertinent instruments authorizing and relating to the issuance of said Bonds, including one of the executed Bonds (Bond Number T-1).

BASED ON SAID EXAMINATION, IT IS OUR OPINION that said Bonds have been duly authorized, issued and delivered in accordance with law; and that said Bonds, except as the enforceability thereof may be limited by laws relating to bankruptcy, insolvency, reorganization, moratorium, liquidation and other similar laws now or hereafter enacted related to creditors' rights generally or by general principle of equity which permit the exercise of judicial discretion, the Bonds constitute valid and legally binding obligations of the City, and that ad valorem taxes sufficient to provide for the payment of the interest on and the principal of the Bonds have been levied and pledged for such purpose, within the limit prescribed by law, on taxable property within the City.

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 City, and, in that capacity, we have been engaged by the City 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 for no other reason or purpose. 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 City, 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 City as to the current outstanding indebtedness of the City and the assessed valuation of taxable property within the City. Our role in connection with the City's Official Statement prepared for use in connection with the sale of the Bonds has been limited as described therein.

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.

Respectfully,

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

CITY OF SAN MARCOS, TEXAS
COMBINATION TAX AND REVENUE CERTIFICATES OF OBLIGATION
SERIES 2013
IN THE AGGREGATE PRINCIPAL AMOUNT OF $11,870,000

AS BOND COUNSEL FOR THE CITY OF SAN MARCOS, TEXAS (the "City") in connection with the issuance of the certificates of obligation described above (the "Certificates"), we have examined into the legality and validity of the Certificates, which bear interest from the dates specified in the text of the Certificates, until maturity or redemption, at the rates and payable on the dates specified in the text of the Certificates and in the ordinance of the City adopted on April 2, 2013 authorizing the issuance of the Certificates and the Pricing Certificate as defined in, and authorized by, the ordinance (collectively, the "Ordinance").

WE HAVE EXAMINED the applicable and pertinent Constitution and laws of the State of Texas, certified copies of the pertinent proceedings of the City, and other pertinent instruments authorizing and relating to the issuance of the Certificates, including one of the executed Certificates (Certificate Number T-1).

BASED ON SAID EXAMINATION, IT IS OUR OPINION that said Certificates have been duly authorized, issued and delivered in accordance with law; and that said Certificates, except as the enforceability thereof may be limited by laws relating to bankruptcy, insolvency, reorganization, moratorium, liquidation and other similar laws now or hereafter enacted related to creditors' rights generally or by general principle of equity which permit the exercise of judicial discretion, the Certificates constitute valid and legally binding obligations of the City; and that ad valorem taxes sufficient to provide for the payment of the interest on and the principal of said Certificates have been levied and pledged for such purpose, within the limit prescribed by law, on taxable property within the City and the Certificates are additionally secured by and payable from a limited pledge of surplus revenue of the City's waterworks and sewer system all as provided in the Ordinance.

IT IS FURTHER OUR OPINION, except as discussed below, that the interest on the Certificates 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 Certificates are not "specified private activity bonds" and that, accordingly, interest on the Certificates 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 certain representations, the accuracy of which we have not independently verified, and assume compliance by the City with certain covenants, regarding the use and investment of the proceeds of the Certificates and the use of the property financed therewith. We call your attention to the fact that if such representations are determined to be inaccurate or upon a failure by the City to comply with such covenants, interest on the Certificates may become includable in gross income retroactively to the date of issuance of the Certificates.

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 result and are not binding on the Internal Revenue Service (the "Service"); rather, such opinions represent our legal judgment based upon our review of existing law and in reliance upon the representations and covenants referenced above that we deem relevant to such opinions. The Service has an ongoing audit program to determine compliance with rules that relate to whether interest on state or local obligations is includable in gross income for federal income tax purposes. No assurance can be given whether or not the Service will commence an audit of the Certificates. If an audit is commenced, in accordance with its current published procedures the Service is likely to treat the City as the taxpayer. We observe that the City has covenanted not to take any action, or omit to take any action within its control, that if taken or omitted, respectively, may result in the treatment of interest on the Certificates as includable in gross income for federal income tax purposes.

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 Certificates. In particular, but not by way of limitation, we express no opinion with respect to the federal, state or local tax consequences arising from the enactment of any pending or future legislation.

WE CALL YOUR ATTENTION TO THE FACT that the interest on tax-exempt obligations, such as the Certificates 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 Certificates, nor as to any such insurance policies issued in the future.

OUR SOLE ENGAGEMENT in connection with the issuance of the Certificates is as Bond Counsel for the City, and, in that capacity, we have been engaged by the City for the sole purpose of rendering an opinion with respect to the legality and validity of the Certificates under the Constitution and laws of the State of Texas, and with respect to the exclusion from gross income of the interest on the Certificates for federal income tax purposes, and for no other reason or purpose. 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 City, or the disclosure thereof in connection with the sale of the Certificates, and have not assumed any responsibility with respect thereto. We express no opinion and make no comment with respect to the marketability of the Certificates and have relied solely on certificates executed by officials of the City as to the current outstanding indebtedness of the City and the assessed valuation of taxable property within the City and the sufficiency of the revenues pledged by the City. Our role in connection with the City's Official Statement prepared for use in connection with the sale of the Certificates has been limited as described therein.

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.

Respectfully,

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