

CHEROKEE COUNTY, TEXAS

ANNUAL FINANCIAL STATEMENTS

SEPTEMBER 30, 2013

CHEROKEE COUNTY, TEXAS
ANNUAL FINANCIAL STATEMENTS
FOR THE YEAR ENDED SEPTEMBER 30, 2013

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ANNUAL FINANCIAL STATEMENTS
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INTRODUCTORY SECTION

CHEROKEE COUNTY, TEXAS

SEPTEMBER 30, 2013

COUNTY JUDGE

Chris Davis

COUNTY COMMISSIONERS

Kelly Traylor

Steven Norton

Katherine Pinotti

Byron Underwood

COUNTY AUDITOR

L. H. Crockett

FINANCIAL SECTION



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

INDEPENDENT AUDITORS' REPORT

To the Honorable County Judge
and County Commissioners
Cherokee County, Texas

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Cherokee County, Texas, as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise the County's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' 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 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, 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, each major fund, and the aggregate remaining fund information of Cherokee County, Texas, as of September 30, 2013, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison information, and the schedules of funding progress 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.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Cherokee County, Texas' basic financial statements. The combining nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining nonmajor fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information 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 combining nonmajor fund financial statements are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 17, 2014, on our consideration of Cherokee County, Texas' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Cherokee County, Texas' internal control over financial reporting and compliance.

Pavullo, Brown & Hill, LLP

Waco, Texas
June 17, 2014

**MANAGEMENT'S
DISCUSSION AND ANALYSIS**

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of Cherokee County, Texas (the "County"), we offer readers of the County's financial statements this narrative overview and analysis of the financial activities of Cherokee County, Texas, for the fiscal year ended September 30, 2013. This analysis should be read in conjunction with the financial statements and related footnotes.

FINANCIAL HIGHLIGHTS

- The assets of Cherokee County exceeded its liabilities at the close of the most recent fiscal year by \$17,999,715 (net position). Of this amount, \$5,684,521 (unrestricted net position) may be used to meet the County's ongoing obligations to citizens and creditors.
- The County's total net position (government-wide) decreased by \$370,159.
- As of the close of the current fiscal year, the County's governmental funds reported combined ending fund balances of \$6,550,762, an increase of \$573,050 in comparison with the prior year. Approximately 72% of this total amount, \$4,726,271, is *available for spending* at the County's discretion (unassigned and assigned fund balance).
- At the end of the current fiscal year, unassigned fund balance for the General Fund was \$3,025,049 or 27% of the total General Fund expenditures.
- The County's long-term liabilities (government-wide) decreased by \$20,309 (1%) during the current fiscal year.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to Cherokee County's basic financial statements. The County's basic financial statements consist of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. The report also contains 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 Cherokee County's finances in a manner similar to a private-sector business.

The Statement of Net Position presents information on all of the County's assets and liabilities. Over time, increases and decreases in net position may serve as a useful indicator of whether the financial position of Cherokee County is improving or deteriorating.

The Statement of Activities presents information showing how the County's net position changed during the fiscal year. All changes in net position 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 unused vacation leave).

In the Statement of Net Position and the Statement of Activities, the County operates the following type of activities:

Governmental Activities – Most of the County's basic services are reported here such as general government, public safety, judicial, community services, and transportation. These activities are principally supported by taxes and intergovernmental revenues.

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. Cherokee County, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of Cherokee County can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

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 government-wide financial statements, governmental fund financial statements focus on how cash resources flow into and out of those funds and balances remaining at year-end that are available for spending. These funds are reported using an accounting method called *modified accrual* accounting, that requires the recognition of revenue when earned, only so long as the funds are collected within the period or soon enough afterwards to be used to pay liabilities of the current period.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the County's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

Cherokee County adopts an annual budget for its General and Special Revenue Funds. A budgetary comparison statement has been provided for the General Fund and major Special Revenue Funds to demonstrate compliance with this budget.

Fiduciary Funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are *not* reflected in the government-wide financial statements because the resources of those funds are *not* available to support the County's own programs.

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.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. In the case of Cherokee County, assets exceeded liabilities by \$17,999,715 as of September 30, 2013.

The largest portion of the County's net position reflects its investment of capital assets. The County uses these capital assets to provide services to citizens; consequently, these assets are *not* available for future spending. Although the County's investment in 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.

CHEROKEE COUNTY NET POSITION

	Governmental Activities	
	2013	2012
Current and other assets	\$ 9,822,198	\$ 9,120,769
Capital assets	10,649,743	11,692,225
Total assets	<u>20,471,941</u>	<u>20,812,994</u>
Long-term liabilities	772,610	792,919
Other liabilities	1,699,616	1,650,201
Total liabilities	<u>2,472,226</u>	<u>2,443,120</u>
Net position:		
Net investment in capital assets	10,484,612	11,444,763
Restricted	1,830,582	2,242,531
Unrestricted	<u>5,684,521</u>	<u>4,682,580</u>
Total net position	<u>\$ 17,999,715</u>	<u>\$ 18,369,874</u>

Governmental Activities. Governmental activities decreased Cherokee County's net position by \$370,159. A key element of this decrease in net position was a \$1,547,773 or 8% increase in fiscal year 2013 expenses as compared to fiscal year 2012 expenses. The largest increase in expenses, \$1,140,924, was in the Infrastructure and Environmental Services function.

CHEROKEE COUNTY CHANGES IN NET POSITION

	Governmental Activities	
	2013	2012
REVENUES		
Program revenues:		
Fees, fines, and charges for services	\$ 3,578,702	\$ 3,448,160
Operating grants and contributions	1,892,436	1,539,624
Capital grants and contributions	-	305,399
General revenues:		
Property taxes	12,641,691	12,230,500
Sales and other taxes	1,851,230	1,616,992
Gain on sale of capital assets	8,191	261,602
Investment income	25,000	29,859
Miscellaneous	13,848	110,174
Total revenues	20,011,098	19,542,310
EXPENSES		
General government	4,493,170	4,195,303
Justice system	3,149,639	3,138,571
Public safety	3,121,000	3,153,070
Corrections and rehabilitation	2,159,420	2,132,975
Health and human services	1,433,883	1,301,227
Community and economic development	228,951	233,894
Infrastructure and environmental	5,788,665	4,647,741
Interest and fiscal charges	6,529	30,703
Total expenses	20,381,257	18,833,484
DECREASE IN NET POSITION	(370,159)	708,826
NET POSITION, BEGINNING	18,369,874	17,661,048
NET POSITION, ENDING	\$ 17,999,715	\$ 18,369,874

FINANCIAL ANALYSIS OF THE COUNTY'S FUNDS

As noted earlier, Cherokee County uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds. The focus of Cherokee County's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing Cherokee County'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 the County completed the year, its governmental funds, as presented in the balance sheet in this report, reported a *combined* fund balance of \$6,550,762 which is an increase of \$573,050 from last year's total of \$5,977,712.

The General Fund is the chief operating fund of the County. At the end of the current fiscal year, unassigned fund balance of the General Fund was \$3,025,049. 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 and total fund balance both represent 27% of the total General Fund expenditures.

GENERAL FUND BUDGETARY HIGHLIGHTS

Total actual revenues, as classified in the budget, exceeded final budgeted amounts by \$467,186. A review of actual expenditures compared to the appropriations in the final budget yields no significant overspending. Total actual expenditures were \$823,087 less than final budgeted appropriations.

CAPITAL ASSETS

Cherokee County's investment in capital assets for its governmental activities as of September 30, 2013, amounts to \$10,649,743 (net of accumulated depreciation), a decrease of \$1,042,482 from the prior year. This investment in capital assets includes land, buildings, vehicles, furniture and equipment.

CHEROKEE COUNTY CAPITAL ASSETS

	Capital Assets	
	2013	2012
Land	\$ 544,383	\$ 544,383
Buildings	12,423,357	12,423,357
Infrastructure	111,448,764	111,448,764
Improvements	2,627,726	2,627,726
Machinery and other equipment	9,667,932	9,433,512
Less: accumulated depreciation	(126,062,419)	(124,785,517)
Total capital assets, net of accumulated depreciation	\$ <u>10,649,743</u>	\$ <u>11,692,225</u>

Additional information regarding the County's capital assets can be found in the notes to financial statements.

LONG-TERM DEBT

At September 30, 2013, the County had outstanding notes payable of \$165,131 which were issued in a prior year to acquire road and bridge equipment and which are secured by that equipment. Principal payments of \$82,331 were made on notes payable in the current year, and interest expense on notes payable for the year was \$6,529. Additional information on the County's long-term debt can be found in the notes to the financial statements.

CHEROKEE COUNTY'S OUTSTANDING DEBT

	<u>2013</u>	<u>2012</u>
Notes payable	165,131	247,462
Compensated absences	255,064	223,921
Other post employment benefits	<u>352,415</u>	<u>321,536</u>
Total outstanding debt	<u>\$ 772,610</u>	<u>\$ 792,919</u>

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

- The tax rate for the fiscal year ended September 30, 2014, saw no increase from the prior year, and remained at .5900 per \$100 valuation.
- Continued increases in the property values in Cherokee County are expected to provide an additional \$170,000 of property tax revenue as compared to the fiscal year ended September 30, 2013.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of Cherokee County's finances for all those with an interest in the County's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Cherokee County Auditor, 502 N. Main Street, Rusk, Texas 75785.

**BASIC
FINANCIAL STATEMENTS**

CHEROKEE COUNTY, TEXAS

STATEMENT OF NET POSITION

SEPTEMBER 30, 2013

	<u>Primary Government</u> <u>Governmental</u> <u>Activities</u>
ASSETS	
Cash and cash equivalents	\$ 901,865
Investments	6,691,180
Receivables, net of allowance	2,008,527
Due from other governments	220,626
Capital assets, net:	
Land	544,383
Buildings and improvements	12,423,357
Infrastructure	111,448,764
Improvements other than buildings	2,627,726
Equipment	9,667,932
Less: accumulated depreciation	(126,062,419)
Total capital assets	<u>10,649,743</u>
 Total assets	 <u>20,471,941</u>
LIABILITIES	
Accounts payable	621,866
Accrued liabilities	8,791
Due to others	962,687
Unearned revenue	106,272
Noncurrent liabilities:	
Due within one year	327,239
Due in more than one year	445,371
Total liabilities	<u>2,472,226</u>
NET POSITION	
Net investment in capital assets	10,484,612
Restricted	1,830,582
Unrestricted	<u>5,684,521</u>
 Total net position	 <u>\$ 17,999,715</u>

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

CHEROKEE COUNTY, TEXAS

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2013**

Functions/Programs	Expenses for Services	Program Revenues		Net (Expense) Revenue and Change in Primary Government Net Position
		Fees, Fines and Charges for Services	Operating Grants and Contributions	Governmental Activities
Primary government				
Governmental activities:				
General government	\$ 4,493,170	\$ 1,256,488	\$ 12,863	\$(3,223,819)
Justice system	3,149,639	983,789	913,582	(1,252,268)
Public safety	3,121,000	153,196	207,198	(2,760,606)
Corrections and rehabilitation	2,159,420	137,433	7,487	(2,014,500)
Health and human services	1,433,883	195,582	623,223	(615,078)
Community and economic development	228,951	3,147	-	(225,804)
Infrastructure and environmental services	5,788,665	849,067	128,083	(4,811,515)
Interest and fiscal charges	6,529	-	-	(6,529)
Total governmental activities	<u>20,381,257</u>	<u>3,578,702</u>	<u>1,892,436</u>	<u>(14,910,119)</u>
Total primary government	<u>\$ 20,381,257</u>	<u>\$ 3,578,702</u>	<u>\$ 1,892,436</u>	<u>(14,910,119)</u>
General revenues				
Taxes:				
				8,977,341
				3,664,350
				1,830,758
				20,472
				8,191
				25,000
				13,848
				<u>14,539,960</u>
				(370,159)
				<u>18,369,874</u>
				<u>\$ 17,999,715</u>

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

CHEROKEE COUNTY, TEXAS

BALANCE SHEET

GOVERNMENTAL FUNDS

SEPTEMBER 30, 2013

	General	Road and Bridge	Other Governmental Funds	Total Governmental Funds
ASSETS				
Cash and cash equivalents	\$ 25,266	\$ 171,755	\$ 704,844	\$ 901,865
Investments	3,055,254	2,793,460	842,466	6,691,180
Receivables (net of allowance for uncollectibles)				
Taxes	1,326,468	389,794	22,600	1,738,862
Accounts	269,665	-	-	269,665
Due from other governments	87,828	-	132,798	220,626
 Total assets	 \$ 4,764,481	 \$ 3,355,009	 \$ 1,702,708	 \$ 9,822,198
 LIABILITIES AND FUND BALANCES				
Liabilities:				
Accounts payable	\$ 306,453	\$ 269,065	\$ 46,348	\$ 621,866
Accrued liabilities	8,791	-	-	8,791
Due to others	122,526	830,000	10,161	962,687
Deferred revenues	1,301,662	350,034	26,396	1,678,092
Total liabilities	1,739,432	1,449,099	82,905	3,271,436
 Fund balances:				
Restricted for:				
General government	-	-	416,998	416,998
Justice system	-	-	495,059	495,059
Public safety	-	-	58,789	58,789
Corrections and rehabilitation	-	-	27,445	27,445
Infrastructure and environmental services	-	772,189	-	772,189
Debt service	-	-	54,011	54,011
Assigned for:				
Health and human services	-	-	230,737	230,737
Infrastructure and environmental services	-	1,133,721	81,252	1,214,973
Capital projects	-	-	261,503	261,503
Unassigned	3,025,049	-	(5,991)	3,019,058
Total fund balances	3,025,049	1,905,910	1,619,803	6,550,762
 Total liabilities and fund balance	 \$ 4,764,481	 \$ 3,355,009	 \$ 1,702,708	 \$ 9,822,198

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

CHEROKEE COUNTY, TEXAS

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

SEPTEMBER 30, 2013

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

Total fund balance - governmental funds	\$ 6,550,762
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.	10,649,743
Some of the County's assets are not available to pay for current period expenditures and, therefore, are deferred as unavailable revenue in the funds.	1,571,820
The net other post employment benefits obligation reported in the governmental activities does not require the use of current financial resources and, therefore, is not reported in the governmental funds.	(352,415)
Long-term liabilities, including notes payable and compensated absences, are not due and payable in the current year and, therefore, are not reported in the governmental funds.	(420,195)
Net position of governmental activities	\$ <u>17,999,715</u>

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

CHEROKEE COUNTY, TEXAS
STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2013

	General	Road and Bridge	Other Governmental Funds	Total Governmental Funds
REVENUES				
Taxes:				
Property	\$ 8,930,190	\$ 3,640,774	\$ -	\$ 12,570,964
Sales	1,830,758	-	-	1,830,758
Mixed beverage	20,472	-	-	20,472
Fees of office	1,012,069	846,941	921,651	2,780,661
Intergovernmental	253,855	116,977	1,498,293	1,869,125
Fines and forfeitures	737,143	-	66,973	804,116
Interest	14,912	8,222	1,866	25,000
Miscellaneous	17,172	5,626	49	22,847
Total revenues	12,816,571	4,618,540	2,488,832	19,923,943
EXPENDITURES				
Current:				
General government	3,713,365	464,041	193,478	4,370,884
Justice system	2,247,046	-	896,943	3,143,989
Public safety	2,710,670	-	190,005	2,900,675
Corrections and rehabilitation	1,910,429	-	97,143	2,007,572
Health and human services	276,656	-	1,154,650	1,431,306
Community and economic development	226,865	-	-	226,865
Infrastructure and environmental services	139,560	4,288,941	456,696	4,885,197
Capital outlay	159,921	192,054	-	351,975
Debt service:				
Principal	-	82,331	-	82,331
Interest	-	6,529	-	6,529
Total expenditures	11,384,512	5,033,896	2,988,915	19,407,323
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	1,432,059	(415,356)	(500,083)	516,620
OTHER FINANCING SOURCES (USES)				
Transfers in	-	-	604,734	604,734
Transfers out	(604,734)	-	-	(604,734)
Proceeds from sale of assets	3,100	-	-	3,100
Proceeds from insurance	47,423	5,907	-	53,330
Total other financing sources (uses)	(554,211)	5,907	604,734	56,430
NET CHANGE IN FUND BALANCES	877,848	(409,449)	104,651	573,050
FUND BALANCES, BEGINNING	2,147,201	2,315,359	1,515,152	5,977,712
FUND BALANCES, ENDING	\$ 3,025,049	\$ 1,905,910	\$ 1,619,803	\$ 6,550,762

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

CHEROKEE COUNTY, TEXAS

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

FOR THE YEAR ENDED SEPTEMBER 30, 2013

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

Net change in fund balance - governmental funds	\$ 573,050
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.	(1,042,482)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the governmental funds.	78,964
Repayment of principal is an expenditure in the governmental funds but reduces the liability in the statement of net position.	82,331
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 the governmental funds.	(<u>62,022</u>)
Change in net position of governmental activities	<u>\$ (370,159)</u>

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

CHEROKEE COUNTY, TEXAS

STATEMENT OF FIDUCIARY ASSETS AND LIABILITIES

SEPTEMBER 30, 2013

	<u>Agency Fund</u>
ASSETS	
Cash	\$ 1,697,549
Investments	<u>688,765</u>
Total assets	<u>\$ 2,386,314</u>
LIABILITIES	
Due to others	\$ <u>2,386,314</u>
Total liabilities	<u>\$ 2,386,314</u>

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

CHEROKEE COUNTY, TEXAS

NOTES TO THE FINANCIAL STATEMENTS

SEPTEMBER 30, 2013

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the County reflected in the accompanying basic financial statements conform to accounting principles generally accepted in the United States of America (GAAP) applicable to state and local governments. Accounting principles generally accepted in the United States of America for local governments include those principles prescribed by the Governmental Accounting Standards Board (GASB), in Governmental Accounting and Financial Reporting Standards. The most significant accounting and reporting policies of the County are described below.

A. Description of the Government-wide Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the nonfiduciary activities of the primary government. All fiduciary activities are reported only in the fund financial statements. The governmental activities presented in the government-wide financial statements are normally supported by taxes, intergovernmental revenues, and other nonexchange transactions.

B. Reporting Entity

Cherokee County (the "County") was created and organized in 1846 from Nacogdoches County by an act of the Texas Legislature. The Commissioners' Court, which is comprised of four commissioners and the County Judge, is the governing body of the County. As authorized by the statutes of the State of Texas, the County provides the following services: general government (e.g., tax collection), justice system (e.g., courts, juries, district attorney, etc.), public safety (e.g., sheriff, etc.), corrections (e.g., jail), health and human services (e.g., indigent health care), infrastructure and environmental services (e.g., road maintenance and repair) and economic development.

In determining the financial reporting entity, Cherokee County, Texas complies with the provisions of GASB Statement No. 14, The Financial Reporting Entity. Under this standard, the County has no component units which are required to be reported, discretely or blended, in combination with the primary government.

C. Basis of Presentation – Government-wide Financial Statements

While separate government-wide and fund financial statements are presented, they are interrelated. The governmental activities column incorporates data from governmental funds. Separate financial statements are provided for governmental funds and fiduciary funds, even though the latter are excluded from the government-wide financial statements. As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements.

D. Basis of Presentation – Fund Financial Statements

The fund financial statements provide information about the government's funds, including its fiduciary funds. The emphasis of fund financial statements is on major governmental funds, each displayed in a separate column. All remaining governmental funds are aggregated and reported as nonmajor funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

The County reports the following major governmental funds:

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

Road and Bridge – The Road and Bridge Fund accounts for resources used in the construction and maintenance of County roads and bridges.

The County also reports fiduciary funds:

Agency Funds – Agency Funds are used to account for assets held by the County as an agent for individuals, private organizations, other governments, and/or other funds. Agency funds are custodial in nature (assets equal liabilities) and do not involve the measurement of results of operations.

During the course of operations the County has activity between funds for various purposes. Any residual balances outstanding at year end are reported as due from/to other funds and advances to/from other funds. While these balances are reported in fund financial statements, balances between the funds included in governmental activities are eliminated in the preparation of government-wide financial statements.

Further, certain activity occurs during the year involving transfers of resources between funds. In fund financial statements these amounts are reported at gross amounts as transfers in/out. These transfers are reported in fund financial statements but are eliminated in the preparation of government-wide financial statements.

E. Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as current financial resources or economic resources. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

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

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences, and claims and judgments, are recorded only when payment is due. General capital asset acquisitions are reported as expenditures in governmental funds. Issuance of long-term debt and acquisitions under capital leases are reported as other financing sources.

Property taxes, sales taxes, licenses, charges for services, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Entitlements are recorded as revenues when all eligibility requirements are met, including any time requirements, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). Expenditure-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other eligibility requirements have been met, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). All other revenue items are considered to be measurable and available only when cash is received by the government.

The agency fund has no measurement focus but utilizes the accrual basis of accounting for reporting its assets and liabilities.

F. Budgetary Information

Annual budgets are adopted on a basis consistent with generally accepted accounting principles. The budget is prepared by the County Budget Officer (the County Judge) with the assistance of the staff of the County Auditor's office and is approved by the Commissioners' Court following a public hearing.

The appropriated budget is prepared by fund, department, and object. Transfers of appropriations between departments require the approval of the Commissioners' Court. The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriations) is the department level. Annual appropriations lapse at fiscal year-end.

Classification of revenues and expenditures could differ between presentation in the financial statements and presentation in the budget.

Encumbrance accounting, under which purchase orders, contracts and other commitments for the expenditure of monies are recorded to reserve that portion of the applicable appropriation, is not employed by the County.

G. Cash and Investments

Cash and cash equivalents include amounts in demand deposits as well as short-term investments. From time to time, the County invests its available funds in time deposits and other short-term interest-bearing securities. Time deposits and securities having a maturity date of three months or less from the date of issuance are classified as cash while those with a maturity of more than three months are classified as investments.

The County records investments at fair market value in accordance with provisions of GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. All investment income is recognized as revenue in the appropriate fund's statement of activity and/or statement of revenues, expenditures, and changes in fund balance.

H. Capital Assets

Capital assets, which include property, plant and equipment, are reported in the government-wide financial statements. Capital assets are defined by the County as assets with an initial, individual cost of more than an adopted threshold and an estimated useful life in excess of one year. The thresholds adopted by the Commissioners' Court are as follows:

Land and land improvements	Capitalize all
Roads and bridges	\$ 200,000
Machinery, equipment and vehicles	1,500
Buildings and building improvements	5,000

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

Buildings and building improvements	31 years
Furniture and equipment	5 - 7 years
Vehicles	5 years
Infrastructure	20 - 25 years

I. 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 County 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.

- **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 the County's highest level of decision making authority. These amounts cannot be used for any other purpose unless the Commissioners Court 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 County's intent to be used for a specific purpose but are neither restricted nor committed. This intent can be expressed by the Commissioners Court.
- **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.

J. Fund Balance Flow Assumption

Sometimes County will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements a flow assumption must be made about the order in which the resources are considered to be applied. It is the County's policy to consider restricted fund balance to have been depleted before using any of the components of unrestricted fund balance. Further, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

K. Net Position Flow Assumption

Sometimes the County will fund outlays for a particular purpose from both restricted and unrestricted resources. In order to calculate the amounts to report as restricted net position and unrestricted net position in the government-wide financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the County's policy to consider restricted net position to have been depleted before unrestricted net position is applied.

L. Program Revenues

Amounts reported as program revenues in the government-wide financial statements include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions (including special assessments) that are restricted to meeting the operational or capital requirements of a particular function or segment. All taxes, including those collected for specific purposes, are reported as general revenues rather than as program revenues.

M. Compensated Absences

The County's policy permits employees to accumulate earned but unused vacation benefits, which are eligible for payment upon separation from government service. The liability for such leave is reported as incurred in the government-wide financial statements. A liability for those amounts is recorded in the governmental funds only if the liability has matured as a result of employee resignations or retirements.

Accumulated sick leave lapses when employees leave the employ of the County and, upon separation from service, no monetary obligation exists.

N. Property Taxes

Ad valorem taxes are levied October 1 of each year and are due and payable from October 1 of the year in which levied until January 31 of the following year without interest or penalty. Taxes become delinquent on February 1 following the year in which levied. Taxes on real property attach as an enforceable lien on January 1 of the year in which levied and are a lien against such property until paid. The combined tax rate for the year ended September 30, 2013, was \$.5900 per \$100 and was allocated as follows:

General fund	\$ 0.4034
General fund - indigent health	0.0116
Road and bridge fund	<u>0.1750</u>
	<u>\$ 0.5900</u>

O. Estimates

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

II. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Deficit Fund Equity

At September 30, 2013, the CDBG Grant fund, a nonmajor fund, had a deficit fund balance of \$5,991. In fiscal year 2012, the County entered into an agreement with a grant subrecipient and the state grantor agency to provide for the repayment of the subrecipient's disallowed costs from a prior grant year. The subrecipient is scheduled to make 24 monthly payments of \$2,035 to the County. The County then remits the same amount to the state grantor agency.

In the prior fiscal year, the County recognized an expenditure and liability to the state grantor agency for the full amount that was to be repaid. The County recognizes revenue for the payments received from the subrecipient as they become available (received within 60 days of year-end). The subrecipient will make its final payment to the County on March 1, 2014.

III. DETAILED NOTES ON ALL FUNDS

A. Cash Deposits with Financial Institutions

Custodial Credit Risk – In the case of deposits, this is the risk that in the event of a bank failure, the County’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, those of its agencies and instrumentalities, or direct obligations of Texas or its agencies instrumentalities that have a fair value of not less than the principal amount of deposits. The County requires all bank deposits to be collateralized at a level not less than 100% of the total uninsured deposits. As of September 30, 2013, the carrying value of the County’s deposit balance was fully collateralized with securities held by the pledging financial institution in the County’s name or by FDIC insurance.

B. Investments

The County invests in local government investment pools and reports these amounts at fair value as cash equivalents. As of September 30, 2013, the County had the following investments:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Weighted Average Maturity (days)</u>	<u>S&P Rating</u>
TexStar	\$ 31,721	52	AAAm

The County utilizes a pooled investment concept for most of its funds to maximize its investment program. Investment income from this internal pooling is allocated to the respective funds based upon the sources of funds invested.

Authorized investments for the County include obligations of the United States, or its agencies and instrumentalities; direct obligations of the State of Texas or its agencies; obligations of states agencies and other local governments having an investment rating of not less than A or its equivalent; certificates of deposit that are guaranteed by the Federal Deposit Insurance Corporation and other investments authorized by the statues governing public funds investment pools.

Interest Rate Risk. In accordance with its investment policy, the County manages its exposure to declines in fair market value by limiting the weighted average maturity of the investment portfolios to a maximum of 180 days.

Credit Risk. It is the County’s policy to limit its investments to investment types with an investment quality rating not less than A or its equivalent by a nationally recognized statistical rating organization.

C. Receivables and Allowance for Uncollectible Accounts

Receivables as of year-end for the governmental activities, individual major governmental funds and other governmental funds, including the applicable allowances for uncollectible accounts are as follows:

	<u>General</u>	<u>Road and Bridge</u>	<u>Other Governmental</u>	<u>Total</u>
Taxes receivable:				
Property tax	\$ 1,053,515	\$ 404,183	\$ 23,434	\$ 1,481,132
Sales tax	304,140	-	-	304,140
Mixed beverage tax	6,318	-	-	6,318
Court fines receivable	4,216,769	-	-	4,216,769
Less: allowance for uncollectibles	<u>(3,984,609)</u>	<u>(14,389)</u>	<u>(834)</u>	<u>(3,999,832)</u>
Net accounts receivable	<u>\$ 1,596,133</u>	<u>\$ 389,794</u>	<u>\$ 22,600</u>	<u>\$ 2,008,527</u>

Governmental funds report deferred revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. 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:

	<u>Unavailable</u>	<u>Unearned</u>
General fund:		
Delinquent property taxes	\$ 920,792	\$ -
Court fines	269,565	-
Grant receivable	5,033	-
Sales tax overpayment	-	106,272
Total general fund	<u>1,195,390</u>	<u>106,272</u>
Road and bridge fund:		
Delinquent property taxes	<u>350,034</u>	<u>-</u>
Total road and bridge fund	<u>350,034</u>	<u>-</u>
Nonmajor governmental funds:		
Delinquent property taxes	20,305	-
Other	<u>6,091</u>	<u>-</u>
Total nonmajor governmental funds	<u>26,396</u>	<u>-</u>
Total governmental funds	<u>\$ 1,571,820</u>	<u>\$ 106,272</u>

D. Unearned Sales Tax Revenue

In October of 1996, the County entered into an agreement with the State Comptroller to repay \$332,207 of local sales tax which was paid to the County in error. The agreement states that \$1,214 will be withheld from the County's sales tax revenues in October 1996, the first month of repayment, and \$1,107 will be withheld in each subsequent month until the year 2021. The remaining balance to be repaid at September 30, 2013, is \$106,272.

E. Due to Others

At September 30, 2013, the County held \$830,000 on deposit by a third party to cover potential repair expenses in the event of road damages resulting from third party activities. At September 30, 2013, the County also held \$171,384 of the state portion of fines and fees collected for the third calendar quarter of 2013.

F. Capital Assets

Capital asset activity for the year ended September 30, 2013, is as follows:

	Balance 09/30/12	Additions	Deletions	Balance 09/30/13
Governmental activities				
Capital assets not depreciated:				
Land	\$ 544,383	\$ -	\$ -	\$ 544,383
Total capital assets not being depreciated	<u>544,383</u>	<u>-</u>	<u>-</u>	<u>544,383</u>
Capital assets being depreciated:				
Buildings	12,423,357	-	-	12,423,357
Infrastructure	111,448,764	-	-	111,448,764
Improvements	2,627,726	-	-	2,627,726
Machinery and other equipment	9,433,512	400,626	166,206	9,667,932
Total capital assets being depreciated	135,933,359	400,626	166,206	136,167,779
Less: accumulated depreciation:				
Buildings	7,217,729	290,976	-	7,508,705
Infrastructure	109,675,444	145,641	-	109,821,085
Improvements	1,207,656	145,825	-	1,353,481
Machinery and other equipment	6,684,688	835,605	141,145	7,379,148
Total capital assets being depreciated	124,785,517	1,418,047	141,145	126,062,419
Total depreciable assets, net	<u>11,147,842</u>	<u>(1,017,421)</u>	<u>25,061</u>	<u>10,105,360</u>
Total capital assets	<u>\$ 11,692,225</u>	<u>\$ (1,017,421)</u>	<u>\$ 25,061</u>	<u>\$ 10,649,743</u>

Depreciation expense was charged to functions of the government-wide statement of activities as follows:

Governmental activities:	
General government	\$ 87,529
Justice system	34,999
Public safety	257,400
Corrections and rehabilitation	148,076
Health and human services	7,183
Community and economic development	1,512
Infrastructure and environmental services	<u>881,348</u>
Total governmental activities depreciation expense	<u>\$ 1,418,047</u>

G. Interfund Transfers

Interfund transfers for the fiscal year ended September 30, 2013, are summarized below:

<u>Transfer from</u>	<u>Amount</u>	<u>Transfer to</u>	<u>Purpose</u>
General fund	<u>604,734</u>	Nonmajor funds	Supplement fund sources
Total transfers	<u>\$ 604,734</u>		

H. Long-term Liabilities

The following is a summary of the changes in long-term liabilities of the County for the year ended September 30, 2013.

	<u>Balance September 30, 2012</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance September 30, 2013</u>	<u>Amounts Due Within One Year</u>
Notes payable	247,462	-	82,331	165,131	84,928
Compensated absences	223,921	224,847	193,704	255,064	242,311
Net OPEB obligation	<u>321,536</u>	<u>199,279</u>	<u>168,400</u>	<u>352,415</u>	<u>-</u>
Total governmental activities	<u>\$ 792,919</u>	<u>\$ 424,126</u>	<u>\$ 444,435</u>	<u>\$ 772,610</u>	<u>\$ 327,239</u>

The compensated absences and OPEB liability attributable to governmental activities were liquidated primarily by the General Fund in prior years.

Notes Payable

The note payable outstanding at September 30, 2013, was issued for the purpose of obtaining road and bridge equipment. The note is secured by the purchased equipment. The original principal amount of \$333,814 is payable in monthly installments with interest of 3.11%. Final maturity of the note is August 25, 2015.

The annual debt service requirements to maturity for notes payable are as follows:

<u>Year Ended September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014	\$ 84,928	\$ 3,932	\$ 88,860
2015	<u>80,203</u>	<u>1,253</u>	<u>81,456</u>
Total	<u>\$ 165,131</u>	<u>\$ 5,185</u>	<u>\$ 170,316</u>

IV. OTHER INFORMATION

A. Pension Plan

Plan Description

The County provides retirement, disability, and death benefits for all of its fulltime employees through a nontraditional defined benefit pension plan in the statewide Texas County and District Retirement System (TCDRS). The Board of Trustees of TCDRS is responsible for the administration of the statewide agent multiple-employer public employee retirement system consisting of approximately 641 nontraditional defined benefit pension plans. TCDRS in the aggregate issues a comprehensive annual financial report (CAFR) on a calendar year basis. The CAFR may be obtained by writing to P. O. Box 149153, Austin, Texas 78714-9153, or may be accessed online at www.TCDRS.org.

The plan provisions are adopted by the governing body of the employer, within the options available in the Texas state statutes governing TCDRS (TCDRS Act). Members can retire at ages 60 and above with 8 or more years of service, with 30 years of service regardless of age, or when the sum of their age and years of service equals 75 or more. Members are vested after 8 years, but must leave their accumulated contributions in the plan to receive any employer-financed benefit. Members who withdraw their personal deposits in a lump sum are not entitled to any accounts contributed by their employer.

Benefit amounts are determined by the sum of the employee's deposits to the plan with interest and employer-financed monetary credits. The level of these monetary credits is adopted by the governing body of the employer with the actuarial constraints imposed by the TCDRS Act so that the resulting benefits can be expected to be adequately financed by the employer's commitment to contribute. At retirement, death, or disability, the benefit is calculated by converting the sum of the employee's accumulated deposits and the employer-financed monetary credits to a monthly annuity using annuity purchase rates prescribed by the TCDRS Act.

Funding Policy

The employer has elected the annually determined contribution rate (variable-rate) plan provisions of the TCDRS Act. The plan is funded by monthly contributions from both employee members and the employer based on the covered payroll of employee members. Under the TCDRS Act, the contribution rate of the employer is actuarially determined annually. The employer contributed using the actuarially determined rate of 8.88% for the months of the accounting year in 2012, and 9.18% for the months in the accounting year 2013.

The deposit rate payable by the employee members for calendar year 2013 is the rate of 7% as adopted by the governing body of the employer. The employee deposit rate and the employer contribution rate may be changed by the governing body of the employer within the options available in the TCDRS Act.

Annual Pension Cost

For the employer's accounting year ended September 30, 2013, the annual pension cost for the TCDRS plan was \$ 754,213 and the actual contributions were \$754,213.

The annual pension cost, percentage of annual pension cost contributed, and net pension obligation for the plan for the current year and each of the two preceding years were as follows:

<u>Accounting Year Ended</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
September 30, 2011	\$ 685,277	100%	\$ -
September 30, 2012	696,529	100%	-
September 30, 2013	754,213	100%	-

Actuarial Methods and Assumptions

The annual required contributions were actuarially determined as a percent of the covered payroll of the participating employees, and were in compliance with the GASB Statement No. 27 parameters based on the actuarial valuations as of December 31, 2010 and December 31, 2011, the basis for determining the contribution rates for calendar years 2012 and 2013. The December 31, 2012 actuarial valuation is the most recent valuation.

Actuarial valuation date	12/31/2010	12/31/11	12/31/12
Actuarial cost method	Entry age	Entry age	Entry age
Amortization method	Level percentage of payroll, closed	Level percentage of payroll, closed	Level percentage of payroll, closed
Amortization period in years	20	20	20
Asset valuation method			
Subdivision Accumulation Fund	10-yr smoothed value	10-yr smoothed value	10-yr smoothed value
Employees Saving Fund	Fund Value	Fund Value	Fund Value
Actuarial assumptions:			
Investment return ¹	8.00%	8.00%	8.00%
Projected salary increases ¹	5.40%	5.40%	5.40%
Inflation	3.50%	3.50%	3.50%
Cost-of-living adjustments	0.00%	0.00%	0.00%

¹Includes inflation at the stated rate

Funded Status and Funding Progress

As of December 31, 2012, the most recent actuarial valuation date, the funded status of the plan was as follow:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (1) (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/2012	\$ 15,351,036	\$ 19,310,125	\$ 3,959,089	79.50%	\$ 7,959,786	49.74%

The schedule of funding progress presented immediately following the basic financial statements as required supplementary information, 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 for benefits.

B. Other Post-employment Benefits

Program Description

In addition to the pension benefits described above, the County makes available health care benefits through the Texas Association of Counties Health and Employee Benefits Pool to all employees who retire from the County and who are receiving benefits from the County sponsored retirement program (TCDRS). The health care plan provides insurance to eligible retirees through the County's group health insurance plan, which covers both active and retired members until age 65 when retirees become eligible and are required to enroll in Medicare Part B, at which time coverage supplements Medicare.

Funding Policy

The County contributions to the Retiree Health Program consist of a pay-as-you-go monthly contribution rate of \$400 per participant. The County contributions to the plan for fiscal year 2013 were \$168,400.

Annual OPEB Cost and Net OPEB Obligation

The County's annual other post-employment benefit (OPEB) cost (expense) for the Retiree Health Program 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 amortize any unfunded actuarial liabilities (of funding excess) over a period not to exceed 30 years.

The following table presents the components of the County's annual OPEB cost for the fiscal year ended September 30, 2013, the amount actually contributed to the plan, and changes in the County's net OPEB obligation.

Annual required contribution (ARC)	\$ 203,907
Interest on net OPEB obligation	14,469
Adjustment to annual required contribution	(19,097)
Annual OPEB cost (expense)	199,279
Contributions made	(168,400)
Change in OPEB obligation	30,879
Net OPEB obligation (asset), beginning	321,536
Net OPEB obligation (asset) ending	\$ 352,415

The County's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the fiscal year ended September 30, 2013, and the two preceding fiscal years were as follows:

Fiscal Year	Annual OPEB Cost	Employer Amount Contributed	Percentage of OPEB Cost Contributed	Net OPEB Obligation
2011	\$ 256,798	\$ 196,167	76.4%	\$ 253,420
2012	264,683	196,567	74.3%	321,536
2013	199,279	168,400	84.5%	352,415

Funded Status and Funding Progress

The funded status of the Retiree Health Program as of the most recent valuation date is as follows:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/2012	\$ -	\$ 2,138,682	\$ 2,138,682	0%	\$ 7,959,786	26.87%

Actuarial valuations for OPEB plans involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. These actuarially determined amounts are subject to continual revisions as actual results are compared to past expectations and new estimates are made about the future. The schedule of funding progress presented immediately following the financial statements as required supplementary information, 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 for benefits.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the type of benefits provided at the time of each valuation and the historical pattern of sharing benefit costs between the employer and plan members to that point. The actuarial calculations of the OPEB plan reflect a long-term perspective. Consistent with this perspective, actuarial valuations use actuarial methods and assumptions that include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

The ARC for the current year was determined as part of the December 31, 2012 actuarial valuation using the following methods and assumptions:

Actuarial Methods and Assumptions	
Actuarial valuation date	12/31/2012
Actuarial cost method	Projected Unit Credit Cost Method
Amortization method	Level dollar amount
Amortization period	Open 30-year period
Inflation rate	3.0% per year
Investment rate of return	4.5%, net of expenses
Health care trend	8.0% in 2013 decreasing by .5% over the next 7 years to an ultimate rate of 4.5%

C. Risk Management

The County 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 County provides for the management of risks through insurance coverage. There were no settlements in excess of the insurance coverage in any of the three prior fiscal years.

D. Contingent Liabilities

The County has received federal and state grants for specific purposes that are subject to review and audit by the grantor agencies. Such audits could lead to requests for reimbursement to the grantor agency for expenditures disallowed under terms of the grants. In the opinion of the County's management, disallowed costs, if any, would not have a material effect on the County's financial position or results of operations.

The County is involved in certain legal actions and claims arising in the ordinary course of its operations. Although the outcome of such lawsuits and other claims is not presently determinable, management believes that such legal actions should be resolved without a material effect on the financial position of the County.

**REQUIRED
SUPPLEMENTARY INFORMATION**

CHEROKEE COUNTY, TEXAS
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCE - BUDGET AND ACTUAL - GENERAL FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2013

	Original Budget	Final Budget	Actual	Variance With Final Budget Positive (Negative)
REVENUES				
Taxes:				
Property	\$ 8,923,289	\$ 8,923,289	\$ 8,930,190	\$ 6,901
Sales	1,456,000	1,456,000	1,830,758	374,758
Mixed beverage	29,000	29,000	20,472	(8,528)
Fees of office	879,700	879,700	1,012,069	132,369
Intergovernmental	219,081	219,081	253,855	34,774
Fines and forfeitures	723,800	723,800	737,143	13,343
Interest	13,226	13,226	14,912	1,686
Miscellaneous	10,800	10,800	17,172	6,372
Proceeds from sale of assets	-	-	3,100	3,100
Proceeds from insurance	-	35,012	47,423	12,411
Transfers	<u>1,595,324</u>	<u>1,595,324</u>	<u>1,485,324</u>	<u>(110,000)</u>
Total revenues, as classified by budget	<u>13,850,220</u>	<u>13,885,232</u>	14,352,418	<u>467,186</u>
Less: other financing sources budgeted as revenues			<u>(1,535,847)</u>	
Total revenues, as classified per GAAP			<u>12,816,571</u>	
EXPENDITURES				
County auditor	238,170	238,170	232,405	5,765
Information technology	134,374	134,374	130,985	3,389
Veterans service office	89,924	89,924	76,009	13,915
Human resources	65,678	65,678	57,470	8,208
Maintenance	350,840	350,840	337,915	12,925
Agricultural agent	169,314	169,314	158,950	10,364
Tax assessor-collector	486,642	486,642	481,117	5,525
District clerk	256,048	256,048	241,616	14,432
Child support	70,084	70,084	69,811	273
County clerk	360,139	360,139	345,029	15,110
Elections	225,854	225,854	186,977	38,877
County treasurer	155,328	155,328	153,553	1,775
Sheriff	2,447,426	2,482,438	2,471,141	11,297
Jail	2,046,706	2,046,706	1,910,429	136,277
Sheriff dept / animal control	53,570	53,570	50,511	3,059
County judge	178,734	178,734	176,642	2,092
County attorney	331,690	331,690	324,542	7,148
District attorney	378,210	378,210	350,681	27,529
Justice of the peace - Pct. #1	100,500	100,500	99,628	872
Justice of the peace - Pct. #2	95,344	95,344	94,335	1,009
Justice of the peace - Pct. #3	93,348	93,348	95,598	(2,250)
Justice of the peace - Pct. #4	92,398	92,398	92,060	338
Constable - Pct. #1	64,998	64,998	64,547	451
Constable - Pct. #2	65,706	65,706	57,772	7,934
Constable - Pct. #3	67,318	67,318	66,567	751
Constable - Pct. #4	66,606	66,606	65,542	1,064

(Continued)

CHEROKEE COUNTY, TEXAS

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCE - BUDGET AND ACTUAL - GENERAL FUND
(Continued)**

FOR THE YEAR ENDED SEPTEMBER 30, 2013

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	Variance With Final Budget Positive (Negative)
EXPENDITURES (Continued)				
2nd judicial district court	\$ 345,426	\$ 345,426	\$ 303,322	\$ 42,104
Court administrator - 2nd / 369th district court	114,576	114,576	112,282	2,294
369th judicial district court	146,432	146,432	118,627	27,805
County court-at-law	581,548	581,548	567,202	14,346
Transfers to other funds	370,925	370,925	370,925	-
Other departmental	1,303,056	1,303,056	920,189	382,867
County special	377,504	377,504	376,166	1,338
County/state special	29,200	29,200	33,412	(4,212)
Juvenile probation	316,971	316,971	316,453	518
Emergency management	59,600	59,600	57,561	2,039
Rural addressing	23,563	23,563	23,635	(72)
DARE program	56,228	56,228	54,933	1,295
Records management	31,000	31,000	33,278	(2,278)
Mental health advocate	96,806	96,806	71,803	25,003
Department of public safety	<u>15,225</u>	<u>15,225</u>	<u>13,314</u>	<u>1,911</u>
Total expenditures - sub-fund 010	<u>12,553,009</u>	<u>12,588,021</u>	<u>11,764,934</u>	<u>823,087</u>
Solid waste - sub-fund 021	112,584	112,584	107,710	4,874
General fund special - sub-fund 025	1,570,100	1,570,100	1,460,100	110,000
Indigent health - sub-fund 045	686,010	686,010	128,844	557,166
Historical commission - sub-fund 050	<u>12,000</u>	<u>12,000</u>	<u>12,982</u>	<u>(982)</u>
Total expenditures, as classified by budget	<u>14,933,703</u>	<u>14,968,715</u>	13,474,570	<u>1,494,145</u>
Less: other financing uses budgeted as expenditures			<u>(2,090,058)</u>	
Total expenditures, as classified per GAAP			<u>11,384,512</u>	
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES			<u>1,432,059</u>	
OTHER FINANCING SOURCES (USES)				
Transfers out			(604,734)	
Proceeds from sale of assets			3,100	
Proceeds from insurance			<u>47,423</u>	
Total other financing sources (uses)			<u>(554,211)</u>	
NET CHANGE IN FUND BALANCES	(1,083,483)	(1,083,483)	877,848	1,961,331
FUND BALANCES, BEGINNING	<u>2,147,201</u>	<u>2,147,201</u>	<u>2,147,201</u>	<u>-</u>
FUND BALANCES, ENDING	<u>\$ 1,063,718</u>	<u>\$ 1,063,718</u>	<u>\$ 3,025,049</u>	<u>\$ 1,961,331</u>

CHEROKEE COUNTY, TEXAS

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCE - BUDGET AND ACTUAL - ROAD AND BRIDGE**

FOR THE YEAR ENDED SEPTEMBER 30, 2013

	Original Budget	Final Budget	Actual	Variance With Final Budget Positive (Negative)
REVENUES				
Taxes	\$ 3,599,990	\$ 3,599,990	\$ 3,640,774	\$ 40,784
Fees of office	714,000	714,000	846,941	132,941
Intergovernmental	45,000	45,000	116,977	71,977
Interest	2,870	2,870	8,222	5,352
Miscellaneous	-	-	5,626	5,626
Total revenues	4,361,860	4,361,860	4,618,540	256,680
EXPENDITURES				
General government	536,366	536,366	464,041	72,325
Infrastructure and environmental services	3,660,972	4,025,729	4,288,941	(263,212)
Capital outlay	146,140	198,165	192,054	6,111
Debt service:				
Principal	82,331	82,331	82,331	-
Interest	6,529	6,529	6,529	-
Total expenditures	4,432,338	4,849,120	5,033,896	(184,776)
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(70,478)	(487,260)	(415,356)	71,904
OTHER FINANCING SOURCES (USES)				
Proceeds from insurance	-	-	5,907	5,907
Total other financing sources (uses)	-	-	5,907	5,907
NET CHANGE IN FUND BALANCES	(70,478)	(487,260)	(409,449)	77,811
FUND BALANCES, BEGINNING	2,315,359	2,315,359	2,315,359	-
FUND BALANCES, ENDING	\$ 2,244,881	\$ 1,828,099	\$ 1,905,910	\$ 77,811

REQUIRED SUPPLEMENTARY INFORMATION

CHEROKEE COUNTY, TEXAS

TEXAS COUNTY AND DISTRICT RETIREMENT SYSTEM

SCHEDULE OF FUNDING PROGRESS

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/2010	\$ 15,066,781	\$ 18,437,437	\$ 3,370,656	81.72%	\$ 7,896,947	42.68%
12/31/2011	15,194,426	18,809,583	3,615,157	80.78%	7,947,225	45.49%
12/31/2012	15,351,036	19,310,125	3,959,089	79.50%	7,959,786	49.74%

CHEROKEE COUNTY, TEXAS

RETIREE HEALTH PROGRAM

SCHEDULE OF FUNDING PROGRESS

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/2008	\$ -	\$ 3,191,774	\$ 3,191,774	- %	\$ 7,490,606	42.61%
12/31/2010	-	2,684,922	2,684,922	- %	7,896,947	34.00%
12/31/2012	-	2,138,682	2,138,682	- %	7,959,786	26.87%

**COMBINING
FUND STATEMENTS**

CHEROKEE COUNTY, TEXAS
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS

SEPTEMBER 30, 2013

	Special Revenue				
	County Health Unit	Airport	Grant	Law Enforcement Education	Juvenile Probation
ASSETS					
Cash and cash equivalents	\$ 38,194	\$ -	\$ 456,346	\$ 16,794	\$ 81,154
Investments	90,601	85,201	-	-	353,695
Receivables (net of allowance for uncollectibles)					
Taxes	-	-	-	-	-
Due from other governments	<u>119,392</u>	<u>-</u>	<u>3,245</u>	<u>-</u>	<u>-</u>
Total assets	<u>\$ 248,187</u>	<u>\$ 85,201</u>	<u>\$ 459,591</u>	<u>\$ 16,794</u>	<u>\$ 434,849</u>
LIABILITIES AND FUND BALANCES					
Liabilities:					
Accounts payable	\$ 17,450	\$ 3,949	\$ 8,010	\$ -	\$ 16,939
Due to others	-	-	-	-	-
Deferred revenue	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total liabilities	<u>17,450</u>	<u>3,949</u>	<u>8,010</u>	<u>-</u>	<u>16,939</u>
Fund balances:					
Restricted for:					
General government	-	-	416,998	-	-
Justice system	-	-	34,304	-	417,910
Public safety	-	-	279	16,794	-
Corrections and rehabilitation	-	-	-	-	-
Debt service	-	-	-	-	-
Assigned for:					
Health and human services	230,737	-	-	-	-
Infrastructure and environmental services	-	81,252	-	-	-
Capital projects	-	-	-	-	-
Unassigned	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total fund balances	<u>230,737</u>	<u>81,252</u>	<u>451,581</u>	<u>16,794</u>	<u>417,910</u>
Total liabilities and fund balances	<u>\$ 248,187</u>	<u>\$ 85,201</u>	<u>\$ 459,591</u>	<u>\$ 16,794</u>	<u>\$ 434,849</u>

Special Revenue

Jail Commissary	District Attorney LEF Special Account	Sheriff LEF Account	Constables LEF Special	CDBG Grant	Debt Service	Capital Projects	Total Nonmajor Governmental
\$ 27,445	\$ 42,845	\$ 19,848	\$ 21,868	\$ 100	\$ 233	\$ 17	\$ 704,844
-	-	-	-	-	51,483	261,486	842,466
-	-	-	-	-	22,600	-	22,600
-	-	-	-	10,161	-	-	132,798
<u>\$ 27,445</u>	<u>\$ 42,845</u>	<u>\$ 19,848</u>	<u>\$ 21,868</u>	<u>\$ 10,261</u>	<u>\$ 74,316</u>	<u>\$ 261,503</u>	<u>\$ 1,702,708</u>
\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 46,348
-	-	-	-	10,161	-	-	10,161
-	-	-	-	6,091	20,305	-	26,396
-	-	-	-	16,252	20,305	-	82,905
-	-	-	-	-	-	-	416,998
-	42,845	-	-	-	-	-	495,059
-	-	19,848	21,868	-	-	-	58,789
27,445	-	-	-	-	-	-	27,445
-	-	-	-	-	54,011	-	54,011
-	-	-	-	-	-	-	230,737
-	-	-	-	-	-	-	81,252
-	-	-	-	-	-	261,503	261,503
-	-	-	-	(5,991)	-	-	(5,991)
<u>27,445</u>	<u>42,845</u>	<u>19,848</u>	<u>21,868</u>	<u>(5,991)</u>	<u>54,011</u>	<u>261,503</u>	<u>1,619,803</u>
<u>\$ 27,445</u>	<u>\$ 42,845</u>	<u>\$ 19,848</u>	<u>\$ 21,868</u>	<u>\$ 10,261</u>	<u>\$ 74,316</u>	<u>\$ 261,503</u>	<u>\$ 1,702,708</u>

CHEROKEE COUNTY, TEXAS

**COMBINING STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES**

NONMAJOR GOVERNMENTAL FUNDS

FOR THE YEAR ENDED SEPTEMBER 30, 2013

	Special Revenue				
	County Health Unit	Airport	Grant	Law Enforcement Education	Juvenile Probation
	REVENUES				
Fees of office	\$ 195,582	\$ 432,023	\$ 227,069	\$ -	\$ -
Intergovernmental	618,573	11,106	51,263	-	658,059
Fines and forfeitures	-	-	52,506	-	4,383
Interest	344	148	1	36	738
Miscellaneous	-	4	-	-	45
Total revenues	<u>814,499</u>	<u>443,281</u>	<u>330,839</u>	<u>36</u>	<u>663,225</u>
EXPENDITURES					
Current:					
General government	-	-	186,941	-	-
Justice system	-	-	86,176	-	804,156
Public safety	-	-	42,431	1,888	-
Corrections and rehabilitation	-	-	12,202	-	-
Health and human services	1,154,650	-	-	-	-
Infrastructure and environmental services	-	456,696	-	-	-
Total expenditures	<u>1,154,650</u>	<u>456,696</u>	<u>327,750</u>	<u>1,888</u>	<u>804,156</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(340,151)</u>	<u>(13,415)</u>	<u>3,089</u>	<u>(1,852)</u>	<u>(140,931)</u>
OTHER FINANCING SOURCES (USES)					
Transfers in	345,701	-	16,000	-	243,033
Total other financing sources and uses	<u>345,701</u>	<u>-</u>	<u>16,000</u>	<u>-</u>	<u>243,033</u>
NET CHANGE IN FUND BALANCES	5,550	(13,415)	19,089	(1,852)	102,102
FUND BALANCES, BEGINNING	<u>225,187</u>	<u>94,667</u>	<u>432,492</u>	<u>18,646</u>	<u>315,808</u>
FUND BALANCES, ENDING	<u>\$ 230,737</u>	<u>\$ 81,252</u>	<u>\$ 451,581</u>	<u>\$ 16,794</u>	<u>\$ 417,910</u>

Special Revenue

Jail Commissary	District Attorney LEF Special Account	Sheriff LEF Account	Constables LEF Special	CDBG Grant	Debt Service	Capital Projects	Total Nonmajor Governmental
\$ 66,977	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 921,651
-	-	-	-	159,292	-	-	1,498,293
-	5,342	4,560	182	-	-	-	66,973
-	-	-	-	-	102	497	1,866
-	-	-	-	-	-	-	49
<u>66,977</u>	<u>5,342</u>	<u>4,560</u>	<u>182</u>	<u>159,292</u>	<u>102</u>	<u>497</u>	<u>2,488,832</u>
-	-	-	-	-	-	6,537	193,478
-	6,611	-	-	-	-	-	896,943
-	-	8,131	2,683	134,872	-	-	190,005
84,941	-	-	-	-	-	-	97,143
-	-	-	-	-	-	-	1,154,650
-	-	-	-	-	-	-	456,696
<u>84,941</u>	<u>6,611</u>	<u>8,131</u>	<u>2,683</u>	<u>134,872</u>	<u>-</u>	<u>6,537</u>	<u>2,988,915</u>
(17,964)	(1,269)	(3,571)	(2,501)	24,420	102	(6,040)	(500,083)
-	-	-	-	-	-	-	604,734
-	-	-	-	-	-	-	604,734
(17,964)	(1,269)	(3,571)	(2,501)	24,420	102	(6,040)	104,651
<u>45,409</u>	<u>44,114</u>	<u>23,419</u>	<u>24,369</u>	<u>(30,411)</u>	<u>53,909</u>	<u>267,543</u>	<u>1,515,152</u>
<u>\$ 27,445</u>	<u>\$ 42,845</u>	<u>\$ 19,848</u>	<u>\$ 21,868</u>	<u>\$ (5,991)</u>	<u>\$ 54,011</u>	<u>\$ 261,503</u>	<u>\$ 1,619,803</u>

**GOVERNMENT AUDITING
STANDARDS**



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

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

To the Honorable County Judge
and County Commissioners
Cherokee County, Texas

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Cherokee County, Texas, as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise the County's basic financial statements, and have issued our report thereon dated June 17, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the County's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control. Accordingly, we do not express an opinion on the effectiveness of the County's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Cherokee County, Texas' financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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

Saxillo, Brown & Hill, LLP

Waco, Texas
June 17, 2014