

CITY OF KEMAH, TEXAS
GALVESTON COUNTY, TEXAS
ANNUAL FINANCIAL REPORT
SEPTEMBER 30, 2016

McCALL GIBSON SWEDLUND BARTFOOT PLLC
Certified Public Accountants

CITY OF KEMAH, TEXAS

GALVESTON COUNTY, TEXAS

ANNUAL FINANCIAL REPORT

SEPTEMBER 30, 2016

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INDEPENDENT AUDITOR'S REPORT

Honorable Mayor and Members of City Council
City of Kemah, Texas
Galveston County, Texas

We have audited the accompanying financial statements of the governmental activities, the discretely presented component units and each major fund of the City of Kemah, Texas (the "City"), as of and for the year ended September 30, 2016, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the preceding table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

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 discretely presented component units and each major fund of the City as of September 30, 2016, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis, the Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual – General Fund, the Schedule of Changes in Net Pension Liability and Related Ratios, and the Schedule of City Contributions be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of the 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.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The other supplementary information, as listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements and is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. The supplementary information, excluding that portion marked "Unaudited" on which we express no opinion, and has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic 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 basic financial statements as a whole.

McCall Gibson Swedlund Barfoot PLLC
Certified Public Accountants
Houston, Texas

February 1, 2017

CITY OF KEMAH, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2016

Management's discussion and analysis of the City of Kemah, Texas (the "City") financial performance provides an overview of the City's financial activities for the fiscal year ended September 30, 2016.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The basic financial statements include: (1) the government-wide financial statements, (2) the fund financial statements, and (3) the notes to the financial statements. This report also includes required and other supplementary information in addition to the basic financial statements.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide financial statements are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business. The government-wide financial statements are prepared utilizing the economic resources measurement focus and the accrual basis of accounting. The Statement of Net Position presents information on all of the City's assets, liabilities and, if applicable deferred inflows and outflows of resources with the difference reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the City is improving or deteriorating. Other non-financial factors should also be taken into consideration, such as changes in the City's property tax base and the condition of the City's infrastructure (i.e. streets and sidewalks, etc.), to assess the overall health or financial condition of the City.

The Statement of Activities presents information showing how the City's net position changed during the most recent fiscal year. All of the revenues and expenses are taken into account as soon as the underlying event giving rise to the item 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.

In the Statement of Net Position and the Statement of Activities, the City is divided into two kinds of activities:

- * Governmental Activities - Most of the City's basic services are reported here, including police, public works, municipal courts, and general administration. Property taxes, sales taxes, franchise fees, fines and forfeitures finance most of these activities.

CITY OF KEMAH, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2016

GOVERNMENT-WIDE FINANCIAL STATEMENTS (Continued)

- * Component Units – The City includes three separate legal entities in its report – the Kemah Community Development Corporation (“KCDC”), the Kemah Public Facilities Corporation (“KPFC”) and the Kemah Public Facilities Transportation Corporation (“KPFTC”). Although legally separate, these component units are included because the City is financially accountable for them. The KCDC issues separate financial statements which are available from the City.

FUND FINANCIAL STATEMENTS

The combined statements also include fund financial statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District has one governmental fund type. The General Fund accounts for resources not accounted for in another fund, general revenues, operating costs and general expenditures.

Governmental funds are reported in the Governmental Funds Balance Sheet and in the Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balances. The focus in the fund statements provides a distinctive view of the City’s governmental funds. These statements report short-term fiscal accountability focusing on the use of spendable resources and balances of spendable resources available at the end of the year. They are useful in evaluating annual financing requirements of the City and the commitment of spendable resources for the near-term.

Since the government-wide focus includes the long-term view, comparisons between these two perspectives may provide insight into the long-term impact of short-term financing decisions. The Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Position and the Reconciliation of the Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balances to the Statement of Activities explain the differences between the two presentations and assist in understanding the differences between these two perspectives.

NOTES TO THE FINANCIAL STATEMENTS

The accompanying notes to the financial statements provide information essential to a full understanding of the government-wide and fund financial statements.

OTHER INFORMATION

In addition to the financial statements and accompanying notes, this report also presents certain required supplementary information (“RSI”) concerning the City’s progress in funding its obligation to provide pension benefits to its employees and a budgetary comparison schedule.

CITY OF KEMAH, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2016

OTHER INFORMATION (Continued)

The City adopts an annual unappropriated budget for its General Fund. A budgetary comparison schedule is included as RSI for the General Fund.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net position may serve over time as a useful indicator of the City's financial position. In the case of the governmental activities of the City, assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources by \$15,206,977 as of September 30, 2016. As of September 30, 2015, assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources by \$14,377,044.

A portion of the City's net position reflects its net investment in capital assets (buildings, land, streets, sidewalks, and infrastructure less any debt used to acquire those assets that is still outstanding).

The following is a comparative analysis of government-wide changes in net position:

	Summary of Changes in the Statement of Net Position - Governmental Activities		
	2016	2015	Change Positive (Negative)
Current and Other Assets	\$ 5,287,261	\$ 4,724,434	\$ 562,827
Capital Assets (Net of Accumulated Depreciation)	9,972,363	9,732,983	239,380
Total Assets	\$ 15,259,624	\$ 14,457,417	\$ 802,207
Deferred Outflows of Resources	\$ 386,397	\$ 106,742	\$ 279,655
Other Liabilities	\$ 432,153	\$ 152,190	\$ (279,963)
Deferred Inflows of Resources	\$ 6,891	\$ 34,925	\$ 28,034
Net Position:			
Net Investment in Capital Assets	\$ 9,972,363	\$ 9,732,983	\$ 239,380
Restricted	1,430,839	1,020,327	410,512
Unrestricted	3,803,775	3,623,734	180,041
Total Net Position	\$ 15,206,977	\$ 14,377,044	\$ 829,933

CITY OF KEMAH, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2016

GOVERNMENT-WIDE FINANCIAL ANALYSIS (Continued)

The following table provides a summary of the City's operations for the years ended September 30, 2016, and September 30, 2015. The City increased its net position by \$829,933, accounting for a 5.8% increase in net position. This compares with a decrease in net position of \$181,799 in the prior year.

	Summary of Changes in the Statement of Activities - Governmental Activities		
	2016	2015	Change Positive (Negative)
Revenues:			
Program Revenues -			
Charges for Services	\$ 617,588	\$ 666,331	\$ (48,743)
Capital Grants and Contributions	49,609	725,532	(675,923)
General Revenues -			
Property Taxes	678,468	655,430	23,038
Sales Taxes	2,776,848	2,730,411	46,437
Investment Revenues	1,705	1,158	547
Other Revenues	1,918,558	1,417,551	501,007
Total Revenues	\$ 6,042,776	\$ 6,196,413	\$ (153,637)
Expenses:			
General Government	\$ 1,400,420	\$ 1,175,976	\$ (224,444)
Public Works	1,183,352	1,135,715	(47,637)
Police Department	2,149,428	2,031,901	(117,527)
Municipal Courts	287,818	262,128	(25,690)
Advertising and Tourism	191,825	272,492	80,667
Intergovernmental Expense	1,500,000	1,500,000	1,500,000
Total Expenses	\$ 5,212,843	\$ 6,378,212	\$ 1,165,369
Change in Net Position	\$ 829,933	\$ (181,799)	\$ 1,011,732
Net Position, Beginning of Year	14,377,044	14,558,843	(181,799)
Net Position, End of Year	\$ 15,206,977	\$ 14,377,044	\$ 829,933

**CITY OF KEMAH, TEXAS
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2016**

FINANCIAL ANALYSIS OF THE CITY'S GOVERNMENTAL FUNDS

The City's fund balance as of the fiscal year ended September 30, 2016, was \$5,078,442, an increase of \$649,991 from the prior year.

The General Fund fund balance increased by \$649,991, primarily due to operating revenues exceeding service operations.

GENERAL FUND BUDGETARY HIGHLIGHTS

The City amended the budget during the current fiscal year to increase projected revenues and expenditures by \$401,000 and \$395,475, respectively. Actual revenue was \$91,404 more than budgeted revenue. Actual expenditures were \$550,062 less than budgeted expenditures.

CAPITAL ASSETS

Capital assets as of September 30, 2016, total \$9,972,363 (net of accumulated depreciation) and include buildings, furniture, fixtures, equipment, and vehicles as well as the streets and culverts within the City.

<u>Capital Assets At Year-End Net of Accumulated Depreciation</u>	
Capital Assets Not Subject to Depreciation:	
Land and Land Improvements	\$ 898,968
Construction in Progress	312,504
Capital Assets Subject to Depreciation:	
Buildings and Improvements	1,146,037
Park Improvements	259,448
Vehicles and Equipment	403,074
Furniture, Software and Office Equipment	139,344
Storm Water Pump Station	956,917
Streets and Culverts	<u>5,856,071</u>
Total Net Capital Assets	<u>\$ 9,972,363</u>

CONTACTING THE CITY'S MANAGEMENT

This financial report is designed to provide a general overview of the City. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the City of Kemah, 1401 State Highway 146, Kemah, Texas 77565.

CITY OF KEMAH, TEXAS
STATEMENT OF NET POSITION
SEPTEMBER 30, 2016

	Primary Government	Discretely Presented Component Units
	Governmental Activities	
ASSETS		
Cash and Cash Equivalents	\$ 4,697,015	\$ 2,375,250
Investments	506,464	974,068
Receivables:		
Property Taxes	31,791	
Other	3,333	
Due from Component Unit	14,895	
Inventory	33,763	
Land	898,968	1,403,725
Construction in Progress	312,504	
Capital Assets (Net of Accumulated Depreciation)	8,760,891	2,326
TOTAL ASSETS	\$ 15,259,624	\$ 4,755,369
DEFERRED OUTFLOWS OF RESOURCES		
Deferred Outflows - Pension	\$ 386,397	\$ -0-
LIABILITIES		
Accounts Payable	\$ 177,028	\$
Net Pension Liability	255,125	
Due to Primary Government		14,895
TOTAL LIABILITIES	\$ 432,153	\$ 14,895
DEFERRED INFLOWS OF RESOURCES		
Deferred Inflows - Pension	\$ 6,891	\$ -0-
NET POSITION		
Net Investment in Capital Assets	\$ 9,972,363	\$ 1,406,051
Restricted for:		
Police Programs	12,615	
Court Security	47,824	
Court Technology	55,117	
Tourism	1,315,283	
Unrestricted	3,803,775	3,334,423
TOTAL NET POSITION	\$ 15,206,977	\$ 4,740,474

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

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**CITY OF KEMAH, TEXAS
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2016**

	Expenses	Program Revenues	
		Charges for Services	Capital Grants and Contributions
GOVERNMENTAL ACTIVITIES			
General Government	\$ 1,400,420	\$ 151,595	\$ -
Public Works	1,183,352		49,609
Police Department	2,149,428	427,199	
Municipal Court	287,818	38,794	
Advertising and Tourism	191,825		
TOTAL GOVERNMENTAL ACTIVITIES	\$ 5,212,843	\$ 617,588	\$ 49,609
COMPONENT UNITS	\$ 833,463	\$ - 0 -	\$ - 0 -

GENERAL REVENUES

- Property Taxes
- Sales Taxes
- Franchise Fees
- Hotel Taxes
- Mixed Beverage Taxes
- Parking Revenues
- Investment Revenues
- Intergovernmental Revenues
- Other

TOTAL GENERAL REVENUES

CHANGE IN NET POSITION

NET POSITION - OCTOBER 1, 2015

NET POSITION - SEPTEMBER 30, 2016

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

Net (Expense) Revenue and Changes in Net Position

<u>Primary Government</u>	
<u>Governmental</u>	<u>Component Units</u>
<u>Activities</u>	
\$ (1,248,825)	\$
(1,133,743)	
(1,722,229)	
(249,024)	
<u>(191,825)</u>	<u></u>
\$ (4,545,646)	\$ - 0 -
\$ - 0 -	\$ (833,463)
\$ 678,468	\$
2,776,848	925,617
251,195	
585,203	
192,900	
57,733	
1,705	2,220
719,240	
<u>112,287</u>	<u>566</u>
\$ 5,375,579	\$ 928,403
\$ 829,933	\$ 94,940
<u>14,377,044</u>	<u>4,645,534</u>
\$ 15,206,977	\$ 4,740,474

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

CITY OF KEMAH, TEXAS
GOVERNMENTAL FUNDS BALANCE SHEET
SEPTEMBER 30, 2016

	<u>General Fund</u>
ASSETS	
Cash and Cash Equivalents	\$ 4,697,015
Investments	506,464
Receivables:	
Property Taxes	31,791
Other	3,333
Due from Component Units	14,895
Inventory	33,763
TOTAL ASSETS	\$ 5,287,261
LIABILITIES	
Accounts Payable	\$ 177,028
DEFERRED INFLOWS OF RESOURCES	
Property Taxes	\$ 31,791
FUND BALANCE	
Nonspendable for Inventory	\$ 33,763
Restricted:	
For Police	12,615
For Court Security	47,824
For Court Technology	55,117
For Tourism	1,315,283
Assigned for Emergencies	506,464
Unassigned	3,107,376
TOTAL FUND BALANCE	\$ 5,078,442
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCE	\$ 5,287,261

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

CITY OF KEMAH, TEXAS
RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET POSITION
SEPTEMBER 30, 2016

Total Fund Balance - Governmental Fund	\$ 5,078,442
Amounts reported for governmental activities in the Statement of Net Position are different because:	
The net pension liability is not a current financial resource and, therefore, is not reported as a liability in the governmental funds.	(255,125)
Capital assets used in governmental activities are not current financial resources and, therefore, are not reported as assets in the governmental funds.	9,972,363
Portions of the change in net pension asset that are not immediately recognized as pension expense are recorded as deferred outflows and inflows of resources.	379,506
Deferred tax revenues for the 2015 and prior tax levies became part of recognized revenue in the governmental activities of the District.	<u>31,791</u>
Total Net Position - Governmental Activities	<u><u>\$ 15,206,977</u></u>

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

CITY OF KEMAH, TEXAS
GOVERNMENTAL FUNDS STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCE
FOR THE YEAR ENDED SEPTEMBER 30, 2016

	<u>General Fund</u>
REVENUES	
Property Taxes and Penalties	\$ 672,964
Sales Taxes	2,776,848
Franchise Fees	251,195
Hotel Taxes	585,203
Mixed Beverage Taxes	192,900
Permits and Licenses	151,595
Fines and Forfeitures	465,993
Parking Revenues	57,733
Investment Revenues	1,705
Grant Revenues	49,609
Intergovernmental Revenues	200,000
Other	112,287
TOTAL REVENUES	\$ 5,518,032
EXPENDITURES	
General Government	\$ 1,376,694
Public Works	875,334
Police Department	2,136,370
Municipal Court	287,818
Advertising and Tourism	191,825
TOTAL EXPENDITURES	\$ 4,868,041
NET CHANGE IN FUND BALANCE	\$ 649,991
FUND BALANCE - OCTOBER 1, 2015	4,428,451
FUND BALANCE - SEPTEMBER 30, 2016	\$ 5,078,442

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

CITY OF KEMAH, TEXAS
RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF
REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2016

Net Change in Fund Balance - Governmental Fund	\$	649,991
<p>Amounts reported for governmental activities in the Statement of Activities are different because:</p>		
<p>Governmental funds report tax revenues when collected. However, in the Statement of Activities, revenue is recorded in the accounting period for which the taxes are levied.</p>		5,504
<p>Governmental funds do not account for depreciation. However, in the Statement of Net Position, capital assets are depreciated and depreciation expense is recorded in the Statement of Activities.</p>		(680,425)
<p>The changes in the net pension asset as well as deferred outflows and inflow of resources are recorded as pension expense in the government-wide financial statements.</p>		(64,942)
<p>Governmental funds report capital expenditures as expenditures in the period purchased. However, in the Statement of Net Position, capital assets are increased by new purchases and the Statement of Activities is not affected.</p>		400,565
<p>Capital assets related to park and street improvements were funded by a component unit and transferred to the City to maintain.</p>		519,240
Change in Net Position - Governmental Activities	\$	829,933

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

**CITY OF KEMAH, TEXAS
 COMPONENT UNITS BALANCE SHEET
 SEPTEMBER 30, 2016**

	KCDC	KPFTC	Total
ASSETS			
Cash and Cash Equivalents	\$ 875,250	\$ 1,500,000	\$ 2,375,250
Investments	974,068		974,068
TOTAL ASSETS	\$ 1,849,318	\$ 1,500,000	\$ 3,349,318
LIABILITIES			
Due to Primary Government	\$ 14,895	\$ - 0 -	\$ 14,895
FUND BALANCES			
Unassigned	\$ 1,834,423	\$ 1,500,000	\$ 3,334,423
TOTAL LIABILITIES AND FUND BALANCES	\$ 1,849,318	\$ 1,500,000	\$ 3,349,318

* The KPFC has a zero fund balance at year-end.

Reconciliation to the Government-wide Statement of Net Position

Fund Balance	\$ 3,334,423
Adjustment for land	1,403,725
Adjustment for capital assets	2,326
Net Position for Discretely Presented Component Units	\$ 4,740,474

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

CITY OF KEMAH, TEXAS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - COMPONENT UNITS
FOR THE YEAR ENDED SEPTEMBER 30, 2016

	<u>KCDC</u>	<u>KPFTC</u>	<u>Total</u>
REVENUES			
City Sales Taxes	\$ 925,617	\$	\$ 925,617
Investment Revenues	2,220		2,220
Other	566		566
TOTAL REVENUES	<u>\$ 928,403</u>	<u>\$ - 0 -</u>	<u>\$ 928,403</u>
EXPENDITURES			
Service Operations:			
Administrative	\$ 211,038	\$	\$ 211,038
Operations	25,000		25,000
Advertising/Promotions	64,613		64,613
City Improvements	530,456		530,456
TOTAL EXPENDITURES	<u>\$ 831,107</u>	<u>\$ - 0 -</u>	<u>\$ 831,107</u>
NET CHANGE IN FUND BALANCES	97,296		97,296
FUND BALANCES - OCTOBER 1, 2015	<u>1,737,127</u>	<u>1,500,000</u>	<u>3,237,127</u>
FUND BALANCES - SEPTEMBER 30, 2016	<u>\$ 1,834,423</u>	<u>\$ 1,500,000</u>	<u>\$ 3,334,423</u>

* The KPFC has a zero fund balance at year-end.

Reconciliation to the Government-wide Statement of Activities

Net Change in Fund Balance	\$ 97,296
Adjustment for depreciation	<u>(2,356)</u>
Change in Net Position	<u>\$ 94,940</u>

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

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CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 1. CREATION OF CITY

The City of Kemah, Texas (the “City”) was incorporated on March 22, 1965, under the provisions of the State of Texas. The City operates under a Council-Mayor form of government and provides the following services as authorized by general law; public safety, maintenance and improvements to highways and streets, public improvements, and general administrative services.

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES

The City is a political subdivision of the State of Texas governed by an elected board. The Governmental Accounting Standards Board (“GASB”) has established the criteria for determining whether or not an entity is a primary government or a component unit of a primary government. The primary criteria are that it has a separately elected governing body, it is legally separate, and it is fiscally independent of other state and local governments. Under these criteria, the City is considered a primary government and is not a component unit of any other government. Additionally, the KCDC, KPFC and KPFTC meet the criteria for inclusion in the City’s financial statement as component units.

The accompanying basic financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as promulgated by the GASB. Based on these considerations, the City’s basic financial statements include the Kemah Community Development Corporation (KCDC), as a component unit of the City. The KCDC was incorporated on October 9, 1998, as a not-for-profit corporation for the specific public purpose of the promotion and development of commercial, industrial and manufacturing enterprises to promote and encourage employment and the public welfare. The KCDC may issue bonds on behalf of the City for the Corporation’s public purpose. The KCDC is managed by a Board of Directors consisting of seven members who serve two year terms. The City Council has sole authority to appoint the Directors of KCDC. The assets are managed by the Board of Directors. The financial records are maintained by City. Copies of the financial statements for KCDC may be obtained from the City Secretary’s office.

The Kemah Public Facilities Corporation (KPFC) also meets the above criteria and is a component unit of the City. The KPFC was incorporated on October 5, 2001, as a non-profit corporation. The KPFC was created under the Texas Public Facility Act to finance, refinance or otherwise provide the costs of public facilities in the City. The KPFC is managed by a Board of Directors made up of the Mayor and Council Members of the City of Kemah. Separate financial statements are not issued on the KPFC. This fund has a zero fund balance at year-end.

The Kemah Public Facility Transportation Corporation (KPFTC) also meets the above criteria and is a component unit of the City. The KPFTC was incorporated in 2014, as a non-profit corporation.

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial Statement Presentation

These financial statements have been prepared in accordance with GASB Codification of Governmental Accounting and Financial Reporting Standards Part II, Financial Reporting.

The GASB Codification sets forth standards for external financial reporting for all state and local government entities, which include a requirement for a Statement of Net Position and a Statement of Activities. It requires the classification of net position into three components: Net Investment in Capital Assets; Restricted; and Unrestricted. These classifications are defined as follows:

- Net Investment in Capital Assets – This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvements of those assets.
- Restricted Net Position – This component of net position consists of external constraints placed on the use of net position imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulation of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- Unrestricted Net Position – This component of net position consists of net position that do not meet the definition of Restricted or Net Investment in Capital Assets.

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

Government-Wide Financial Statements

The Statement of Net Position and the Statement of Activities display information about the City as a whole. The Statement of Net Position is reported by adjusting the governmental fund types to report on the full accrual basis, economic resource basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations. Any amounts recorded due to and due from other funds are eliminated in the Statement of Net Position.

The Statement of Activities is reported by adjusting the governmental fund types to report only items related to current year revenues and expenditures. Items such as capital outlay are

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Government-Wide Financial Statements (Continued)

allocated over their estimated useful lives as depreciation expense. Internal activities between governmental funds, if any, are eliminated by adjustment to obtain total revenue and expense of the government-wide Statement of Activities.

Fund Financial Statements

The City's fund financial statements include a Balance Sheet and a Statement of Revenues, Expenditures and Changes in Fund Balances.

Governmental Funds

The City has one major governmental fund.

General Fund - To account for resources not required to be accounted for in another fund, general revenues, costs and general expenditures.

Basis of Accounting

The City uses the modified accrual basis of accounting for governmental fund types. The modified accrual basis of accounting recognizes revenues when both "measurable and available." Measurable means the amount can be determined. Available means collectable within the current period or soon enough thereafter to pay current liabilities. The City considers revenue reported in governmental funds to be available if they are collectable within 60 days after year end. Also, under the modified accrual basis of accounting, expenditures are recorded when the related fund liability is incurred, except for principal and interest on long-term debt, which are recognized as expenditures when payment is due.

In the government-wide Statement of Net Position and Statement of Activities, the governmental activities are presented using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used. Revenues, expenses, gains, losses, assets, and liabilities resulting from exchange and exchange-like transactions are recognized when the exchange takes place.

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets, are reported in the government-wide Statement of Net Position. All capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Donated assets are valued at their fair market value on the date donated. Repairs and maintenance are recorded as expenditures in the governmental fund incurred and as an expense in the government-wide Statement of Activities. Capital asset additions, improvements and preservation costs that extend the life of an asset are capitalized and depreciated over the estimated useful life of the asset. Interest costs, including developer interest, engineering fees and certain other costs are capitalized as part of the asset.

All City infrastructure assets with a useful life of at least two years and a total cost of \$5,000; infrastructure assets with a useful life of at least two years and a total cost of \$10,000 such as roads and sidewalks and other capital assets with a total cost of \$10,000 or more (including installation costs, if any, and associated professional fees) shall be capitalized and depreciated using no salvage value and the straight line method of depreciation. Estimated useful lives are as follows:

	Years
Buildings	40
Furniture and Fixtures	3-20
Machinery and Equipment	5-20
Vehicles	5
Roads and Sidewalks	10
Streets and Culverts	30
Infrastructure	10-45
Other Assets	10

Program Revenues

In the Statement of Activities, program revenues include fines and forfeitures, licenses and permits, and grant proceeds.

Compensated Absences

Full-time, permanent employees are granted vacation benefits in varying amounts to specified maximums depending on tenure with the City. Sick leave accrues to full-time, permanent employees to specified maximums. Generally, such leave may be accumulated to the following year; however, at no time may unused sick leave be paid in monetary compensation either during employment or upon termination. Vacation pay accrues and becomes payable after one year of

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Compensated Absences (Continued)

employment. Unused vacation pay can be carried over, but only up to 240 hours. Upon termination, any unused vacation time is paid.

Budgeting

In compliance with governmental accounting principles, the City Council annually adopts an unappropriated budget for the General Fund. The budget was amended during the current fiscal year.

Pensions

For employees of the City, a pension plan has been established (see Note 8).

Inventory

Inventory is recorded at the replacement cost basis. Replacement cost is based upon the current cost to replace the individual item (See Note 5).

Measurement Focus

Measurement focus is a term used to describe which transactions are recognized within the various financial statements. In the government-wide Statement of Net Position and Statement of Activities, the governmental activities are presented using the economic resources measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net position, financial position, and cash flows. All assets and liabilities associated with the activities are reported. Fund equity is classified as net position.

Governmental fund types are accounted for on a spending or financial flow measurement focus. Accordingly, only current assets and current liabilities are included on the Balance Sheet, and the reported fund balances provide an indication of available spendable or appropriable resources. Operating statements of governmental fund types report increases and decreases in available spendable resources. Fund balances in governmental funds are classified using the following hierarchy:

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Measurement Focus (Continued)

Nonspendable: amounts that cannot be spent either because they are in nonspendable form or because they are legally or contractually required to be maintained intact.

Restricted: amounts that can be spent only for specific purposes because of constitutional provisions, or enabling legislation, or because of constraints that are imposed externally.

Committed: amounts that can be spent only for purposes determined by a formal action of the Board of Directors. The Board is the highest level of decision-making authority for the City. This action must be made no later than the end of the fiscal year. Commitments may be established, modified, or rescinded only through ordinances or resolutions approved by the Board. The City does not have any committed fund balances.

Assigned: amounts that do not meet the criteria to be classified as restricted or committed, but that are intended to be used for specific purposes. The City has not adopted a formal policy regarding the assignment of fund balances. The City has assigned \$506,464 for emergencies. See Note 7 for more detail.

Unassigned: all other spendable amounts in the General Fund.

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

Revenue Recognition - Property Taxes

Property taxes considered available by the City and included in revenue included taxes collected during the year and taxes collected after year end which were considered available to defray the expenditures of the current year. Deferred tax revenues are those taxes which the City does not reasonably expect to be collected soon enough in the subsequent period to finance current expenditures.

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition - Property Taxes (Continued)

The City's tax calendar is as follows:

- Levy Date - October 1, as soon thereafter as practicable.
- Lien Date - January 1.
- Due Date - Upon receipt, but not later than January 31.
- Delinquent Date - February 1, at which time the taxpayer is liable for penalty and interest.

Accounting Estimates

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

NOTE 3. MAINTENANCE TAX

During the year ended September 30, 2016, the City levied an ad valorem maintenance tax rate of \$0.254011 per \$100 of assessed valuation, which resulted in a tax levy of \$679,764 on the adjusted assessed property valuation of approximately \$267,187,944. At the balance sheet date, the City recorded taxes receivable of \$31,791 in the General Fund.

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 4. DEPOSITS AND INVESTMENTS

Deposits

Custodial credit risk is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The City's deposit policy for custodial credit risk requires compliance with the provisions of Texas statutes.

Texas statutes require that any cash balance in any fund shall, to the extent not insured by the Federal Deposit Insurance Corporation or its successor, be continuously secured by a valid pledge to the City of securities eligible under the laws of Texas to secure the funds of the City, having an aggregate market value, including accrued interest, at all times equal to the uninsured cash balance in the fund to which such securities are pledged. At fiscal year end, the carrying amount of the City's, KCDC's and KPFTC's deposits was \$8,552,797 and the bank balance was \$8,589,451. Of the bank balance, \$1,500,000 was covered by federal depository insurance and the remainder was collateralized with securities held in a third party depository in the City's, KCDC's and KPFTC's names.

The carrying values of the deposits are included in the Governmental Funds Balance Sheet and the Statement of Net Position at September 30, 2016, as listed below:

	<u>Cash</u>	<u>Certificates of Deposit</u>	<u>Total</u>
GENERAL FUND	\$ 4,697,015	\$ 506,464	\$ 5,203,479
COMPONENT UNITS	<u>2,375,250</u>	<u>974,068</u>	<u>3,349,318</u>
TOTAL DEPOSITS	<u>\$ 7,072,265</u>	<u>\$ 1,480,532</u>	<u>\$ 8,552,797</u>

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 4. DEPOSITS AND INVESTMENTS (Continued)

Investments

Under Texas law, the City is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity and that address investment diversification, yield, maturity, and the quality and capability of investment management, and all City funds must be invested in accordance with the following investment objectives: understanding the suitability of the investment to the City's financial requirements, first; preservation and safety of principal, second; liquidity, third; marketability of the investments if the need arises to liquidate the investment before maturity, fourth; diversification of the investment portfolio, fifth; and yield, sixth. 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." No person may invest City funds without express written authority from the City Council.

Texas statutes include specifications for and limitations applicable to the City and its authority to purchase investments as defined in the Public Funds Investment Act. Authorized investments are summarized as follows: (1) obligations of the United States or its agencies and instrumentalities, (2) direct obligations of the State of Texas or its agencies and instrumentalities, (3) certain collateralized mortgage obligations, (4) other obligations, the principal of and interest on which are unconditionally guaranteed or insured by the State of Texas or the United States or its 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) certain A rated or higher obligations of states, agencies, counties, cities, and other political subdivisions of any state, (6) bonds issued, assumed or guaranteed by the State of Israel, (7) insured or collateralized certificates of deposit, (8) certain fully collateralized repurchase agreements secured by delivery, (9) certain bankers' acceptances with limitations, (10) commercial paper rated A-1 or P-1 or higher and a maturity of 270 days or less, (11) no-load money market mutual funds and no-load mutual funds with limitations, (12) certain guaranteed investment contracts, (13) certain qualified governmental investment pools and (14) a qualified securities lending program.

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 4. DEPOSITS AND INVESTMENTS (Continued)

Investments (Continued)

As of September 30, 2016, the City had the following investments and maturities:

<u>Fund and Investment Type</u>	<u>Fair Value</u>	<u>Maturities Less Than 1 Year</u>	<u>Thereafter</u>
<u>GENERAL FUND</u>			
Certificate of Deposit	\$ 506,464	\$ 506,464	\$
<u>COMPONENT UNITS</u>			
Certificates of Deposit	<u>974,068</u>	<u>974,068</u>	<u> </u>
TOTAL INVESTMENTS	<u>\$ 1,480,532</u>	<u>\$ 1,480,532</u>	<u>\$ - 0 -</u>

Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. The City manages credit risk by typically investing in certificates of deposit with balances below FDIC coverage.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The City manages interest rate risk by investing in certificates of deposit with maturities of less than one year.

Restrictions

All cash and investments of the Component Units are restricted for activities of each specific component unit.

NOTE 5. INVENTORY

Inventory consists of materials and supplies on hand at September 30, 2016, stated at replacement cost. Inventory in the amount of \$33,763 has been recorded as of September 30, 2016.

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 6. CAPITAL ASSETS AND DEPRECIATION

The following is a summary of changes in capital assets for the year ended September 30, 2016.

	October 1, 2015	Increases	Decreases	September 30, 2016
Capital Assets Not Being Depreciated				
Land and Land Improvements	\$ 760,783	\$ 138,185	\$	\$ 898,968
Construction in Progress	<u>108,464</u>	<u>781,620</u>	<u>577,580</u>	<u>312,504</u>
Total Capital Assets Not Being Depreciated	<u>\$ 869,247</u>	<u>\$ 919,805</u>	<u>\$ 577,580</u>	<u>\$ 1,211,472</u>
Capital Assets Subject to Depreciation				
Buildings and Improvements	\$ 2,050,490	\$	\$	\$ 2,050,490
Park Improvements	690,712			690,712
Vehicles and Equipment	1,458,195	211,439	67,261	1,602,373
Furniture, Software and Office Equipment	748,265	26,205		774,470
Storm Water Pump Station	1,229,410			1,229,410
Street and Culverts	<u>9,253,967</u>	<u>339,936</u>		<u>9,593,903</u>
Total Capital Assets Subject to Depreciation	<u>\$ 15,431,039</u>	<u>\$ 577,580</u>	<u>\$ 67,261</u>	<u>\$ 15,941,358</u>
Less Accumulated Depreciation				
Buildings and Improvements	\$ 835,297	\$ 69,156	\$	\$ 904,453
Park Improvements	341,854	89,410		431,264
Vehicles and Equipment	1,113,949	152,611	67,261	1,199,299
Furniture, Software and Office Equipment	588,108	47,018		635,126
Storm Water Pump Station	210,854	61,639		272,493
Street and Culverts	<u>3,477,241</u>	<u>260,591</u>		<u>3,737,832</u>
Total Accumulated Depreciation	<u>\$ 6,567,303</u>	<u>\$ 680,425</u>	<u>\$ 67,261</u>	<u>\$ 7,180,467</u>
Total Depreciable Capital Assets, Net of Accumulated Depreciation	<u>\$ 8,863,736</u>	<u>\$ (102,845)</u>	<u>\$ - 0 -</u>	<u>\$ 8,760,891</u>
Total Capital Assets, Net of Accumulated Depreciation	<u>\$ 9,732,983</u>	<u>\$ 816,960</u>	<u>\$ 577,580</u>	<u>\$ 9,972,363</u>

Depreciation categorized by department at September 30, 2016, is as follows:

General Government	\$ 95,715
Police Department	123,293
Public Works	<u>461,417</u>
Total	<u>\$ 680,425</u>

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 6. CAPITAL ASSETS AND DEPRECIATION (Continued)

The following is a summary of changes in the capital assets of the KCDC for the year ended September 30, 2016.

	October 1, 2015	Increases	Decreases	September 30, 2016
Capital Assets Not Being Depreciated				
Land and Land Improvements	\$ 95,725	\$ - 0 -	\$ - 0 -	\$ 95,725

The following is a summary of changes in the capital assets of the KPFC for the year ended September 30, 2016.

	October 1, 2015	Increases	Decreases	September 30, 2016
Capital Assets Not Being Depreciated				
Land and Land Improvements	\$ 1,308,000	\$ - 0 -	\$ - 0 -	\$ 1,308,000
Capital Assets Subject to Depreciation				
Parking Lot	\$ 35,249	\$ - 0 -	\$ - 0 -	\$ 35,249
Less Accumulated Depreciation				
Parking Lot	\$ 30,567	\$ 2,356	\$ - 0 -	\$ 32,923
Total Depreciable Capital Assets, Net of Accumulated Depreciation	\$ 4,682	\$ (2,356)	\$ - 0 -	\$ 2,326
Total Capital Assets, Net of Accumulated Depreciation	\$ 1,312,682	\$ (2,356)	\$ - 0 -	\$ 1,310,326

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 7. FUND BALANCES - GENERAL FUND

As of October 1, 2009, the City assigned \$500,671, plus interest earnings to be used solely for emergencies that may arise in the future. Interest earned to date by the City is \$5,793. Therefore, as of September 30, 2016, the amount of the fund balance assigned for emergencies is \$506,464.

During the current fiscal year, the City collected \$585,203 in hotel occupancy taxes. These funds can only be used to directly enhance and promote tourism and the convention and hotel industry. The City expended \$191,825 in such endeavors and earned \$963 in interest on these funds. At September 30, 2016, \$1,315,283 remains restricted for tourism expenditures.

The City collects fees restricted for improving court security and court technology on certain fines in the municipal court. At year end, \$47,824 was restricted for court security and \$55,117 was restricted for court technology.

The City also occasionally receives contra-band collections from the state for seizures made in the City. These funds must be spent on items that assist the police departments' narcotics division. At year end, \$12,615 of contra-band collections was restricted for the police department.

NOTE 8. PENSION PLAN

Plan Description

The City participates as one of 866 plans in the nontraditional, joint contributory, hybrid defined benefit plan administered by the Texas Municipal Retirement System ("TMRS"). TMRS is an agency created by the State of Texas and administered in accordance with the TMRS Act, Subtitle G, Title 8, Texas Government Code (the TMRS Act) as an agent multiple-employer retirement system for municipal employees in the State of Texas. The TMRS Act places the general administration and management of the system with a six-member Board of Trustees. Although the Governor, with the advice and consent of the Senate, appoints the Board, TMRS is not fiscally dependent on the State of Texas. TMRS's defined benefit pension plan is a tax-qualified plan under Section 401(a) of the Internal Revenue Code. TMRS issues a publicly available comprehensive annual financial report (CAFR) that can be obtained from TMRS' website at www.TMRS.com.

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

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 8. PENSION PLAN (Continued)

Benefits Provided

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

At retirement, the benefit is calculated as if the sum of the employee's contributions, with interest, and the city-financed monetary credits with interest were used to purchase an annuity. Members may choose to receive their retirement benefit in one of seven payment options. Members may also choose to receive a portion of their benefit as a Partial Lump Sum Distribution in an amount equal to 12, 24, or 36 monthly payments, which cannot exceed 75% of the member's deposits and interest. A member city may elect to increase the annuities of its retirees, either annually or on an annually repeating basis, effective January 1 of a calendar year.

The plan provisions are adopted by the governing body of each city, within the options available in the state statutes governing TMRS. The City has elected that members can retire at age 60 and above with 5 or more years of service or with 20 years of service regardless of age. Members may work for more than one TMRS city during their career. If a member is vested in one TMRS city, he or she is immediately vested upon employment with another TMRS city. Similarly, once a member has met the eligibility requirements for retirement in a TMRS city, he or she is eligible in other TMRS cities as well.

At December 31, 2015 valuation and measurement date, the following employees were covered by the benefit terms:

Inactive employees or beneficiaries currently receiving benefits	8
Inactive employees entitled to but not yet receiving benefits	34
Active employees	34
Total	76

Contributions

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

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 8. PENSION PLAN (Continued)

Contributions (Continued)

Employees for the City were required to contribute 7% of their annual gross earnings during the current fiscal year. The contribution rates for the City were 5.28% and 5.23% in calendar years 2015 and 2016. The City's contributions to TMRS for the year ended September 30, 2016, were \$107,717 and were equal to the required contributions.

Actuarial Assumptions

The total pension liability in the December 31, 2015 actuarial valuation was determined using the following actuarial assumption:

Actuarial valuation date	12/31/15
Actuarial cost method	Entry Age Normal
Amortization method	Level percentage of payroll, closed
Remaining Amortization period	28 years
Asset Valuation Method	10-year smoothed market; 15% soft corridor
Actuarial Assumptions:	
Investment return	6.75%
Projected salary increases	3.5% to 10.5% including inflation
Inflation	2.5%
Cost-of-living adjustments	0.00%

These actuarial assumptions were developed primarily from the actuarial investigation of the experience of TMRS over the four year period from December 31, 2010 to December 31, 2014. They were adopted in 2015 and first used in the December 31, 2015 actuarial valuation. The post-retirement mortality assumption for healthy annuitants and Annuity Purchase Rate (APRs) are based on the Mortality Experience Investigation Study covering 2009 through 2011 and dated December 31, 2013. In conjunction with these changes first used in the December 31, 2013 valuation, the System adopted the Entry Age Normal actuarial cost method and a one-time change to the amortization policy. These assumptions apply to both the Pension Trust and the Supplemental Death Benefits Fund as applicable.

The Total Pension Liability in the December 31, 2015, actuarial valuation was determined using the following actuarial assumptions: inflation 2.5% per year, overall payroll growth 2.3% per year and investment rate of return 6.75%, net of pension plan investment expense, including inflation. Salary increases were based on a service-related table. Mortality rates for active members, retirees, and beneficiaries were based on the gender-distinct RP2000 Combined Healthy Mortality Table, with male rates multiplied by 109% and female rates multiplied by

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 8. PENSION PLAN (Continued)

Actuarial Assumptions (Continued)

103%. The rates are projected on a fully generational basis by scale BB to account for future mortality improvements. For disabled annuitants, the gender-distinct RP2000 Disabled Retiree Mortality Table is used, with slight adjustments.

The long-term expected rate of return on pension plan investments is 6.75%. The pension plan's policy in regard to the allocation of invested assets is established and may be amended by the TMRS Board of Trustees. TMRS has chosen to adopt a rebalancing policy that is governed by allocation ranges rather than time periods. The ranges specified in the table below, are a function of the volatility of each asset class and the proportion of the total funds allocated to the asset class.

Asset Class	Minimum %	Target %	Maximum %
U.S. Equities	12.5%	17.5%	22.5%
International Equities	12.5%	17.5%	22.5%
Core Fixed Income	5.0%	10.0%	15.0%
Non-Core Fixed Income	15.0%	20.0%	25.0%
Real Estate	5.0%	10.0%	15.0%
Real Return	5.0%	10.0%	15.0%
Absolute Return	5.0%	10.0%	15.0%
Private Equity	0.0%	5.0%	10.0%
Cash Equivalents	0.0%	0.0%	10.0%

The goal of the rebalancing policy is to ensure that the integrity of the strategic target allocation is preserved through a disciplined process that allows investment staff the flexibility to rebalance the portfolio within TMRS approved ranges, to adjust for market movements and consider current market conditions, or valuations, in portfolio allocations.

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

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 8. PENSION PLAN (Continued)

Changes in Net Pension Liability/(Asset) for the measurement year ended December 31, 2015, are as follows:

	Increase (Decrease)		
	Total Pension Liability (a)	Fiduciary Net Position (b)	Net Position Liability/(Asset) (a)-(b)
Balances of December 31, 2014	\$ 3,558,960	\$ 3,676,466	\$ (117,506)
Changes for the year:			
Service cost	230,065		230,065
Interest on total pension liability	253,802		253,802
Difference between expected and actual experience	(8,654)		(8,654)
Benefit Payments, including refunds of employee contributions	(96,491)	(96,491)	
Changes in Assumptions	131,805		131,805
Administrative expenses		(3,304)	3,304
Employer Contributions		99,882	(99,882)
Employee Contributions		132,547	(132,547)
Net Investment Income		5,425	(5,425)
Other		(163)	163
Balances of December 31, 2015	<u>\$ 4,069,487</u>	<u>\$ 3,814,362</u>	<u>\$ 255,125</u>

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

	1% Decrease	Current Discount Rate	1% Increase
	5.75%	6.75%	7.75%
Net pension liability/(asset)	<u>\$ 880,583</u>	<u>\$ 255,125</u>	<u>\$ (258,694)</u>

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 8. PENSION PLAN (Continued)

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

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended September 30, 2016, the City recognized pension expense of \$107,717.

At September 30, 2016, the City reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	\$	\$ 6,891
Changes in actuarial assumptions	104,961	-0-
Difference between projected and actual earnings	201,542	-0-
Contributions subsequent to the measurement date	79,894	-0-
Total	386,397	6,891

\$79,894 reported as deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending September 30, 2017. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:	
2016	\$ 76,517
2017	76,517
2018	76,517
2019	68,673
2020	-0-
Thereafter	-0-
Total	298,224

NOTE 9. SUPPLEMENTAL DEATH BENEFITS PLAN

The City also participates in the cost-sharing multiple-employer defined benefit group term life insurance plan operated by the 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

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 9. SUPPLEMENTAL DEATH BENEFITS PLAN (Continued)

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.

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 the employee's entire careers.

The City's contribution for the retirees to the TMRS SBDF for the years ended 2016, 2015 and 2014 were \$2,618, \$2,292, and \$2,150, respectively, which equaled the required contributions each year.

NOTE 10. RISK ASSESSMENT

The City is exposed to various risks of loss related to torts, theft of, damage to and destruction of assets, errors and omissions and natural disasters. The City participates in the Texas Municipal League Intergovernmental Risk Pool (TML) to provide property, general liability, automobile, boiler and machinery, mobile equipment, law enforcement, crime coverage, errors and omissions and workers compensation coverage. The City, along with other participating entities, contributes annual amounts determined by TML's management. As claims arise, they are submitted and paid by TML. There have been no significant reductions in coverage from the prior year and settlements have not exceeded coverage in the past three years.

NOTE 11. GRANT PROGRAM

On December 14, 2015, the City was awarded a grant under Title 1 of the Housing and Community Development Act of 1974 from the Texas Department of Agriculture (the "Department") in the amount of \$350,000. The award will be used to fund the construction and engineering of water line improvements on Kipp Avenue, from Bel Road to 10th Street.

CITY OF KEMAH, TEXAS
NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2016

NOTE 12. AGREEMENT FOR DEVELOPMENT AND OPERATION OF PUBLIC PARK

On December 7, 2009, the City entered into the Agreement with the County of Galveston for development and operation of a public park located in the M. Muldoon League. The City agrees to build and construct public park recreational amenities and landscaping (Improvements) as conceptualized in that one certain Master Plan dated May 11, 2007. The Improvements will also be constructed within time parameters agreed to by both parties and in accordance with mutually agreed upon plans and specifications. The Improvements constructed by City shall belong to and remain the property of City during the full term of this Agreement. The term of this agreement is 30 years as of the commencement date.

CITY OF KEMAH, TEXAS
REQUIRED SUPPLEMENTARY INFORMATION
SEPTEMBER 30, 2016

CITY OF KEMAH, TEXAS
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCE - BUDGET AND ACTUAL - GENERAL FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2016

	Original Budget	Final Amended Budget	Actual	Variance Positive (Negative)
REVENUES				
Property Taxes and Penalties	\$ 655,779	\$ 673,379	\$ 672,964	\$ (415)
Sales Taxes	2,550,000	2,776,000	2,776,848	848
Franchise Fees	220,299	220,299	251,195	30,896
Hotel Taxes	525,500	525,500	585,203	59,703
Mixed Beverage Taxes	180,000	192,000	192,900	900
Permits and Licenses	92,900	167,900	151,595	(16,305)
Fines and Forfeitures	432,600	436,700	465,993	29,293
Investment Revenues	150	150	1,705	1,555
Parking Revenues	24,400	50,400	57,733	7,333
Grant Revenues			49,609	49,609
Intergovernmental Revenues	250,000	250,000	200,000	(50,000)
Other	94,000	134,300	112,287	(22,013)
TOTAL REVENUES	<u>\$ 5,025,628</u>	<u>\$ 5,426,628</u>	<u>\$ 5,518,032</u>	<u>\$ 91,404</u>
EXPENDITURES				
General Government	\$ 1,178,391	\$ 1,393,391	\$ 1,376,694	\$ 16,697
Public Works	843,387	942,427	875,334	67,093
Police Department	2,226,003	2,296,438	2,136,370	160,068
Municipal Court	252,347	252,347	287,818	(35,471)
Advertising and Tourism	522,500	533,500	191,825	341,675
TOTAL EXPENDITURES	<u>\$ 5,022,628</u>	<u>\$ 5,418,103</u>	<u>\$ 4,868,041</u>	<u>\$ 550,062</u>
NET CHANGE IN FUND BALANCE	\$ 3,000	\$ 8,525	\$ 649,991	\$ 641,466
FUND BALANCE - OCTOBER 1, 2015	<u>4,428,451</u>	<u>4,428,451</u>	<u>4,428,451</u>	
FUND BALANCE - SEPTEMBER 30, 2016	<u>\$ 4,431,451</u>	<u>\$ 4,436,976</u>	<u>\$ 5,078,442</u>	<u>\$ 641,466</u>

See accompanying independent auditor's report.

CITY OF KEMAH, TEXAS
SCHEDULE OF CHANGES IN NET PENSION LIABILITY AND RELATED RATIOS
TEXAS MUNICIPAL RETIREMENT SYSTEM
FOR THE YEAR ENDED SEPTEMBER 30, 2016

	Measurement Date December 31, 2015	Measurement Date December 31, 2014
Total Pension Liability		
Service cost	\$ 230,065	\$ 220,535
Interest on total pension liability	253,802	231,348
Difference between expected and actual experience	(8,654)	(42,521)
Changes of assumptions	131,805	(42,521)
Benefit payments/refunds of contributions	(96,491)	(90,225)
Net change in total pension liability	\$ 510,527	\$ 319,137
Total pension liability, beginning	3,558,960	3,239,823
Total pension liability, ending (a)	\$ 4,069,487	\$ 3,558,960
Plan Fiduciary Net Position		
Employer contributions	\$ 99,882	\$ 66,906
Employee contributions	132,547	129,450
Investment income net of investment expenses	5,425	193,311
Benefit payments/refund of contributions	(96,491)	(90,225)
Administrative expenses	(3,304)	(2,018)
Other	(163)	(166)
Net change in plan fiduciary net position	\$ 137,896	\$ 297,258
Plan Fiduciary net position, beginning	3,676,466	3,379,208
Plan Fiduciary net position, ending (b)	\$ 3,814,362	\$ 3,676,466
Net pension liability/(asset), ending = (a) – (b)	\$ 255,125	\$ (117,506)
Plan Fiduciary net position as a percentage of total pension liability	93.73%	103.30%
Covered – employee payroll	\$ 1,893,535	\$ 1,843,935
Net pension liability/(asset) as a percentage of covered payroll	13.47%	(6.37)%

A full 10-year schedule will be displayed as it becomes available.

See accompanying independent auditor's report.

CITY OF KEMAH, TEXAS
SCHEDULE OF CITY CONTRIBUTIONS
TEXAS MUNICIPAL RETIREMENT SYSTEM
SEPTEMBER 30, 2016

Fiscal Year Ending September 30	Actuarially Determined Contribution	Actual Employer Contribution	Contribution Deficiency (Excess)	Pensionable Covered Payroll	Actual Contribution as a % of Covered Payroll
2016	\$ 107,717	\$ 107,717	\$ -0-	\$2,054,563	5.3%
2015	\$ 91,881	\$ 91,881	\$ -0-	\$1,909,971	4.8%

A full 10-year schedule will be displayed as it becomes available.

See accompanying independent auditor's report.

CITY OF KEMAH, TEXAS
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED SEPTEMBER 30, 2016

NOTE 1. NET PENSION LIABILITY - TEXAS MUNICIPAL RETIREMENT SYSTEM

Assumptions

The following methods and assumptions were used to determine contribution rates:

Valuation Date	Actuarially determined contribution rates are calculated as of December 31, and become effective in January, 13 months later.
Actuarial Cost Method	Entry Age Normal
Amortization method	Level percentage of payroll, closed
Remaining amortization period	28 years
Asset Valuation Method	10-year, smoothed market; 15% soft corridor
Inflation	2.5%
Salary Increases	3.50% to 10.50%, including inflation
Investment Rate of Return	6.75%
Retirement Age	Experience-based table of rate that are specific to the City's plan of benefits. Last updated for the 2015 calculation pursuant to an experience study of the period 2010 – 2014.
Mortality	RP-2000 Combined Mortality Table with Blue Collar Adjustment with male rates multiplied by 109% and female rates multiplied by 103% and projected on a fully generational basis with scale BB.
Other Information:	There were no benefit changes during the year.

See accompanying independent auditor's report.

CITY OF KEMAH, TEXAS

OTHER SUPPLEMENTARY INFORMATION

SEPTEMBER 30, 2016

CITY OF KEMAH, TEXAS
SCHEDULE OF EXPENDITURES BY DEPARTMENT
- BUDGET AND ACTUAL – GENERAL FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2016

	Administration			Variance Positive (Negative)
	Original Budget	Final Amended Budget	Actual	
ADMINISTRATION				
Personnel	\$ 614,522	\$ 614,522	\$ 610,867	\$ 3,655
Professional Fees:				
Legal	100,000	100,000	86,104	13,896
Delinquent Tax Attorney			2,196	(2,196)
Audit	25,000	25,000	27,900	(2,900)
Community Center	45,000	52,000	53,410	(1,410)
Dues and Subscriptions	6,000	6,000	5,428	572
Insurance	30,000	30,000	21,395	8,605
Maintenance and Repairs	22,000	35,000	36,927	(1,927)
Supplies and Materials	33,000	31,500	36,915	(5,415)
Training	15,000	16,500	22,301	(5,801)
Utilities	33,000	33,000	43,349	(10,349)
Other Operations Costs	254,869	254,869	292,971	(38,102)
Capital Outlay		195,000	136,931	58,069
TOTAL ADMINISTRATION	<u>\$ 1,178,391</u>	<u>\$ 1,393,391</u>	<u>\$ 1,376,694</u>	<u>\$ 16,697</u>

	Public Works Department			Variance Positive (Negative)
	Original Budget	Final Amended Budget	Actual	
PUBLIC WORKS				
Personnel	\$ 394,729	\$ 394,729	\$ 378,802	\$ 15,927
Insurance	25,000	25,000	9,785	15,215
Supplies	34,000	34,000	13,217	20,783
Solid Waste Disposal	101,000	101,000	103,928	(2,928)
Storm Water Management	10,000	40,000	39,048	952
Utilities	80,000	80,000	92,744	(12,744)
Other Operations Costs	158,300	158,300	84,411	73,889
Capital Outlay	40,358	109,398	153,399	(44,001)
TOTAL PUBLIC WORKS	<u>\$ 843,387</u>	<u>\$ 942,427</u>	<u>\$ 875,334</u>	<u>\$ 67,093</u>

See accompanying independent auditor's report.

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CITY OF KEMAH, TEXAS
SCHEDULE OF EXPENDITURES – BY DEPARTMENT
- BUDGET AND ACTUAL – GENERAL FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2016

	Police Department			Variance Positive (Negative)
	Original Budget	Final Amended Budget	Actual	
POLICE DEPARTMENT				
Personnel	\$ 1,886,526	\$ 1,886,526	\$ 1,760,484	\$ 126,042
Equipment	20,700	20,700	14,577	6,123
Insurance	30,000	30,000	45,452	(15,452)
Maintenance	18,000	18,000	11,466	6,534
Utilities	5,200	5,200	4,291	909
Supplies	70,650	70,650	47,849	22,801
Training	15,000	15,000	16,835	(1,835)
Other Operations Costs	143,950	143,950	125,181	18,769
Capital Outlay	35,977	106,412	110,235	(3,823)
TOTAL POLICE DEPARTMENT	<u>\$ 2,226,003</u>	<u>\$ 2,296,438</u>	<u>\$ 2,136,370</u>	<u>\$ 160,068</u>

	Municipal Court			Variance Positive (Negative)
	Original Budget	Final Amended Budget	Actual	
MUNICIPAL COURT				
Personnel	\$ 171,497	\$ 171,497	\$ 145,077	\$ 26,420
Professional Fees:				
Legal	28,000	28,000	25,725	2,275
Delinquent Collection Fees	100	100	44,653	(44,553)
Dues and Subscriptions	550	550	390	160
Supplies	4,700	4,700	1,846	2,854
Technology Costs	8,000	8,000	4,486	3,514
Training	4,500	4,500	889	3,611
Other Operations Costs	35,000	35,000	64,752	(29,752)
TOTAL MUNICIPAL COURT	<u>\$ 252,347</u>	<u>\$ 252,347</u>	<u>\$ 287,818</u>	<u>\$ (35,471)</u>

See accompanying independent auditor's report.

