



(See “Continuing Disclosure Information” herein)

**NEW ISSUE – Book-Entry-Only**

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

**OFFICIAL STATEMENT**

**Dated November 28, 2018**

**Ratings:**  
**Moody’s: “Aaa” / “A1”**  
**S&P: “AAA” / “AA-”**  
**PSF Guaranteed**  
**(See “Other Information - Ratings” and “The Permanent School Fund Guarantee Program” herein)**

**THE BONDS HAVE NOT BEEN DESIGNATED AS “QUALIFIED TAX-EXEMPT OBLIGATIONS” FOR FINANCIAL INSTITUTIONS**

**\$37,160,000**  
**CLEVELAND INDEPENDENT SCHOOL DISTRICT**  
**(Liberty, Montgomery and San Jacinto Counties, Texas)**  
**UNLIMITED TAX SCHOOL BUILDING BONDS, SERIES 2018A**

**Dated Date: December 1, 2018**

**Interest Accrual Date: Delivery Date, as shown below**

**Due: As shown on Page 2**

**PAYMENT TERMS . . .** Interest on the \$37,160,000 Cleveland Independent School District Unlimited Tax School Building Bonds, Series 2018A (the “Bonds”) will accrue from the date of initial delivery to the Underwriters (the “Delivery Date”, anticipated to be on or about December 20, 2018), will be payable February 15 and August 15 of each year commencing on February 15, 2019, until maturity or prior redemption and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The Bonds will be issued as fully registered obligations in the denominations of \$5,000 of principal amount or any integral multiple thereof for any one stated maturity. The definitive Bonds will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company (“DTC”) pursuant to the Book-Entry-Only System described herein. Beneficial ownership of the Bonds may be acquired in authorized denominations thereof. **No physical delivery of the Bonds will be made to the beneficial owners thereof.** The principal and interest on the Bonds will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Bonds. See “THE BONDS - Book-Entry-Only System” herein. The initial Paying Agent/Registrar is U.S. Bank National Association, Dallas, Texas (see “THE BONDS - Paying Agent/Registrar”).

**AUTHORITY FOR ISSUANCE . . .** The Bonds are issued pursuant to the Constitution and general laws of the State of Texas (the “State”), including Sections 45.001 and 45.003(b)(1) of the Texas Education Code, as amended, Chapter 1371, Texas Government Code (“Chapter 1371”), as amended, an election held in the Cleveland Independent School District (the “District”) on May 6, 2017, and an order (the “Bond Order”) adopted by the Board of Trustees (the “Board”) of the District on November 12, 2018. In the Bond Order, the Board delegated pricing of the Bonds and certain other matters to the “Pricing Officer” who approved a “Pricing Certificate” which contains the final terms of sale and completed the sale of the Bonds (the Bond Order and the Pricing Certificate are collectively referred to as the “Order”). The Bonds are direct and voted obligations of the District, payable from an annual ad valorem tax levied, without legal limitation as to rate or amount, on all taxable property located within the District, as provided in the Order (see “THE BONDS - Authority for Issuance”). **An application has been filed and the District has received conditional approval for the payment of the Bonds to be guaranteed by the Permanent School Fund of Texas (see “THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM” herein).**

**PURPOSE . . .** Proceeds from the sale of the Bonds will be used (1) to construct, equip and renovate school buildings in the District and (2) to pay the costs associated with the issuance of the Bonds.

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

**DELIVERY . . .** It is expected that the Bonds will be available for delivery through the facilities of DTC on or about December 20, 2018.

**MATURITY SCHEDULE**  
**See Schedule on Page 2**

**SAMCO CAPITAL MARKETS, INC.**

**RBC CAPITAL MARKETS**

**MATURITY SCHEDULE**

**CUSIP<sup>(1)</sup> Prefix: 186612**

Maturity (2/15)	Principal Amount	Interest Rate	Initial Yield	CUSIP <sup>(1)</sup> Suffix	Maturity (2/15)	Principal Amount	Interest Rate	Initial Yield	CUSIP <sup>(1)</sup> Suffix
2025	\$ 135,000	4.000%	2.470%	QZ3	2036	\$ 1,825,000	5.000%	3.250% <sup>(2)</sup>	RL3
2026	465,000	5.000%	2.580%	RA7	2037	1,900,000	4.000%	3.670% <sup>(2)</sup>	RM1
2027	745,000	5.000%	2.680%	RB5	2038	2,255,000	4.000%	3.710% <sup>(2)</sup>	RN9
2028	920,000	5.000%	2.760%	RC3	2039	2,340,000	4.000%	3.740% <sup>(2)</sup>	RP4
2029	970,000	5.000%	2.840% <sup>(2)</sup>	RD1	***	***	***	***	***
2030	1,050,000	4.000%	3.040% <sup>(2)</sup>	RE9	2042	2,720,000	5.000%	3.470% <sup>(2)</sup>	RS8
2031	1,105,000	5.000%	2.980% <sup>(2)</sup>	RF6	2043	2,855,000	5.000%	3.480% <sup>(2)</sup>	RT6
2032	555,000	5.000%	3.060% <sup>(2)</sup>	RG4	2044	3,010,000	5.000%	3.490% <sup>(2)</sup>	RU3
2033	560,000	5.000%	3.130% <sup>(2)</sup>	RH2	***	***	***	***	***
2034	1,990,000	4.000%	3.490% <sup>(2)</sup>	RJ8	2048	4,615,000	4.000%	4.030%	RV1
2035	2,090,000	5.000%	3.190% <sup>(2)</sup>	RK5					

**\$5,055,000 5.000% Term Bonds due February 15, 2041 Priced to Yield 3.450%<sup>(2)</sup> - CUSIP<sup>(1)</sup> Suffix: RR0**

**(Interest to accrue from the Delivery Date)**

(1) CUSIP is a registered trademark of the American Bankers Association. CUSIP data is provided by CUSIP Global Services, managed by S&P Global Market Intelligence on behalf of the American Bankers Association. This data is not intended to create a database and does not serve in any way as a substitute for the CUSIP services. None of the District, the Financial Advisor, or the Underwriters take any responsibility for the accuracy of CUSIP numbers.

(2) Yield shown is yield to first call date, February 15, 2028.

**OPTIONAL REDEMPTION** . . . The District reserves the right, at its option, to redeem Bonds having stated maturities on and after February 15, 2029, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2028, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption (see “THE BONDS – Optional Redemption”).

**MANDATORY SINKING FUND REDEMPTION** . . . The Term Bonds maturing on February 15, 2041 are subject to mandatory sinking fund redemption prior to maturity on the dates and in the amounts described herein under “THE BONDS – Mandatory Sinking Fund Redemption”.

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

Certain information set forth herein has been obtained from the District and other sources which are believed to be reliable but is not guaranteed as to accuracy or completeness, and is not to be construed as a representation by the Financial Advisor or the Underwriters. Any information and expressions of opinion herein contained are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the District or other matters described herein since the date hereof. See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM – PSF Continuing Disclosure Undertaking" and "CONTINUING DISCLOSURE INFORMATION" for a description of the undertakings of the Texas Education Agency (the "TEA") and the District, respectively, to provide certain information on a continuing basis.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement pursuant to its respective responsibilities to investors under the federal securities laws, but the Underwriters do not guarantee the accuracy or completeness of such information.

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

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

NONE OF THE DISTRICT, ITS FINANCIAL ADVISOR, OR THE UNDERWRITERS MAKE ANY REPRESENTATION OR WARRANTY WITH RESPECT TO THE INFORMATION CONTAINED IN THIS OFFICIAL STATEMENT REGARDING THE DEPOSITORY TRUST COMPANY OR ITS BOOK-ENTRY ONLY SYSTEM OR THE AFFAIRS OF THE TEA DESCRIBED UNDER "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM", AS SUCH INFORMATION HAS BEEN PROVIDED BY THE DEPOSITORY TRUST COMPANY AND THE TEA, RESPECTIVELY.

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

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

## OFFICIAL STATEMENT SUMMARY

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

- THE DISTRICT**..... The Cleveland Independent School District (the “District”) is a political subdivision of the State of Texas (the “State”) located in Liberty, Montgomery and San Jacinto Counties. The District encompasses approximately 143 square miles in area (see “INTRODUCTION – The District”).
- THE BONDS** ..... The \$37,160,000 Unlimited Tax School Building Bonds, Series 2018A (the “Bonds”) are issued in part as serial bonds maturing on February 15 in the years 2025 through 2039, 2042 through 2044 and 2048; and in part as term bonds maturing on February 15, 2041 (see “THE BONDS - Description of the Bonds”).
- PAYMENT OF INTEREST** ..... Interest on the Bonds accrues from the date of their delivery, and is payable on February 15, 2019 and each February 15 and August 15 thereafter until maturity or prior redemption (see “THE BONDS - Description of the Bonds”, “THE BONDS - Optional Redemption” and “THE BONDS – Mandatory Sinking Fund Redemption”).
- AUTHORITY FOR ISSUANCE**..... The Bonds are being issued pursuant to the Constitution and general laws of the State of Texas, including Sections 45.001 and 45.003(b)(1) of the Texas Education Code, as amended, Chapter 1371, Texas Government Code (“Chapter 1371”), as amended, an election held in the District on May 6, 2017, and an order (the “Bond Order”) adopted by the Board of Trustees (the “Board”) of the District on November 12, 2018 (see “THE BONDS - Authority for Issuance”). In the Bond Order, the Board delegated pricing of the Bonds and certain other matters to the “Pricing Officer” who approved a “Pricing Certificate” which contains the final terms of sale and completed the sale of the Bonds (the Bond Order and the Pricing Certificate are collectively referred to as the “Order”).
- SECURITY FOR THE BONDS** ..... The Bonds constitute direct obligations of the District, payable from a continuing direct annual ad valorem tax levied by the District, without legal limit as to rate or amount, on all taxable property within the District. Additionally, an application has been filed and the District has received conditional approval for the payment of the Bonds to be guaranteed by the corpus of the Permanent School Fund of Texas (see “THE BONDS - Security and Source of Payment”).
- PERMANENT SCHOOL FUND**
- GUARANTEE** ..... The District has received conditional approval from the Texas Education Agency for the payment of the Bonds to be guaranteed by the corpus of the Permanent School Fund of the State of Texas (see “THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM”).
- OPTIONAL REDEMPTION** ..... The District reserves the right, at its option, to redeem Bonds having stated maturities on and after February 15, 2029, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2028, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption (see “THE BONDS - Optional Redemption”).
- MANDATORY SINKING FUND REDEMPTION** ..... Additionally, the term bonds maturing on February 15, 2041 are subject to mandatory sinking fund redemption prior to maturity at a price of par plus accrued interest to the redemption date (see “THE BONDS – Mandatory Sinking Fund Redemption”).
- NOT QUALIFIED TAX-EXEMPT OBLIGATIONS**..... The Bonds have not been designated as “Qualified Tax-Exempt Obligations” for financial institutions.
- TAX EXEMPTION** ..... In the opinion of Bond Counsel, the interest on the Bonds will be excludable from gross income for federal income tax purposes under statutes, regulations, published rulings and court decisions existing on the date thereof, subject to the matters described under “TAX MATTERS” herein.
- USE OF PROCEEDS** ..... Proceeds from the sale of the Bonds will be used (1) to construct, equip and renovate school buildings in the District and (2) to pay the costs associated with the issuance of the Bonds.

**RATINGS** ..... The Bonds have been rated “Aaa” by Moody’s Investors Service, Inc. (“Moody’s”) and “AAA” by S&P Global Ratings, a division of Standard & Poor’s Financial Services LLC (“S&P”) by virtue of the guarantee of the Permanent School Fund of the State of Texas. The Bonds and the presently outstanding tax supported debt of the District are rated “A1” by Moody’s Investors Service, Inc. (“Moody’s”) and “AA-” by S&P Global Ratings, a division of Standard & Poor’s Financial Services LLC (“S&P”) without regard to credit enhancement. The District also has outstanding bonds which are rated “Aaa” by Moody’s and “AAA” by S&P by virtue of the guarantee of the Permanent School Fund of the State of Texas (see “OTHER INFORMATION - Ratings” and “THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM”).

**BOOK-ENTRY-ONLY SYSTEM** ..... The definitive Bonds will be initially registered and delivered only to Cede & Co., the nominee of DTC pursuant to the Book-Entry-Only System described herein. Beneficial ownership of the Bonds may be acquired in denominations of \$5,000 or integral multiples thereof. No physical delivery of the Bonds will be made to the beneficial owners thereof. Principal of, premium, if any, and interest on the Bonds will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Bonds (see “THE BONDS - Book-Entry-Only System”).

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

**SELECTED FINANCIAL INFORMATION**

Fiscal Year Ended 8/31	Estimated District Population <sup>(1)</sup>	Taxable Assessed Valuation <sup>(2)</sup>	Per Capita Taxable Assessed Valuation	Tax Supported Debt at End of Fiscal Year	Per Capita Tax Supported Debt	Ratio Tax Supported Debt to Taxable Assessed Valuation	% of Total Tax Collections
2015	21,517	\$ 850,307,008	\$ 39,518	\$ 35,397,395	\$ 1,645	4.16%	97.36%
2016	23,137	932,700,302	40,312	64,639,845	2,794	6.93%	97.17%
2017	26,912	1,071,937,872	39,831	67,856,765	2,522	6.33%	93.60%
2018	27,376	1,195,276,649	43,661	97,725,498	3,571	8.18%	100.66% <sup>(4)</sup>
2019	28,745	1,390,654,833	48,379	134,044,989 <sup>(3)</sup>	4,664 <sup>(3)</sup>	9.64% <sup>(3)</sup>	N/A

- (1) Source: Municipal Advisory Council of Texas.
- (2) As reported by the Appraisal District (defined herein) on the District’s annual State Property Tax Reports and such values are subject to change during the ensuing year.
- (3) Includes the Bonds. Does not include any “other obligations” outstanding (see “Table 10 - Other Obligations”).
- (4) Unaudited collections as of August 31, 2018.

For additional information regarding the District, please contact:

<p>Dr. Darrell Myers          Superintendent  <i>Cleveland Independent School District</i>          316 East Dallas          Cleveland, Texas 77327          (281) 592-8717</p>	or	<p>Jeff Robert          Managing Director  <i>Hilltop Securities Inc.</i>          1201 Elm Street, Ste. 3500          Dallas, Texas 75270          (214) 953-8744</p>
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**DISTRICT OFFICIALS, STAFF AND CONSULTANTS**

**ELECTED OFFICIALS**

<u>Board of Trustees</u>	<u>Length of Service</u>	<u>Term Expires</u>	<u>Occupation</u>
Chris Wood President	18 Years	2021	Self Employed (Insurance)
Christina Purkerson Vice President	6 Years	2021	Accountant
Kelly Jenkel-Axton Secretary	6 Years	2021	Self Employed - Propane
Ronnie Lewis Board Member	12 Years	2019	Retired
Sharica Lewis Board Member	2 Years	2019	Deputy Clerk (Liberty County District Clerk's Office)
Aaron Montesnieto Board Member	1 Year	2020	Union Plumber
Kellie Whitmire Board Member	1 Year	2020	Teacher

**SELECTED ADMINISTRATIVE STAFF**

<u>Name</u>	<u>Position</u>	<u>Length of Service with the District</u>	<u>Total School District Service</u>
Dr. Darrell Myers	Superintendent	4 Years	35 Years
Karen Billingsley	Chief Financial Officer	18 Years	18 Years

**CONSULTANTS AND ADVISORS**

Auditors ..... Singleton, Clark & Company, PC  
Cedar Park, Texas

Bond Counsel ..... Norton Rose Fulbright US LLP  
Dallas, Texas

Financial Advisor ..... Hilltop Securities Inc.  
Dallas, Texas

**OFFICIAL STATEMENT  
RELATING TO  
  
\$37,160,000  
CLEVELAND INDEPENDENT SCHOOL DISTRICT  
UNLIMITED TAX SCHOOL BUILDING BONDS, SERIES 2018A**

**INTRODUCTION**

This Official Statement, which includes the Appendices hereto, provides certain information regarding the issuance of \$37,160,000 Cleveland Independent School District Unlimited Tax School Building Bonds, Series 2018A (the “Bonds”). Capitalized terms used in this Official Statement have the same meanings assigned to such terms in the Order (hereinafter defined) authorizing the issuance and sale of the Bonds, except as otherwise indicated herein.

There follows in this Official Statement descriptions of the Bonds and certain information regarding the Cleveland Independent School District (the “District” or “Issuer”) and its finances. All descriptions of documents contained herein are only summaries and are qualified in their entirety by reference to each such document. Copies of such documents may be obtained from the District’s Financial Advisor, Hilltop Securities Inc., Dallas, Texas.

**THE DISTRICT . . .** The District is a political subdivision located primarily in Liberty County, Texas, with territory extending into Montgomery and San Jacinto Counties. The District is governed by a seven-member Board of Trustees (the “Board”) who serve staggered three-year terms with elections being held in May of each year. Policy-making and supervisory functions are the responsibility of, and are vested in, the Board. The Board delegates administrative responsibilities to the Superintendent of Schools who is the chief administrative officer of the District. Support services are supplied by consultants and advisors. The District covers approximately 143 square miles in Liberty, Montgomery and San Jacinto Counties, encompassing the City of Cleveland, Texas.

**IMPACT OF HURRICANE HARVEY . . .** The greater Houston area, including the District, is subject to occasional severe weather events, including tropical storms and hurricanes. If the District were to sustain damage to its facilities requiring substantial repair or replacement, or if substantial damage were to occur to taxable property within the District as a result of such a weather event, the investment security of the Bonds could be adversely affected.

The greater Houston area, including the District, has experienced three storms exceeding a 0.2% probability (i.e. “500-year flood” events) since 2015. The most recent event was Hurricane Harvey, which made landfall along the Texas Gulf Coast on August 26, 2017, and brought historic levels of rainfall during the successive four days. According to the District, as a result of Hurricane Harvey District officials cancelled classes beginning on August 25, 2017 and classes resumed on September 2, 2017. The District assessed the impact of the rainfall on the District’s facilities and has determined that no material damage inhibiting the continued operation and use of the District’s facilities has occurred. Additionally, although parts of the District experienced localized flooding, the District does not expect any long term material financial challenges resulting from damage related to Hurricane Harvey.

If a future weather event significantly damaged all or part of the improvements within the District, the assessed value of property within the District could be substantially reduced, which could result in a decrease in tax revenues and/or necessitate an increase the District’s tax rate. Further, there can be no assurance that a casualty loss to taxable property within the District will be covered by insurance (or that property owners will even carry flood or other casualty insurance), that any insurance company will fulfill its obligation to provide insurance proceeds, or that insurance proceeds will be used to rebuild or repair any damaged improvements within the District. Even if insurance proceeds are available and improvements are rebuilt, there could be a lengthy period in which assessed values within the District could be adversely affected.

**THE BONDS**

**DESCRIPTION OF THE BONDS . . .** The Bonds will be dated December 1, 2018 and mature on the dates and in the amounts shown on page 2 of this Official Statement. Interest on the Bonds will accrue from the date of their initial delivery to the underwriters identified on the cover page hereof (the “Underwriters”) and will be computed on the basis of a 360-day year of twelve 30-day months. Such interest will be payable on February 15 and August 15 of each year commencing on February 15, 2019, until maturity or prior redemption. The definitive Bonds will be issued only in fully registered form in any integral multiple of \$5,000 for any one maturity and will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company (“DTC”) pursuant to the Book-Entry-Only System described herein. **No physical delivery of the Bonds will be made to the beneficial owners thereof.** Principal of, premium, if any, and interest on the Bonds will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Bonds. See “THE BONDS - Book-Entry-Only System” herein.

**AUTHORITY FOR ISSUANCE** . . . The Bonds are issued and the tax is levied for their payment pursuant to authority conferred by the Constitution and the laws of the State of Texas, including Sections 45.001 and 45.003(b)(1) of the Texas Education Code, as amended, Chapter 1371, Texas Government Code (“Chapter 1371”), as amended, an election held in the District on May 6, 2017, and by the order adopted by the Board on November 12, 2018 (the “Bond Order”). In the Bond Order, the Board delegated pricing of the Bonds and certain other matters to the “Pricing Officer” who approved a “Pricing Certificate” which contains the final terms of sale and completed the sale of the Bonds (the Bond Order and the Pricing Certificate are collectively referred to as the “Order”).

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

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

**PURPOSE** . . . Proceeds from the sale of the Bonds will be used (1) to construct, equip and renovate school buildings in the District and (2) to pay the costs associated with the issuance of the Bonds.

**OPTIONAL REDEMPTION** . . . The District reserves the right, at its option, to redeem Bonds having stated maturities on and after February 15, 2029, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2028, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption. If less than all of the Bonds are to be redeemed, the District may select the maturities of Bonds to be redeemed. If less than all the Bonds of any maturity are to be redeemed, the Paying Agent/Registrar (or DTC while the Bonds are in Book-Entry-Only form) shall determine by lot the Bonds, or portions thereof, within such maturity to be redeemed.

**MANDATORY SINKING FUND REDEMPTION** . . . The Term Bonds maturing on February 15, 2041 (the “Term Bonds”) are subject to mandatory sinking fund redemption prior to maturity at a price of par plus accrued interest to the mandatory redemption date as follows:

Term Bonds Maturing February 15, 2041	
Year	Amount
2/15/2040	\$ 2,475,000
2/15/2041 <sup>(1)</sup>	2,580,000

(1) Stated Maturity.

Approximately forty-five (45) days prior to each mandatory redemption date for the Term Bonds, the Paying Agent/Registrar shall select by lot the numbers of the Term Bonds within the applicable Stated Maturity to be redeemed on the next following February 15 from moneys set aside for that purpose in the Interest and Sinking Fund. Any Term Bonds not selected for prior redemption shall be paid on the date of their Stated Maturity.

The principal amount of the Term Bonds for a Stated Maturity required to be redeemed on a mandatory redemption date may be reduced, at the option of the District, by the principal amount of Term Bonds of like Stated Maturity which, at least 50 days prior to the mandatory redemption date, (1) shall have been acquired by the District at a price not exceeding the principal amount of such Term Bonds plus accrued interest to the date of purchase thereof, and delivered to the Paying Agent/Registrar for cancellation or (2) shall have been redeemed pursuant to the optional redemption provisions set forth above and not theretofore credited against a mandatory sinking fund redemption requirement.

**NOTICE OF REDEMPTION** . . . Not less than 30 days prior to a redemption date for the Bonds, the District shall cause a notice of redemption to be sent by United States mail, first class, postage prepaid, to the registered owners of the Bonds to be redeemed, in whole or in part, at the address of the registered owner appearing on the registration books of the Paying Agent/Registrar at the close of business on the business day next preceding the date of mailing such notice. ANY NOTICE SO MAILED SHALL BE CONCLUSIVELY PRESUMED TO HAVE BEEN DULY GIVEN, WHETHER OR NOT THE REGISTERED OWNER RECEIVES SUCH NOTICE. NOTICE HAVING BEEN SO GIVEN AND ANY OTHER CONDITION TO REDEMPTION SATISFIED, THE BONDS CALLED FOR REDEMPTION SHALL BECOME DUE AND PAYABLE ON THE SPECIFIED

REDEMPTION DATE, AND NOTWITHSTANDING THAT ANY BOND OR PORTION THEREOF HAS NOT BEEN SURRENDERED FOR PAYMENT, INTEREST ON SUCH BOND OR PORTION THEREOF SHALL CEASE TO ACCRUE.

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

**DEFEASANCE . . .** The Order provides for the defeasance of the Bonds when the payment of the principal of and premium, if any, on such Bonds, plus interest thereon to the due date thereof (whether such due date be by reason of maturity, redemption, or otherwise), is provided by irrevocably depositing with the Paying Agent/Registrar, or other authorized escrow agent, in trust (1) money sufficient to make such payment or (2) Government Securities to mature as to principal and interest in such amounts and at such times to ensure the availability, without reinvestment, of sufficient money to make such payment, and all necessary and proper fees, compensation and expenses of the paying agent for the Bonds. The Order provides that "Government Securities" means (a) direct, noncallable obligations of the United States of America, including obligations that are unconditionally guaranteed by the United States of America, (b) noncallable obligations of an agency or instrumentality of the United States of America, including obligations that are unconditionally guaranteed or insured by the agency or instrumentality and that, on the date of their acquisition or purchase by the District, are rated as to investment quality by a nationally recognized investment rating firm not less than "AAA" or its equivalent, (c) noncallable obligations of a state or an agency or a county, municipality, or other political subdivision of a state that have been refunded and that, on the date of their acquisition or purchase by the District, are rated as to investment quality by a nationally recognized investment rating firm not less than "AAA" or its equivalent, and (d) any other then authorized securities or obligations that may be used to defease obligations such as the Bonds under applicable laws of the State of Texas. The District has the right, subject to satisfying the requirements of (1) and (2) above, to substitute other Government Securities for the Government Securities originally deposited, to reinvest the uninvested moneys on deposit for such defeasance and to withdraw for the benefit of the District moneys in excess of the amount required for such defeasance.

There is no assurance that the current law will not be changed in a manner which would permit investments other than those described above to be made with amounts deposited to defease the Bonds. Because the Order does not contractually limit such investments, registered owners may be deemed to have consented to defeasance with such other investments, notwithstanding the fact that such investments may not be of the same investment quality as those currently permitted under State law. There is no assurance that the ratings for U.S. Treasury securities used as Government Securities or that for any other Government Security will be maintained at any particular rating category.

Upon such deposit as described above, such Bonds shall no longer be regarded to be outstanding or unpaid and will cease to be outstanding obligations secured by the Order or treated as debt of the District for purposes of taxation or applying any limitation on the District's ability to issue debt or for any other purpose. After firm banking and financial arrangements for the discharge and final payment or redemption of the Bonds have been made as described above, all rights of the District to initiate proceedings to call the Bonds for redemption or take any other action amending the terms of the Bonds are extinguished; provided, however, that the right to call the Bonds for redemption is not extinguished if the District: (i) in the proceedings providing for the firm banking and financial arrangements, expressly reserves the right to call the Bonds for redemption; (ii) gives notice of the reservation of that right to the owners of the Bonds immediately following the making of the firm banking and financial arrangements; and (iii) directs that notice of the reservation be included in any redemption notices that it authorizes.

Furthermore, the Permanent School Fund Guarantee will terminate with respect to the Bonds defeased in the manner provided above.

**AMENDMENTS . . .** The District may amend the Order without the consent of or notice to any registered owners of the Bonds in any manner not detrimental to the interest of the registered owners, including the curing of any ambiguity, inconsistency, or formal defect or omission therein. In addition, the District may, with the written consent of the holders of a majority in aggregate principal amount of the Bonds then outstanding, amend, add to, or rescind any of the provisions of the Order; except that, without consent of the registered owners of all of the Bonds then outstanding, no such amendment, addition or rescission may (1) extend the time or times of payment of the principal of and interest on the Bonds, reduce the principal amount thereof, the redemption price, or the rate of interest thereon, or in any other way modify the terms of payment of the principal of or interest on the Bonds, (2) give any preference to any Bond over any other Bond, or (3) reduce the aggregate principal amount of Bonds required to be held by holders for consent to any such amendment, addition, or rescission.

**BOOK-ENTRY-ONLY SYSTEM . . .** *This section describes how ownership of the Bonds is to be transferred and how the principal of, premium, if any, and interest on the Bonds are to be paid to and credited by The Depository Trust Company (“DTC”), New York, New York, while the Bonds are registered in its nominee name. The information in this section concerning DTC and the Book-Entry-Only System has been provided by DTC for use in disclosure documents such as this Official Statement. The District, the Financial Advisor and the Underwriters believe the source of such information to be reliable, but take no responsibility for the accuracy or completeness thereof.*

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

DTC will act as securities depository for the Bonds. The Bonds will be issued as fully-registered Bonds registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Bond certificate will be issued for each maturity of the Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

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

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

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

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

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

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

All payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the District or the Paying Agent/Registrar, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with Bonds held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Paying Agent/Registrar, or the District, subject to any statutory or regulatory requirements as may be in effect from time to time. All payments on the Bonds to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) are the responsibility of the District or the Paying Agent/Registrar, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

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

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

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

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

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

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

In the event the Book-Entry-Only System should be discontinued, interest on the Bonds will be paid to the registered owners appearing on the registration books of the Paying Agent/Registrar at the close of business on the Record Date (hereinafter defined), and such interest will be paid (i) by check sent United States mail, first class postage prepaid to the address of the registered owner recorded in the registration books of the Paying Agent/Registrar or (ii) by such other method, acceptable to the Paying Agent/Registrar requested by, and at the risk and expense of, the registered owner. Principal of the Bonds will be paid to the registered owner at the stated maturity or earlier redemption upon presentation to the designated payment/transfer office of the Paying Agent/Registrar; provided, however, that so long as Cede & Co. (or other DTC nominee) is the registered owner of the Bonds, all payments will be made as described under "THE BONDS - Book-Entry-Only System" herein. If the date for the payment of the principal of or interest on the Bonds is a Saturday, Sunday, a legal holiday or a day when banking institutions in the city where the designated payment/transfer office of the Paying Agent/Registrar is located are authorized to close, then the date for such payment will be the next succeeding day which is not such a day, and payment on such date will have the same force and effect as if made on the date payment was due.

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

**RECORD DATE FOR INTEREST PAYMENT . . .** The record date (“Record Date”) for the interest payable on the Bonds on any interest payment date means the close of business on the last business day of the preceding month.

In the event of a non-payment of interest on a scheduled payment date, and for 30 days thereafter, a new record date for such interest payment (a “Special Record Date”) will be established by the Paying Agent/Registrar, if and when funds for the payment of such interest have been received from the District. Notice of the Special Record Date and of the scheduled payment date of the past due interest (“Special Payment Date”, which shall be 15 days after the Special Record Date) shall be sent at least five business days prior to the Special Record Date by United States mail, first class, postage prepaid, to the address of each registered owner of a Bond appearing on the registration books of the Paying Agent/Registrar at the close of business on the last business day next preceding the date of mailing of such notice.

**BONDHOLDERS’ REMEDIES . . .** The Order does not establish specific events of default with respect to the Bonds. If the District defaults in the payment of principal, interest or redemption price on the Bonds when due, or if it fails to make payments into any fund or funds created in the Order, or defaults in the observation or performance of any other covenants, conditions or obligations set forth in the Order, and the State fails to honor the Permanent School Fund Guarantee as hereinafter discussed, the registered owners may seek a writ of mandamus to compel District officials to carry out their legally imposed duties with respect to the Bonds if there is no other available remedy at law to compel performance of the covenants contained in the Bonds or in the Order and the District’s obligations are not uncertain or disputed. The issuance of a writ of mandamus is controlled by equitable principles and rests with the discretion of the court, but may not be arbitrarily refused. There is no acceleration of maturity of the Bonds in the event of default and, consequently, the remedy of mandamus may have to be relied upon from year to year. The Order does not provide for the appointment of a trustee to represent the interest of the bondholders upon any failure of the District to perform in accordance with the terms of the Order, or upon any other condition and accordingly all legal actions to enforce such remedies would have to be undertaken at the initiative of, and be financed by, the registered owners. The Texas Supreme Court has ruled in *Tooke v. City of Mexia*, 197 S.W.3d 325 (Tex. 2006), that a waiver of sovereign immunity in a contractual dispute must be provided for by statute in “clear and unambiguous” language. Because it is unclear whether the Texas legislature has effectively waived the District’s sovereign immunity from a suit for money damages, bondholders may not be able to bring such a suit against the District for breach of the Bonds or Order covenants. Chapter 1371, which pertains to the issuance of public securities by issuers such as the District, permits the District to waive sovereign immunity in the proceedings authorizing its bonds, but in connection with the issuance of the Bonds, the District has not waived sovereign immunity and is not using the legal authority provided by Chapter 1371 for such purpose. Even if a judgment against the District could be obtained, it could not be enforced by direct levy and execution against the District’s property. Further, the registered owners cannot themselves foreclose on property within the District or sell property within the District to enforce the tax lien on taxable property to pay the principal of and interest on the Bonds. Furthermore, the District is eligible to seek relief from its creditors under Chapter 9 of the U.S. Bankruptcy Code (“Chapter 9”). Although Chapter 9 provides for the recognition of a security interest represented by a specifically pledged source of revenues, the pledge of ad valorem taxes in support of a general obligation of a bankrupt entity is not specifically recognized as a security interest under Chapter 9. Chapter 9 also includes an automatic stay provision that would prohibit, without Bankruptcy Court approval, the prosecution of any other legal action by creditors or bondholders of an entity which has sought protection under Chapter 9. Therefore, should the District avail itself of Chapter 9 protection from creditors, the ability to enforce would be subject to the approval of the Bankruptcy Court (which could require that the action be heard in Bankruptcy Court instead of other federal or state court); and the Bankruptcy Code provides for broad discretionary powers of a Bankruptcy Court in administering any proceeding brought before it. See “THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM” herein for a description of the procedures to be followed for payment of the Bonds by the Permanent School Fund in the event the District fails to make a payment on the Bonds when due. The opinion of Bond Counsel will note that all opinions relative to the enforceability of the Bonds are qualified with respect to

the customary rights of debtors relative to their creditors and by general principles of equity which permit the exercise of judicial discretion.

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

<u>Sources of Funds</u>	
Par Amount of the Bonds	\$ 37,160,000.00
Plus: Net Reoffering Premium	3,343,985.20
Total Sources of Funds	<u>\$ 40,503,985.20</u>
<u>Uses of Funds</u>	
Deposit to Construction Fund	\$ 40,000,000.00
Underwriter's Discount and Costs of Issuance	503,985.20
Total Uses of Funds	<u>\$ 40,503,985.20</u>

### **THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM**

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

This disclosure statement provides information relating to the program (the “Guarantee Program”) administered by the Texas Education Agency (the “TEA”) with respect to the Texas Permanent School Fund guarantee of tax-supported bonds issued by Texas school districts and the guarantee of revenue bonds issued by or for the benefit of Texas charter districts. The Guarantee Program was authorized by an amendment to the Texas Constitution in 1983 and by Subchapter C of Chapter 45 of the Texas Education Code, as amended (the “Act”). While the Guarantee Program applies to bonds issued by or for both school districts and charter districts, as described below, the Act and the program rules for the two types of districts have some distinctions. For convenience of description and reference, those aspects of the Guarantee Program that are applicable to school district bonds and to charter district bonds are referred to herein as the “School District Bond Guarantee Program” and the “Charter District Bond Guarantee Program,” respectively.

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

#### **HISTORY AND PURPOSE**

The PSF was created with a \$2,000,000 appropriation by the Texas Legislature (the “Legislature”) in 1854 expressly for the benefit of the public schools of Texas. The Constitution of 1876 stipulated that certain lands and all proceeds from the sale of these lands should also constitute the PSF. Additional acts later gave more public domain land and rights to the PSF. In 1953, the U.S. Congress passed the Submerged Lands Act that relinquished to coastal states all rights of the U.S. navigable waters within state boundaries. If the state, by law, had set a larger boundary prior to or at the time of admission to the Union, or if the boundary had been approved by Congress, then the larger boundary applied. After three years of litigation (1957-1960), the U. S. Supreme Court on May 31, 1960, affirmed Texas’ historic three marine leagues (10.35 miles) seaward boundary. Texas proved its submerged lands property rights to three leagues into the Gulf of Mexico by citing historic laws and treaties dating back to 1836. All lands lying within that limit belong to the PSF. The proceeds from the sale and the mineral-related rental of these lands, including bonuses, delay rentals and royalty payments, become the corpus of the Fund. Prior to the approval by the voters of the State of an amendment to the constitutional provision under which the Fund is established and administered, which occurred on September 13, 2003 (the “Total Return Constitutional Amendment”), and which is further described below, the PSF had as its main sources of revenues capital gains from securities transactions and royalties from the sale of oil and natural gas. The Total Return Constitutional Amendment provides that interest and dividends produced by Fund investments will be additional revenue to the PSF. The State School Land Board (“SLB”) maintains the land endowment of the Fund on behalf of the Fund and is authorized to manage the investments of the capital gains, royalties and other investment income relating to the land endowment. The SLB is a three member board, the membership of which consists of the Commissioner of the Texas General Land Office (the “Land Commissioner”) and two citizen members, one appointed by the Governor and one by the Texas Attorney General (the “Attorney General”). As of August 31, 2017, the General Land Office (the “GLO”) managed approximately 21% of the PSF, as reflected in the fund balance of the PSF at that date.

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

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

In 2011, legislation was enacted that established the Charter District Bond Guarantee Program as a new component of the Guarantee Program. That legislation authorized the use of the PSF to guarantee revenue bonds issued by or for the benefit of certain open-enrollment charter schools that are designated as “charter districts” by the Commissioner. On approval by the Commissioner, bonds properly issued by a charter district participating in the Program are fully guaranteed by the corpus of the PSF. As described below, the implementation of the Charter District Bond Guarantee Program was deferred pending receipt of guidance from the Internal Revenue Service (the “IRS”) which was received in September 2013, and the establishment of regulations to govern the program, which regulations became effective on March 3, 2014. See “The Charter District Bond Guarantee Program.”

State law also permits charter schools to be chartered and operated by school districts and other political subdivisions, but bond financing of facilities for school district-operated charter schools is subject to the School District Bond Guarantee Program, not the Charter District Bond Guarantee Program.

While the School District Bond Guarantee Program and the Charter District Bond Guarantee Program relate to different types of bonds issued for different types of Texas public schools, and have different program regulations and requirements, a bond guaranteed under either part of the Guarantee Program has the same effect with respect to the guarantee obligation of the Fund thereto, and all guaranteed bonds are aggregated for purposes of determining the capacity of the Guarantee Program (see “Capacity Limits for the Guarantee Program”). The Charter District Bond Guarantee Program as enacted by State law has not been reviewed by any court, nor has the Texas Attorney General been requested to issue an opinion, with respect to its constitutional validity.

The sole purpose of the PSF is to assist in the funding of public education for present and future generations. Prior to the adoption of the Total Return Constitutional Amendment, all interest and dividends produced by Fund investments flowed into the Available School Fund (the “ASF”), where they are distributed to local school districts and open-enrollment charter schools based on average daily attendance. Any net gains from investments of the Fund accrue to the corpus of the PSF. Prior to the approval by the voters of the State of the Total Return Constitutional Amendment, costs of administering the PSF were allocated to the ASF. With the approval of the Total Return Constitutional Amendment, the administrative costs of the Fund have shifted from the ASF to the PSF. In fiscal year 2018, preliminary, unaudited distributions to the ASF amounted to an estimated \$246.92 per student and the total amount distributed to the ASF was \$1,235.8 million.

Audited financial information for the PSF is provided annually through the PSF Comprehensive Annual Financial Report (the “Annual Report”), which is filed with the Municipal Securities Rulemaking Board (“MSRB”). The Annual Report includes the Message of the Executive Administrator of the Fund (the “Message”) and the Management’s Discussion and Analysis (“MD&A”). The Annual Report for the year ended August 31, 2017, as filed with the MSRB in accordance with the PSF undertaking and agreement made in accordance with Rule 15c2-12 (“Rule 15c2-12”) of the federal Securities and Exchange Commission (the “SEC”), as described below, is hereby incorporated by reference into this disclosure. Information included herein for the year ended August 31, 2017 is derived from the audited financial statements of the PSF, which are included in the Annual Report when it is filed and posted. Reference is made to the Annual Report for the complete Message and MD&A for the year ended August 31, 2017 and for a description of the financial results of the PSF for the year ended August 31, 2017, the most recent year for which audited financial information regarding the Fund is available. The 2017 Annual Report speaks only as of its date and the TEA has not obligated itself to update the 2017 Annual Report or any other Annual Report. The TEA posts each Annual Report, which includes statistical data regarding the Fund as of the close of each fiscal year, the most recent disclosure for the Guarantee Program, the Statement of Investment Objectives, Policies and Guidelines of the Texas Permanent School Fund, which is codified at 19 Texas Administrative Code, Chapter 33 (the “Investment Policy”), monthly updates with respect to the capacity of the Guarantee Program (collectively, the “Web Site Materials”) on the TEA web site at [http://tea.texas.gov/Finance\\_and\\_Grants/Permanent\\_School\\_Fund/](http://tea.texas.gov/Finance_and_Grants/Permanent_School_Fund/) and with the MSRB at [www.emma.msrb.org](http://www.emma.msrb.org). Such monthly updates regarding the Guarantee Program are also incorporated herein and made a part hereof for all purposes. In addition to the Web Site Materials, the Fund is required to make quarterly filings with the SEC under Section 13(f) of the Securities Exchange Act of 1934. Such filings, which consist of a list of the Fund’s holdings of securities specified in Section 13(f), including exchange-traded (*e.g.*, NYSE) or NASDAQ-quoted stocks, equity options and warrants, shares of closed-end investment companies and certain convertible debt securities, is available from the SEC at [www.sec.gov/edgar.shtml](http://www.sec.gov/edgar.shtml). A list of the Fund’s equity and fixed income holdings as of August 31 of each year is posted to the TEA web site and filed with the MSRB. Such list excludes holdings in the Fund’s securities lending program. Such list, as filed, is incorporated herein and made a part hereof for all purposes.

## THE TOTAL RETURN CONSTITUTIONAL AMENDMENT

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

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

See “2011 Constitutional Amendment” below for a discussion of the historic and current Distribution Rates, and a description of amendments made to the Texas Constitution on November 8, 2011 that may affect Distribution Rate decisions.

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

With respect to the management of the Fund’s financial assets portfolio, the single most significant change made to date as a result of the Total Return Constitutional Amendment has been new asset allocation policies adopted from time to time by the SBOE. The SBOE generally reviews the asset allocations during its summer meeting in even numbered years. The first asset allocation policy adopted by the SBOE following the Total Return Constitutional Amendment was in February 2004, and the policy was reviewed and modified or reaffirmed in the summers of each even-numbered year, most recently in 2018. The Fund’s investment policy provides for minimum and maximum ranges among the components of each of the asset classifications: equities, fixed income and alternative asset investments. The 2004 asset allocation policy decreased the fixed income target from 45% to 25% of Fund investment assets and increased the allocation for equities from 55% to 75% of investment assets. Subsequent asset allocation policies have continued to diversify Fund assets, and have added an alternative asset allocation to the fixed income and equity allocations. The alternative asset allocation category includes real estate, real return, absolute return and private equity components. Alternative asset classes diversify the SBOE-managed assets and are not as correlated to traditional asset classes, which is intended to increase investment returns over the long run while reducing risk and return volatility of the portfolio. The most recent asset allocation, from 2016, which was reviewed and reaffirmed in June 2018, is as follows: (i) an equity allocation of 35% (consisting of U.S. large cap equities targeted at 13%, international equities at 14% and emerging international equities at 3%) and U.S. small/mid cap equities at 5%), (ii) a fixed income allocation of 19% (consisting of a 12% allocation for core bonds and a 7% allocation for emerging market debt in local currency) and (iii) an alternative asset allocation of 46% (consisting of a private equity allocation of 13%, a real estate allocation of 10%, an absolute return allocation

of 10%, a risk parity allocation of 7% and a real return allocation of 6%). The 2016 asset allocation decreased U.S. large cap equities and international equities by 3% and 2%, respectively, and increased the allocations for private equity and real estate by 3% and 2%, respectively.

For a variety of reasons, each change in asset allocation for the Fund, including the 2016 modifications, have been implemented in phases, and that approach is likely to be carried forward when and if the asset allocation policy is again modified. At August 31, 2018, the Fund's financial assets portfolio was invested as follows: 40.54% in public market equity investments; 13.25% in fixed income investments; 10.37% in absolute return assets; 9.12% in private equity assets; 7.48% in real estate assets; 6.79% in risk parity assets; 5.96% in real return assets; 6.21% in emerging market debt; and 0.28% in unallocated cash. August 31, 2018 data is unaudited, which is subject to adjustment.

Following on previous decisions to create strategic relationships with investment managers in certain asset classes, in September 2015 and January 2016, the SBOE approved the implementation of direct investment programs in private equity and absolute return assets, respectively, which has continued to reduce administrative costs with respect to those portfolios. The Attorney General has advised the SBOE in Op. Tex. Att'y Gen. No. GA-0998 (2013) ("GA-0998"), that the PSF is not subject to requirements of certain State competitive bidding laws with respect to the selection of investments. In GA-0998, the Attorney General also advised that the SBOE generally must use competitive bidding for the selection of investment managers and other third party providers of investment services, such as record keeping and insurance, but excluding certain professional services, such as accounting services, as State law prohibits the use of competitive bidding for specified professional services. GA-0998 provides guidance to the SBOE in connection with the direct management of alternative investments through investment vehicles to be created by the SBOE, in lieu of contracting with external managers for such services, as has been the recent practice of the PSF. The PSF staff and the Fund's investment advisor are tasked with advising the SBOE with respect to the implementation of the Fund's asset allocation policy, including the timing and manner of the selection of any external managers and other consultants.

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

The asset allocation of the Fund's financial assets portfolio is subject to change by the SBOE from time to time based upon a number of factors, including recommendations to the SBOE made by internal investment staff and external consultants, changes made by the SBOE without regard to such recommendations and directives of the Legislature. Fund performance may also be affected by factors other than asset allocation, including, without limitation, the general performance of the securities markets in the United States and abroad; political and investment considerations including those relating to socially responsible investing; economic impacts relating to domestic and international climate change; development of hostilities in and among nations; cybersecurity issues that affect the securities markets, changes in international trade policies, economic activity and investments, in general, application of the prudent person investment standard, which may eliminate certain investment opportunities for the Fund; management fees paid to external managers and embedded management fees for some fund investments; and limitations on the number and compensation of internal and external investment staff, which is subject to legislative oversight. The Guarantee Program could also be impacted by changes in State or federal law or the implementation of new accounting standards.

#### **MANAGEMENT AND ADMINISTRATION OF THE FUND**

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

The Total Return Constitutional Amendment provides that expenses of managing the PSF are to be paid "by appropriation" from the PSF. In January 2005, at the request of the SBOE, the Attorney General issued a legal opinion, Op. Tex. Att'y Gen. No. GA-0293 (2005), that the Total Return Constitutional Amendment requires that SBOE expenditures for managing or administering

PSF investments, including payments to external investment managers, be paid from appropriations made by the Legislature, but that the Total Return Constitutional Amendment does not require the SBOE to pay from such appropriated PSF funds the indirect management costs deducted from the assets of a mutual fund or other investment company in which PSF funds have been invested.

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

The SBOE contracts with its securities custodial agent to measure the performance of the total return of the Fund's financial assets. A consultant is typically retained for the purpose of providing consultation with respect to strategic asset allocation decisions and to assist the SBOE in selecting external fund management advisors. The SBOE also contracts with financial institutions for custodial and securities lending services. Like other State agencies and instrumentalities that manage large investment portfolios, the PSF has implemented an incentive compensation plan that may provide additional compensation for investment personnel, depending upon the criteria relating to the investment performance of the Fund.

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

#### **CAPACITY LIMITS FOR THE GUARANTEE PROGRAM**

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

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

On September 16, 2013, the IRS published proposed regulations (the “Proposed IRS Regulations”) that, among other things, would enact the IRS Notice. The preamble to the Proposed IRS Regulations provides that issuers may elect to apply the Proposed IRS Regulations, in whole or in part, to bonds sold on or after September 16, 2013, and before the date that final regulations become effective.

On July 18, 2016, the IRS issued final regulations enacting the IRS Notice (the “Final IRS Regulations”). The Final IRS Regulations are effective for bonds sold on or after October 17, 2016. The IRS Notice, the Proposed IRS Regulations and the Final IRS Regulations establish a static capacity for the Guarantee Program based upon the cost value of Fund assets on December 16, 2009 multiplied by five. On December 16, 2009, the cost value of the Guarantee Program was \$23,463,730,608 (estimated and unaudited), thereby producing an IRS Limit of approximately \$117.3 billion. The State Capacity Limit is determined on the basis of the cost value of the Fund from time to time multiplied by the capacity multiplier determined annually by the SBOE, but not to exceed a multiplier of five. The capacity of the Guarantee Program will be limited to the lower of the State Capacity Limit or the IRS Limit. On May 21, 2010, the SBOE modified the regulations that govern the School District Bond Guarantee Program (the “SDBGP Rules”), and increased the State Law Capacity to an amount equal to three times the cost value of the PSF. Such modified regulations, including the revised capacity rule, became effective on July 1, 2010. The SDBGP Rules provide that the Commissioner may reduce the multiplier to maintain the AAA credit rating of the Guarantee Program, but provide that any changes to the multiplier made by the Commissioner are to be ratified or rejected by the SBOE at the next meeting following the change. See “Valuation of the PSF and Guaranteed Bonds,” below.

At its September 2015 meeting, the SBOE voted to modify the SDBGP Rules and the CDBGP Rules to increase the State Law Capacity from 3 times the cost value multiplier to 3.25 times. At that meeting, the SBOE also approved a new 5% capacity reserve for the Charter District Bond Guarantee Program. The change to the State Law Capacity became effective on February 1, 2016. At its November 2016 meeting, the SBOE again voted to increase the State Law Capacity and, in accordance with applicable requirements for the modification of SDBGP and CDBGP Rules, a second and final vote to approve the increase in the State Law Capacity occurred on February 3, 2017. As a result, the State Law Capacity increased from 3.25 times the cost value multiplier to 3.50 times effective March 1, 2017 and increased again to 3.75 times effective September 1, 2017; however, as described under “2017 Legislative Changes to the Charter District Bond Guarantee Program,” the SBOE took action at its Winter 2018 meeting to rollback of a portion of the multiplier increase, which became effective in late March 2018. Based upon the unaudited cost basis of the Fund at August 31, 2018, the State Law Capacity increased from \$111,568,711,072 on August 31, 2017 to \$118,867,137,998 on August 31, 2018 (but at such date the IRS Limit was lower, \$117,318,653,038, so it is the currently effective capacity limit for the Fund).

Since July 1991, when the SBOE amended the Guarantee Program Rules to broaden the range of bonds that are eligible for guarantee under the Guarantee Program to encompass most Texas school district bonds, the principal amount of bonds guaranteed under the Guarantee Program has increased sharply. In addition, in recent years a number of factors have caused an increase in the amount of bonds issued by school districts in the State. See the table “Permanent School Fund Guaranteed Bonds” below. Effective September 1, 2009, the Act provides that the SBOE may annually establish a percentage of the cost value of the Fund to be reserved from use in guaranteeing bonds. The capacity of the Guarantee Program in excess of any reserved portion is referred to herein as the “Capacity Reserve.” The SDBGP Rules provide for a minimum Capacity Reserve for the overall Guarantee Program of no less than 5%, and provide that the amount of the Capacity Reserve may be increased by a majority vote of the SBOE. The CDBGP Rules provide for an additional 5% reserve of CDBGP capacity. The Commissioner is authorized to change the Capacity Reserve, which decision must be ratified or rejected by the SBOE at its next meeting following any change made by the Commissioner. The current Capacity Reserve is noted in the monthly updates with respect to the capacity of the Guarantee Program on the TEA web site at [http://tea.texas.gov/Finance\\_and\\_Grants/Permanent\\_School\\_Fund/](http://tea.texas.gov/Finance_and_Grants/Permanent_School_Fund/), which are also filed with the MSRB.

Based upon historical performance of the Fund, the legal restrictions relating to the amount of bonds that may be guaranteed has generally resulted in a lower ratio of guaranteed bonds to available assets as compared to many other types of credit enhancements that may be available for Texas school district bonds and charter district bonds. However, changes in the value of the Fund due to changes in securities markets, investment objectives of the Fund, an increase in bond issues by school districts in the State or legal restrictions on the Fund, the implementation of the Charter District Bond Guarantee Program, or an increase in the calculation base of the Fund for purposes of making transfers to the ASF, among other factors, could adversely affect the ratio of Fund assets to guaranteed bonds and the growth of the Fund in general. It is anticipated that the issuance of the IRS Notice and the Proposed IRS Regulations will likely result in a substantial increase in the amount of bonds guaranteed under the Guarantee Program. The implementation of the Charter School Bond Guarantee Program is also expected to increase the amount of guaranteed bonds.

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

## **THE SCHOOL DISTRICT BOND GUARANTEE PROGRAM**

The School District Bond Guarantee Program requires an application be made by a school district to the Commissioner for a guarantee of its bonds. If the conditions for the School District Bond Guarantee Program are satisfied, the guarantee becomes effective upon approval of the bonds by the Attorney General and remains in effect until the guaranteed bonds are paid or defeased, by a refunding or otherwise.

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

If a school district fails to pay principal or interest on a bond as it is stated to mature, other amounts not due and payable are not accelerated and do not become due and payable by virtue of the district's default. The School District Bond Guarantee Program does not apply to the payment of principal and interest upon redemption of bonds, except upon mandatory sinking fund redemption, and does not apply to the obligation, if any, of a school district to pay a redemption premium on its guaranteed bonds. The guarantee applies to all matured interest on guaranteed school district bonds, whether the bonds were issued with a fixed or variable interest rate and whether the interest rate changes as a result of an interest reset provision or other bond order provision requiring an interest rate change. The guarantee does not extend to any obligation of a school district under any agreement with a third party relating to guaranteed bonds that is defined or described in State law as a "bond enhancement agreement" or a "credit agreement," unless the right to payment of such third party is directly as a result of such third party being a bondholder.

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

Generally, the SDBGP Rules limit guarantees to certain types of notes and bonds, including, with respect to refunding bonds issued by school districts, a requirement that the bonds produce debt service savings, and that bonds issued for capital facilities of school districts must have been voted as unlimited tax debt of the issuing district. The Guarantee Program Rules include certain accreditation criteria for districts applying for a guarantee of their bonds, and limit guarantees to districts that have less than the amount of annual debt service per average daily attendance that represents the 90th percentile of annual debt service per average daily attendance for all school districts, but such limitation will not apply to school districts that have enrollment growth of at least 25% over the previous five school years. The SDBGP Rules are codified in the Texas Administrative Code at 19 TAC section 33.65, and are available at <http://ritter.tea.state.tx.us/rules/tac/chapter033/ch033a.html#33.65>.

## **THE CHARTER DISTRICT BOND GUARANTEE PROGRAM**

The Charter District Bond Guarantee Program became effective March 3, 2014. The SBOE published final regulations in the Texas Register that provide for the administration of the Charter District Bond Guarantee Program (the "CDBGP Rules"). The CDBGP Rules are codified at 19 TAC section 33.67, and are available at <http://ritter.tea.state.tx.us/rules/tac/chapter033/ch033a.html#33.67>.

The Charter District Bond Guarantee Program has been authorized through the enactment of amendments to the Act, which provide that a charter holder may make application to the Commissioner for designation as a "charter district" and for a guarantee by the PSF under the Act of bonds issued on behalf of a charter district by a non-profit corporation. If the conditions for the Charter District Bond Guarantee Program are satisfied, the guarantee becomes effective upon approval of the bonds by the Attorney General and remains in effect until the guaranteed bonds are paid or defeased, by a refunding or otherwise.

As of February 21, 2018 (the most recent date for which data is available), the percentage of students enrolled in open-enrollment charter schools (excluding charter schools authorized by school districts) to the total State scholastic census was approximately 5.5%. As of November 5, 2018, there were 177 active open-enrollment charter schools in the State and there were 754 charter school campuses operating under such charters. Section 12.101, Texas Education Code, as amended by the Legislature in 2013, limits the number of charters that the Commissioner may grant to 215 charters as of the end of fiscal year 2014, with the number increasing in each fiscal year thereafter through 2019 to a total number of 305 charters. While legislation limits the number of charters that may be granted, it does not limit the number of campuses that may operate under a particular charter. For information regarding the capacity of the Guarantee Program, see "Capacity Limits for the Guarantee Program." The Act provides that the Commissioner may not approve the guarantee of refunding or refinanced bonds under the Charter District Bond Guarantee Program in a total amount that exceeds one-half of the total amount available for the guarantee of charter district bonds under the Charter District Bond Guarantee Program.

In accordance with the Act, the Commissioner may not approve charter district bonds for guarantee if such guarantees will result in lower bond ratings for public school district bonds that are guaranteed under the School District Bond Guarantee Program. To be eligible for a guarantee, the Act provides that a charter district's bonds must be approved by the Attorney General, have an unenhanced investment grade rating from a nationally recognized investment rating firm, and satisfy a limited investigation conducted by the TEA.

The Charter District Bond Guarantee Program does not apply to the payment of principal and interest upon redemption of bonds, except upon mandatory sinking fund redemption, and does not apply to the obligation, if any, of a charter district to pay a redemption premium on its guaranteed bonds. The guarantee applies to all matured interest on guaranteed charter district bonds, whether the bonds were issued with a fixed or variable interest rate and whether the interest rate changes as a result of an interest reset provision or other bond resolution provision requiring an interest rate change. The guarantee does not extend to any obligation of a charter district under any agreement with a third party relating to guaranteed bonds that is defined or described in State law as a "bond enhancement agreement" or a "credit agreement," unless the right to payment of such third party is directly as a result of such third party being a bondholder.

The Act provides that immediately following receipt of notice that a charter district will be or is unable to pay maturing or matured principal or interest on a guaranteed bond, the Commissioner is required to instruct the Comptroller to transfer from the Charter District Reserve Fund to the district's paying agent an amount necessary to pay the maturing or matured principal or interest. If money in the Charter District Reserve Fund is insufficient to pay the amount due on a bond for which a notice of default has been received, the Commissioner is required to instruct the Comptroller to transfer from the PSF to the district's paying agent the amount necessary to pay the balance of the unpaid maturing or matured principal or interest. If a total of two or more payments are made under the Charter District Bond Guarantee Program on charter district bonds and the Commissioner determines that the charter district is acting in bad faith under the program, the Commissioner may request the Attorney General to institute appropriate legal action to compel the charter district and its officers, agents, and employees to comply with the duties required of them by law in regard to the guaranteed bonds. As is the case with the School District Bond Guarantee Program, the Act provides a funding "intercept" feature that obligates the Commissioner to instruct the Comptroller to withhold the amount paid with respect to the Charter District Bond Guarantee Program, plus interest, from the first State money payable to a charter district that fails to make a guaranteed payment on its bonds. The amount withheld will be deposited, first, to the credit of the PSF, and then to restore any amount drawn from the Charter District Reserve Fund as a result of the non-payment.

The CDBGP Rules provide that the PSF may be used to guarantee bonds issued for the acquisition, construction, repair, or renovation of an educational facility for an open-enrollment charter holder and equipping real property of an open-enrollment charter school and/or to refinance promissory notes executed by an open-enrollment charter school, each in an amount in excess of \$500,000 the proceeds of which loans were used for a purposes described above (so-called new money bonds) or for refinancing bonds previously issued for the charter school that were approved by the attorney general (so-called refunding bonds). Refunding bonds may not be guaranteed under the Charter District Bond Guarantee Program if they do not result in a present value savings to the charter holder.

The CDBGP Rules provide that an open-enrollment charter holder applying for charter district designation and a guarantee of its bonds under the Charter District Bond Guarantee Program satisfy various provisions of the regulations, including the following: It must (i) have operated at least one open-enrollment charter school with enrolled students in the State for at least three years; (ii) agree that the bonded indebtedness for which the guarantee is sought will be undertaken as an obligation of all entities under common control of the open-enrollment charter holder, and that all such entities will be liable for the obligation if the open-enrollment charter holder defaults on the bonded indebtedness, provided, however, that an entity that does not operate a charter school in Texas is subject to this provision only to the extent it has received state funds from the open-enrollment charter holder; (iii) have had completed for the past three years an audit for each such year that included unqualified or unmodified audit opinions; and (iv) have received an investment grade credit rating within the last year. Upon receipt of an application for guarantee under the Charter District Bond Guarantee Program, the Commissioner is required to conduct an investigation into the financial status of the applicant charter district and of the accreditation status of all open-enrollment charter schools operated under the charter, within the scope set forth in the CDBGP Rules. Such financial investigation must establish that an applying charter district has a historical debt service coverage ratio, based on annual debt service, of at least 1.1 for the most recently

completed fiscal year, and a projected debt service coverage ratio, based on projected revenues and expenses and maximum annual debt service, of at least 1.2. The failure of an open-enrollment charter holder to comply with the Act or the applicable regulations, including by making any material misrepresentations in the charter holder's application for charter district designation or guarantee under the Charter District Bond Guarantee Program, constitutes a material violation of the open-enrollment charter holder's charter.

Beginning in July 2015, TEA began limiting new guarantees under the Charter District Bond Guarantee Program to conform to the Act and, subsequently, with CDBGP Rules that require the maintenance of a capacity reserve for the Charter District Bond Guarantee Program. Following the increase in the Program multiplier in February 2016 and the update of the percentage of students enrolled in open-enrollment charter schools to the total State scholastic census in March 2016, some new capacity became available under the Charter District Bond Guarantee Program, but that capacity was quickly exhausted. In accordance with the action of the SBOE on February 3, 2017, additional capacity for the Charter District Bond Guarantee Program became effective in two increments, implemented on March 1, 2017 and on September 1, 2017 (as described under "2017 Legislative Changes to the Charter District Bond Guarantee Program," an item to reverse the September 1, 2017 increase in the Program multiplier was approved by the SBOE at its Winter 2018 meeting). In addition, legislation enacted during the Legislature's 2017 regular session modifies the manner of calculating the capacity of the Charter District Bond Guarantee Program (the "CDBGP Capacity"), which further increases the amount of the CDBGP Capacity, beginning with State fiscal year 2018, but that provision of the law does not increase overall Program capacity, it merely allocates capacity between the School District Bond Guarantee Program and the Charter District Bond Guarantee Program. See "Capacity Limits for the Guarantee Program" and "2017 Legislative Changes to the Charter District Bond Guarantee Program." Other factors that could increase the CDBGP Capacity include Fund investment performance, future increases in the Guarantee Program multiplier, changes in State law that govern the calculation of the CDBGP Capacity, as described below, growth in the relative percentage of students enrolled in open-enrollment charter schools to the total State scholastic census, legislative and administrative changes in funding for charter districts, changes in level of school district or charter district participation in the Program, or a combination of such circumstances.

#### **2017 LEGISLATIVE CHANGES TO THE CHARTER DISTRICT BOND GUARANTEE PROGRAM**

The CDBGP Capacity is established by the Act. During the 85th Texas Legislature, which concluded on May 29, 2017, Senate Bill 1480 ("SB 1480") was enacted. The complete text of SB 1480 can be found at <http://www.capitol.state.tx.us/tlodocs/85R/billtext/pdf/SB01480F.pdf#navpanes=0>. SB 1480 modified how the CDBGP Capacity will be established under the Act effective as of September 1, 2017, and made other substantive changes to the Act that affects the Charter District Bond Guarantee Program. Prior to the enactment of SB 1480, the CDBGP Capacity was calculated as the State Capacity Limit less the amount of outstanding bond guarantees under the Guarantee Program multiplied by the percentage of charter district scholastic population relative to the total public school scholastic population. As of September 30, 2018, the amount of outstanding bond guarantees represented 68.04% of the IRS Limit (which is currently the applicable capacity limit) for the Guarantee Program (based on unaudited data). SB 1480 amended the CDBGP Capacity calculation so that the State Capacity Limit is multiplied by the percentage of charter district scholastic population relative to the total public school scholastic population prior to the subtraction of the outstanding bond guarantees, thereby potentially substantially increasing the CDBGP Capacity. However, certain provisions of SB 1480, described below, and other additional factors described herein, could result in less than the maximum amount of the potential increase provided by SB 1480 being implemented by the SBOE or otherwise used by charter districts. Still other factors used in determining the CDBGP Capacity, such as the percentage of the charter district scholastic population to the overall public school scholastic population, could, in and of itself, increase the CDBGP Capacity, as that percentage has grown from 3.53% in September, 2012 to 5.50% in September 2018, representing a cumulative growth during that period of 55.81%. TEA is unable to predict how the ratio of charter district students to the total State scholastic population will change over time.

SB 1480 provides that the implementation of the new method of calculating the CDBGP Capacity will begin with the State fiscal year that commences September 1, 2021 (the State's fiscal year 2022). However, for the intervening four fiscal years, beginning with fiscal year 2018, SB 1480 provides that the SBOE may establish a CDBGP Capacity that increases the amount of charter district bonds that may be guaranteed by up to a cumulative 20% in each fiscal year (for a total maximum increase of 80% in fiscal year 2021) as compared to the capacity figure calculated under the Act as of January 1, 2017. However, SB 1480 provides that in making its annual determination of the magnitude of an increase for any year, the SBOE may establish a lower (or no) increase if the SBOE determines that an increase in the CDBGP Capacity would likely result in a negative impact on the bond ratings for the Bond Guarantee Program (see "Ratings of Bonds Guaranteed Under the Guarantee Program") or if one or more charter districts default on payment of principal or interest on a guaranteed bond, resulting in a negative impact on the bond ratings of the Bond Guarantee Program. The provisions of SB 1480 that provide for discretionary, incremental increases in the CDBGP expire September 1, 2022. If the SBOE makes a determination for any year based upon the potential ratings impact on the Bond Guarantee Program and modifies the increase that would otherwise be implemented under SB 1480 for that year, the SBOE may also make appropriate adjustments to the schedule for subsequent years to reflect the modification, provided that the CDBGP Capacity for any year may not exceed the limit provided in the schedule set forth in SB 1480. In September 2017 and June 2018, the SBOE authorized the full 20% increase in the amount of charter district bonds that may be guaranteed for fiscal

years 2018 and 2019, respectively, which increases the relative capacity of the Charter District Bond Guarantee Program to the School District Bond Guarantee Program for those fiscal years.

Taking into account the enactment of SB 1480 and the increase in the CDBGP Capacity effected thereby, at Winter 2018 meeting the SBOE approved the second of two required readings amending the SDBGP Rules to rollback the multiplier from 3.75 times market value to 3.50 times, and the rollback became effective in late March 2018.

In addition to modifying the manner of determining the CDBGP Capacity, SB 1480 provides that the Commissioner, in making a determination as to whether to approve a guarantee for a charter district, may consider any additional reasonable factor that the Commissioner determines to be necessary to protect the Bond Guarantee Program or minimize risk to the PSF, including: (1) whether the charter district had an average daily attendance of more than 75 percent of its student capacity for each of the preceding three school years, or for each school year of operation if the charter district has not been in operation for the preceding three school years; (2) the performance of the charter district under certain performance criteria set forth in Education Code Sections 39.053 and 39.054; and (3) any other indicator of performance that could affect the charter district's financial performance. Also, SB 1480 provides that the Commissioner's investigation of a charter district application for guarantee may include an evaluation of whether the charter district bond security documents provide a security interest in real property pledged as collateral for the bond and the repayment obligation under the proposed guarantee. The Commissioner may decline to approve the application if the Commissioner determines that sufficient security is not provided. The Act and the CDBGP Rules previously required the Commissioner to make an investigation of the accreditation status and certain financial criteria for a charter district applying for a bond guarantee, which remain in place.

Since the initial authorization of the Charter District Bond Guarantee Program, the Act has established a bond guarantee reserve fund in the State treasury (the "Charter District Reserve Fund"). Formerly, the Act provided that each charter district that has a bond guaranteed must annually remit to the Commissioner, for deposit in the Charter District Reserve Fund, an amount equal to 10 percent of the savings to the charter district that is a result of the lower interest rate on its bonds due to the guarantee by the PSF. SB 1480 modified the Act insofar as it pertains to the Charter District Reserve Fund. Effective September 1, 2017, the Act provides that a charter district that has a bond guaranteed must remit to the Commissioner, for deposit in the Charter District Reserve Fund, an amount equal to 20 percent of the savings to the charter district that is a result of the lower interest rate on the bond due to the guarantee by the PSF. The amount due shall be paid on receipt by the charter district of the bond proceeds. However, the deposit requirement will not apply if the balance of the Charter District Reserve Fund is at least equal to three percent (3.00%) of the total amount of outstanding guaranteed bonds issued by charter districts. As of September 30, 2018, the Charter District Reserve Fund represented approximately 0.50% of the guaranteed charter district bonds. SB 1480 also authorized the SBOE to manage the Charter District Reserve Fund in the same manner as it manages the PSF. Previously, the Charter District Reserve Fund was held by the Comptroller, but effective April 1 2018, the management of the Reserve Fund was transferred to the PSF division of TEA, where it will be held and invested as a non-commingled fund under the administration of the PSF staff.

#### **CHARTER DISTRICT RISK FACTORS**

Open-enrollment charter schools in the State may not charge tuition and, unlike school districts, charter districts have no taxing power. Funding for charter district operations is largely from amounts appropriated by the Legislature. The amount of such State payments a charter district receives is based on a variety of factors, including the enrollment at the schools operated by a charter district. The overall amount of education aid provided by the State for charter schools in any year is also subject to appropriation by the Legislature. The Legislature may base its decisions about appropriations for charter schools on many factors, including the State's economic performance. Further, because some public officials, their constituents, commentators and others have viewed charter schools as controversial, political factors may also come to bear on charter school funding, and such factors are subject to change.

Other than credit support for charter district bonds that is provided to qualifying charter districts by the Charter District Bond Guarantee Program, under current law, open-enrollment charter schools generally do not receive a dedicated funding allocation from the State to assist with the construction and acquisition of new facilities. However, during the 85th Regular Session of the Legislature in 2017, legislation was enacted that, for the first time, provided a limited appropriation in the amount of \$60 million for the 2018-2019 biennium for charter districts having an acceptable performance rating. A charter district that receives funding under this program may use the funds to lease or pay property taxes imposed on an instructional facility; to pay debt service on bonds that financed an instructional facility; or for any other purpose related to the purchase, lease, sale, acquisition, or maintenance of an instructional facility. Charter schools generally issue revenue bonds to fund facility construction and acquisition, or fund facilities from cash flows of the school. Some charter districts have issued non-guaranteed debt in addition to debt guaranteed under the Charter District Bond Guarantee Program, and such non-guaranteed debt is likely to be secured by a deed of trust covering all or part of the charter district's facilities. In March 2017, the TEA began requiring charter districts to provide the TEA with a lien against charter district property as a condition to receiving a guarantee under the Charter District Bond Guarantee Program. However, charter district bonds issued and guaranteed under the Charter District Bond Guarantee Program prior to the implementation of the new requirement did not have the benefit of a security interest in real property,

although other existing debts of such charter districts that are not guaranteed under the Charter District Bond Guarantee Program may be secured by real property that could be foreclosed on in the event of a bond default.

The maintenance of a State-granted charter is dependent upon on-going compliance with State law and TEA regulations, and TEA monitors compliance with applicable standards. TEA has a broad range of enforcement and remedial actions that it can take as corrective measures, and such actions may include the loss of the State charter, the appointment of a new board of directors to govern a charter district, the assignment of operations to another charter operator, or, as a last resort, the dissolution of an open-enrollment charter school.

As described above, the Act includes a funding “intercept” function that applies to both the School District Bond Guarantee Program and the Charter District Bond Guarantee Program. However, school districts are viewed as the “educator of last resort” for students residing in the geographical territory of the district, which makes it unlikely that State funding for those school districts would be discontinued, although the TEA can require the dissolution and merger into another school district if necessary to ensure sound education and financial management of a school district. That is not the case with a charter district, however, and open-enrollment charter schools in the State have been dissolved by TEA from time to time. If a charter district that has bonds outstanding that are guaranteed by the Charter District Bond Guarantee Program should be dissolved, debt service on guaranteed bonds of the district would continue to be paid to bondholders in accordance with the Charter District Bond Guarantee Program, but there would be no funding available for reimbursement of the PSF by the Comptroller for such payments. As described under “The Charter District Bond Guarantee Program,” the Act establishes a Charter District Reserve Fund, which could in the future be a significant reimbursement resource for the PSF. At September 30, 2018, the Charter District Reserve Fund contained \$7,164,188.

#### **POTENTIAL IMPACT OF HURRICANE HARVEY ON THE PSF**

Hurricane Harvey struck coastal Texas on August 26, 2017, resulting in historic levels of rainfall. The Governor designated the impacted area for disaster relief, and TEA believes that the storm impacted more than 1.3 million students enrolled in some 157 school districts, and approximately 58,000 students in 27 charter schools in the designated area. Many of the impacted school districts and two charter districts have bonds guaranteed by the PSF. It is possible that the affected districts will need to borrow to repair or replace damaged facilities, which could require increased bond issuance and applications to the TEA for PSF bond guarantees. In addition, the storm damage and any lingering economic damage in the area could adversely affect the tax base (for school districts) and credit quality of school districts and charter districts with bonds that are or will be guaranteed by the PSF.

The TEA, members of the Legislature and the Governor, among others, have stated that they are developing programs to provide financial assistance to affected school districts and charter districts, particularly with regard to funding assistance for facility repairs and construction and to offset tax base and/or revenue loss to affected districts. The composition of any final programs that may be implemented cannot be predicted, and are likely to be subject to future State legislative and administrative actions, available amounts of federal and private disaster relief for affected schools, and other factors. For fiscal year 2018, TEA initiated programs designed to hold school districts and charter districts harmless for the loss of State funding associated with declines in average daily attendance. In the past, storm damage has caused multiple year impacts to affected schools with respect to both attendance figures and tax base (for school districts). In June 2018 TEA received results of a survey of tax appraisal districts in the area affected by the hurricane with respect to the impact of the hurricane on the tax rolls of affected school districts. In aggregate, the tax rolls of affected districts appear to have increased slightly for fiscal 2018 over 2017, but the increases were at a lower rate than had been anticipated in the State’s general appropriation act for the biennium. TEA notes that as of June 2018 the negative effect of the hurricane on the average daily attendance of districts in the affected area appears to have been less than TEA had initially anticipated.

Many of the school districts and two charter districts in the designated disaster area have bonds guaranteed by the PSF. TEA notes that no district has applied for financial exigency or failed to timely pay bond payments as a result of the hurricane or otherwise. The PSF is managed to maintain liquidity for any draws on the program. Moreover, as described under “The School District Bond Guarantee Program” and “The Charter District Bond Guarantee Program,” both parts of the Bond Guarantee Program operate in accordance with the Act as “intercept” programs, providing liquidity for guaranteed bonds, and draws on the PSF are required to be restored from the first State money payable to a school district or a charter district that fails to make a guaranteed payment on its bonds.

#### **RATINGS OF BONDS GUARANTEED UNDER THE GUARANTEE PROGRAM**

Moody’s Investors Service, S&P Global Ratings and Fitch Ratings rate bonds guaranteed by the PSF “Aaa,” “AAA” and “AAA,” respectively. Not all districts apply for multiple ratings on their bonds, however. See “Ratings” herein.

**VALUATION OF THE PSF AND GUARANTEED BONDS**

**Permanent School Fund Valuations**

<u>Fiscal Year Ended 8/31</u>	<u>Book Value<sup>(1)</sup></u>	<u>Market Value<sup>(1)</sup></u>
2014	\$ 27,596,692,541	\$ 38,445,519,225
2015	29,081,052,900	36,196,265,273
2016	30,128,037,903	37,279,799,335
2017	31,870,581,428	41,438,672,573
2018 <sup>(2)</sup>	33,962,040,017	43,918,273,565

<sup>(1)</sup> SLB managed assets are included in the market value and book value of the Fund. In determining the market value of the PSF from time to time during a fiscal year, the TEA uses current, unaudited values for TEA managed investment portfolios and cash held by the SLB. With respect to SLB managed assets shown in the table above, market values of land and mineral interests, internally managed real estate, investments in externally managed real estate funds and cash are based upon information reported to the PSF by the SLB. The SLB reports that information to the PSF on a quarterly basis. The valuation of such assets at any point in time is dependent upon a variety of factors, including economic conditions in the State and nation in general, and the values of these assets, and, in particular, the valuation of mineral holdings administered by the SLB, can be volatile and subject to material changes from period to period.

<sup>(2)</sup> At August 31, 2018, mineral assets, sovereign and other lands and internally managed discretionary real estate, external discretionary real estate investments, domestic equities, and cash managed by the SLB had book values of approximately \$13.43 million, \$240.90 million, \$3,082.83 million, \$7.58 million, and \$4,247.36 million, respectively, and market values of approximately \$1,870.22 million, \$642.00 million, \$3,164.04 million, \$4.71 million, and \$4,247.36 million, respectively. At September 30, 2018, the PSF had a book value of \$33,937,270,391 and a market value of \$43,724,325,619. August 31, 2018 and September 30, 2018 values are based on unaudited data, which is subject to adjustment.

**Permanent School Fund Guaranteed Bonds**

<u>At 8/31</u>	<u>Principal Amount<sup>(1)</sup></u>
2014	\$ 58,364,350,783
2015	63,955,449,047
2016	68,303,328,445
2017	74,266,090,023
2018	79,080,901,069 <sup>(2)</sup>

<sup>(1)</sup> Represents original principal amount; does not reflect any subsequent accretions in value for compound interest bonds (zero coupon securities). The amount shown excludes bonds that have been refunded and released from the Guarantee Program. The TEA does not maintain records of the accreted value of capital appreciation bonds that are guaranteed under the Guarantee Program.

<sup>(2)</sup> As of August 31, 2018 (the most recent date for which such data is available), the TEA expected that the principal and interest to be paid by school districts over the remaining life of the bonds guaranteed by the Guarantee Program was \$123,361,625,817, of which \$44,280,724,748 represents interest to be paid. As shown in the table above, at August 31, 2018, there were \$79,080,901,069 in principal amount of bonds guaranteed under the Guarantee Program, and using the IRS Limit at that date of \$117,318,653,038 (the IRS Limit is currently the lower of the two federal and State capacity limits of Program capacity), 98.21% of Program capacity was available to the School District Bond Guarantee Program and 1.79% was available to the Charter District Bond Guarantee Program. August 31, 2018 values are based on unaudited data, which is subject to adjustment.

**Permanent School Fund Guaranteed Bonds by Category<sup>(1)</sup>**

<u>Fiscal Year Ended</u>	<u>School District Bonds</u>		<u>Charter District Bonds</u>		<u>Totals</u>	
	<u>No. of Issues</u>	<u>Principal Amount</u>	<u>No. of Issues</u>	<u>Principal Amount</u>	<u>No. of Issues</u>	<u>Principal Amount</u>
2014 <sup>(2)</sup>	2,869	\$ 58,061,805,783	10	\$ 302,545,000	2,879	\$ 58,364,350,783
2015	3,089	63,197,514,047	28	757,935,000	3,117	63,955,449,047
2016	3,244	67,342,303,445	35	961,025,000	3,279	68,303,328,445
2017	3,253	72,884,480,023	40	1,381,610,000	3,293	74,266,090,023
2018 <sup>(3)</sup>	3,249	77,647,966,069	44	1,432,935,000	3,293	79,080,901,069

<sup>(1)</sup> Represents original principal amount; does not reflect any subsequent accretions in value for compound interest bonds (zero coupon securities). The amount shown excludes bonds that have been refunded and released from the Guarantee Program.

<sup>(2)</sup> Fiscal 2014 was the first year of operation of the Charter District Bond Guarantee Program.

<sup>(3)</sup> At September 30, 2018 (based on unaudited data, which is subject to adjustment), there were \$79,828,771,069 of bonds guaranteed under the Guarantee Program, representing 3,265 school district issues, aggregating \$78,395,836,069 in principal amount and 45 charter district issues, aggregating \$1,432,935,000 in principal amount. At September 30, 2018, the capacity allocation of the Charter District Bond Guarantee Program was \$3,109,688,908 (based on unaudited data, which is subject to adjustment). 2018 data is unaudited, which is subject to adjustment.

#### **DISCUSSION AND ANALYSIS PERTAINING TO FISCAL YEAR ENDED AUGUST 31, 2017**

The following discussion is derived from the Annual Report for the year ended August 31, 2017, including the Message of the Executive Administrator of the Fund and the Management's Discussion and Analysis contained therein, and will be updated upon the release of the Annual Report for the year ended August 31, 2018. Reference is made to the Annual Report, when filed, for the complete Message and MD&A. Investment assets managed by the fifteen member SBOE are referred to throughout this MD&A as the PSF(SBOE) assets. As of August 31, 2017, the Fund's land, mineral rights and certain real assets are managed by the three-member SLB and these assets are referred to throughout as the PSF(SLB) assets. The current PSF asset allocation policy includes an allocation for real estate investments, and as such investments are made, and become a part of the PSF investment portfolio, those investments will be managed by the SBOE and not the SLB.

At the end of fiscal 2017, the Fund balance was \$41.4 billion, an increase of \$4.2 billion from the prior year. This increase is primarily due to overall increases in value of all asset classes in which the Fund has invested. During the year, the SBOE continued implementing the long term strategic asset allocation, diversifying the PSF(SBOE) to strengthen the Fund. The asset allocation is projected to increase returns over the long run while reducing risk and portfolio return volatility. The PSF(SBOE) annual rates of return for the one-year, five-year, and ten-year periods ending August 31, 2017, were 11.96%, 8.26% and 5.49%, respectively (total return takes into consideration the change in the market value of the Fund during the year as well as the interest and dividend income generated by the Fund's investments). In addition, the SLB continued its shift into externally managed real asset investment funds, and the one-year, three-year, and five-year annualized total returns for the PSF(SLB) real assets, including cash, were 10.35%, 7.19%, and 7.77%, respectively.

The market value of the Fund's assets is directly impacted by the performance of the various financial markets in which the assets are invested. The most important factors affecting investment performance are the asset allocation decisions made by the SBOE and SLB. The current SBOE long term asset allocation policy allows for diversification of the PSF(SBOE) portfolio into alternative asset classes whose returns are not as positively correlated as traditional asset classes. The implementation of the long term asset allocation will occur over several fiscal years and is expected to provide incremental total return at reduced risk. As of August 31, 2017, the PSF(SBOE) portion of the Fund had diversified into emerging market and large cap international equities, absolute return funds, real estate, private equity, risk parity, real return Treasury Inflation-Protected Securities, real return commodities, and emerging market debt.

As of August 31, 2017, the SBOE has approved and the Fund made capital commitments to externally managed real estate investment funds in a total amount of \$3.31 billion and capital commitments to private equity limited partnerships for a total of \$3.83 billion. Unfunded commitments at August 31, 2017, totaled \$1.35 billion in real estate investments and \$1.54 billion in private equity investments.

The PSF(SLB) portfolio is generally characterized by three broad categories: (1) discretionary real assets investments, (2) sovereign and other lands, and (3) mineral interests. Discretionary real assets investments consist of externally managed real estate, infrastructure, and energy/minerals investment funds; internally managed direct real estate investments, and cash. Sovereign and other lands consist primarily of the lands set aside to the PSF when it was created. Mineral interests consist of all of the minerals that are associated with PSF lands. The investment focus of PSF(SLB) discretionary real assets investments has shifted from internally managed direct real estate investments to externally managed real assets investment funds. The PSF(SLB) makes investments in certain limited partnerships that legally commit it to possible future capital contributions. At August 31, 2017, the remaining commitments totaled approximately \$2.042 billion.

The PSF(SBOE)'s investment in domestic large cap, domestic small/mid cap, international large cap, and emerging market equity securities experienced returns of 16.30%, 12.80%, 19.04%, and 26.28%, respectively, during the fiscal year ended August 31, 2017. The PSF(SBOE)'s investment in domestic fixed income securities produced a return of 1.61% during the fiscal year and absolute return investments yielded a return of 7.32%. The PSF(SBOE) real estate and private equity investments returned 10.52% and 16.35%, respectively. Risk parity assets produced a return of 8.77%, while real return assets yielded 2.38%. Emerging market debt produced a return of 11.84%. Combined, all PSF(SBOE) asset classes produced an investment return of 11.96% for the fiscal year ended August 31, 2017, out-performing the benchmark index of 10.66% by approximately 130 basis points. All PSF(SLB) real assets (including cash) returned 10.35% for the fiscal year ending August 31, 2017.

For fiscal year 2017, total revenues, inclusive of unrealized gains and losses and net of security lending rebates and fees, totaled \$5.4 billion, an increase of \$2.7 billion from fiscal year 2016 earnings of \$2.7 billion. This increase reflects the performance of the securities markets in which the Fund was invested in fiscal year 2017. In fiscal year 2017, revenues earned by the Fund included lease payments, bonuses and royalty income received from oil, gas and mineral leases; lease payments from

commercial real estate; surface lease and easement revenues; revenues from the resale of natural and liquid gas supplies; dividends, interest, and securities lending revenues; the net change in the fair value of the investment portfolio; and, other miscellaneous fees and income.

Expenditures are paid from the Fund before distributions are made under the total return formula. Such expenditures include the costs incurred by the SLB to manage the land endowment, as well as operational costs of the Fund, including external management fees paid from appropriated funds. Total operating expenditures, net of security lending rebates and fees, increased 30.6% for the fiscal year ending August 31, 2017. This increase is primarily attributable to an increase in PSF(SLB) operational costs and generally larger quantities of purchased gas for resale in the State Energy Management Program, which is administered by the SLB as part of the Fund.

The Fund supports the public school system in the State by distributing a predetermined percentage of its asset value to the ASF. For fiscal years 2016 and 2017, the distribution from the SBOE to the ASF totaled \$1.06 billion and \$1.06 billion, respectively. There was no contribution to the ASF by the SLB in fiscal year 2017.

At the end of the 2017 fiscal year, PSF assets guaranteed \$74.27 billion in bonds issued by 858 local school districts and charter districts, the latter of which entered into the Program during the 2014 fiscal year. Since its inception in 1983, the Fund has guaranteed 6,980 school district and charter district bond issues totaling \$166.3 billion in principal amount. During the 2017 fiscal year, the number of outstanding issues guaranteed under the Guarantee Program increased by 14, or 0.4%. The dollar amount of guaranteed school and charter bond issues outstanding increased by \$6.0 billion or 8.7%. The guarantee capacity of the Fund increased by \$13.9 billion, or 13.9%, during fiscal year 2017 due to continued growth in the cost basis of the Fund and the increase in the cost multiplier (from 3.25 to 3.50, as discussed above) used to calculate Program capacity.

## **2011 CONSTITUTIONAL AMENDMENT**

On November 8, 2011, a referendum was held in the State as a result of legislation enacted that year that proposed amendments to various sections of the Texas Constitution pertaining to the PSF. At that referendum, voters of State approved non-substantive changes to the Texas Constitution to clarify references to the Fund, and, in addition, approved amendments that effected an increase to the base amount used in calculating the Distribution Rate from the Fund to the ASF, and authorized the SLB to make direct transfers to the ASF, as described below.

The amendments approved at the referendum included an increase to the base used to calculate the Distribution Rate by adding to the calculation base certain discretionary real assets and cash in the Fund that is managed by entities other than the SBOE (at present, by the SLB). The value of those assets were already included in the value of the Fund for purposes of the Guarantee Program, but prior to the amendment had not been included in the calculation base for purposes of making transfers from the Fund to the ASF. While the amendment provided for an increase in the base for the calculation of approximately \$2 billion, no new resources were provided for deposit to the Fund. As described under “The Total Return Constitutional Amendment” the SBOE is prevented from approving a Distribution Rate or making a pay out from the Fund if the amount distributed would exceed 6% of the average of the market value of the Fund, excluding real property in the Fund, but including discretionary real asset investments on the last day of each of the sixteen State fiscal quarters preceding the Regular Session of the Legislature that begins before that State fiscal biennium or if such pay out would exceed the Ten Year Total Return.

If there are no reductions in the percentage established biennially by the SBOE to be the Distribution Rate, the impact of the increase in the base against which the Distribution Rate is applied will be an increase in the distributions from the PSF to the ASF. As a result, going forward, it may be necessary for the SBOE to reduce the Distribution Rate in order to preserve the corpus of the Fund in accordance with its management objective of preserving intergenerational equity.

The Distribution Rates for the Fund were set at 3.5%, 2.5%, 4.2%, 3.3%, 3.5% and 3.7% for each of two year periods 2008-2009, 2010-2011, 2012-2013, 2014-2015, 2016-2017 and 2018-2019, respectively. In November 2018, the SBOE approved a \$2.2 billion distribution to the ASF for State fiscal biennium 2020-2021, to be made in equal monthly increments of \$92.2 million, which represents a 2.981% Distribution Rate for the biennium and a per student distribution of \$220.97, based on 2018 preliminary student average daily attendance of 5,004,998. In making the 2020-2021 biennium distribution decision, the SBOE took into account a commitment of the SLB transfer \$10 to the PSF in fiscal year 2020 and \$45 million in fiscal year 2021.

Changes in the Distribution Rate for each biennial period has been based on a number of financial and political reasons, as well as commitments made by the SLB in some years to transfer certain sums to the ASF. The new calculation base described above has been used to determine all payments to the ASF from the Fund beginning with the 2012-13 biennium. The broader base for the Distribution Rate calculation could increase transfers from the PSF to the ASF, although the effect of the broader calculation base has been somewhat offset since the 2014-2015 biennium by the establishment by the SBOE of somewhat lower Distribution Rates than for the 2012-2013 biennium. In addition, the changes made by the amendment that increased the calculation base that could affect the corpus of the Fund include the decisions that are made by the SLB or others that are, or may in the future be, authorized to make transfers of funds from the PSF to the ASF.

The constitutional amendments approved on November 8, 2011 also provide authority to the GLO or any other entity other than the SBOE that has responsibility for the management of land or other properties of the Fund to determine whether to transfer an amount each year from Fund assets to the ASF revenue derived from such land or properties, with the amount transferred limited to \$300 million. Any amount transferred to the ASF by an entity other than the SBOE is excluded from the 6% Distribution Rate limitation applicable to SBOE transfers.

#### **OTHER EVENTS AND DISCLOSURES**

The State Investment Ethics Code governs the ethics and disclosure requirements for financial advisors and other service providers who advise certain State governmental entities, including the PSF. In accordance with the provisions of the State Investment Ethics Code, the SBOE periodically modifies its code of ethics, which occurred most recently in April 2018. The SBOE code of ethics includes prohibitions on sharing confidential information, avoiding conflict of interests and requiring disclosure filings with respect to contributions made or received in connection with the operation or management of the Fund. The code of ethics applies to members of the SBOE as well as to persons who are responsible by contract or by virtue of being a TEA PSF staff member for managing, investing, executing brokerage transactions, providing consultant services, or acting as a custodian of the PSF, and persons who provide investment and management advice to a member of the SBOE, with or without compensation under certain circumstances. The code of ethics is codified in the Texas Administrative Code at 19 TAC sections 33.5 et seq., and is available on the TEA web site at <http://ritter.tea.state.tx.us/rules/tac/chapter033/ch033a.html#33.5>.

In addition, the GLO has established processes and controls over its administration of real estate transactions and is subject to provisions of the Texas Natural Resources Code and its own internal procedures in administering real estate transactions for assets it manages for the Fund.

Since 2007, TEA has made supplemental appropriation requests to the Legislature for the purpose of funding the implementation of the 2008 Asset Allocation Policy, but those requests have been denied or partly funded. In the 2011 legislative session, the Legislature approved an increase of 31 positions in the full-time equivalent employees for the administration of the Fund, which was funded as part of an \$18 million appropriation for each year of the 2012-13 biennium, in addition to the operational appropriation of \$11 million for each year of the biennium. The TEA has begun increasing the PSF administrative staff in accordance with the 2011 legislative appropriation, and the TEA received an appropriation of \$30.2 million for the administration of the PSF for fiscal years 2016 and 2017, respectively, and \$30.4 million for each of the fiscal years 2018 and 2019.

As of August 31, 2017, certain lawsuits were pending against the State and/or the GLO, which challenge the Fund's title to certain real property and/or past or future mineral income from that property, and other litigation arising in the normal course of the investment activities of the PSF. Reference is made to the Annual Report, when filed, for a description of such lawsuits that are pending, which may represent contingent liabilities of the Fund.

#### **PSF CONTINUING DISCLOSURE UNDERTAKING**

The SBOE has adopted an investment policy rule (the "TEA Rule") pertaining to the PSF and the Guarantee Program. The TEA Rule is codified in Section I of the TEA Investment Procedure Manual, which relates to the Guarantee Program and is posted to the TEA web site at [http://tea.texas.gov/Finance\\_and\\_Grants/Texas\\_Permanent\\_School\\_Fund/Texas\\_Permanent\\_School\\_Fund\\_Disclosure\\_Statement\\_-\\_Bond\\_Guarantee\\_Program/](http://tea.texas.gov/Finance_and_Grants/Texas_Permanent_School_Fund/Texas_Permanent_School_Fund_Disclosure_Statement_-_Bond_Guarantee_Program/). The most recent amendment to the TEA Rule was adopted by the SBOE on November 16, 2018, and is summarized below. Through the adoption of the TEA Rule and its commitment to guarantee bonds, the SBOE has made the following agreement for the benefit of the issuers, holders and beneficial owners of guaranteed bonds. The TEA (or its successor with respect to the management of the Guarantee Program) is required to observe the agreement for so long as it remains an "obligated person," within the meaning of Rule 15c2-12, with respect to guaranteed bonds. Nothing in the TEA Rule obligates the TEA to make any filings or disclosures with respect to guaranteed bonds, as the obligations of the TEA under the TEA Rule pertain solely to the Guarantee Program. The issuer or an "obligated person" of the guaranteed bonds has assumed the applicable obligation under Rule 15c-12 to make all disclosures and filings relating directly to guaranteed bonds, and the TEA takes no responsibility with respect to such undertakings. Under the TEA agreement, the TEA will be obligated to provide annually certain updated financial information and operating data, and timely notice of specified material events, to the MSRB.

The MSRB has established the Electronic Municipal Market Access ("EMMA") system, and the TEA is required to file its continuing disclosure information using the EMMA system. Investors may access continuing disclosure information filed with the MSRB at [www.emma.msrb.org](http://www.emma.msrb.org), and the continuing disclosure filings of the TEA with respect to the PSF can be found at <https://emma.msrb.org/IssueView/Details/ER355077> or by searching for "Texas Permanent School Fund Bond Guarantee Program" on EMMA.

## **ANNUAL REPORTS**

The TEA will annually provide certain updated financial information and operating data to the MSRB. The information to be updated includes all quantitative financial information and operating data with respect to the Guarantee Program and the PSF of the general type included in this Official Statement under the heading “THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM.” The information also includes the Annual Report. The TEA will update and provide this information within six months after the end of each fiscal year.

The TEA may provide updated information in full text or may incorporate by reference certain other publicly-available documents, as permitted by Rule 15c2-12. The updated information includes audited financial statements of, or relating to, the State or the PSF, when and if such audits are commissioned and available. Financial statements of the State will be prepared in accordance with generally accepted accounting principles as applied to state governments, as such principles may be changed from time to time, or such other accounting principles as the State Auditor is required to employ from time to time pursuant to State law or regulation. The financial statements of the Fund were prepared to conform to U.S. Generally Accepted Accounting Principles as established by the Governmental Accounting Standards Board.

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

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

## **EVENT NOTICES**

The TEA will also provide timely notices of certain events to the MSRB. Such notices will be provided not more than ten business days after the occurrence of the event. The TEA will provide notice of any of the following events with respect to the Guarantee Program: (1) principal and interest payment delinquencies; (2) non-payment related defaults, if such event is material within the meaning of the federal securities laws; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions, the issuance by the IRS of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB), or other material notices or determinations with respect to the tax-exempt status of the Guarantee Program, or other material events affecting the tax status of the Guarantee Program; (7) modifications to rights of holders of bonds guaranteed by the Guarantee Program, if such event is material within the meaning of the federal securities laws; (8) bond calls, if such event is material within the meaning of the federal securities laws, and tender offers; (9) defeasances; (10) release, substitution, or sale of property securing repayment of bonds guaranteed by the Guarantee Program, if such event is material within the meaning of the federal securities laws; (11) rating changes; (12) bankruptcy, insolvency, receivership, or similar event of the Guarantee Program (which is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent, or similar officer for the Guarantee Program in a proceeding under the United States Bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the Guarantee Program, or if such jurisdiction has been assumed by leaving the existing governing body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement, or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the Guarantee Program); (13) the consummation of a merger, consolidation, or acquisition involving the Guarantee Program or the sale of all or substantially all of its assets, other than in the ordinary course of business, the entry into of a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; (14) the appointment of a successor or additional trustee with respect to the Guarantee Program or the change of name of a trustee, if such event is material within the meaning of the federal securities laws; (15) the incurrence of a financial obligation of the Guarantee Program, if material, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the Program, any of which affect security holders, if material; and (16) default, event of acceleration, termination event, modification of terms, or other similar events under the terms of a financial obligation of the Guarantee Program, any of which reflect financial difficulties. (Neither the Act nor any other law, regulation or instrument pertaining to the Guarantee Program make any provision with respect to the Guarantee Program for bond calls, debt service reserves, credit enhancement, liquidity enhancement, early redemption or the appointment of a trustee with respect to the Guarantee Program.) In addition, the TEA will provide timely notice of any failure by the TEA to provide information, data, or financial statements in accordance with its agreement described above under “Annual Reports.”

## **AVAILABILITY OF INFORMATION**

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

## **LIMITATIONS AND AMENDMENTS**

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

The continuing disclosure agreement of the TEA is made only with respect to the PSF and the Guarantee Program. The issuer of guaranteed bonds or an obligated person with respect to guaranteed bonds may make a continuing disclosure undertaking in accordance with Rule 15c2-12 with respect to its obligations arising under Rule 15c2-12 pertaining to financial and operating data concerning such entity and notices of material events relating to such guaranteed bonds. A description of such undertaking, if any, is included elsewhere in the Official Statement.

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

## **COMPLIANCE WITH PRIOR UNDERTAKINGS**

During the last five years, the TEA has not failed to substantially comply with its previous continuing disclosure agreements in accordance with Rule 15c2-12.

## **SEC EXEMPTIVE RELIEF**

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

## **STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS**

### **LITIGATION RELATING TO THE TEXAS PUBLIC SCHOOL FINANCE SYSTEM**

On seven occasions in the last thirty years, the Texas Supreme Court (the “Court”) has issued decisions assessing the constitutionality of the Texas public school finance system (the “Finance System”). The litigation has primarily focused on whether the Finance System, as amended by the Texas Legislature (the “Legislature”) from time to time (i) met the requirements of article VII, section 1 of the Texas Constitution, which requires the Legislature to “establish and make suitable provision for the support and maintenance of an efficient system of public free schools,” or (ii) imposed a statewide ad valorem tax in violation of article VIII, section 1-e of the Texas Constitution because the statutory limit on property taxes levied by school districts for maintenance and operation purposes had allegedly denied school districts meaningful discretion in setting their tax rates. In response to the Court’s previous decisions, the Legislature enacted multiple laws that made substantive changes in the way the Finance System is funded in efforts to address the prior decisions declaring the Finance System unconstitutional.

On May 13, 2016, the Court issued its opinion in the most recent school finance litigation, *Morath v. The Texas Taxpayer & Student Fairness Coal.*, 490 S.W.3d 826 (Tex. 2016) (“Morath”). The plaintiffs and intervenors in the case had alleged that the Finance System, as modified by the Legislature in part in response to prior decisions of the Court, violated article VII, section 1 and article VIII, section 1-e of the Texas Constitution. In its opinion, the Court held that “despite the imperfections of the current school funding regime, it meets minimum constitutional requirements.” The Court also noted that:

Lawmakers decide if laws pass, and judges decide if those laws pass muster. But our lenient standard of review in this policy-laden area counsels modesty. The judicial role is not to second-guess whether our system is optimal, but whether it is constitutional. Our Byzantine school funding “system” is undeniably imperfect, with immense room for improvement. But it satisfies minimum constitutional requirements.

#### **POSSIBLE EFFECTS OF CHANGES IN LAW ON DISTRICT BONDS**

The Court’s decision in *Morath* upheld the constitutionality of the Finance System but noted that the Financing System was “undeniably imperfect”. While not compelled by the *Morath* decision to reform the Finance System, the Legislature could enact future changes to the Finance System. Any such changes could benefit or be a detriment to the District. If the Legislature enacts future changes to, or fails adequately to fund the Finance System, or if changes in circumstances otherwise provide grounds for a challenge, the Finance System could be challenged again in the future. In its 1995 opinion in *Edgewood Independent School District v. Meno*, 917 S.W.2d 717 (Tex. 1995), the Court stated that any future determination of unconstitutionality “would not, however, affect the district’s authority to levy the taxes necessary to retire previously issued bonds, but would instead require the Legislature to cure the system’s unconstitutionality in a way that is consistent with the Contract Clauses of the U.S. and Texas Constitutions” (collectively, the “Contract Clauses”), which prohibit the enactment of laws that impair prior obligations of contracts.

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

### **CURRENT PUBLIC SCHOOL FINANCE SYSTEM**

#### **OVERVIEW**

The following language constitutes only a summary of the Finance System as it is currently structured. For a more complete description of school finance and fiscal management in the State, reference is made to Chapters 41 through 46 of the Texas Education Code, as amended.

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

Local funding is derived from collections of ad valorem taxes levied on property located within each district’s boundaries. School districts are authorized to levy two types of property taxes: a limited M&O tax to pay current expenses and an unlimited interest and sinking fund (“I&S”) tax to pay debt service on bonds. Generally, under current law, M&O tax rates are subject to a statutory maximum rate of \$1.17 per \$100 of taxable value for most school districts (although a few districts can exceed the \$1.17 limit as a result of authorization approved in the 1960s). Current law also requires school districts to demonstrate their ability to pay debt service on outstanding indebtedness through the levy of an ad valorem tax at a rate of not to exceed \$0.50 per \$100 of taxable property at the time bonds are issued. Once bonds are issued, however, districts may levy a tax to pay debt service on such bonds unlimited as to rate or amount (see “TAX INFORMATION – Tax Rate Limitations” herein). As noted above, because property

values vary widely among school districts, the amount of local funding generated by the same tax rate is also subject to wide variation among school districts.

### **LOCAL FUNDING FOR SCHOOL DISTRICTS**

The primary source of local funding for school districts is collections from ad valorem taxes levied against taxable property located in each school district. Prior to reform legislation that became effective during the 2006-2007 fiscal year (the "Reform Legislation"), the maximum M&O tax rate for most school districts was generally limited to \$1.50 per \$100 of taxable value. At the time the Reform Legislation was enacted, the majority of school districts were levying an M&O tax rate of \$1.50 per \$100 of taxable value. The Reform Legislation required each school district to "compress" its tax rate by an amount equal to the "State Compression Percentage". The State Compression Percentage is set by legislative appropriation for each State fiscal biennium or, in the absence of legislative appropriation, by the Commissioner. For the 2018-19 State fiscal biennium, the State Compression Percentage has been set at 66.67%, effectively setting the maximum compressed M&O tax rate for most school districts at \$1.00 per \$100 of taxable value. School districts are permitted, however, to generate additional local funds by raising their M&O tax rate by up to \$0.04 above the compressed tax rate without voter approval (for most districts, up to \$1.04 per \$100 of taxable value). In addition, if the voters approve a tax rate increase through a local referendum, districts may, in general, increase their M&O tax rate up to a maximum M&O tax rate of \$1.17 per \$100 of taxable value and receive State equalization funds for such taxing effort (see "TAX INFORMATION – Public Hearing and Rollback Tax Rate" herein). Elections authorizing the levy of M&O taxes held in certain school districts under older laws, however, may subject M&O tax rates in such districts to other limitations (see "TAX INFORMATION – Tax Rate Limitations" herein).

### **STATE FUNDING FOR SCHOOL DISTRICTS**

State funding for school districts is provided through the Foundation School Program, which provides each school district with a minimum level of funding (a "Basic Allotment") for each student in average daily attendance ("ADA"). The Basic Allotment is calculated for each school district using various weights and adjustments based on the number of students in average daily attendance and also varies depending on each district's compressed tax rate. This Basic Allotment formula determines most of the allotments making up a district's basic level of funding, referred to as "Tier One" of the Foundation School Program. The basic level of funding is then "enriched" with additional funds known as "Tier Two" of the Foundation School Program. Tier Two provides a guaranteed level of funding for each cent of local tax effort that exceeds the compressed tax rate (for most districts, M&O tax rates above \$1.00 per \$100 of taxable value). The Finance System also provides an Existing Debt Allotment ("EDA") to subsidize debt service on eligible outstanding school district bonds, an Instructional Facilities Allotment ("IFA") to subsidize debt service on newly issued bonds, and a New Instructional Facilities Allotment ("NIFA") to subsidize operational expenses associated with the opening of a new instructional facility. IFA primarily addresses the debt service needs of property-poor school districts. In 2017, the 85th Texas Legislature appropriated funds in the amount of \$1,378,500,000 for the 2018-19 State fiscal biennium for the EDA, IFA, and NIFA.

Tier One and Tier Two allotments represent the State's share of the cost of M&O expenses of school districts, with local M&O taxes representing the district's local share. EDA and IFA allotments supplement a school district's local I&S taxes levied for debt service on eligible bonds issued to construct, acquire and improve facilities. Tier One and Tier Two allotments and existing EDA and IFA allotments are generally required to be funded each year by the Texas Legislature. Since future-year IFA awards were not funded by the Texas Legislature for the 2018-19 State fiscal biennium and debt service assistance on school district bonds that are not yet eligible for EDA is not available, debt service on new bonds issued by districts to construct, acquire and improve facilities must be funded solely from local I&S taxes.

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

As described above, the cost of the basic program is based on an allotment per student known as the "Basic Allotment". For the 2018-19 State fiscal biennium, the Basic Allotment is \$5,140 for each student in average daily attendance. The Basic Allotment is then adjusted for all districts by several different weights to account for inherent differences between school districts. These weights consist of (i) a cost adjustment factor intended to address varying economic conditions that affect teacher hiring known as the "cost of education index", (ii) district-size adjustments for small and mid-size districts, and (iii) an adjustment for the sparsity of the district's student population. The cost of education index, district-size and population sparsity adjustments, as applied to the Basic Allotment, create what is referred to as the "Adjusted Allotment". The Adjusted Allotment is used to compute a "regular program allotment", as well as various other allotments associated with educating students with other specified educational needs.

Tier Two supplements the basic funding of Tier One and provides two levels of enrichment with different guaranteed yields (i.e., guaranteed levels of funding by the State) depending on the district's local tax effort. The first six cents of tax effort that exceeds the compressed tax rate (for most districts, M&O tax rates ranging from \$1.00 to \$1.06 per \$100 of taxable value) will, for most districts, generate a guaranteed yield of \$99.41 and \$106.28 per cent per weighted student in average daily attendance ("WADA") in the 2017-18 and 2018-19 State fiscal years, respectively. The second level of Tier Two is generated by tax effort that exceeds the district's

compressed tax rate plus six cents (for most districts eligible for this level of funding, M&O tax rates ranging from \$1.06 to \$1.17 per \$100 of taxable value) and has a guaranteed yield per cent per WADA of \$31.95 for the 2018-19 State fiscal biennium. Property-wealthy school districts that have an M&O tax rate that exceeds the district's compressed tax rate plus six cents are subject to recapture above this tax rate level at the equivalent wealth per student of \$319,500 (see "Wealth Transfer Provisions" below).

Previously, a district with a compressed tax rate below \$1.00 per \$100 of taxable value (known as a "fractionally funded district") received a Basic Allotment which was reduced proportionately to the degree that the district's compressed tax rate fell short of \$1.00. Beginning in the 2017-2018 fiscal year, the compressed tax rate of a fractionally funded district now includes the portion of such district's current M&O tax rate in excess of the first six cents above the district's compressed tax rate until the district's compressed tax rate is equal to the state maximum compressed tax rate of \$1.00. Thus, for fractionally funded districts, each eligible one cent of M&O tax levy above the district's compressed tax rate plus six cents will have a guaranteed yield based on Tier One funding instead of the Tier Two yield, thereby reducing the penalty against the Basic Allotment.

In addition to the operations funding components of the Foundation School Program discussed above, the Foundation School Program provides a facilities funding component consisting of the Instructional Facilities Allotment (IFA) program and the Existing Debt Allotment (EDA) program. These programs assist school districts in funding facilities by, generally, equalizing a district's I&S tax effort. The IFA guarantees each awarded school district a specified amount per student (the "IFA Guaranteed Yield") in State and local funds for each cent of tax effort to pay the principal of and interest on eligible bonds issued to construct, acquire, renovate or improve instructional facilities. The guaranteed yield per cent of local tax effort per student in ADA has been \$35 since this program first began in 1997. New awards of IFA are only available if appropriated funds are allocated for such purpose by the State Legislature. To receive an IFA award, in years where the State Legislature allocates appropriated funds for new IFA awards, a school district must apply to the Commissioner in accordance with rules adopted by the Commissioner before issuing the bonds to be paid with IFA state assistance. The total amount of debt service assistance over a biennium for which a district may be awarded is limited to the lesser of (1) the actual debt service payments made by the district in the biennium in which the bonds are issued; or (2) the greater of (a) \$100,000 or (b) \$250 multiplied by the number of students in ADA. The IFA is also available for lease-purchase agreements and refunding bonds meeting certain prescribed conditions. Once a district receives an IFA award for bonds, it is entitled to continue receiving State assistance for such bonds without reapplying to the Commissioner. The guaranteed level of State and local funds per student per cent of local tax effort applicable to the bonds may not be reduced below the level provided for the year in which the bonds were issued. The 85th State Legislature did not appropriate any funds for new IFA awards for the 2018-2019 State fiscal biennium; however, awards previously granted in years the State Legislature did appropriate funds for new IFA awards will continue to be funded. State financial assistance is provided for certain existing eligible debt issued by school districts through the EDA program. The EDA guaranteed yield (the "EDA Yield") was the same as the IFA Guaranteed Yield (\$35 per cent of local tax effort per student in ADA). The 85th Texas Legislature changed the EDA Yield to the lesser of (i) \$40 or a greater amount for any year provided by appropriation; or (ii) the amount that would result in a total additional EDA of \$60 million more than the EDA to which districts would have been entitled to if the EDA Yield were \$35. The yield for the 2017-2018 fiscal year is approximately \$37. The portion of a district's local debt service rate that qualifies for EDA assistance is limited to the first 29 cents of debt service tax (or a greater amount for any year provided by appropriation by the Texas Legislature). In general, a district's bonds are eligible for EDA assistance if (i) the district made payments on the bonds during the final fiscal year of the preceding State fiscal biennium, or (ii) the district levied taxes to pay the principal of and interest on the bonds for that fiscal year. Each biennium, access to EDA funding is determined by the debt service taxes collected in the final year of the preceding biennium. A district may not receive EDA funding for the principal and interest on a series of otherwise eligible bonds for which the district receives IFA funding.

A district may also qualify for a NIFA allotment, which provides assistance to districts for operational expenses associated with opening new instructional facilities. The 85th Texas Legislature appropriated funds in the amount of \$23,750,000 for each of the 2017-18 and 2018-19 State fiscal years for NIFA allotments.

## **2006 LEGISLATION**

Since the enactment of the Reform Legislation in 2006, most school districts in the State have operated with a "target" funding level per student ("Target Revenue") that is based upon the "hold harmless" principles embodied in the Reform Legislation. This system of Target Revenue was superimposed on the Foundation School Program and made existing funding formulas substantially less important for most school districts. The Reform Legislation was intended to lower M&O tax rates in order to give school districts "meaningful discretion" in setting their M&O tax rates, while holding school districts harmless by providing them with the same level of overall funding they received prior to the enactment of the Reform Legislation. To make up for this shortfall, the Reform Legislation authorized Additional State Aid for Tax Reduction ("ASATR") for each school district in an amount equal to the difference between the amount that each district would receive under the Foundation School Program and the amount of each district's Target Revenue funding level. However, in subsequent legislative sessions, the Texas Legislature has gradually reduced the reliance on ASATR by increasing the funding formulas, and beginning with the 2017-18 school year, the statutes authorizing ASATR were repealed (eliminating revenue targets and ASATR funding).

## **2017 LEGISLATION**

The 85th Texas Legislature, including the regular session which concluded on May 29, 2017 and the special session which concluded on August 15, 2017, did not enact substantive changes to the Finance System. However, certain bills during the regular session and House Bill 21, which was passed during the special session and signed by the Governor on August 16, 2017, revised certain aspects of the formulas used to determine school district entitlements under the Finance System. In addition to amounts previously discussed, the 85th Texas Legislature additionally appropriated funds to (i) establish a Financial Hardship Transition Program, which provides grants (“Hardship Grants”) to those districts which were heavily reliant on ASATR funding, and (ii) provide an Adjustment for Rapid Decline in Taxable Value of Property (“DPV Decline Adjustment”) for districts which experienced a decline in their tax base of more than four percent for tax years 2015 and 2016. A district may receive either a Hardship Grant or a DPV Decline Adjustment, but cannot receive both. In a case where a district would have been eligible to receive funding under both programs, the district will receive the greater of the two amounts.

## **WEALTH TRANSFER PROVISIONS**

Some districts have sufficient property wealth per student in WADA (“wealth per student”) to generate their statutory level of funding through collections of local property taxes alone. Districts whose wealth per student generates local property tax collections in excess of their statutory level of funding are referred to as “Chapter 41” districts because they are subject to the wealth equalization provisions contained in Chapter 41 of the Texas Education Code. Chapter 41 districts may receive State funds for certain competitive grants and a few programs that remain outside the Foundation School Program. Otherwise, Chapter 41 districts are not eligible to receive State funding. Furthermore, Chapter 41 districts must exercise certain options in order to reduce their wealth level to equalized wealth levels of funding, as determined by formulas set forth in the Reform Legislation. For most Chapter 41 districts, this equalization process entails paying the portion of the district’s local taxes collected in excess of the equalized wealth levels of funding to the State (for redistribution to other school districts) or directly to other school districts with a wealth per student that does not generate local funds sufficient to meet the statutory level of funding, a process known as “recapture”.

The equalized wealth levels that subject Chapter 41 districts to recapture for the 2018-2019 State fiscal biennium are set at (i) \$514,000 per student in WADA with respect to that portion of a district’s M&O tax effort that does not exceed its compressed tax rate (for most districts, the first \$1.00 per \$100 of taxable value) and (ii) \$319,500 per WADA with respect to that portion of a district’s M&O tax effort that is beyond its compressed rate plus \$.06 (for most districts, M&O taxes levied above \$1.06 per \$100 in taxable value). So long as the State’s equalization program under Chapter 42 of the Texas Education Code is funded to provide tax revenue equivalent to that raised by the Austin Independent School District on the first six pennies of tax effort that exceed the compressed tax rate, then M&O taxes levied above \$1.00 but at or below \$1.06 per \$100 of taxable value (“Golden Pennies”) are not subject to the wealth equalization provisions of Chapter 41. Because funding at the Austin Independent School District level is currently being provided to school districts under Chapter 42 of the Texas Education Code, no recapture is currently associated with the Golden Pennies. Chapter 41 districts with a wealth per student above the lower equalized wealth level but below the higher equalized wealth level must equalize their wealth only with respect to the portion of their M&O tax rate, if any, in excess of \$1.06 per \$100 of taxable value. Under Chapter 41, a district has five options to reduce its wealth per student so that it does not exceed the equalized wealth levels: (1) a district may consolidate by agreement with one or more districts to form a consolidated district; all property and debt of the consolidating districts vest in the consolidated district; (2) a district may detach property from its territory for annexation by a property-poor district; (3) a district may purchase attendance credits from the State; (4) a district may contract to educate nonresident students from a property-poor district by sending money directly to one or more property-poor districts; or (5) a district may consolidate by agreement with one or more districts to form a consolidated taxing district solely to levy and distribute either M&O taxes or both M&O taxes and I&S taxes. A Chapter 41 district may also exercise any combination of these remedies. Options (3), (4) and (5) require prior approval by the Chapter 41 district’s voters.

A district may not adopt a tax rate until its effective wealth per student is at or below the equalized wealth level. If a district fails to exercise a permitted option, the Commissioner must reduce the district’s property wealth per student to the equalized wealth level by detaching certain types of property from the district and annexing the property to a property-poor district or, if necessary, consolidate the district with a property-poor district. Provisions governing detachment and annexation of taxable property by the Commissioner do not provide for assumption of any of the transferring district’s existing debt. The Commissioner has not been required to detach property in the absence of a district failing to select another wealth-equalization option.

## **THE SCHOOL FINANCE SYSTEM AS APPLIED TO THE DISTRICT**

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

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

## TAX INFORMATION

**AD VALOREM TAX LAW** . . . The appraisal of property within the District is the responsibility of the respective County Appraisal Districts within which territory the District is located (collectively, the "Appraisal District"). Excluding agricultural and open-space land, which may be taxed on the basis of productive capacity, the Appraisal District is required under Title I of the Texas Tax Code (the "Property Tax Code") to appraise all property within the Appraisal District on the basis of 100% of its market value and is prohibited from applying any assessment ratios. In determining the market value of property, different methods of appraisal may be used, including the cost method of appraisal, the income method of appraisal and the market data comparison method of appraisal, and the method considered most appropriate by the chief appraiser is to be used. Effective January 1, 2010, State law requires the appraised value of a residence homestead to be based solely on the property's value as a residence homestead, regardless of whether residential use is considered to be the highest and best use of the property. State law further limits the appraised value of a residence homestead for a tax year to an amount that would not exceed the lesser of (1) the market value of the property for the most recent tax year that the market value was determined by the appraisal office or (2) the sum of (a) 10% of the property's appraised value in the preceding tax year, plus (b) the property's appraised value in the preceding tax year, plus (c) the market value of all new improvements to the property. The value placed upon property within the Appraisal District is subject to review by an Appraisal Review Board within the Appraisal District, consisting of members appointed by the Board of Directors of the Appraisal District. The Appraisal District is required to review the value of property within the Appraisal District at least every three years. The District may require annual review at its own expense, and is entitled to challenge the determination of appraised value of property within the District by petition filed with the Appraisal Review Board.

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

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

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

\$25,000 (effective January 1, 2015); and an additional \$10,000 for those 65 years of age or older, or the disabled. A person over 65 and disabled may receive only one \$10,000 exemption, and only one such exemption may be received per family, per residence homestead. State law also mandates a freeze on taxes paid on residence homesteads of persons who are 65 years of age or older or disabled, to the extent that such persons are eligible for the \$10,000 exemption. Such residence homesteads shall be appraised and taxes calculated as on any other property, but taxes shall never exceed the amount imposed in the first year in which the property received the \$10,000 exemption. The freeze on ad valorem taxes on the homesteads of persons who are 65 years of age or older or disabled is also transferable to a different residence homestead. If improvements (other than repairs or improvements required to comply with governmental requirements) are made to the property, the value of the improvements is taxed at the then current tax rate, and the total amount of taxes imposed is increased to reflect the new improvements with the new amount of taxes then serving as the ceiling on taxes for the following years. A "disabled" person is one who is "under a disability for purposes of payment of disability insurance benefits under the Federal Old Age, Survivors and Disability Insurance". Also, a surviving spouse of a taxpayer who qualifies for the freeze on ad valorem taxes is entitled to the same exemption so long as the property was the residence homestead of the surviving spouse when the deceased spouse died and remains the residence homestead of the surviving spouse and the spouse was at least 55 years of age at the time of the death of the individual's spouse. Pursuant to a constitutional amendment approved by the voters on May 12, 2007, legislation was enacted to reduce the school property tax limitation imposed by the freeze on taxes paid on residence homesteads of persons who are 65 years of age or over or disabled to correspond to reductions in local school district tax rates from the 2005 tax year to the 2006 tax year and from the 2006 tax year to the 2007 tax year (see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM – General"). The school property tax limitation provided by the constitutional amendment and enabling legislation apply to the 2007 and subsequent tax years.

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

- (i) An exemption of not less than \$3,000 of the market value of the residence homestead of persons 65 years of age or older and the disabled from all ad valorem taxes thereafter levied by the political subdivision;

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

After the exemption described in (i) above is authorized, such exemption may be repealed or decreased or increased in amount (a) by the governing body of the political subdivision or (b) by a favorable vote of a majority of the qualified voters at an election called by the governing body of the political subdivision, which election must be called upon receipt of a petition signed by at least 20% of the number of qualified voters who voted in the preceding election of the political subdivision. In the case of a decrease, the amount of the exemption may not be reduced to less than \$3,000 of the market value. However, the governing body of a political subdivision is prohibited from repealing or reducing the amount of the exemption described in (ii), above, if such exemption was in place for the 2014 tax year (fiscal year 2015) for a period ending December 31, 2019.

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

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

State law and Section 2, Article VIII, mandate an additional property tax exemption for disabled veterans or the surviving spouse or children of a deceased veteran who died while on active duty in the armed forces; the exemption applies to either real or personal property with the amount of assessed valuation exempted ranging from \$5,000 to a maximum of \$12,000; provided, however, that beginning in the 2009 tax year, a disabled veteran who receives from the United States Department of Veterans Affairs or its successor 100 percent disability compensation due to a service-connected disability and a rating of 100 percent disabled or of individual unemployability is entitled to an exemption from taxation of the total appraised value of the veteran's residence homestead. In addition, effective January 1, 2012, and subject to certain conditions, surviving spouses of a deceased veteran who had received a disability rating of 100% will be entitled to receive a residential homestead exemption equal to the exemption received by the deceased spouse until such surviving spouse remarries.

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

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

Article VIII, Section 1-j of the Texas Constitution provides for "freeport property" to be exempted from ad valorem taxation. Freeport property is defined as goods detained in Texas for 175 days or less for the purpose of assembly, storage, manufacturing, processing or fabrication. Notwithstanding such exemption, counties, school districts, junior college districts and cities may tax such tangible personal property provided official action to tax the same was taken before April 1, 1990. Decisions to continue to tax may be reversed in the future; decisions to exempt freeport property are not subject to reversal.

Article VIII, Section 1-n of the Texas Constitution provides for the exemption from taxation of "goods-in-transit." "Goods-in-transit" is defined by Section 11.253 of the Tax Code, which is effective for tax years 2008 and thereafter, as personal property acquired or imported into Texas and transported to another location in the State or outside of the State within 175 days of the date the property was acquired or imported into Texas. The exemption excludes oil, natural gas, petroleum products, aircraft and special inventory, including motor vehicle, vessel and out-board motor, heavy equipment and manufactured housing inventory. Section 11.253 permits local governmental entities, on a local option basis, to take official action, after holding a public hearing, by January 1 of the first tax year in which the governing body proposes to tax goods-in-transit. A taxpayer may receive only one of the freeport exemption or the goods-in-transit exemption for items of personal property.

A city or county may create a tax increment financing district ("TIF") within the city or county with defined boundaries and establish a base value of taxable property in the TIF at the time of its creation. Overlapping taxing units, including school districts, may agree with the city or county to contribute all or part of future ad valorem taxes levied and collected against the "incremental value" (taxable value in excess of the base value) of taxable real property in the TIF to pay or finance the costs of certain public improvements in the TIF, and such taxes levied and collected for and on behalf of the TIF are not available for general use by such contributing taxing units. Prior to September 1, 2001, school districts were allowed to enter into tax abatement agreements to encourage economic development. Under such agreements, a property owner agrees to construct certain improvements on its property. The school district in turn agrees not to levy a tax on all or part of the increased value attributable to the improvements until the expiration of the agreement. The abatement agreement could last for a period of up to 10 years. School districts have been prohibited from entering into new tax abatement agreements since September 1, 2001. In addition, credit will not be given by the Commissioner of Education in determining a district's property value wealth per student for (1) the appraised value, in excess of the "frozen" value, of property that is located in a TIF created after May 31,

1999 (except in certain limited circumstances where the municipality creating the tax increment financing zone gave notice prior to May 31, 1999 to all other taxing units that levy ad valorem taxes in the TIF of its intention to create the TIF and the TIF was created and had its final project and financing plan approved by the municipality prior to August 31, 1999), or (2) for the loss of value of abated property under any abatement agreement entered into after May 31, 1993. Notwithstanding the foregoing, in 2001 the Legislature enacted legislation known as the Texas Economic Development Act, which provides incentives for school districts to grant limitations on appraised property values and provide ad valorem tax credits to certain corporations and limited liability companies to encourage economic development within the district. Generally, during the last eight years of the ten-year term of a tax limitation agreement, the school district may only levy and collect ad valorem taxes for maintenance and operation purposes on the agreed-to limited appraised property value. The taxpayer is entitled to a tax credit from the school district for the amount of taxes imposed during the first two years of the tax limitation agreement on the appraised value of the property above the agreed-to limited value. Additional State funding is provided to a school district for each year of such tax limitation in the amount of the tax credit provided to the taxpayer. During the first two years of a tax limitation agreement, the school district may not adopt a tax rate that exceeds the district's rollback tax rate (see "TAX INFORMATION - Public Hearing and Rollback Tax Rate" and "TAX INFORMATION – District Application of Tax Code").

**TAX RATE LIMITATIONS** . . . A school district is authorized to levy maintenance and operation ("M&O") taxes subject to approval of a proposition submitted to district voters under Section 45.003(d) of the Texas Education Code, as amended. The maximum M&O tax rate that may be levied by a district cannot exceed the voted maximum rate or the maximum rate described in the succeeding paragraphs. The maximum voted M&O tax rate for the District is \$1.50 per \$100 of assessed valuation as approved by the voters at an election held on September 6, 2000, under Chapter 20, Texas Education Code (now codified at Section 45.003, Texas Education Code).

The maximum tax rate per \$100 of assessed valuation that may be adopted by the District may not exceed the lesser of (A) \$1.50 and (B) the sum of (1) the rate of \$0.17, and (2) the product of the "State Compression Percentage" multiplied by \$1.50. The State Compression Percentage has been set, and will remain, at 66.67% for the 2018-19 State fiscal biennium. The State Compression Percentage is set by legislative appropriation for each State fiscal biennium or, in the absence of legislative appropriation, by the Commissioner. For a more detailed description of the State Compression Percentage, see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM – Local Funding for School Districts". Furthermore, a school district cannot annually increase its tax rate in excess of the district's "rollback tax rate" without submitting such tax rate to a referendum election and a majority of the voters voting at such election approving the adopted rate. See "TAX INFORMATION - Public Hearing and Rollback Tax Rate."

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

Section 45.0031, Texas Education Code, as amended ("Section 45.0031"), requires a district to demonstrate to the Texas Attorney General that it has the prospective ability to pay its maximum annual debt service on a proposed issue of bonds and all previously issued bonds, other than bonds approved by district voters at an election held on or before April 1, 1991 and issued before September 1, 1992 (or debt issued to refund such bonds, collectively, "exempt bonds"), from a tax levied at a rate of \$0.50 per \$100 of assessed valuation before bonds may be issued. In demonstrating the ability to pay debt service at a rate of \$0.50, a district may take into account EDA and IFA allotments to the district, which effectively reduce the district's local share of debt service, and may also take into account Tier One funds allotted to the district. The District is required to deposit any State allotments provided solely for payment of debt service into the District's interest and sinking fund upon receipt of such amounts. In addition, the District must, prior to levying an interest and sinking fund tax rate that exceeds \$0.50 per \$100 of assessed valuation, credit to the interest and sinking fund other State assistance, including Tier One funds that may be used for either operating purposes or for payment of debt service, in an amount equal to the amount needed to demonstrate compliance with the threshold tax rate test and which is received or to be received in that year. Once the prospective ability to pay such tax has been shown and the bonds are issued, a district may levy an unlimited tax to pay debt service. Taxes levied to pay refunding bonds issued pursuant to Chapter 1207, Texas Government Code, are not subject to the \$0.50 tax rate test; however, taxes levied to pay debt service on such bonds (other than bonds issued to refund exempt bonds) are included in maximum annual debt service for calculation of the \$0.50 threshold tax rate test when applied to subsequent bond issues. The Bonds are issued as "new debt" and are subject to the \$0.50 threshold tax rate test. Under current law, a district may demonstrate its ability to comply with the \$0.50 threshold tax rate test by applying the \$0.50 tax rate to an amount equal to 90% of projected future taxable value of property in the district, as certified by a registered professional appraiser, anticipated for the earlier of the tax year five years after the current tax year or the tax year in which the final payment for the bonds is due. However, if a district uses projected future taxable values to meet the \$0.50 threshold tax rate test and subsequently imposes a tax at a rate greater than \$0.50 per \$100 of valuation to pay for bonds subject to the test, then for subsequent bond issues, the Texas Attorney General must find that the district has the projected ability to pay principal and interest on the proposed bonds and all previously issued bonds subject to the \$0.50 threshold tax rate test from a tax rate of \$0.45 per \$100 of valuation. The District has not used and will not use projected property values to satisfy this threshold test.

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

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

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

**PROPERTY ASSESSMENT AND TAX PAYMENT . . .** Property within the District is generally assessed as of January 1 of each year. Business inventory may, at the option of the taxpayer, be assessed as of September 1. Oil and gas reserves are assessed on the basis of a valuation process which uses pricing information contained in either the standard edition of the Annual Energy Outlook or, if the most recently published edition of the Annual Energy Outlook was published before December 1 of the preceding calendar year, the Short-Term Energy Outlook report published in January of the current calendar year. Taxes become due October 1 of the same year, and become delinquent on February 1 of the following year. Taxpayers 65 years old or older are permitted by State law to pay taxes on homesteads in four installments with the first installment due on February 1 of each year and the final installment due on August 1.

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

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

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

Taxes levied by the District are a personal obligation of the owner of the property. On January 1 of each year, a tax lien attaches to property to secure the payment of all taxes, penalties and interest ultimately imposed for the year on the property. The lien exists in favor of the State and each taxing unit, including the District, having the power to tax the property. The District's tax lien is on a parity with tax liens of all other such taxing units. A tax lien on real property has priority over the claim of most creditors and other holders of liens on the property encumbered by the tax lien, whether or not the debt or lien existed before the attachment of the tax lien. Personal property under certain circumstances is subject to seizure and sale for the payment of delinquent taxes, penalty and interest. Except with respect to taxpayers who are 65 years of age or older or disabled. At any time after taxes on property become delinquent, the District may file suit to foreclose the lien securing payment of the tax, to enforce personal liability for the tax, or both. In filing a suit to foreclose a tax lien on real property, the District must join other taxing units that have claims for delinquent taxes against all or part of the same property. The ability of the District to collect delinquent taxes by foreclosure may be adversely affected by the amount of taxes owed to other taxing units, adverse market conditions, taxpayer redemption rights, or bankruptcy proceedings which restrain the collection of a taxpayer's debt. **Federal bankruptcy law provides that an automatic stay of actions by creditors and other entities, including governmental units, goes into effect with the filing of any petition in bankruptcy. The automatic stay prevents governmental units from foreclosing on property and prevents liens for post-petition taxes from attaching to property and obtaining secured creditor status unless, in either case, an order lifting the stay is obtained from the bankruptcy court. In many cases post-petition taxes are paid as an administrative expense of the estate in bankruptcy or by order of the bankruptcy court.**

**DISTRICT APPLICATION OF TAX CODE . . .** The District has not granted any part of the additional exemption of up to 20% of the market value of residence homesteads. The District has granted an additional \$3,000 exemption of the market value of the residence homestead of persons 65 years of age or older and the disabled.

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

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

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

The District does not permit split payments of taxes, and discounts for early payment of taxes are not allowed.

The District does not tax freeport property.

The District has not adopted a tax abatement policy or entered into any tax limitation agreements.

The District does not participate in any Tax Increment Finance ("TIF") Zones.

**TABLE 1 - VALUATION, EXEMPTIONS AND TAX SUPPORTED DEBT**

2018/19 Market Valuation Established by the Appraisal District (excluding totally exempt property)		\$ 1,699,332,967
Less Exemptions/Reductions at 100% Market Value:		
State Mandated Residential Homestead Exemptions	\$ 91,179,970	
State Mandated Over 65 Homestead Exemptions	12,328,058	
State Mandated Disabled Persons Homestead Exemptions	2,547,412	
Disabled Veterans Exemptions	7,107,430	
Over 65-Local Exemptions	3,530,418	
Pollution Control	1,008,920	
Productivity Loss	133,116,943	
Capped Value Loss	12,432,697	
Prorated Exemptions	740	
Freeze Value Loss	45,425,546	(308,678,134)
2018/19 Taxable Assessed Valuation		\$ 1,390,654,833
Debt Payable from Ad Valorem Taxes estimated as of 12/20/18		
Outstanding Unlimited Tax Bonds <sup>(1)</sup>	\$ 97,725,498	
The Bonds	37,160,000	
Total Debt Payable from Ad Valorem Taxes estimated as of 12/20/18 <sup>(1)(2)</sup>		\$ 134,885,498
Ratio Tax Supported Debt to Taxable Assessed Valuation <sup>(1)</sup>		9.70%

Current Estimated District Population - 28,745  
Per Capita Taxable Assessed Valuation - \$48,379  
Per Capita General Obligation Debt - \$4,692

(1) Does not include any "other obligations" outstanding (see "Table 10 - Other Obligations").

**TABLE 2 - TAXABLE ASSESSED VALUATIONS BY CATEGORY**

Category	Taxable Appraised Value for Fiscal Year Ended August 31,					
	2019		2018		2017	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Real, Residential, Single-Family	\$ 606,221,385	35.67%	\$ 525,738,831	35.42%	\$ 457,209,768	34.40%
Real, Residential, Multi-Family	18,451,678	1.09%	17,431,619	1.17%	15,930,333	1.20%
Real, Vacant Lots/Tracts	383,967,919	22.60%	314,535,393	21.19%	277,828,358	20.91%
Acreage (Land Only)	150,167,589	8.84%	140,887,197	9.49%	122,437,033	9.21%
Farm & Ranch Improvements	147,066,601	8.65%	125,180,007	8.43%	101,337,157	7.63%
Real, Commercial and Industrial	161,689,263	9.51%	148,158,482	9.98%	142,076,470	10.69%
Oil, Mineral & Gas and Non-Producing Minerals	3,955,755	0.23%	2,561,560	0.17%	2,395,323	0.18%
Utilities	57,735,270	3.40%	59,039,120	3.98%	54,478,420	4.10%
Tangible Personal, Business & Industrial	103,517,047	6.09%	97,920,593	6.60%	109,674,993	8.25%
Tangible Personal, Mobile Homes	52,713,380	3.10%	40,583,560	2.73%	32,357,040	2.43%
Real Property and Special, Inventory	13,847,080	0.81%	12,181,910	0.82%	13,226,690	1.00%
Total Appraised Value Before Exemptions	\$ 1,699,332,967	100.00%	\$ 1,484,218,272	100.00%	\$ 1,328,951,585	100.00%
Less: Total Exemptions/Reductions	(308,678,134)		(288,941,623)		(252,704,299)	
Adjustments	-		-		(4,309,414)	
Taxable Assessed Value	<u>\$ 1,390,654,833</u>		<u>\$ 1,195,276,649</u>		<u>\$ 1,071,937,872</u>	

Category	Taxable Appraised Value for Fiscal Year Ended August 31,			
	2016		2015	
	Amount	% of Total	Amount	% of Total
Real, Residential, Single-Family	\$ 400,385,292	34.48%	\$ 408,797,937	38.94%
Real, Residential, Multi-Family	15,513,432	1.34%	16,534,912	1.57%
Real, Vacant Lots/Tracts	188,063,489	16.20%	127,756,021	12.17%
Acreage (Land Only)	110,774,460	9.54%	104,152,214	9.92%
Farm & Ranch Improvements	91,886,022	7.91%	58,553,112	5.58%
Real, Commercial and Industrial	138,173,191	11.90%	133,293,900	12.70%
Oil, Mineral & Gas and Non-Producing Minerals	9,781,343	0.84%	19,852,310	1.89%
Utilities	50,605,170	4.36%	47,736,740	4.55%
Tangible Personal, Business & Industrial	97,661,922	8.41%	100,383,586	9.56%
Tangible Personal, Mobile Homes	24,676,520	2.13%	24,554,660	2.34%
Real Property and Special, Inventory	33,700,880	2.90%	8,327,240	0.79%
Total Appraised Value Before Exemptions	\$ 1,161,221,721	100.00%	\$ 1,049,942,632	100.00%
Less: Total Exemptions/Reductions	(231,907,085)		(191,327,427)	
Adjustments	3,385,666		(8,308,197)	
Taxable Assessed Value	<u>\$ 932,700,302</u>		<u>\$ 850,307,008</u>	

Valuations shown are certified taxable assessed values reported by the Appraisal District to the State Comptroller of Public Accounts. Certified values are subject to change throughout the year as contested values are resolved and the Appraisal District updates records.

**TABLE 3 - VALUATION AND TAX SUPPORTED DEBT HISTORY**

Fiscal Year Ended 8/31	Estimated Population <sup>(1)</sup>	Taxable Assessed Valuation <sup>(2)</sup>	Taxable Assessed Valuation Per Capita	Tax Debt Outstanding at End of Fiscal Year	Ratio of Tax Debt to Taxable Assessed Valuation	Tax Debt Per Capita
2015	21,517	\$ 850,307,008	\$ 39,518	\$ 35,397,395	4.16%	\$ 1,645
2016	23,137	932,700,302	40,312	64,639,845	6.93%	2,794
2017	26,912	1,071,937,872	39,831	67,856,765	6.33%	2,521
2018	27,376	1,195,276,649	43,661	97,725,498	8.18%	3,570
2019	28,745	1,390,654,833	48,379	134,044,989 <sup>(3)</sup>	9.64% <sup>(3)</sup>	4,663 <sup>(3)</sup>

(1) Source: Municipal Advisory Council of Texas.

(2) As reported by the Appraisal District on the District's annual State Property Tax Reports and is subject to change during the ensuing year.

(3) Includes the Bonds. Does not include any "other obligations" outstanding (see "Table 10 - Other Obligations").

**TABLE 4 - TAX RATE, LEVY AND COLLECTION HISTORY**

Fiscal Year Ended 8/31	Tax Rate			Tax Levy	% Current Collections	% Total Collections
	Local Maintenance	Interest & Sinking	Total Rate			
2015	\$ 1.04000	\$ 0.27500	\$ 1.31500	\$ 11,181,537	89.12%	97.36%
2016	1.04000	0.27500	1.31500	12,265,009	89.21%	97.17%
2017	1.04000	0.34000	1.38000	14,792,743	87.56%	93.60%
2018	1.04000	0.37500	1.41500	17,384,292	91.50% <sup>(1)</sup>	100.66% <sup>(1)</sup>
2019	1.04000	0.37500	1.41500	19,719,549	N/A	N/A

(1) Unaudited collections as of August 31, 2018.

**TABLE 5 - TEN LARGEST TAXPAYERS**

Name of Taxpayer	Nature of Property	2018/19 Taxable Assessed Valuation	% of Total Taxable Assessed Valuation
Colony Ridge Development LLC	Housing Development	\$ 42,919,350	3.09%
Entergy Texas Inc.	Electric Utility	23,879,260	1.72%
5G LP	Real Estate	10,967,455	0.79%
Tennessee Gas Pipeline	Pipeline	9,471,700	0.52%
Walmart Real Estate	Real Estate	8,029,950	0.45%
Union Pacific Railroad Co.	Railroad	7,217,390	0.49%
BNSF Railway Co.	Railroad	6,822,810	0.38%
Waste Services of Texas, LLC	Waste Collection Services	6,291,220	0.37%
Pavers Supply Co.	Construction	5,266,060	0.58%
Wal-Mart Store #249	Retail	5,083,730	0.68%
		<u>\$ 125,948,925</u>	<u>9.06%</u>

**TABLE 6 - ESTIMATED OVERLAPPING DEBT**

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

Taxing Jurisdiction	2018/19	2018/19	Total	Estimated	District's
	Taxable		Tax		Overlapping
	Assessed	Tax	Supported	%	Tax
	Value	Rate	Debt As Of	Applicable	Supported
			12/20/2018		Debt As Of
					12/20/2018
Cleveland ISD	\$ 1,390,654,833	\$ 1.4150	\$ 134,885,498 <sup>(1)</sup>	100.00%	\$ 134,885,498 <sup>(1)</sup>
City of Cleveland	402,986,781	0.7700	14,810,000	100.00%	14,810,000
Liberty County	6,071,290,406	0.5880	10,150,000	20.49%	2,079,735
Montgomery County	54,281,981,939	0.4667	545,775,000	0.03%	163,733
San Jacinto County	1,887,044,110	0.4712	1,645,000	6.98%	114,821
Total Direct and Overlapping Tax Supported Debt					\$ 152,053,787
Ratio of Direct and Overlapping Tax Supported Debt to Taxable Assessed Valuation					10.93%
Per Capita Direct and Overlapping Tax Supported Debt					\$ 5,290

(1) Includes the Bonds. Does not include any “other obligations” outstanding payable from the District’s M&O tax (see “Table 10 - Other Obligations”).

**DEBT INFORMATION**

**TABLE 7 - TAX SUPPORTED DEBT SERVICE REQUIREMENTS**

Fiscal Year Ending	Outstanding Debt <sup>(1)</sup>			The Bonds			Total Debt Service Requirements	% of Principal Retired
	Principal	Interest	Total	Principal	Interest	Total		
2019	\$ 840,510	\$ 5,244,915	\$ 6,085,425	\$ -	\$ 1,119,612	\$ 1,119,612	\$ 7,205,037	0.62%
2020	2,000,000	4,293,425	6,293,425	-	1,715,150	1,715,150	8,008,575	2.11%
2021	2,040,000	4,233,125	6,273,125	-	1,715,150	1,715,150	7,988,275	3.62%
2022	2,215,000	4,169,800	6,384,800	-	1,715,150	1,715,150	8,099,950	5.26%
2023	2,225,000	4,102,350	6,327,350	-	1,715,150	1,715,150	8,042,500	6.91%
2024	2,320,000	4,028,550	6,348,550	-	1,715,150	1,715,150	8,063,700	8.63%
2025	1,680,204	4,898,959	6,579,163	135,000	1,712,450	1,847,450	8,426,613	9.98%
2026	1,654,785	4,874,740	6,529,525	465,000	1,698,125	2,163,125	8,692,650	11.55%
2027	2,635,000	3,827,500	6,462,500	745,000	1,667,878	2,412,878	8,875,378	14.05%
2028	2,790,000	3,719,000	6,509,000	920,000	1,626,250	2,546,250	9,055,250	16.80%
2029	2,945,000	3,604,300	6,549,300	970,000	1,579,000	2,549,000	9,098,300	19.71%
2030	3,070,000	3,484,269	6,554,269	1,050,000	1,533,750	2,583,750	9,138,019	22.76%
2031	3,190,000	3,359,619	6,549,619	1,105,000	1,485,125	2,590,125	9,139,744	25.94%
2032	3,920,000	3,217,700	7,137,700	555,000	1,443,625	1,998,625	9,136,325	29.26%
2033	4,105,000	3,057,200	7,162,200	560,000	1,415,750	1,975,750	9,137,950	32.72%
2034	2,875,000	2,909,125	5,784,125	1,990,000	1,361,950	3,351,950	9,136,075	36.33%
2035	3,005,000	2,774,150	5,779,150	2,090,000	1,269,900	3,359,900	9,139,050	40.10%
2036	3,150,000	2,627,775	5,777,775	1,825,000	1,172,025	2,997,025	8,774,800	43.79%
2037	3,320,000	2,468,825	5,788,825	1,900,000	1,088,400	2,988,400	8,777,225	47.66%
2038	3,195,000	2,307,375	5,502,375	2,255,000	1,005,300	3,260,300	8,762,675	51.70%
2039	3,365,000	2,143,375	5,508,375	2,340,000	913,400	3,253,400	8,761,775	55.93%
2040	3,535,000	1,970,875	5,505,875	2,475,000	804,725	3,279,725	8,785,600	60.39%
2041	3,715,000	1,789,625	5,504,625	2,580,000	678,350	3,258,350	8,762,975	65.06%
2042	3,900,000	1,599,250	5,499,250	2,720,000	545,850	3,265,850	8,765,100	69.96%
2043	4,100,000	1,399,250	5,499,250	2,855,000	406,475	3,261,475	8,760,725	75.12%
2044	4,305,000	1,189,125	5,494,125	3,010,000	259,850	3,269,850	8,763,975	80.54%
2045	7,880,000	884,500	8,764,500	-	184,600	184,600	8,949,100	86.38%
2046	8,285,000	480,375	8,765,375	-	184,600	184,600	8,949,975	92.53%
2047	5,465,000	136,625	5,601,625	-	184,600	184,600	5,786,225	96.58%
2048	-	-	-	4,615,000	92,300	4,707,300	4,707,300	100.00%
	<u>\$ 97,725,498</u>	<u>\$ 84,795,702</u>	<u>\$ 182,521,201</u>	<u>\$ 37,160,000</u>	<u>\$ 34,009,640</u>	<u>\$ 71,169,640</u>	<u>\$253,690,841</u>	

(1) "Outstanding Debt" does not include any "other obligations" outstanding (see "Table 10 - Other Obligations").

**TABLE 8 - INTEREST AND SINKING FUND BUDGET PROJECTION**

Tax Supported Debt Service Requirements, Fiscal Year Ending 8/31/19		\$ 7,205,037
Unaudited Interest and Sinking Fund Balance (as of 8/31/18)	\$ 6,389,455	
Estimated Interest and Sinking Fund Tax Revenues	5,143,562	
Existing Debt Allotment	891,814 <sup>(1)</sup>	
Instructional Facilities Allotment Funds	400,220 <sup>(1)</sup>	
Total Projections		<u>\$ 12,825,051</u>
Estimated Balance, Fiscal Year Ending 8/31/19		<u>\$ 5,620,014</u>

(1) The amount of State aid for debt service (i.e., Existing Debt Allotment and Instructional Facilities Allotment) may substantially differ from year to year depending on a number of factors, including property tax base, average student daily attendance, and the amounts, if any, appropriated for that purpose by the Texas Legislature (see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM").

**TABLE 9 - AUTHORIZED BUT UNISSUED UNLIMITED TAX BONDS**

After the issuance of the Bonds, the District will not have any authorized but unissued unlimited tax bonds.

**ANTICIPATED ISSUANCE OF ADDITIONAL UNLIMITED TAX DEBT** . . . The District does not plan to issue additional unlimited tax debt within the next twelve months.

**TABLE 10 - OTHER OBLIGATIONS**

The District has the following commitments under operating (noncapitalized) lease agreements for copiers which provides for minimum future rental payments beyond the current year:

Fiscal Year Ending <u>August 31</u>	<u>Total</u>
2018	\$ 207,438
2019	161,499
2020	161,499
2021	161,499
2022	<u>148,041</u>
Total minimum lease payments	\$ 839,976
Rental Expenditures for the Fiscal Year Ending August 31, 2017	\$ 208,047

The District had no capital leases outstanding during the current year.

**PENSION FUND** . . . Pension funds for employees of Texas school districts, and any employee in public education in Texas, are administered by the Teacher Retirement System of Texas (the “System”). The individual employees contribute a fixed amount of their salary to the System, currently 7.7%, and the State of Texas contributes funds to the System based on statutory required minimum salary for certified personnel, except any District personnel paid by Federally funded programs. (For more detailed information concerning the retirement plan, see Appendix B, “Excerpts from the District’s Annual Financial Report” - Note 8.)

Contribution requirements are established or amended pursuant to Article 16, section 67 of the Texas Constitution which requires the Texas legislature to establish a member contribution rate of not less than 6% of the member’s annual compensation and a state contribution rate of not less than 6% and not more than 10% of the aggregate annual compensation paid to members of the system during the fiscal year. Texas Government Code section 821.006 prohibits benefit improvements, if as a result of the particular action, the time required to amortize TRS’ unfunded actuarial liabilities would be increased to a period that exceeds 31 years, or, if the amortization period already exceeds 31 years, the period would be increased by such action.

Employee contribution rates are set in state statute, Texas Government Code 825.402. Senate Bill 1458 of the 83<sup>rd</sup> Texas Legislature amended Texas Government Code 825.402 for member contributions and established employee contribution rates for fiscal 2014 thru 2017. It also added a 1.5% contribution for employers not paying Old Age Survivor and Disability Insurance (OASDI) on certain employees effective for fiscal 2015 as discussed in Note 1 of the TRS 2014 CAFR. The 83<sup>rd</sup> Texas Legislature, General Appropriations Act (GAA) established the employer contribution rates for fiscal years 2014 and 2015. The 84<sup>th</sup> Texas Legislature, General Appropriations Act established the employer contribution rates for fiscal years 2016 and 2017 (using the state year end of August 31) as follows:

<u>Contribution Rates</u>	<u>2016</u>	<u>2017</u>
Member	7.2%	7.7%
Non-Employer Contributing Entity (State)	6.8%	6.8%
Employers	6.8%	6.8%
 <u>Contribution Amounts</u>		
Employer Contributions	\$ 725,127	\$ 760,469
Member Contributions	1,550,198	1,847,174
NECE On-Behalf Contributions	1,352,998	1,416,210

**RETIREE HEALTH PLAN . . .** The District contributes to the Texas Public School Retired Employees Group Insurance Program (TRS-Care), a cost-sharing multiple-employer defined benefit postemployment health care plan administered by the Teacher Retirement System of Texas. Contribution requirements are not actuarially determined but are legally established each biennium by the Texas Legislature. TIC, Sections 1575.202, 203 and 204 establish state, active employee and public school contributions, respectively. Funding for free basic coverage is provided by the program based upon public school district payroll. Per TIC, Chapter 1575, the public school contribution may not be less than 0.25% or greater than 0.75% of the salary of each active employee of the public school. Funding for optional coverage is provided by those participants selecting the optional coverage. The State of Texas and active public school employee contribution rates were 1.0% and 0.65% of the public school payroll, respectively, with school districts contributing a percentage of payrolls set at 0.55% for fiscal years 2016 and 2017.

**OTHER POST EMPLOYMENT BENEFITS . . .** As a result of its participation in the System and having no other post-retirement benefit plans, the District has no obligations for other post-employment benefits within the meaning of Governmental Accounting Standards Board Statement 45.

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**FINANCIAL INFORMATION**

**TABLE 11 - SCHEDULE OF CHANGES IN NET POSITION**

	Fiscal Year Ended August 31,				
	2017	2016	2015	2014	2013
<b>REVENUES:</b>					
<b>Program Revenues:</b>					
Charges for Services	\$ 357,650	\$ 640,194	\$ 648,545	\$ 671,934	\$ 613,881
Operating Grants and Contributions	5,671,913	6,974,700	6,210,629	5,836,696	4,982,448
<b>General Revenues:</b>					
Property Taxes, Levied for General Purposes	11,625,062	9,670,352	8,892,729	7,828,297	7,475,350
Property Taxes, Levied for Debt Service	3,698,545	2,565,572	2,351,248	2,050,702	1,956,714
State Aid - Formula Grants	26,183,383	24,674,595	21,988,875	20,695,340	18,670,837
Grants and Contributions (not restricted)	2,400,902	-	-	-	-
Investment Earnings	229,747	151,766	91,538	80,523	160,098
Penalty and Interest - Taxes	-	-	-	571,675	621,516
Miscellaneous	446,659	589,804	501,898	98,598	307,229
Total Revenues	\$ 50,613,861	\$ 45,266,983	\$ 40,685,462	\$ 37,833,765	\$ 34,788,073
<b>EXPENSES:</b>					
Instruction, Curriculum and Media Services	\$ 24,080,389	\$ 22,686,206	\$ 19,610,526	\$ 18,901,591	\$ 17,010,616
Instructional and School Leadership	2,938,080	2,581,017	2,291,296	1,971,183	1,796,238
Student Support Services	3,074,202	2,840,450	2,563,245	2,917,973	2,515,839
Food Services	2,555,520	2,519,009	2,123,640	1,944,016	1,913,779
Cocurricular Activities	1,146,820	971,397	821,881	817,079	721,352
General Administration	1,891,273	1,495,925	1,419,083	1,329,514	1,003,142
Plant Maintenance, Security and Data Processing	5,193,544	4,772,513	4,278,491	4,686,829	3,752,009
Community Services	14,440	8,191	1,758	7,284	31,898
Debt Services - Interest and Fees	2,992,648	2,097,645	1,757,147	1,812,615	1,536,997
Capital Outlay	-	41,410	-	-	-
Payments Related to Shared Service Arrangements	590,880	392,609	499,361	394,033	492,560
Other Intergovernmental Charges-CAD	337,199	299,612	269,617	256,973	252,618
Total Expenses	\$ 44,814,995	\$ 40,705,984	\$ 35,636,045	\$ 35,039,090	\$ 31,027,048
Gain (Loss) on Sale of Assets	23,541	-	-	-	-
Increase in Net Assets	\$ 5,822,407	\$ 4,560,999	\$ 5,049,417	\$ 2,794,675	\$ 3,761,025
Net Assets Beginning	34,176,263	29,615,264	28,299,774	25,505,099	22,246,906
Prior Period Adjustment	-	-	(3,733,927) <sup>(1)</sup>	-	(502,832)
Net Assets at August 31	\$ 39,998,670	\$ 34,176,263	\$ 29,615,264	\$ 28,299,774	\$ 25,505,099

(1) As a result of the implementation of GASB Statement No. 68, an adjustment was made to record the District's proportionate share of the Net Pension Liability of the Teachers Retirement System of Texas.

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

	Fiscal Years Ended August 31,				
	2017	2016	2015	2014	2013
<u>Revenues:</u>					
Local and Intermediate Sources	\$ 11,472,058	\$ 10,346,905	\$ 9,516,539	\$ 8,525,238	\$ 8,356,302
State Sources	27,671,508	24,818,820	22,113,506	20,831,851	18,415,663
Federal Sources	1,214,010	610,098	698,067	338,975	343,670
Total Revenues	<u>\$ 40,357,576</u>	<u>\$ 35,775,823</u>	<u>\$ 32,328,112</u>	<u>\$ 29,696,064</u>	<u>\$ 27,115,635</u>
<u>Expenditures:</u>					
Instruction	\$ 20,189,352	\$ 18,207,987	\$ 15,882,560	\$ 14,558,757	\$ 13,441,572
Instructional Resources and Media Services	270,604	281,044	279,512	326,345	312,545
Curriculum and Instructional Staff Development	323,508	215,088	272,302	475,814	376,690
Instructional Leadership	165,945	133,904	131,852	20,982	-
School Leadership	2,616,473	2,317,903	2,135,505	1,890,777	1,730,838
Guidance, Counseling and Evaluation Services	830,960	768,422	678,687	690,667	597,924
Social Work Services	-	-	17,643	14,154	-
Health Services	307,498	303,720	267,077	306,682	242,835
Student (Pupil) Transportation	2,416,457	2,103,828	1,666,085	1,844,982	1,317,685
Extracurricular Activities	1,082,484	922,193	788,979	775,645	682,197
General Administration	1,584,857	1,429,198	1,397,255	1,290,295	963,923
Facilities Maintenance and Operations	3,720,387	3,391,367	3,179,768	3,439,209	2,806,759
Security and Monitoring Services	605,620	530,165	442,313	571,608	363,937
Data Processing Services	474,361	542,317	425,671	458,834	370,899
Community Services	884	1,098	255	-	-
Facilities Acquisition and Construction	2,528,051	501,949	-	-	-
Payments to Fiscal Agent/Member Districts of SSA	564,966	392,609	499,361	394,033	492,560
Other Intergovernmental Charges	322,411	299,612	269,617	256,973	252,618
Total Expenditures	\$ 38,004,818	\$ 32,342,404	\$ 28,334,442	\$ 27,315,757	\$ 23,952,982
Other Resources and (Uses) & Special Items	<u>\$ 23,541</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Excess (Deficiency) of					
Revenues Over Expenditures	\$ 2,376,299	\$ 3,433,419	\$ 3,993,670	\$ 2,380,307	\$ 3,162,653
Beginning Fund Balance on					
September 1	<u>\$ 25,010,272</u>	<u>\$ 21,576,853</u>	<u>\$ 17,583,183</u>	<u>\$ 15,202,876</u>	<u>\$ 12,040,223</u>
Ending Fund Balance on					
August 31	<u>\$ 27,386,571</u>	<u>\$ 25,010,272</u>	<u>\$ 21,576,853</u>	<u>\$ 17,583,183</u>	<u>\$ 15,202,876</u>

**FINANCIAL POLICIES**

**Summary of Significant Accounting Policies** . . . The financial statements of the District have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to local government units in conjunction with the Texas Education Agency’s Financial Accountability System Resource Guide (FAR). The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

**Basis of Presentation** . . . *Government-wide financial statements* - The statement of net assets and the statement of activities display information about the District as a whole. These statements include the financial activities of the primary government, except for fiduciary funds. Internal Service fund activity is eliminated to avoid overstatement of revenues and expenses. The statements distinguish between governmental and business-type activities of the District.

The government-wide statements are prepared using the economic resources measurement focus. This is the same approach used in the preparation of proprietary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. Governmental fund financial statements therefore include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds.

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each function or program of the governmental activities of the District. Direct expenses are those that are specifically associated with a service, program or department and therefore are clearly identifiable to a particular function. Program revenues include

amounts paid by the recipient of goods or services offered by the program and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. All taxes and revenues not classified as program revenues are presented as general revenues of the District.

*Fund Financial Statements* - Fund financial statements report detailed information about the District. Their focus is on major funds rather than reporting funds by type. Each major governmental aid fund is presented in a separate column, and all nonmajor funds are aggregated into one column. Fiduciary funds are reported by fund type.

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

**Basis of Accounting** . . . Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements.

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

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the District considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures are generally recorded when a liability is incurred, as under accrual accounting.

Revenues from state and federal grants are recognized as earned when the related program expenditures are incurred. Revenues from local sources consist primarily of property taxes. Property tax revenues are recognized under the susceptible to accrual concept. Funds received but unearned are reflected as deferred revenues, and funds expended but not yet received are shown as receivables. For state entitlements, the District has adopted a budgetary basis of accounting for Foundation School Program revenues. Such entitlements are recorded as received.

Interest revenue and building rentals are recorded when earned since they are measurable and available. Other revenues such as fees, tuition, local food service revenue, and miscellaneous revenues are accounted for on the cash basis.

Expenditures are recognized in the accounting period in which the fund liability is incurred when measurable, except expenditures for debt service including unmatured interest on long-term debt. Expenditures for principal and interest on long-term debt are recognized when due.

**Budgetary Data** . . . Budgets are presented on the modified accrual basis of accounting for the General, Food Service, and Debt Service funds. The budget is prepared and controlled at the function level.

The official school budget is prepared for adoption for required governmental funds prior to August 20 of the preceding fiscal year for the subsequent fiscal year beginning September 1. The Board formally adopts the budget at a public meeting held at least ten days after public notice has been given. Once adopted, the budget can be amended by subsequent Board action. The Board properly amended the budget throughout the year.

Such amendments are before the fact and are reflected in the official minutes of the Board.

## INVESTMENTS

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

**LEGAL INVESTMENTS** . . . Under State law, the District is authorized to invest in (1) obligations, including letters of credit, of the United States or its agencies and instrumentalities; (2) direct obligations of the State or its agencies and instrumentalities; (3) collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States; (4) other obligations, the principal of and interest on which is unconditionally guaranteed or insured by, or backed by the full faith and credit of, the State or the United States or their respective agencies and instrumentalities, including obligations that are fully guaranteed or insured by the Federal

Deposit Insurance Corporation or by the explicit full faith and credit of the United States; (5) obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent; (6) obligations issued, assumed or guaranteed by the State of Israel; (7) interest-bearing banking deposits that are guarantee or insured by the Federal Deposit Insurance Corporation or the National Credit Union Share Insurance Fund or their respective successors; (8) certificates of deposit or share certificates (i) that are issued by an institution that has its main office or a branch office in the State of Texas and are guaranteed or insured by the Federal Deposit Insurance Corporation or the National Credit Union Share Insurance Fund, or their respective successors, and are secured as to principal by obligations described in clauses (1) through (7) or in any other manner and provided for by law for District deposits, or (ii) where (a) the funds are invested by the District through (A) a broker that has its main office or a branch office in the State of Texas and is selected from a list adopted by the District as required by law, or (B) a depository institution that has its main office or branch office in the State of Texas that is selected by the District, (b) the broker or the depository institution selected by the District arranges for the deposit of the funds in certificates of deposit in one or more federally insured depository institutions, wherever located, for the account of the District, (c) the full amount of the principal and accrued interest of each of the certificates of deposit is insured by the United States or an instrumentality of the United States, and (d) the District appoints the depository institution selected under (a) above, a custodian as described by Section 2257.041(d) of the Texas Government Code, or a clearing broker-dealer registered with the Securities and Exchange Commission and operating pursuant to Securities and Exchange Commission Rule 15c3-3 (17 C.F.R. Section 240.15c3-3) as custodian for the District with respect to the certificates of deposit; (9) fully collateralized repurchase agreements that (i) have a defined termination date, (ii) are fully secured by a combination of cash and obligations described in clause (1) above, (iii) require the securities being purchased by the District or cash held by the District to be pledged to the District, held in the District's name, and deposited at the time the investment is made with the District or with a third party selected and approved by the District, and (iv) are placed through a primary government securities dealer, as defined by the Federal Reserve, or a financial institution doing business in the State of Texas; (10) securities lending programs if (i) the securities loaned under the program are 100% collateralized, a loan made under the program allows for termination at any time and a loan under the program is either secured by (a) obligations that are described in clauses (1) through (7) above, (b) irrevocable letters of credit issued by a state or national bank that is continuously rated by a nationally recognized investment rating firm of not less than A or its equivalent or (c) cash invested in obligations described in clauses (1) through (6) above, clauses (12) through (14) below, or an authorized investment pool, (ii) securities held as collateral under a loan are pledged to the District, held in the District's name and deposited at the time the investment is made with the governmental body or a third party designated by the governmental body, (iii) a loan made under the program is placed through either a primary government securities dealer or a financial institution doing business in the State of Texas, and (iv) the agreement to lend securities obligations of the accepting bank or its parents are rated at least A-1 or P-1 or the equivalent by at least one nationally recognized credit rating agency; (11) certain bankers' acceptances with the remaining term of 270 days or less, if the short-term obligations of the accepting bank or its parent are rated at least A-1 or P-1 or the equivalent by at least one nationally recognized credit rating agency; (12) commercial paper with a stated maturity of 270 days or less that is rated at least A-1 or P-1 or the equivalent by either (a) two nationally recognized credit rating agencies or (b) one nationally recognized credit rating agency if the paper is fully secured by an irrevocable letter of credit issued by a U.S. or state bank; (13) no-load money market mutual funds registered with and regulated by the Securities and Exchange Commission that comply with Securities and Exchange Commission Rule 2a-7; and (14) no-load mutual funds registered with the Securities and Exchange Commission that have an average weighted maturity of less than two years, and either have a duration of one year or more and invest exclusively in obligations described in this paragraph, or have a duration of less than one year and the investment portfolio is limited to investment grade securities, excluding asset-backed securities. In addition, bond proceeds may be invested in guaranteed investment contracts that have a defined termination date and are secured by obligations, including letters of credit, of the United States or its agencies and instrumentalities in an amount at least equal to the amount of bond proceeds invested under such contract, other than the prohibited obligations described in the next succeeding paragraph.

The District may invest in such obligations directly or through government investment pools that invest solely in such obligations provided that the pools are rated no lower than AAA or AAAM or an equivalent by at least one nationally recognized rating service or no lower than investment grade by at least one nationally recognized rating service with a weighted average maturity no greater than 90 days. The District may also contract with an investment management firm registered under the Investment Advisers Act of 1940 (15 U.S.C. Section 80b-1 et seq.) or with the State Securities Board to provide for the investment and management of its public funds or other funds under its control for a term up to two years, but the District retains ultimate responsibility as fiduciary of its assets. In order to renew or extend such a contract, the District must do so by order, ordinance, or resolution.

The District is also authorized to purchase, sell, and invest its funds in corporate bonds. "Corporate bond" is defined as a senior secured debt obligation issued by a domestic business entity and rated not lower than "AA-" or the equivalent by a nationally recognized investment rating firm (does not include convertible bonds or unsecured debt). The corporate bonds must have a stated final maturity that is not later than 3 years of the date the corporate bonds were purchased. The District may not (1) invest more than 15 percent of its monthly average fund balance (excluding bond proceeds, reserves, and other funds held for the payment of debt service), in corporate bonds; or (2) invest more than 25 percent of the funds invested in corporate bonds in any one domestic business entity, including subsidiaries and affiliates of the entity. The District must sell corporate bonds if they are rated "AA-" or its equivalent and are either downgraded or placed on negative credit watch. Corporate bonds are not an eligible investment for a public funds investment pool.

The District is specifically prohibited from investing in: (1) obligations whose payment represents the coupon payments on the outstanding principal balance of the underlying mortgage-backed security collateral and pays no principal; (2) obligations whose payment represents the principal stream of cash flow from the underlying mortgage-backed security and bears no interest; (3) collateralized mortgage obligations that have a stated final maturity of greater than 10 years; and (4) collateralized mortgage obligations the interest rate of which is determined by an index that adjusts opposite to the changes in a market index.

Under Texas law, the District is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity; that address investment diversification, yield, maturity, and the quality and capability of investment management; and that include a list of authorized investments for District funds, the maximum allowable stated maturity of any individual investment, the maximum average dollar-weighted maturity allowed for pooled fund groups, methods to monitor the market price of investments acquired with public funds, a requirement for settlement of all transactions, except investment pool funds and mutual funds, on a delivery versus payment basis, and procedures to monitor rating changes in investments acquired with public funds and the liquidation of such investments consistent with the PFIA. All District funds must be invested consistent with a formally adopted "Investment Strategy Statement" that specifically addresses each fund's investment. Each Investment Strategy Statement will describe its objectives concerning: (1) suitability of investment type, (2) preservation and safety of principal, (3) liquidity, (4) marketability of each investment, (5) diversification of the portfolio, and (6) yield.

**INVESTMENT POLICIES . . .** Under Texas law, the District is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity; that address investment diversification, yield, maturity, and the quality and capability of investment management; and that include a list of authorized investments for District funds, the maximum allowable stated maturity of any individual investment, the maximum average dollar-weighted maturity allowed for pooled fund groups, methods to monitor the market price of investments acquired with public funds, a requirement for settlement of all transactions, except investment pool funds and mutual funds, on a delivery versus payment basis, and procedures to monitor rating changes in investments acquired with public funds and the liquidation of such investments consistent with the Public Funds Investment Act. All District funds must be invested consistent with a formally adopted "Investment Strategy Statement" that specifically addresses each funds' investment. Each Investment Strategy Statement will describe its objectives concerning: (1) suitability of investment type, (2) preservation and safety of principal, (3) liquidity, (4) marketability of each investment, (5) diversification of the portfolio, and (6) yield.

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

**ADDITIONAL PROVISIONS . . .** Under Texas law, the District is additionally required to: (1) annually review its adopted policies and strategies, (2) adopt a rule, order, ordinance or resolution stating that it has reviewed its investment policy and investment strategies and records any changes made to either its investment policy or investment strategy in the respective rule, order, ordinance or resolution, (3) require any investment officers with personal business relationships or relatives with firms seeking to sell securities to the District to disclose the relationship and file a statement with the Texas Ethics Commission and the Board of Trustees; (4) require the qualified representative of firms offering to engage in an investment transaction with the District to: (a) receive and review the District's investment policy, (b) acknowledge that reasonable controls and procedures have been implemented to preclude investment transactions conducted between the District and the business organization that are not authorized by the District's investment policy (except to the extent that this authorization is dependent on an analysis of the makeup of the District's entire portfolio or requires an interpretation of subjective investment standards), and (c) deliver a written statement in a form acceptable to the District and the business organization attesting to these requirements; (5) perform an annual audit of the management controls on investments and adherence to the District's investment policy; (6) provide specific investment training for the Treasurer, Chief Financial Officer and investment officers; (7) restrict reverse repurchase agreements to not more than 90 days and restrict the investment of reverse repurchase agreement funds to no greater than the term of the reverse purchase agreement; (8) restrict the investment in no-load mutual funds in the aggregate to no more than 15% of the District's monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service; (9) require local government investment pools to conform to the new disclosure, rating, net asset value, yield calculation, and advisory board requirements, and (10) at least annually review, revise, and adopt a list of qualified brokers that are authorized to engage in investment transactions with the District.

**TABLE 12 - CURRENT INVESTMENTS**

As of August 31, 2018, the District’s investable funds were invested in the following categories:

<u>Description of Investment</u>	<u>Percent</u>	<u>Market Value</u>
Investment Pools	47.43%	\$ 12,152,070
Certificates of Deposit	11.80%	3,022,563
Checking Accounts	40.78%	10,448,256
	<u>100.00%</u>	<u>\$ 25,622,889</u>

**TAX MATTERS**

**TAX EXEMPTION . . .** The delivery of the Bonds is subject to the opinion of Bond Counsel to the effect that interest on the Bonds for federal income tax purposes (1) will be excludable from gross income, as defined in section 61 of the Internal Revenue Code of 1986, as amended to the date of such opinion (the “Code”), pursuant to section 103 of the Code and existing regulations, published rulings, and court decisions, and (2) will not be included in computing the alternative minimum taxable income of the owners thereof. A form of Bond Counsel’s opinion is reproduced as Appendix C. The statutes, regulations, rulings, and court decisions on which such opinion is based are subject to change.

In rendering the foregoing opinions, Bond Counsel will rely upon representations and certifications of the District made in a certificate dated the date of delivery of the Bonds pertaining to the use, expenditure, and investment of the proceeds of the Bonds and will assume continuing compliance by the District with the provisions of the Order subsequent to the issuance of the Bonds. The Order contains covenants by the District with respect to, among other matters, the use of the proceeds of the Bonds and the facilities financed therewith by persons other than state or local governmental units, the manner in which the proceeds of the Bonds are to be invested, the periodic calculation and payment to the United States Treasury of arbitrage “profits” from the investment of proceeds, and the reporting of certain information to the United States Treasury. Failure to comply with any of these covenants may cause interest on the Bonds to be includable in the gross income of the owners thereof from the date of the issuance of the Bonds.

Bond Counsel’s opinion is not a guarantee of a result, but represents its legal judgment based upon its review of existing statutes, regulations, published rulings and court decisions and the representations and covenants of the District described above. No ruling has been sought from the Internal Revenue Service (the “IRS”) with respect to the matters addressed in the opinion of Bond Counsel, and Bond Counsel’s opinion is not binding on the IRS. The IRS has an ongoing program of auditing the tax-exempt status of the interest on tax-exempt obligations. If an audit of the Bonds is commenced, under current procedures the IRS is likely to treat the District as the “taxpayer,” and the owners of the Bonds would have no right to participate in the audit process. In responding to or defending an audit of the tax-exempt status of the interest on the Bonds, the District may have different or conflicting interests from the owners of the Bonds. Public awareness of any future audit of the Bonds could adversely affect the value and liquidity of the Bonds during the pendency of the audit, regardless of its ultimate outcome.

Except as described above, Bond Counsel expresses no other opinion with respect to any other federal, state or local tax consequences under present law, or proposed legislation, resulting from the receipt or accrual of interest on, or the acquisition or disposition of, the Bonds. Prospective purchasers of the Bonds should be aware that the ownership of tax-exempt obligations such as the Bonds may result in collateral federal tax consequences to, among others, financial institutions, life insurance companies, property and casualty insurance companies, certain foreign corporations doing business in the United States, S corporations with subchapter C earnings and profits, individual recipients of Social Security or Railroad Retirement benefits, individuals otherwise qualifying for the earned income tax credit, owners of an interest in a financial asset securitization investment trust (“FASIT”), and taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry, or who have paid or incurred certain expenses allocable to, tax-exempt obligations. Prospective purchasers should consult their own tax advisors as to the applicability of these consequences to their particular circumstances.

Existing law may change to reduce or eliminate the benefit to bondholders of the exclusion of interest on the Bonds from gross income for federal income tax purposes. Any proposed legislation or administrative action, whether or not taken, could also affect the value and marketability of the Bonds. Prospective purchasers of the Bonds should consult with their own tax advisors with respect to any proposed or future changes in tax law.

**TAX ACCOUNTING TREATMENT OF DISCOUNT AND PREMIUM ON CERTAIN BONDS. . .**The initial public offering price of certain Bonds (the “Discount Bonds”) may be less than the amount payable on such Bonds at maturity. An amount equal to the difference between the initial public offering price of a Discount Bond (assuming that a substantial amount of the Discount Bonds of that maturity are sold to the public at such price) and the amount payable at maturity constitutes original issue discount to the initial purchaser of such Discount Bond. A portion of such original issue discount allocable to the holding period of such Discount Bond by the initial purchaser will, upon the disposition of such Discount Bond (including by reason of its payment at maturity), be treated as interest excludable from gross income, rather than as taxable gain, for federal income tax purposes, on the same terms and conditions as those for other interest on the Bonds described above under “Tax Exemption.” Such interest is considered to be accrued actuarially in accordance with the constant interest method over the life of a Discount Bond, taking into account the semiannual compounding of accrued interest, at the yield to

maturity on such Discount Bond and generally will be allocated to an initial purchaser in a different amount from the amount of the payment denominated as interest actually received by the initial purchaser during the tax year.

However, such interest may be required to be taken into account in determining the amount of the branch profits tax applicable to certain foreign corporations doing business in the United States, even though there will not be a corresponding cash payment. In addition, the accrual of such interest may result in certain other collateral federal income tax consequences to, among others, financial institutions, life insurance companies, property and casualty insurance companies, S corporations with “subchapter C” earnings and profits, individual recipients of Social Security or Railroad Retirement benefits, individuals otherwise qualifying for the earned income tax credit, owners of an interest in a FASIT, and taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry, or who have paid or incurred certain expenses allocable to, tax-exempt obligations. Moreover, in the event of the redemption, sale or other taxable disposition of a Discount Bond by the initial owner prior to maturity, the amount realized by such owner in excess of the basis of such Discount Bond in the hands of such owner (adjusted upward by the portion of the original issue discount allocable to the period for which such Discount Bond was held) is includable in gross income.

Owners of Discount Bonds should consult with their own tax advisors with respect to the determination of accrued original issue discount on Discount Bonds for federal income tax purposes and with respect to the state and local tax consequences of owning and disposing of Discount Bonds. It is possible that, under applicable provisions governing determination of state and local income taxes, accrued interest on Discount Bonds may be deemed to be received in the year of accrual even though there will not be a corresponding cash payment.

The initial public offering price of certain Bonds (the “Premium Bonds”) may be greater than the amount payable on such Bonds at maturity. An amount equal to the difference between the initial public offering price of a Premium Bond (assuming that a substantial amount of the Premium Bonds of that maturity are sold to the public at such price) and the amount payable at maturity constitutes premium to the initial purchaser of such Premium Bonds. The basis for federal income tax purposes of a Premium Bond in the hands of such initial purchaser must be reduced each year by the amortizable bond premium, although no federal income tax deduction is allowed as a result of such reduction in basis for amortizable bond premium. Such reduction in basis will increase the amount of any gain (or decrease the amount of any loss) to be recognized for federal income tax purposes upon a sale or other taxable disposition of a Premium Bond. The amount of premium which is amortizable each year by an initial purchaser is determined by using such purchaser's yield to maturity.

Purchasers of the Premium Bonds should consult with their own tax advisors with respect to the determination of amortizable bond premium on Premium Bonds for federal income tax purposes and with respect to the state and local tax consequences of owning and disposing of Premium Bonds.

#### **CONTINUING DISCLOSURE INFORMATION**

In the Order, the District has made the following agreement for the benefit of the holders and beneficial owners of the Bonds. The District is required to observe the agreement for so long as it remains obligated to advance funds to pay the Bonds pursuant to the United States Securities and Exchange Commission's (the “SEC”) rule 15c2-12 (the “Rule”). Under the agreement, the District will be obligated to provide certain updated financial information and operating data annually, and timely notice of certain specified events, to the Municipal Securities Rulemaking Board (the “MSRB”). See “THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM” for a description of the TEA's continuing disclosure undertaking to provide certain updated financial information and operating data annually with respect to the Permanent School Fund and the State of Texas, as the case may be, and to provide timely notice of certain specified events related to the guarantee to the MSRB.

**ANNUAL REPORTS . . .** The District shall provide annually to the MSRB, (1) within six months after the end of each fiscal year of the District ending in or after 2018, financial information and operating data with respect to the District of the general type included in this Official Statement under Tables numbered 1 through 5 and 7 through 12 and (2) if not provided as part such financial information and operating data, audited financial statements of the District, when and if available. Any financial statements to be provided shall be (i) prepared in accordance with the accounting principles described in Appendix B hereto or such other accounting principles as the District may be required to employ from time to time pursuant to state law or regulation, and in substantially the form included in Appendix B hereto, and (ii) audited, if the District commissions an audit of such financial statements and the audit is completed within the period during which they must be provided. If the audit of such financial statements is not complete within 12 months after any such fiscal year end, then the District shall file unaudited financial statements within such 12-month period and audited financial statements for the applicable fiscal year, when and if the audit report on such statements becomes available. Any such financial statements will be prepared in accordance with the accounting principles described in Appendix B or such other accounting principles as the District may be required to employ from time to time pursuant to State law or regulation.

If the District changes its fiscal year, it will file notice of the change (and of the date of the new fiscal year end) with the MSRB prior to the next date by which the District otherwise would be required to provide financial information and operating data pursuant to this Section. The District's current fiscal year end is August 31. Accordingly, the District must provide updated financial information and operating data by the last day of February in each year and provide its audited financial statements (or unaudited financial statements if audited financial statements are not available) by August 31.

**NOTICE OF CERTAIN EVENTS . . .** The District will also provide timely notices of certain events to the MSRB. The District will provide notice of any of the following events with respect to the Bonds to the MSRB in a timely manner (but not in excess of ten business days after the occurrence of the event): (1) principal and interest payment delinquencies; (2) non-payment related defaults, if material; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB), or other material notices or determinations with respect to the tax status of the Bonds, or other material events affecting the tax status of the Bonds; (7) modifications to rights of holders of the Bonds, if material; (8) Bond calls, if material, and tender offers; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the Bonds, if material; (11) rating changes; (12) bankruptcy, insolvency, receivership, or similar event of the District, which shall occur as described below; (13) the consummation of a merger, consolidation, or acquisition involving the District or the sale of all or substantially all of its assets, other than in the ordinary course of business, the entry into of a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; and (14) appointment of a successor or additional trustee or the change of name of a trustee, if material. In addition, the District will provide timely notice of any failure by the District to provide annual financial information in accordance with their agreement described above under “Annual Reports”. Neither the Bonds nor the Order make any provisions for a bond trustee, debt service reserves, credit enhancement (except for the Permanent School Fund Guarantee), or liquidity enhancement.

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

**AVAILABILITY OF INFORMATION FROM MSRB . . .** The District has agreed to provide the foregoing information only as described above. Investors will be able to access continuing disclosure information filed with the MSRB free of charge at [www.emma.msrb.org](http://www.emma.msrb.org).

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

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

**FORMAT, IDENTIFYING INFORMATION, AND INCORPORATION BY REFERENCE . . .** All financial information, operating data, financial statements, and notices required to be provided to the MSRB shall be provided in an electronic format and be accompanied by identifying information prescribed by the MSRB.

Financial information and operating data to be provided as set forth above under the subcaption “Annual Reports” may be set forth in full in one or more documents or may be included by specific reference to any document (including an official statement or other offering document) available to the public on the MSRB’s Internet Web site or filed with the SEC.

**COMPLIANCE WITH PRIOR UNDERTAKINGS...** During the last five years, the District has complied in all material respects with all continuing disclosure agreements made by it in accordance with the Rule.

## **OTHER INFORMATION**

### **RATINGS**

The Bonds have been rated “Aaa” by Moody’s Investors Service, Inc. (“Moody’s”) and “AAA” by S&P Global Ratings, a division of Standard & Poor’s Financial Services LLC (“S&P”) by virtue of the guarantee of the Permanent School Fund of the State of Texas. The Bonds and the presently outstanding tax supported debt of the District are rated “A1” by Moody’s and “AA-” by S&P without regard to credit enhancement. The District also has outstanding bonds which are rated “Aaa” by Moody’s and “AAA” by S&P by virtue of the guarantee of the Permanent School Fund of the State of Texas. An explanation of the significance of such ratings may be obtained from the company furnishing the rating. The ratings reflect only the respective views of such organizations and the District makes no representation as to the appropriateness of the ratings. There is no assurance that such ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by either one or both of such rating companies, if in the judgment of either one or both of such companies, circumstances so warrant. Any such downward revision or withdrawal of such ratings, or either of them, may have an adverse effect on the market price of the Bonds.

### **LITIGATION**

The District is not a party to any litigation or other proceeding pending or, to its knowledge, threatened, in any court, agency or other administrative body (either state or federal) which, if decided adversely to the District, would have a material adverse effect on the financial condition of the District. At the time of the initial delivery of the Bonds, the District will provide the Underwriters with a certificate to the effect that no litigation of any nature has been filed or is then pending challenging the issuance of the Bonds or that affects the payment and security of the Bonds or in any other manner questioning the issuance, sale or delivery of the Bonds.

### **REGISTRATION AND QUALIFICATION OF BONDS FOR SALE**

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

### **LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS**

Section 1201.041 of the Public Security Procedures Act (Chapter 1201, Texas Government Code) provides that the Bonds are negotiable instruments, investment securities governed by Chapter 8, Texas Business and Commerce Code, and are legal and authorized investments for insurance companies, fiduciaries, and trustees, and for the sinking funds of municipalities or other political subdivisions or public agencies of the State of Texas. In addition, various provisions of the Texas Finance Code provide that, subject to a prudent investor standard, the Bonds are legal investments for state banks, savings banks, trust companies with at least \$1 million of capital, and savings and loan associations. In accordance with the Public Funds Investment Act, Chapter 2256, Texas Government Code, the Bonds must be rated not less than “A” or its equivalent as to investment quality by a national rating agency in order for most municipalities or other political subdivisions or public agencies of the State of Texas to be authorized to invest in the Bonds, except for purchases for interest and sinking funds of such entities. See “OTHER INFORMATION – Ratings” herein. Moreover, municipalities or other political subdivisions or public agencies of the State of Texas that have adopted investment policies and guidelines in accordance with the Public Funds Investment Act may have other, more stringent requirements for purchasing securities, including the Bonds. The Bonds are eligible to secure deposits of any public funds of the State, its agencies, and its political subdivisions, and are legal security for those deposits to the extent of their market value.

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

## **LEGAL MATTERS**

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

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

## **FINANCIAL ADVISOR**

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

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

## **UNDERWRITING**

The Underwriters have agreed, subject to certain conditions, to purchase the Bonds from the District, at an underwriting discount of \$232,472.96. The Underwriters will be obligated to purchase all of the Bonds if any Bonds are purchased. The Bonds to be offered to the public may be offered and sold to certain dealers (including the Underwriters and other dealers depositing Bonds into investment trusts) at prices lower than the public offering prices of such Bonds, and such public offering prices may be changed, from time to time, by the Underwriters.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement pursuant to their respective responsibilities to investors under federal securities laws, but the Underwriters do not guarantee the accuracy or completeness of such information.

RBC Capital Markets, LLC (“RBCCM”) has provided the following information for inclusion in this Official Statement. RBCCM is a full-service financial institution engaged in various activities, that may include securities trading, commercial and investment banking, municipal advisory, brokerage, and asset management. In the ordinary course of business, RBCCM may actively trade debt and, if applicable, equity securities (or related derivative securities) and provide financial instruments (which may include bank loans, credit support or interest rate swaps). RBCCM may engage in transactions for its own accounts involving the securities and instruments made the subject of this securities offering or other offerings of the District. RBCCM may also communicate independent investment recommendations, market color or trading ideas and publish independent research views in respect of this securities offering or other offerings of the District. RBCCM may make a market in credit default swaps with respect to municipal securities in the future.

#### **FORWARD-LOOKING STATEMENTS DISCLAIMER**

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

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

#### **MISCELLANEOUS**

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

As authorized by the Board in the Bond Order, the Pricing Officer has approved the form and content of this Official Statement and any addenda, supplement, or amendment hereto, and authorized its use in the reoffering of the Bonds by the Underwriters.

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KAREN BILLINGSLEY  
Pricing Officer  
Cleveland Independent School District

**APPENDIX A**

GENERAL INFORMATION REGARDING THE DISTRICT

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**THE DISTRICT . . .** The District is a political subdivision of the State of Texas and is located in the northwest corner of Liberty County, approximately 47 miles north of downtown Houston, with 143 square miles of land included in its corporate boundary. The District’s boundaries also overlap into portions of Montgomery and San Jacinto Counties.

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

**CAMPUS INFORMATION**

<u>Campus</u>	<u>Number of Schools</u>	<u>Capacity</u>	<u>Number of Portables</u>
Elementary Schools	3	3,467	28
Middle Schools	1	1,130	7
High Schools	1	1,303	6
Totals	<u>5</u>	<u>5,900</u>	<u>41</u>

Source: District staff

**DISTRICT ENROLLMENT**

<u>FYE 8/31</u>	<u>Total Enrollment</u>	<u>Average Daily Attendance</u>
2014	3,763	3,571
2015	4,052	3,918
2016	4,149	3,921
2017	4,975	4,711
2018	5,697	5,340

Source: District staff.

**SCHOOL AND EMPLOYEE INFORMATION**

Number of teachers holding masters degrees	47
Number of teachers holding bachelors degrees	297
Employee Information	
Number of Employees	697
Number of Teachers	344
Pupil/Teacher ratios:	
Elementary School	18/1
Intermediate School	21/1
Middle School	16/1
High School	14/1

Source: District staff.

**HISTORICAL EMPLOYMENT DATA (ANNUAL AVERAGE DATA)**

	Annual Averages				
	2018 <sup>(1)</sup>	2017	2016	2015	2014
<b>Liberty County</b>					
Civilian Labor Force	32,222	31,471	31,345	31,466	31,086
Total Employment	30,251	29,034	29,274	29,290	28,386
Unemployment	1,971	2,437	2,071	2,176	2,700
Percent Unemployment	6.1%	7.7%	6.6%	6.9%	8.7%
<b>Montgomery County</b>					
Civilian Labor Force	273,275	262,178	252,136	252,448	247,251
Total Employment	262,689	249,763	241,647	241,416	234,013
Unemployment	10,586	12,415	10,489	11,032	13,238
Percent Unemployment	3.9%	4.7%	4.2%	4.4%	5.4%
<b>San Jacinto County</b>					
Civilian Labor Force	11,605	11,438	11,305	11,478	11,493
Total Employment	11,018	10,736	10,679	10,817	10,633
Unemployment	587	702	626	661	860
Percent Unemployment	5.1%	6.1%	5.5%	5.8%	7.5%
<b>State of Texas</b>					
Civilian Labor Force	13,800,519	13,455,755	13,086,716	13,111,548	12,904,629
Total Employment	13,251,775	12,833,841	12,517,627	12,447,551	12,104,092
Unemployment	548,744	621,914	569,089	663,997	800,537
Percent Unemployment	4.0%	4.6%	4.3%	5.1%	6.2%

(1) Averages through September 2018.  
Source: Texas Employment Commission.

**APPENDIX B**

EXCERPTS FROM THE  
CLEVELAND INDEPENDENT SCHOOL DISTRICT  
ANNUAL FINANCIAL REPORT  
For the Year Ended August 31, 2017

The information contained in this Appendix consists of excerpts from the Cleveland Independent School District Annual Financial Report for the Year Ended August 31, 2017, and is not intended to be a complete statement of the District's financial condition. Reference is made to the complete Report for further information.

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## INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of  
Cleveland Independent School District

### 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 Cleveland Independent School District as of and for the year ended August 31, 2017, and the related notes to the financial statements, which collectively comprise the District'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.

### 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 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 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.

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## **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 Cleveland Independent School District as of August 31, 2017, and the respective changes in financial position and, where applicable, cash flows thereof, and the respective budgetary comparison for the General Fund 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 section which precedes the basic financial statements and the pension related schedules following the notes to the financial statements 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 Supplementary Information*

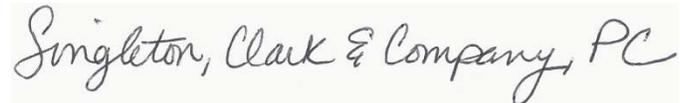
Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Cleveland Independent School District's basic financial statements. The Texas Education Agency required schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by *Title 2 U.S. Code of Federal Regulations (CFR) Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, and is also not a required part of the basic financial statements.

The Texas Education Agency required schedules and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the 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 Texas Education Agency required schedules, and the schedule of expenditures of federal awards are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

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## **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October 20, 2017 on our consideration of Cleveland Independent School District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 Cleveland Independent School District's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "Singleton, Clark & Company, PC". The signature is written in black ink on a light-colored background.

Singleton, Clark & Company, PC  
Cedar Park, Texas

October 20, 2017

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CLEVELAND INDEPENDENT SCHOOL DISTRICT  
MANAGEMENT’S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED AUGUST 31, 2017

**MANAGEMENT’S DISCUSSION AND ANALYSIS**

In this section of the Annual Financial and Compliance Report, we, the managers of Cleveland Independent School District (the “District”) discuss and analyze the financial performance of the District for the fiscal year ended August 31, 2017. Please read this information in conjunction with the District’s basic financial statements, which follow this section.

**FINANCIAL HIGHLIGHTS**

- The District’s net position for governmental activities increased by \$5,822,407 as a result of this year’s operations, to end at \$39,998,670.
- Total governmental funds of the District (the General Fund plus all Special Revenue Funds, the Capital Projects Funds and the Debt Service Fund) reported an overall fund balance decrease of \$13,792,501, to end at \$50,436,724.
- The General Fund of the District reported a fund balance increase of \$2,376,299 for the year, to end at \$27,386,571.

**OVERVIEW OF THE FINANCIAL SECTION**

The Financial Section is the most substantial part of this Annual Financial and Compliance Report. It consists of the independent auditor’s report, management’s discussion and analysis (this section), a set of basic financial statements with required note disclosures, and finally required supplementary information and other supporting statements and schedules as applicable.

Independent Auditor’s Report

State law requires the District’s financial statements to be audited by an independent certified public accountant each year. The primary purpose of the annual audit is for the auditor to express an opinion as to whether the financial statements of the District appear to be free from material misstatement. In addition, the auditor reports any deficiencies noted within the financial internal controls of the District and whether any noncompliance with rules, regulations, or grant agreements was observed.

Management’s Discussion and Analysis

The Management’s Discussion and Analysis (MD&A) section of the report is intended to introduce the financial statements and to provide discussion and analysis regarding the financial performance of the District during the year. The MD&A is written by management of the District and provides for a less formal presentation of the financial activities of the District than is found within the basic financial statements themselves.

Basic Financial Statements

The Basic Financial Statements consist of a series of financial statements and required note disclosures. These statements include government-wide financial statements which present the District in a consolidated and long-term manner using full-accrual accounting similar to that of a business enterprise, and fund financial statements which present a more detailed view of the District using a more short-term view and traditional modified-accrual governmental accounting. These financial statements are followed with detailed notes which provide narrative explanations and additional data for full disclosure of information.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED AUGUST 31, 2017

Required Supplementary Information

The previously discussed Management's Discussion and Analysis section is considered to be required supplementary information, however, the governmental reporting framework requires that it be presented before the financial statements. When applicable, additional required supplementary information must follow the financial statements. Within this financial report, the District presents required schedules related to its participation in the Teacher Retirement System of Texas pension plan.

Individual Fund Statements and Schedules

This section includes schedules required by the Texas Education Agency to report tax collection information and budget to actual information for the District's debt service and child nutrition functions.

**Reporting the District as a Whole**

*The Statement of Net Position and the Statement of Activities*

The analysis of the District's overall financial condition and operations begins with the government-wide financial statements which immediately follow this section. The government-wide financial statements include the Statement of Net Position and the Statement of Activities. The primary purpose of these financial statements is to show whether the District is better off or worse off as a result of the year's activities. The Statement of Net Position includes all the District's assets and liabilities at the end of the year while the Statement of Activities includes all the revenues and expenses generated by the District's operations during the year. These apply the accrual basis of accounting which is the basis used by private sector companies.

All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid. The District's revenues are divided into those provided by outside parties who share the costs of some programs, such as tuition received from students from outside the district and grants provided by the U.S. Department of Education to assist children with disabilities or from disadvantaged backgrounds (program revenues), and revenues provided by the taxpayers or by the State of Texas in equalization funding processes (general revenues). All the District's assets are reported whether they serve the current year or future years. Liabilities are considered regardless of whether they must be paid in the current or future years.

The Statement of Net Position and the Statement of Activities report the District's net position and changes in net position. The District's net position (the difference between assets and liabilities) provides one measure of the District's financial health. Over time, increases or decreases in the District's net position are one indicator of whether its financial health is improving or deteriorating. To fully assess the overall health of the District, however, you should consider nonfinancial factors as well, such as changes in the District's average daily attendance or its property tax base and the condition of the District's facilities.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED AUGUST 31, 2017

In the Statement of Net Position and the Statement of Activities, school districts divide up their financial activities as follows:

- Governmental activities – School districts report basic services here, including the instruction of students, counseling, co-curricular activities, child nutrition services, transportation, maintenance, community services, and general administration. Property taxes, state block grants based on student attendance and demographics, and other state and federal grants finance most of these activities.
- Business-type activities – School districts may charge a fee to "customers" to help it cover all or most of the cost of services it provides for child care programs or other activities that closely model a business venture.

Our District reported governmental activities this year, however, we did not engage in business-type activities.

### **Reporting the District's Most Significant Funds**

#### ***Fund Financial Statements***

The fund financial statements follow the government-wide statements and provide detailed information about the most significant funds of the District, not the District as a whole. Laws and regulations require the District to establish separate funds, such as for grants received from the state and federal government, money received from bond issues for capital projects, or for money raised specifically for debt service purposes, in order to clearly display financial accountability for use of these funds.

School districts use two different kinds of funds for operations, governmental funds and proprietary funds, which use different accounting approaches.

- A school district will use *governmental funds* to account for basic services. These use modified accrual accounting (a method that measures the receipt and disbursement of cash and all other financial assets that can be readily converted to cash) and report balances that are available for future spending. The governmental fund statements provide a detailed short-term view of the District's general operations and the basic services it provides. We describe the differences between governmental activities (reported in the Statement of Net Position and the Statement of Activities) and governmental funds in reconciliation schedules following each of the fund financial statements.
- A school district will use *proprietary funds* to account for the activities for which it charges users (whether outside customers or other units of the district). Proprietary funds use the same accounting methods employed in the Statement of Net Position and the Statement of Activities. In fact, when a district utilizes enterprise funds, (one category of proprietary funds) these are the business-type activities reported in the government-wide statements but they contain more detail and additional information, such as cash flows. Internal service funds (the other category of proprietary funds) report activities that provide supplies and services for a district's other programs and activities, such as a district's self-insurance programs.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED AUGUST 31, 2017

**The District as Trustee**

*Reporting the District's Fiduciary Responsibilities*

The District is the trustee, or fiduciary, for money raised by student activities and scholarship programs. All of the District's fiduciary activities are reported in separate Statements of Fiduciary Net Position and Changes in Fiduciary Net Position on pages that follow the governmental fund and proprietary fund financial statements. We exclude these resources from the District's other financial statements because the District cannot use these assets to finance its operations. The District is however responsible for applying sound financial internal controls over these funds and for ensuring that these resources are used for their intended purposes.

**GOVERNMENT-WIDE FINANCIAL ANALYSIS**

The following analysis focuses on the net position (Table I) and changes in net position (Table II) of the District's governmental activities.

Net position of the District's governmental activities increased from \$34,176,263 to \$39,998,670. Unrestricted net position – the part of net position that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation, or other legal requirements – was \$11,349,698 at August 31, 2017. The increase in governmental net position was primarily due to higher than expected revenues.

**Table I  
CLEVELAND INDEPENDENT SCHOOL DISTRICT  
NET POSITION**

	Governmental Activities 2017	Governmental Activities 2016	Change
Current & other assets	\$ 61,378,756	\$ 71,096,580	\$ (9,717,824)
Capital assets	64,753,165	42,099,349	22,653,816
Deferred outflows	7,109,944	5,611,671	1,498,273
Total assets and deferred outflows	<u>133,241,865</u>	<u>118,807,600</u>	<u>14,434,265</u>
Current liabilities	5,991,942	2,478,829	3,513,113
Long-term liabilities	85,814,411	81,621,066	4,193,345
Deferred inflows	1,436,842	531,442	905,400
Total liabilities and deferred inflows	<u>93,243,195</u>	<u>84,631,337</u>	<u>8,611,858</u>
Net Position:			
Net investment in capital assets	4,156,078	2,590,467	1,565,611
Restricted	24,492,894	6,982,167	17,510,727
Unrestricted	11,349,698	24,603,629	(13,253,931)
Total net position	<u>\$ 39,998,670</u>	<u>\$ 34,176,263</u>	<u>\$ 5,822,407</u>

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED AUGUST 31, 2017

**Table II**  
**CLEVELAND INDEPENDENT SCHOOL DISTRICT**  
**CHANGES IN NET POSITION**

	Governmental		Change
	Activities 2017	Activities 2016	
Revenues:			
Program Revenues:			
Charges for services	\$ 357,650	\$ 640,194	\$ (282,544)
Operating grants & contributions	5,671,913	6,974,700	(1,302,787)
General Revenues:			
Maintenance & operations taxes	11,625,062	9,670,352	1,954,710
Debt service taxes	3,698,545	2,565,572	1,132,973
State aid - formula grants	26,183,383	24,674,595	1,508,788
Grants & contributions not restr.	2,400,902	-	2,400,902
Investment earnings	229,747	151,766	77,981
Miscellaneous	446,659	589,804	(143,145)
Total Revenue	<u>50,613,861</u>	<u>45,266,983</u>	<u>5,346,878</u>
Expenses:			
Instruction	23,223,083	22,686,206	536,877
Instr. resources & media services	283,437	-	283,437
Curriculum and staff development	573,869	-	573,869
Instructional leadership	176,542	-	176,542
School leadership	2,761,538	2,581,017	180,521
Guidance/counseling services	876,042	-	876,042
Health services	322,586	-	322,586
Student transportation	1,875,574	2,840,450	(964,876)
Food services	2,555,520	2,519,009	36,511
Cocurricular/extracurricular act.	1,146,820	971,397	175,423
General administration	1,891,273	1,495,925	395,348
Plant maintenance and operations	4,112,025	4,772,513	(660,488)
Security and monitoring services	594,855	-	594,855
Data processing services	486,664	-	486,664
Community services	14,440	8,191	6,249
Debt service	2,992,648	2,097,645	895,003
Capital outlay	-	41,410	(41,410)
Payments to fiscal agents	590,880	392,609	198,271
Other intergovernmental charges	337,199	299,612	37,587
Total Expenses	<u>44,814,995</u>	<u>40,705,984</u>	<u>4,109,011</u>
Gain (Loss) on sale of assets	23,541	-	23,541
Change in net position	<u>5,822,407</u>	<u>4,560,999</u>	<u>1,261,408</u>
Net position at 9/1/16 and 9/1/15	<u>34,176,263</u>	<u>29,615,264</u>	<u>4,560,999</u>
Net position at 8/31/17 and 8/31/16	<u>\$ 39,998,670</u>	<u>\$ 34,176,263</u>	<u>\$ 5,822,407</u>

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED AUGUST 31, 2017

**THE DISTRICT'S FUNDS**

As the District completed this annual period, the General Fund reported a fund balance of \$27,386,571, which is \$2,376,299 more than last year's total of \$25,010,272. The increase in fund balance is mainly attributable to greater than expected state program revenues.

The District's Debt Service Fund reported a fund balance of \$5,638,353 which is \$237,584 more than last year's total of \$5,400,769. The Debt Service fund balance was more at August 31, 2017, as compared to the prior year end, due to greater than expected local revenue. The purpose of the Debt Service Fund is to provide for the payment of bond principal and interest payments as it becomes due.

The District's Capital Projects Funds reported a fund balance of \$16,211,332 which is \$16,750,146 less than last year's total of \$32,961,478. The Capital Projects fund balance was less at August 31, 2017, as compared to the prior year end, due to the construction of new facilities.

The District's other governmental funds reported a combined ending fund balance of \$1,200,468. This combined balance is \$343,762 more than the previous year.

Over the course of the year, the Board of Trustees generally revises the District's budget based on financial updates provided by management of the District. These amendments involve moving funds from programs that did not need all the resources originally appropriated to them to programs with resource needs, or to react to originally unforeseen circumstances, such as unanticipated new revenues or unavoidable new costs. None of the budget amendments made during the year were considered significant.

**CAPITAL ASSET AND DEBT ADMINISTRATION**

**Capital Assets**

As of August 31, 2017, the District had \$64,753,165 (net of accumulated depreciation) invested in a broad range of capital assets, including facilities and equipment for instruction, transportation, athletics, administration, and maintenance.

A summary of the ending balances of capital assets by major category for both 2017 and 2016 is a follows:

	Governmental Activities 2017	Governmental Activities 2016	Change
Land	\$ 2,546,269	\$ 1,019,259	\$ 1,527,010
Construction in Progress	21,368,686	2,082,313	19,286,373
Buildings	60,240,686	57,448,380	2,792,306
Furniture and Equipment	6,051,534	5,743,728	307,806
Total	<u>90,207,175</u>	<u>66,293,680</u>	<u>23,913,495</u>
Less Accumulated Depreciation	<u>(25,454,010)</u>	<u>(24,194,331)</u>	<u>(1,259,679)</u>
Capital assets, net of depreciation	<u>\$ 64,753,165</u>	<u>\$ 42,099,349</u>	<u>\$ 22,653,816</u>

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED AUGUST 31, 2017

**Debt**

At year end, the District had \$85,814,411 in bonds and other long-term debt outstanding versus \$81,477,071 last year. The increase is attributable to debt issuance during the fiscal year.

A summary of the ending balances of long-term debt by type for both 2017 and 2016 is as follows:

	Governmental Activities 2017	Governmental Activities 2016	Change
General Obligation Bonds	\$ 77,141,372	\$ 74,335,085	\$ 2,806,287
Net Pension Liability	8,673,039	7,141,986	1,531,053
Total	<u>\$ 85,814,411</u>	<u>\$ 81,477,071</u>	<u>\$ 4,337,340</u>

**ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES**

The District's elected and appointed officials considered many factors when setting the fiscal year 2017-2018 budget and tax rates. Those factors include property values, changes in enrollment, the economy, projections of future budget years, and legislative mandates. The District has adopted a General Fund budget of approximately \$46.4 million for the 2017-2018 fiscal year. This reflects an approximate increase of \$9.8 million in budgeted expenditures from fiscal year 2016-2017 to fiscal year 2017-2018.

For the 2017-2018 budget year, the District has held constant its maintenance and operations tax rate at \$1.04 per hundred of taxable value. The District has the capability to call a tax ratification election which could authorize up to \$1.17 cents for maintenance and operations. The District has no current plans to call a tax ratification election. The District adopted a debt service tax rate of \$.375 for the 2017-2018 budget year in order to fund required debt payments in the coming year. The combined tax rate of the District for the 2017-2018 budget year is \$1.415 per hundred of taxable value.

**CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT**

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District's Business Office, at Cleveland Independent School District, 316 East Dallas, Cleveland, Texas 77327, or by calling (281) 592-8717.

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**BASIC FINANCIAL STATEMENTS**

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
STATEMENT OF NET POSITION  
AUGUST 31, 2017

Data Control Codes	Primary Government 1 Governmental Activities
<b>ASSETS</b>	
1110 Cash and Cash Equivalents	\$ 49,134,245
1225 Property Taxes Receivable, net	5,019,171
1240 Due from Other Governments	7,189,106
1290 Other Receivables, net	29,468
1300 Inventories	6,766
Capital Assets:	
1510 Land	2,546,269
1520 Buildings and Improvements, net	38,597,691
1530 Furniture and Equipment, net	2,240,519
1580 Construction in Progress	21,368,686
1000 Total Assets	<u>126,131,921</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>	
1700 Deferred Outflows-Bond Refundings	1,703,603
1705 Deferred Outflows-Pension	5,406,341
Total Deferred Outflows of Resources	<u>7,109,944</u>
<b>LIABILITIES</b>	
2110 Accounts Payable	4,029,814
2140 Interest Payable	106,958
2150 Payroll Deductions & Withholdings	80,232
2160 Accrued Wages Payable	1,722,731
2200 Accrued Expenses	35,892
2300 Unearned Revenue	16,315
Noncurrent Liabilities:	
2501 Bonds, Loans & Other Payable-Due Within One Year	1,935,000
2502 Bonds Payable - Due in More than One Year	68,937,141
2516 Unamortized Premium (Discount) on Bonds	6,269,231
2540 Net Pension Liability	8,673,039
2000 Total Liabilities	<u>91,806,353</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>	
2605 Deferred Inflows-Pension	1,436,842
Total Deferred Inflows of Resources	<u>1,436,842</u>
<b>NET POSITION</b>	
3200 Net Investment in Capital Assets	4,156,078
Restricted for:	
3820 Federal & State Programs	1,200,468
3850 Debt Service	6,710,327
3860 Capital Projects	16,211,332
3890 Other Restricted	370,767
3900 Unrestricted	11,349,698
3000 Total Net Position	<u>\$ 39,998,670</u>

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

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED AUGUST 31, 2017

Data Control Codes	1 Expenses	Program Revenues		Net (Expense) Rev. & Changes in Net Position
		3 Charges for Services	4 Operating Grants and Contributions	6 Primary Gov. Governmental Activities
<b>Primary Government:</b>				
GOVERNMENTAL ACTIVITIES:				
11 Instruction	\$ 23,223,083	\$ -	\$ 3,749,002	\$ (19,474,081)
12 Instructional Resources & Media Services	283,437	-	-	(283,437)
13 Curriculum & Staff Development	573,869	-	457,648	(116,221)
21 Instructional Leadership	176,542	-	-	(176,542)
23 School Leadership	2,761,538	-	-	(2,761,538)
31 Guidance/Counseling/Evaluation Services	876,042	-	-	(876,042)
33 Health Services	322,586	-	-	(322,586)
34 Student Transportation	1,875,574	-	-	(1,875,574)
35 Food Services	2,555,520	311,997	-	(2,243,523)
36 Extracurricular Activities	1,146,820	36,590	-	(1,110,230)
41 General Administration	1,891,273	9,063	-	(1,882,210)
51 Plant Maintenance and Operations	4,112,025	-	386,042	(3,725,983)
52 Security and Monitoring Services	594,855	-	1,888	(592,967)
53 Data Processing Services	486,664	-	-	(486,664)
61 Community Services	14,440	-	26,643	12,203
72 Interest on Long-Term Debt	2,762,911	-	1,050,690	(1,712,221)
73 Bond Issuance Cost & Fees	229,737	-	-	(229,737)
93 Payments to Fiscal Agent/Member Dist. of SSA	590,880	-	-	(590,880)
99 Other Intergovernmental Charges	337,199	-	-	(337,199)
TG Total Governmental Activities:	<u>44,814,995</u>	<u>357,650</u>	<u>5,671,913</u>	<u>(38,785,432)</u>
TP TOTAL PRIMARY GOVERNMENT:	<u>\$ 44,814,995</u>	<u>\$ 357,650</u>	<u>\$ 5,671,913</u>	<u>(38,785,432)</u>
General Revenues:				
Taxes:				
MT Property Taxes, Levied for General Purposes				11,625,062
DT Property Taxes, Levied for Debt Service				3,698,545
SF State Aid - Formula Grants				26,183,383
GC Grants and Contributions, not Restricted				2,400,902
IE Investment Earnings				229,747
MI Miscellaneous Local and Intermediate Revenue				446,659
Total General Revenues				<u>44,584,298</u>
S1 Sale of Property				23,541
TR Total General Revenues and Special Item				<u>44,607,839</u>
CN Change in Net Position				5,822,407
NB Net Position -- Beginning				34,176,263
NE Net Position -- Ending				<u>\$ 39,998,670</u>

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

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
BALANCE SHEET  
GOVERNMENTAL FUNDS  
AUGUST 31, 2017

Data	10	50	60		98
Control	General	Debt	Capital	Other	Total
Codes	Fund	Service Fund	Projects Funds	Funds	Governmental Funds
<b>ASSETS</b>					
1110 Cash and Cash Equivalents	\$ 23,047,380	\$ 5,631,762	\$ 19,559,660	\$ 762,516	\$ 49,001,318
1220 Property Taxes - Delinquent	4,385,775	1,191,082	-	-	5,576,857
1230 Allowance for Uncollectible Taxes (Credit)	(438,578)	(119,108)	-	-	(557,686)
1240 Due from Other Governments	6,646,887	-	-	542,219	7,189,106
1260 Due from Other Funds	423,694	-	-	1,579	425,273
1290 Other Receivables	22,877	6,591	-	-	29,468
1310 Inventories	-	-	-	6,766	6,766
1000A Total Assets	<u>\$ 34,088,035</u>	<u>\$ 6,710,327</u>	<u>\$ 19,559,660</u>	<u>\$ 1,313,080</u>	<u>\$ 61,671,102</u>
<b>LIABILITIES</b>					
2110 Accounts Payable	\$ 302,752	\$ -	\$ 3,348,328	\$ 70,924	\$ 3,722,004
2150 Payroll Ded. and Withholdings Payable	80,232	-	-	-	80,232
2160 Accrued Wages Payable	1,697,385	-	-	25,346	1,722,731
2170 Due to Other Funds	638,033	-	-	-	638,033
2200 Accrued Expenditures	35,865	-	-	27	35,892
2300 Unearned Revenues	-	-	-	16,315	16,315
2000 Total Liabilities	<u>2,754,267</u>	<u>-</u>	<u>3,348,328</u>	<u>112,612</u>	<u>6,215,207</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>					
2600 Deferred Inflows-Unavailable Revenues	3,947,197	1,071,974	-	-	5,019,171
Total Deferred Inflows of Resources	<u>3,947,197</u>	<u>1,071,974</u>	<u>-</u>	<u>-</u>	<u>5,019,171</u>
<b>FUND BALANCES</b>					
Restricted for:					
3450 Federal or State Funds Restricted	-	-	-	1,200,468	1,200,468
3470 Capital Acq. and Contractual Oblig.	-	-	16,211,332	-	16,211,332
3480 Retirement of Long-Term Debt	-	5,638,353	-	-	5,638,353
3490 Other Restricted Fund Balance	370,767	-	-	-	370,767
Assigned for:					
3550 Construction	6,800,000	-	-	-	6,800,000
3590 Other Assigned Fund Balance	2,000,000	-	-	-	2,000,000
3600 Unassigned Fund Balance	18,215,804	-	-	-	18,215,804
3000 Total Fund Balances	<u>27,386,571</u>	<u>5,638,353</u>	<u>16,211,332</u>	<u>1,200,468</u>	<u>50,436,724</u>
4000 Total Liab., Def. Inflows, and Fund Balances	<u>\$ 34,088,035</u>	<u>\$ 6,710,327</u>	<u>\$ 19,559,660</u>	<u>\$ 1,313,080</u>	<u>\$ 61,671,102</u>

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

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
 RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE  
 STATEMENT OF NET POSITION  
 AUGUST 31, 2017

		1
<b>Total Fund Balances - Governmental Funds</b>	<b>\$</b>	<b>50,436,724</b>
<p>1 Capital assets used in governmental activities are not current financial resources and, therefore, are not reported in the governmental funds.</p>		
Governmental capital assets	\$	90,207,175
Less accumulated depreciation	<u>(25,454,010)</u>	64,753,165
<p>2 Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the funds.</p>		
Bonds payable, including unamortized premiums	(77,141,372)	
Net pension liability	<u>(8,673,039)</u>	(85,814,411)
<p>3 Accrued interest on long-term debt related to governmental fund activities is not due and payable in the current period and, therefore, not reported in the governmental funds.</p>		
		(106,958)
<p>4 Deferred outflows and inflows of resources related to pensions are applicable to future periods and, therefore, are not reported in the funds.</p>		
Deferred outflows of resources related to pensions	5,406,341	
Deferred inflows of resources related to pensions	<u>(1,436,842)</u>	3,969,499
<p>5 Property taxes are recognized as revenue in the governmental funds when collected, but recognized on the Statement of Activities in the year levied. Therefore, property taxes receivable, net of allowance for uncollectible accounts, is added to the Statement of Net Position for governmental activities.</p>		
		5,019,171
<p>6 Deferred amounts from bond refundings, net of amortization, are not reported in the governmental funds.</p>		
		1,703,603
<p>7 The District uses an Internal Service Fund to charge the costs of certain activities, such as the provision of workers compensation insurance, to other individual funds. Even though the Internal Service Fund is a proprietary fund, the assets and liabilities of this fund are added to the Statement of Net Position for governmental activities.</p>		
		37,877
<b>19 Net Position of Governmental Activities</b>	<b>\$</b>	<b><u>39,998,670</u></b>

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

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE  
GOVERNMENTAL FUNDS  
FOR THE YEAR ENDED AUGUST 31, 2017

Data	10	50	60	98	
Control	General	Debt	Capital	Other	Total
Codes	Fund	Service Fund	Projects Funds	Funds	Funds
<b>REVENUES</b>					
5700 Local and Intermediate Sources	\$11,472,058	\$ 3,549,770	\$ 98,224	\$ 346,164	\$15,466,216
5800 State Program Revenues	27,671,508	1,050,690	-	366,968	29,089,166
5900 Federal Program Revenues	1,214,010	-	-	4,302,484	5,516,494
5020 Total Revenues	<u>40,357,576</u>	<u>4,600,460</u>	<u>98,224</u>	<u>5,015,616</u>	<u>50,071,876</u>
<b>EXPENDITURES</b>					
0011 Instruction	20,189,352	-	-	1,818,429	22,007,781
0012 Instructional Resources & Media Services	270,604	-	-	-	270,604
0013 Curriculum & Inst. Staff Development	323,508	-	-	221,979	545,487
0021 Instructional Leadership	165,945	-	-	-	165,945
0023 School Leadership	2,616,473	-	-	-	2,616,473
0031 Guidance, Counseling & Eval. Services	830,960	-	-	-	830,960
0033 Health Services	307,498	-	-	-	307,498
0034 Student (Pupil) Transportation	2,416,457	-	-	-	2,416,457
0035 Food Services	-	-	-	2,430,360	2,430,360
0036 Cocurricular/Extracurricular Activities	1,082,484	-	-	-	1,082,484
0041 General Administration	1,584,857	-	-	-	1,584,857
0051 Plant Maintenance and Operations	3,720,387	-	-	187,247	3,907,634
0052 Security and Monitoring Services	605,620	-	-	916	606,536
0053 Data Processing Services	474,361	-	-	-	474,361
0061 Community Services	884	-	-	12,923	13,807
0071 Debt Service - Principal	-	708,079	-	-	708,079
0072 Debt Service - Interest	-	3,653,447	-	-	3,653,447
0073 Debt Service - Bond Issuance Costs	-	118,790	110,947	-	229,737
0081 Facilities Acquisition and Construction	2,528,051	-	21,148,370	-	23,676,421
0093 Payments to Fiscal Agent of SSA	564,966	-	-	-	564,966
0099 Other Intergovernmental Charges	322,411	-	-	-	322,411
6030 Total Expenditures	<u>38,004,818</u>	<u>4,480,316</u>	<u>21,259,317</u>	<u>4,671,854</u>	<u>68,416,305</u>
1100 Excess (Deficiency) of Revenues Over (Under) Expenditures	<u>2,352,758</u>	<u>120,144</u>	<u>(21,161,093)</u>	<u>343,762</u>	<u>(18,344,429)</u>
<b>OTHER FINANCING SOURCES (USES)</b>					
7911 Capital-Related Debt Issued	-	4,975,000	4,015,000	-	8,990,000
7912 Sale of Property	23,541	-	-	-	23,541
7916 Premium or Discount on Issuance of Bonds	-	227,700	395,947	-	623,647
8949 Other (Uses)	-	(5,085,260)	-	-	(5,085,260)
7080 Total Other Financing Sources (Uses)	<u>23,541</u>	<u>117,440</u>	<u>4,410,947</u>	<u>-</u>	<u>4,551,928</u>
1200 Net Change in Fund Balance	2,376,299	237,584	(16,750,146)	343,762	(13,792,501)
0100 Fund Balance - Beginning	25,010,272	5,400,769	32,961,478	856,706	64,229,225
3000 Fund Balance - Ending	<u>\$27,386,571</u>	<u>\$ 5,638,353</u>	<u>\$16,211,332</u>	<u>\$ 1,200,468</u>	<u>\$50,436,724</u>

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

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES,  
EXPENDITURES, AND CHANGES IN FUND BALANCE TO THE STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED AUGUST 31, 2017

<b>Total Net Change in Fund Balances – Governmental Funds</b>		\$ (13,792,501)
1	Governmental funds report the portion of capital outlay for capitalized assets as expenditures. However, in the Statement of Activities, the costs of those assets are allocated over their estimated useful lives as depreciation expense.	
	Expenditures for capitalized assets	\$ 24,334,224
	Less current year depreciation	<u>(1,841,530)</u>
		22,492,694
2	Repayment of principal on bonds, notes, and capital leases is an expenditure in the governmental funds, but this expenditure is removed from the Statement of Activities and the repayments instead reduce long-term liabilities on the Statement of Net Position.	6,660,000
3	Issuance of long-term debt increases current financial resources to governmental funds, but this increase is not shown on the Statement of Activities and instead increases long-term liabilities on the Statement of Net Position.	(9,613,647)
4	Accumulated accretion on bonds issued by governmental activities is recognized only when paid in the governmental funds, but is treated as interest expense on the Statement of Activities as it accretes.	(126,754)
5	Since long-term debt is not recorded in governmental funds, amortization of related issuance premiums and discounts is also not recorded.	274,114
6	The change in accrued interest due on long-term debt issued for governmental activities does not affect current financial resources and therefore is not reported in the governmental funds.	37,637
7	Property taxes are recognized as revenue in the governmental funds when collected but recognized on the Statement of Activities in the year levied. Therefore the uncollected amount of the current year levy is added to current year property tax revenue on the Statement of Activities.	750,326
8	Governmental funds report pension contributions as expenditures. However, pension contributions are reported as deferred outflows of resources on the Statement of Net Position if made after the net pension liability measurement date. In addition, the change in the net pension liability, adjusted for changes in deferred pension items, is reported as pension expense in the Statement of Activities.	(777,058)
9	The District uses an Internal Service Fund to charge the costs of certain activities, such as the provision of workers compensation insurance, to other individual funds. Even though the Internal Service Fund is a proprietary fund, this fund is consolidated with the governmental activities column on the Statement of Activities.	(82,404)
<b>19 Change in Net Position of Governmental Activities</b>		<b>\$ 5,822,407</b>

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

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CLEVELAND INDEPENDENT SCHOOL DISTRICT  
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE  
BUDGET AND ACTUAL – GENERAL FUND  
FOR THE YEAR ENDED AUGUST 31, 2017

Data Control Codes	Budgeted Amounts		Actual Amounts	Variance With Final Budget	
	Original	Final	(GAAP BASIS)		
<b>REVENUES</b>					
5700	Local & Intermediate Sources	\$ 10,432,700	\$ 11,531,471	\$ 11,472,058	\$ (59,413)
5800	State Program Revenues	23,462,568	26,358,628	27,671,508	1,312,880
5900	Federal Program Revenues	523,000	1,208,564	1,214,010	5,446
5020	Total Revenues	34,418,268	39,098,663	40,357,576	1,258,913
<b>EXPENDITURES</b>					
Current:					
0011	Instruction	20,760,380	20,533,433	20,189,352	344,081
0012	Instructional Resources & Media Services	296,029	281,195	270,604	10,591
0013	Curriculum and Staff Development	359,560	339,047	323,508	15,539
0021	Instructional Leadership	138,397	171,174	165,945	5,229
0023	School Leadership	2,447,157	2,638,812	2,616,473	22,339
0031	Guidance/Counseling/Evaluation Services	796,573	846,035	830,960	15,075
0033	Health Services	383,833	323,212	307,498	15,714
0034	Student Transportation	2,327,151	2,618,056	2,416,457	201,599
0036	Extracurricular Activities	1,182,556	1,143,881	1,082,484	61,397
0041	General Administration	1,548,310	1,624,163	1,584,857	39,306
0051	Facilities Maintenance & Operations	4,351,477	4,109,592	3,720,387	389,205
0052	Security and Monitoring Services	522,096	654,401	605,620	48,781
0053	Data Processing Services	618,014	541,963	474,361	67,602
0061	Community Services	2,800	1,884	884	1,000
Capital Outlay:					
0081	Facilities Acquisition & Construction	55,127	3,485,556	2,528,051	957,505
Intergovernmental:					
0093	Payments to Fiscal Agent/Member Dist. of SSA	504,000	568,000	564,966	3,034
0099	Other Intergovernmental Charges	350,000	350,000	322,411	27,589
6030	Total Expenditures	36,643,460	40,230,404	38,004,818	2,225,586
1100	Excess (Deficiency) of Revenues Over (Under) Expenditures	(2,225,192)	(1,131,741)	2,352,758	3,484,499
<b>OTHER FINANCING SOURCES (USES)</b>					
7912	Sale of Property	3,000	23,541	23,541	-
7080	Total Other Financing Sources (Uses)	3,000	23,541	23,541	-
1200	Net Change in Fund Balances	(2,222,192)	(1,108,200)	2,376,299	3,484,499
0100	Fund Balance-September 1 (Beginning)	25,010,272	25,010,272	25,010,272	-
3000	Fund Balance-August 31 (Ending)	\$ 22,788,080	\$ 23,902,072	\$ 27,386,571	\$ 3,484,499

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

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
STATEMENT OF NET POSITION  
PROPRIETARY FUNDS  
AUGUST 31, 2017

Data Control Codes	Governmental Activities Internal Service Fund
<b>ASSETS</b>	
1110 Cash and Cash Equivalents	\$ 132,927
1260 Due from Other Funds	212,760
1000 Total Assets	<u>345,687</u>
<b>LIABILITIES</b>	
Current Liabilities:	
2110 Accounts Payable	307,810
2000 Total Liabilities	<u>307,810</u>
<b>NET POSITION</b>	
3900 Unrestricted Net Position	37,877
3000 Total Net Position	<u><u>\$ 37,877</u></u>

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

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION  
PROPRIETARY FUNDS  
FOR THE YEAR ENDED AUGUST 31, 2017

Data Control Codes	Governmental Activities Internal Service Fund
<b>OPERATING REVENUES</b>	
5700 Local and Intermediate Sources	\$ 140,800
5020 Total Operating Revenues	<u>140,800</u>
<b>OPERATING EXPENSES</b>	
6400 Operating Costs	223,525
6030 Total Operating Expenses	<u>223,525</u>
Operating Income (Loss)	(82,725)
7955 Earnings - Temporary Investments	<u>321</u>
1300 Change in Net Position	(82,404)
0100 Total Net Position - Beginning	<u>120,281</u>
3300 Total Net Position - Ending	<u><u>\$ 37,877</u></u>

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

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CLEVELAND INDEPENDENT SCHOOL DISTRICT  
STATEMENT OF CASH FLOWS  
PROPRIETARY FUNDS  
FOR THE YEAR ENDED AUGUST 31, 2017

Data Control Codes	Governmental Activities Internal Service Fund
<u>Cash Flows from Operating Activities</u>	
Cash Received from User Charges	\$ 190,800
Cash Payments for Operating Activities	(118,580)
Net Cash provided by (Used for) Operating Activities	72,220
<u>Cash Flows from Investing Activities</u>	
Dividends/Interest Received	321
Net Cash provided by (Used for) Investing Activities	321
Net Increase (Decrease) in Cash and Cash Equivalents	72,541
Cash and Cash Equivalents at Beginning of the Year	60,386
Cash and Cash Equivalents at the End of the Year:	\$ 132,927
<u>Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used for) Operating Activities</u>	
Operating Income (Loss):	\$ (82,725)
Effect of Increases and Decreases in Current Assets and Liabilities:	
Increase (Decrease) in Accounts Receivable	50,000
Increase (Decrease) in Accounts Payable	104,945
Net Cash Provided by (Used for) Operating Activities	\$ 72,220

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

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
STATEMENT OF NET POSITION  
FIDUCIARY FUNDS  
AUGUST 31, 2017

Data Control Codes	Private Purpose Trust	
	Fund	Agency Funds
<b>ASSETS</b>		
1110 Cash and Cash Equivalents	\$ 2,035	\$ 90,579
1000 Total Assets	<u>2,035</u>	<u>90,579</u>
<b>LIABILITIES</b>		
Current Liabilities:		
2180 Due to Other Governments	-	23,159
2190 Due to Student Groups	-	67,420
2000 Total Liabilities	<u>-</u>	<u>\$ 90,579</u>
<b>NET POSITION</b>		
3800 Held in Trust	<u>2,035</u>	
3000 Total Net Position	<u>\$ 2,035</u>	

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

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
STATEMENT OF CHANGES IN NET POSITION  
FIDUCIARY FUNDS  
FOR THE YEAR ENDED AUGUST 31, 2017

Data Control Codes	Private Purpose Trust Fund
<b>ADDITIONS</b>	
5700 Local and Intermediate Sources	\$ 2,011
5020 Total Revenues	<u>2,011</u>
<b>DEDUCTIONS</b>	
6200 Scholarships Distributed	2,500
6030 Total Expenses	<u>2,500</u>
1200 Change in Net Position	(489)
0100 Net Position - Beginning	<u>2,524</u>
3000 Net Position - Ending	<u><u>\$ 2,035</u></u>

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

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CLEVELAND INDEPENDENT SCHOOL DISTRICT  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED AUGUST 31, 2017

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### **The Financial Reporting Entity**

This report includes those activities, organizations and functions related to Cleveland Independent School District (the "District"), which are controlled by or dependent upon the District's governing body, the Board of Trustees (the "Board"). The Board, a seven-member group, is the level of government having governance responsibilities over all activities related to public elementary and secondary school education within the jurisdiction of the District. Since the District receives funding from local, state, and federal government sources, it must comply with the requirements of the entities providing those funds. However, the District is not included in any other governmental "reporting entity" as defined by Statement No. 14 of the Governmental Accounting Standards Board (GASB), since Board members are elected by the public and have decision making authority. Furthermore, there are no legally separate organizations, known as "component units", included within the reporting entity.

The accounting policies of the District comply with the rules prescribed by the Texas Education Agency (TEA) in its Financial Accountability System Resource Guide (FASRG). These accounting policies conform to generally accepted accounting principles applicable to state and local governments.

### **Government-wide and Fund 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 District. The effect of interfund activity has been removed from these statements. Governmental activities, which are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely on fees and charges for support. Currently however, the District has no business-type activities.

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

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds are reported as separate columns in the fund financial statements.

### **Measurement Focus, Basis of Accounting, and Financial Statement Presentation**

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Agency funds have no measurement focus. 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. Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided and 2) operating grants and contributions. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes. As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED AUGUST 31, 2017

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 sixty 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 are recorded only when payment is due.

Major revenue sources considered susceptible to accrual include state and federal program revenues and property taxes. No accrual for property taxes collected within sixty days of year end has been made as such amounts are deemed immaterial; delinquent property taxes at year end are reported as deferred inflows of resources within the fund governmental fund financial statements.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

**Major Funds and Fund Types**

The District reports the following major governmental funds:

The General Fund includes financial resources that are not required to be reported separately in another fund. It is a budgeted fund, and any unrestricted fund balances are considered to be resources available for current operations.

The Debt Service Fund includes debt service taxes and other revenues collected to retire bond principal and to pay interest due. It is a budgeted fund.

The Capital Projects Funds are used to account for the construction, improvement and renovation of school buildings in the District along with the acquisition of land and equipment. These funds are budgeted on a project basis rather than annually.

Additionally, the District reports the following fund types:

Special revenue funds are governmental funds which include resources restricted, committed, or assigned for specific purposes by a grantor or the Board. Federally financed programs where unused balances are returned to the grantor at the close of specified project periods are accounted for in these funds.

Internal service funds are proprietary funds used to account for activities such as workers' compensation self-insurance, self-funded health insurance, and employee health savings accounts. The District utilizes an Internal Service Fund to account for its participation in a workers' compensation shared risk pool.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED AUGUST 31, 2017

Private purpose trust funds are fiduciary funds used to account for donations for which the donors have stipulated that both the principal and the income may be used for purposes that benefit parties outside the District. The District utilizes this fund type to account for money collected and held for the purpose of awarding scholarships to selected students.

Agency funds are fiduciary funds used to account for resources held for others in a custodial capacity. The District utilizes this fund type to account for funds held on behalf of student clubs and organizations.

### **Budgetary Information**

Budgets are prepared annually for the General Fund, the Debt Service Fund, and the Child Nutrition Fund on the modified accrual basis, which is consistent with generally accepted accounting principles. A formal budget is prepared by the end of August and is adopted by the Board at a public meeting after public notice of the meeting has been given no earlier than the 30th day or later than the 10th day before the public hearing. The legal level of control for budgeted expenditures is the function level within the budgeted funds. Amendments to the budget are required prior to expending amounts greater than the budgeted amounts at the function level. Budgets are controlled at the departmental or campus level, the same level at which responsibility for operations is assigned. The budget was monitored by the administration throughout the year and amendments were brought to the Board as needed.

### **Assets, Deferred Outflows of Resources, Liabilities, Deferred Inflows of Resources, and Net Position or Fund Balance**

Investments - The District's investment policies and types of investments are governed by Section 2256 of the Texas Government Code (Public Funds Investment Act). The types of investments allowed under the Public Funds Investment Act are detailed in Note 2 - Deposits and Investments. The District's management believes that it complied with the requirements of the Public Funds Investment Act and the District's investment policies. The District accrues interest on temporary investments based on the terms and effective interest rates of the specific investments. For the year and as of year end, the District did not have any balances classified as investments.

Inventories - Inventories are generally not recorded in the General Fund or Child Nutrition Fund due to amounts of expendable supplies held or purchased food not being deemed material. When inventories are recorded, they are charged to expenditures when consumed. Amounts recorded are offset by a fund balance classification titled "nonspendable" which indicates that the inventory does not represent "available expendable resources."

Capital Assets - Capital assets, which include land, buildings and improvements, construction in progress, furniture and equipment, and vehicles are reported in the governmental activities column in the government-wide financial statements. Capital assets are defined by the District as assets with an initial, individual cost of at least \$5,000 and a useful life of greater than one year. Such assets are recorded at historical cost, if purchased, or estimated fair value at the date of donation, if donated. The costs of normal maintenance and repairs that do not add to the value of the assets or materially extend assets lives are not capitalized. Capital assets (other than land and construction in progress) are depreciated using the straight-line method over the following estimated useful lives: buildings and improvements - fifteen to thirty years, furniture and equipment - three to twenty years, and vehicles - five to ten years.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED AUGUST 31, 2017

Prepaid Items - Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements. Prepaid items are charged to expenditures when consumed. When prepaid items are recorded, they are charged to expenditures when the value represented by the prepaid item has been used. Amounts recorded are offset by a fund balance classification titled “nonspendable” which indicates that the prepaid item amount does not represent “available expendable resources.”

Ad Valorem Property Taxes - Delinquent taxes, when received, are prorated between maintenance and debt service based on rates adopted for the year of the levy. Allowances for uncollectibles within the General and Debt Service Funds are based upon historical experience in collecting property taxes. Uncollectible personal property taxes are periodically reviewed and written off, but the District is prohibited from writing off real property taxes without specific statutory authority from the Texas Legislature.

Accumulated Sick Leave Liability - The State of Texas (the “State”) has created a minimum sick leave program consisting of five days of sick leave per year with no limit on accumulation and transferability among districts for every person regularly employed in Texas public schools. Each district’s local Board is required to establish a sick leave plan. Local school districts may provide additional sick leave beyond the state minimum.

Pensions - The fiduciary net position of the Teacher Retirement System of Texas (TRS) has been determined using the flow of economic resources measurement focus and full accrual basis of accounting. This includes for purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, pension expense, and information about assets, liabilities and additions to/deductions from TRS’s fiduciary net position. Benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with benefit terms. Investments are reported at fair value.

Deferred Outflows and Deferred Inflows of Resources - The District complies with GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which provides guidance for reporting the financial statement elements of deferred outflows of resources, which represent a consumption of the District’s net position that is applicable to a future reporting period, and deferred inflows of resources, which represent the District’s acquisition of net position applicable to a future reporting period.

The District complies with GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities.

Fund Balance/Deficit - The District complies with GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED AUGUST 31, 2017

Statement of Cash Flows - For purposes of the statement of cash flows when Proprietary Funds are used, cash and cash equivalents include demand deposits.

Fair Value Measurements - The District adopted GASB Statement No. 72, *Fair Value Measurement and Application*, which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction. Fair value accounting requires characterization of the inputs used to measure fair value into a three-level fair value hierarchy as follows:

- Level 1 inputs are based on unadjusted quoted market prices for identical assets or liabilities in an active market the entity has the ability to access
- Level 2 inputs are observable inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from sources independent from the entity
- Level 3 are unobservable inputs that reflect the entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available

There are three general valuation techniques that may be used to measure fair value:

- Market approach - uses prices generated by market transactions involving identical or comparable assets or liabilities
- Cost approach - uses the amount that currently would be required to replace the service capacity of an asset (replacement cost)
- Income approach - uses valuation techniques to convert future amounts to present amounts based on current market expectations

**Data Control Codes**

The Data Control Codes shown on the financial statements refer to the account code structure prescribed by the FASRG. TEA requires school districts to display these codes in their financial statements to ensure accuracy in building a state-wide data base for policy development and funding plans.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED AUGUST 31, 2017

## 2. DEPOSITS AND INVESTMENTS

The Public Funds Investment Act authorizes the District to invest in funds under a written investment policy, which is approved annually by the Board. The primary objectives of the District's investment strategy for operating and agency funds, in order of priority, are safety, investment liquidity, and maturity sufficient to meet anticipated cash flow requirements. The primary objective of the District's investment strategy for Debt Service and Capital Projects Funds is sufficient investment liquidity to meet related obligations.

The District is authorized to invest in the following investment instruments provided that they meet the guidelines established in the investment policy:

- Obligations of, or guaranteed by, governmental entities
- Certificates of deposit and share certificates
- Fully collateralized repurchase agreements
- Securities lending program
- Banker's acceptances
- Commercial paper
- No-load money market mutual funds and no-load mutual funds
- Guaranteed investment contracts as an investment vehicle for bond proceeds
- Public funds investment pools

The District's funds are required to be deposited and invested under the terms of a depository contract pursuant to the School Depository Act. The depository bank deposits for safekeeping and trust with the District's agent approved pledged securities in an amount sufficient to protect District funds on a day-to-day basis during the period of the contract. The pledge of approved securities is waived only to the extent of the dollar amount of Federal Deposit Insurance Corporation (FDIC) insurance. Therefore, the District is not exposed to custodial credit risk.

Under the depository contract, the District, at its own discretion, may invest funds in time deposits and certificates of deposit provided by the depository bank at interest rates approximating United States Treasury Bill rates.

At August 31, 2017, the carrying amount of the District's cash and deposits was \$49,226,859 and the bank balance was \$49,946,792. The District's deposits with financial institutions at August 31, 2017 and during the year ended August 31, 2017 were entirely covered by FDIC insurance or by pledged collateral held by the District's agent bank in the District's name. The deposits were collateralized in accordance with Texas law and TEA maintains copies of all safekeeping receipts in the name of the District.

The District maintains a cash pool consisting of demand deposits. The combined pool is available for use by most Special Revenue Funds. If a fund overdraws its share of the pool, the overdraft is reported as an interfund payable in that fund. The offsetting interfund receivable is reported in the General Fund.

The following is disclosed regarding coverage of combined balances on the date of highest deposit:

- a) Name of depository bank: Prosperity Bank
- b) The amount of bond and/or security pledged as of the date of the highest combined balance on deposit was \$79,680,645.
- c) The largest cash, savings and time deposit combined account balance amounted to \$69,629,388 and occurred during the month of January 2017.
- d) Total amount of FDIC coverage at the time of highest combined balance was \$250,000.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED AUGUST 31, 2017

Credit Risk - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The ratings of securities by nationally recognized agencies are designed to give an indication of credit risk.

Custodial Credit Risk - Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized, collateralized with securities held by the pledging financial institution, or collateralized with securities held by the pledging financial institution's trust department or agent but not in the District's name. Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the District, and are held by either the counterparty or the counterparty's trust department or agent but not in the District's name. At August 31, 2017, the District was not exposed to custodial credit risk.

Concentration of Credit Risk - Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investments in a single issuer. Information regarding investments in any one issuer that represents five percent or more of the District's total investments must be disclosed under GASB Statement No. 40, excluding investments issued or explicitly guaranteed by the U.S. government.

Interest Rate Risk - As a means of minimizing risk of loss due to interest rate fluctuations, the District's investment policy requires that maturities will not exceed the weighted average maturity of 180 days for any internally created pool fund group and one year from the time of purchase for any other individual investment. The Board may specifically authorize a longer maturity for a given investment, within legal limits. The District considers the holdings in the local governmental investment pools to have a one day weighted average maturity due to the fact that the share position can usually be redeemed each day at the discretion of the shareholders, unless there has been a significant change in value. At August 31, 2017, the District had no investments.

### **3. PROPERTY TAXES**

The Texas Legislature in 1979 adopted a comprehensive Property Tax Code (the "Code") which established a county-wide appraisal district and an appraisal review board in each county in the State. The Liberty Central Appraisal District, Montgomery Central Appraisal District and San Jacinto Central Appraisal District (the "Appraisal Districts") are responsible for the recording and appraisal of all property in the District. Under the Code, the school board sets the tax rates on property and the Liberty County Tax Assessor/Collector provides tax collection services. The Appraisal Districts are required under the Code to assess property at 100% of its appraised value. Further, real property must be reappraised at least every three years. Under certain circumstances, taxpayers and taxing units, including the District, may challenge orders of the Appraisal Review Board through various appeals and, if necessary, legal action.

Property taxes are levied as of October 1 in conformity with Subtitle E, Texas Property Tax Code. Taxes are due on receipt of the tax bill and are delinquent if not paid before February 1 of the year following the year in which imposed. On January 1 of each year, a tax lien attaches to property to secure the payment of all taxes and penalties and interest that are ultimately imposed. Property tax revenues are considered available when they become due or past due and receivable within the current period, including those property taxes expected to be collected during a 60-day period after the end of the District's fiscal year. The assessed value at January 1, 2016, upon which the October 2016 levy was based was \$1,071,937,872.

The District levied taxes based on a combined tax rate of \$1.38 per \$100 of assessed valuation for local maintenance (general governmental services) and Debt Service.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
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**4. DUE FROM/TO OTHER GOVERNMENTS**

The District participates in a variety of federal and state programs from which it receives grants to partially or fully fund certain activities. The District also receives entitlements from the state through the School Foundation and Per Capita Programs. Grants and entitlements are recorded as revenue when earned, therefore at year end amounts earned but not yet received in cash may be recorded as due from the grantor government. Amounts already received in cash but not yet earned are recorded as due to the grantor government.

A summary of amounts recorded as Due From/Due To Other Governments in the basic financial statements as of August 31, 2017 are summarized below:

Due From Other Governments:	General Fund	Non-Major Governmental Funds	Total
<b>Governmental Activities:</b>			
Foundation & Per Capita entitlements	\$ 6,641,441	\$ -	\$ 6,641,441
State grants	-	89,481	89,481
Federal grants	5,446	452,738	458,184
Total - Governmental Activities	\$ 6,646,887	\$ 542,219	\$ 7,189,106

**5. INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS**

During the course of operations, the individual funds of the District may engage in temporary borrowings of money between one another to meet liquidity needs. These interfund receivables and payables are recorded on the balance sheet of the loaning fund as “Due from Other Funds” and on the balance sheet of the borrowing fund as “Due to Other Funds”. Amounts are repaid when funds are available in the borrowing fund.

Individual funds may also make payments between one another which are intended to be permanent and therefore not repaid. These transactions are recorded on the statement of revenues, expenditures, and changes in fund balance as “Transfers Out” for the paying fund and “Transfers In” for the receiving fund.

The composition of interfund balances as of August 31, 2017 was as follows:

Receivable Fund	Payable Fund	Amount
General Fund	General Fund	\$ 423,694
Total General Fund		423,694
Special Revenue Funds	General Fund	1,579
Total Special Revenue Funds		1,579
Internal Service Fund	General Fund	212,760
Total Internal Service Fund		212,760
Grand Total		\$ 638,033

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
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**6. CAPITAL ASSETS**

Capital asset activity for the year ended August 31, 2017 was as follows:

	Beginning Balance 9/1/16	Additions	Retirements	Ending Balance 8/31/17
Governmental Activities:				
Capital assets, not being depreciated:				
Land	\$ 1,019,259	\$ 1,527,010	\$ -	\$ 2,546,269
Construction in progress	2,082,313	19,286,373	-	21,368,686
Total capital assets, not being depreciated	<u>3,101,572</u>	<u>20,813,383</u>	<u>-</u>	<u>23,914,955</u>
Capital assets, being depreciated:				
Buildings and improvements	57,448,380	2,812,306	(20,000)	60,240,686
Furniture and equipment	5,743,728	869,657	(561,851)	6,051,534
Total capital assets, being depreciated	<u>63,192,108</u>	<u>3,681,963</u>	<u>(581,851)</u>	<u>66,292,220</u>
Less accumulated depreciation for:				
Buildings and improvements	(20,223,896)	(1,439,099)	20,000	(21,642,995)
Furniture and equipment	(3,970,435)	(402,431)	561,851	(3,811,015)
Total accumulated depreciation	<u>(24,194,331)</u>	<u>(1,841,530)</u>	<u>581,851</u>	<u>(25,454,010)</u>
Governmental Activities Capital Assets, Net	<u>\$ 42,099,349</u>	<u>\$ 22,653,816</u>	<u>\$ -</u>	<u>\$ 64,753,165</u>

Depreciation expense was charged to the functions of the District as follows:

Function	Depreciation Allocation
Instruction	\$ 1,009,450
Instructional Resources & Media	12,412
Curriculum & Staff Development	25,020
Instructional Leadership	7,612
School Leadership	120,012
Guidance/Counseling/Evaluation Services	38,114
Health Services	14,104
Student Transportation	110,838
Food Services	111,475
Cocurricular/Extracurricular Activities	49,651
General Administration	72,694
Plant Maintenance and Operations	179,235
Security and Monitoring Services	27,820
Data Processing Services	21,758
Community Services	633
Payments related to SSAs	25,914
Other Intergovernmental Charges	14,788
Totals	<u>\$ 1,841,530</u>

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
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**7. BONDS, NOTES, AND OTHER LONG-TERM LIABILITIES**

Governmental activities long-term debt obligations at August 31, 2017 consisted of the following:

General Long-Term Debt Description	Outstanding at August 31, 2017
\$9,324,989 Unlimited Tax Refunding Bond, Series 2006; due in two remaining installments of \$190,204 and \$174,785 in 2025 and 2026, respectively; interest at 4.0% to 4.375%.	\$ 364,989
\$20,875,812 Unlimited Tax Refunding Bond, Series 2010; due in remaining annual installments ranging from \$510 to \$2,975,000 through 2033; interest at 3.0% to 4.0%.	20,641,777
\$7,370,000 Unlimited Tax Refunding Bond, Series 2015; due in remaining installments ranging from \$60,000 to \$1,370,000 through 2031; interest at 2.0% to 4.0%.	7,170,000
\$30,715,000 Unlimited Tax Building Bond, Series 2016; due in remaining installments ranging from \$50,000 to \$3,085,000 through 2046; interest at 3.0% to 5.0%.	30,715,000
\$4,975,000 Unlimited Tax Refunding Bond, Series 2017; due in remaining annual installments ranging from \$390,000 to \$850,000 through 2024; interest at 2.0% to 3.0%.	4,950,000
\$4,015,000 Unlimited Tax Building Bond, Series 2017; due in remaining annual installments ranging from \$155,000 to \$285,000 through 2037; interest at 2.0% to 4.0%.	4,015,000
Capital Appreciation Bonds, Series 2006 and Series 2010.	3,015,375
Total General Obligation and Refunding Bonds	<u>\$ 70,872,141</u>

The following is a summary of changes in long-term liabilities for the year ended August 31, 2017:

Type	Outstanding 9/1/16	Additions	Deletions	Current Accretion	Outstanding 8/31/17	Due in One Year
Bonds Payable:						
General Oblig. & Refunding Bonds	\$68,415,387	\$ 8,990,000	\$(6,660,000)	\$ 126,754	\$70,872,141	\$1,935,000
Premium on Issuance of Bonds	5,919,698	623,647	(274,114)	-	6,269,231	-
Total Bonds	<u>74,335,085</u>	<u>9,613,647</u>	<u>(6,934,114)</u>	<u>126,754</u>	<u>77,141,372</u>	<u>1,935,000</u>
Other Long-Term Liabilities:						
Net Pension Liability	7,141,986	1,531,053	-	-	8,673,039	-
Total Other Long-Term Debt	<u>7,141,986</u>	<u>1,531,053</u>	<u>-</u>	<u>-</u>	<u>8,673,039</u>	<u>-</u>
Total Governmental Activities	<u>\$81,477,071</u>	<u>\$11,144,700</u>	<u>\$(6,934,114)</u>	<u>\$ 126,754</u>	<u>\$85,814,411</u>	<u>\$1,935,000</u>

For the general obligation bonds, the District has pledged as collateral the proceeds of a continuing, direct annual tax levied against taxable property within the District. The Texas Education Code generally limits issuance of additional ad valorem tax bonds if the tax rate needed to pay aggregate principal and interest amounts of the District's tax bond indebtedness would exceed \$0.50 per \$100 of assessed valuation of taxable property within the District.

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During the year, the District issued \$4,015,000 of Unlimited Tax School Building Bonds, Series 2017, to provide funding to construct, equip and/or renovate buildings in the District. Additionally, during the year the District issued \$4,975,000 of Unlimited Tax Refunding Bonds, Series 2017. The proceeds from this issue were used to refund approximately \$5 million of Series 2007 bonds. The refunding was undertaken to obtain a more favorable average interest rate and as a result reduce future debt service payments. The resulting decrease in total future debt service payments is \$320,662 representing a net present value savings of \$292,455.

Annual principal installments for outstanding bonds vary each year. The debt service requirements to maturity for general obligation bonds as of August 31, 2017 are as follows:

Year Ended August 31,	General Obligations			Total Requirements
	Principal	Accumulated Accretion	Interest	
2018	\$ 1,031,267	\$ 903,733	\$ 3,754,533	\$ 5,689,533
2019	840,510	909,490	3,743,465	5,493,465
2020	2,000,000	-	2,791,975	4,791,975
2021	2,040,000	-	2,731,675	4,771,675
2022	2,115,000	-	2,669,350	4,784,350
2023-2027	10,349,990	1,202,152	14,245,374	25,797,516
2028-2032	14,950,000	-	9,946,688	24,896,688
2033-2037	11,605,000	-	7,046,975	18,651,975
2038-2042	11,460,000	-	4,355,750	15,815,750
2043-2046	11,465,000	-	1,182,375	12,647,375
Totals	\$ 67,856,766	\$ 3,015,375	\$ 52,468,160	\$ 123,340,301

The District had no capital leases outstanding during the year. However, the District has the following annual obligations related to copier and portable building operating leases as of year end:

Year Ending August 31,	Amount
2018	\$ 207,438
2019	161,499
2020	161,499
2021	161,499
2022	148,041
Total Minimum Rentals	\$ 839,976
Rental Expenditures for the fiscal year ended August 31, 2017	\$ 208,047

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**8. DEFINED BENEFIT PENSION PLAN**

*Plan Description*

Cleveland Independent School District participates in a cost-sharing multiple-employer defined benefit pension plan that has a special funding situation. The plan is administered by the Teacher Retirement System of Texas (TRS). TRS's defined benefit pension plan is established and administered in accordance with the Texas Constitution, Article XVI, Section 67 and Texas Government Code, Title 8, Subtitle C. The pension trust fund is a qualified pension trust under Section 401(a) of the Internal Revenue Code. The Texas Legislature establishes benefits and contribution rates within the guidelines of the Texas Constitution. The pension's Board of Trustees does not have the authority to establish or amend benefit terms.

All employees of public, state-supported education institutions in Texas who are employed for one-half or more of the standard work load and who are not exempted from membership under Texas Government Code, Title 8, Section 822.002 are covered by the system.

*Pension Plan Fiduciary Net Position*

Detailed information about the Teacher Retirement System's fiduciary net position is available in a separately issued Comprehensive Annual Financial Report that includes financial statements and required supplementary information. That report may be obtained on the Internet at <http://www.trs.state.tx.us/about/documents/cafr.pdf#CAFR>; by writing to TRS at 1000 Red River Street, Austin, Texas, 78701-2698; or by calling (512) 542-6592. The information provided in the Notes to the Financial Statements in the 2016 Comprehensive Annual Financial Report for TRS provides the following information regarding the Pension Plan fiduciary net position as of August 31, 2016.

<u>Net Pension Liability</u>	<u>Total</u>
Total Pension Liability	\$ 171,797,150,487
Less: Plan Fiduciary Net Position	(134,008,637,473)
Net Pension Liability	<u>\$ 37,788,513,014</u>
Net Position as a Percentage of Total Pension Liability	78.00%

*Benefits Provided*

TRS provides service and disability retirement, as well as death and survivor benefits, to eligible employees (and their beneficiaries) of public and higher education in Texas. The pension formula is calculated using 2.3 percent (multiplier) times the average of the five-highest annual creditable salaries times years of credited service to arrive at the annual standard annuity except for members who are grandfathered, the three highest annual salaries are used. The normal service retirement is at age 65 with 5 years of credited service or when the sum of the member's age and years of credited service equals 80 or more years. Early retirement is at age 55 with 5 years of service credit or earlier than 55 with 30 years of service credit. There are additional provisions for early retirement if the sum of the member's age and years of service credit total at least 80, but the member is less than age 60 or 62 depending on the date of employment, or if the member was grandfathered under a previous rule. There are no automatic post-employment benefit changes; including automatic cost-of-living-adjustments (COLAs). Ad hoc post-employment benefit changes, including ad hoc COLAs can be granted by the Texas Legislature as noted in the Plan description above.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
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*Contributions*

Contribution requirements are established or amended pursuant to Article 16, section 67 of the Texas Constitution which requires the Texas legislature to establish a member contribution rate of not less than 6% of the member's annual compensation and a state contribution rate of not less than 6% and not more than 10% of the aggregate annual compensation paid to members of the system during the fiscal year. Texas Government Code section 821.006 prohibits benefit improvements, if as a result of the particular action, the time required to amortize TRS' unfunded actuarial liabilities would be increased to a period that exceeds 31 years, or, if the amortization period already exceeds 31 years, the period would be increased by such action.

Employee contribution rates are set in state statute, Texas Government Code 825.402. Senate Bill 1458 of the 83<sup>rd</sup> Texas Legislature amended Texas Government Code 825.402 for member contributions and established employee contribution rates for fiscal years 2014 thru 2017. The 84<sup>th</sup> Texas Legislature, General Appropriations Act (GAA) established the employer contribution rates for fiscal years 2016 and 2017.

<u>Contribution Rates</u>	<u>2016</u>	<u>2017</u>
Member	7.2%	7.7%
Non-Employer Contributing Entity (State)	6.8%	6.8%
Employers	6.8%	6.8%
 <u>Contribution Amounts</u>		
Employer Contribution	\$ 725,127	\$ 760,469
Member Contributions	1,550,198	1,847,174
State On-Behalf Contributions	1,352,998	1,416,210

Contributors to the plan include members, employers, and the State of Texas as the only non-employer contributing entity (NECE). The State contributes to the plan in accordance with state statutes and the GAA.

As the non-employer contributing entity for public education, the State of Texas contributes to the retirement system an amount equal to the current employer contribution rate times the aggregate annual compensation of all participating members of the pension trust fund during that fiscal year reduced by the amounts described below which are paid by the employers. Public school employers are required to pay the employer contribution rate in the following instances:

- On the portion of the member's salary that exceeds the statutory minimum for members entitled to the statutory minimum under Section 21.402 of the Texas Education Code
- During a new member's first 90 days of employment
- When any part or all of an employee's salary is paid by federal funding sources, a privately sponsored source, from non-educational and general, or local funds

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In addition to the employer contributions listed above, there are two additional surcharges an employer is subject to:

- When employing a retiree of the Teacher Retirement System the employer shall pay both the member contribution and the state contribution as an employment after retirement surcharge
- When a school district does not contribute to the Federal Old-Age, Survivors, and Disability Insurance (OASDI) Program for certain employees, they must contribute 1.5% of the state contribution rate for certain instructional or administrative employees; and 100% of the state contribution rate for all other employees

*Actuarial Assumptions*

The total pension liability in the August 31, 2016 actuarial valuation was determined using the following actuarial assumptions:

Valuation Date	August 31, 2016
Actuarial Cost Method	Individual Entry Age Normal
Asset Valuation Method	Market Value
Actuarial Assumptions:	
Single Discount Rate	8.00%
Long-Term Expected Investment Rate of Return	8.00%
Municipal Bond Rate*	N/A*
Last year ending August 31 in the 2016 to 2115	
Projection period (100 years)	2115
Inflation	2.50%
Salary Increases	3.50% to 9.50% including inflation
Benefit Changes During the Year	None
Ad Hoc Post-Employment Benefit Changes	None

\*If a municipal bond rate was to be used, the rate would be 2.84% as of August 2016 (i.e. the weekly rate closest to but not later than the Measurement Date). The source for the rate is the Federal Reserve Statistical Release H.15, citing the Bond Buyer Index of general obligation bonds with 20 years to maturity and an average AA credit rating.

The total pension liability is determined by an annual actuarial valuation. The actuarial methods and assumptions have been selected by the Board of Trustees based upon analysis and recommendations by the System's actuary. The Board of Trustees has sole authority to determine the actuarial assumptions used for the plan. The actuarial methods and assumptions are primarily based on a study of actual experience for the four-year period ending August 31, 2014 and were adopted in September 2015.

The active mortality rates were based on 90% of the RP 2014 Employee Mortality Tables for males and females. The Post-retirement mortality rates were based on the 2015 TRS of Texas Healthy Pensioner Mortality Tables.

*Discount Rate*

A single discount rate of 8.0 % was used to measure the total pension liability. There was no change in the discount rate since the previous fiscal year. This single discount rate was based on the expected rate of return on pension plan investments of 8.0%. The projection of cash flows used to determine this single discount rate assumed that contributions from plan members and those of the contributing employers and the non-employer contributing entity will be made at the rates set by the legislature during the 2013 legislative session.

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Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all future benefit payments of current plan members. 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 with no cross-over point to a municipal bond rate.

The long-term expected rate of return on pension plan investments is 8.0%. The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimates ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation.

Best estimates of geometric real rates of return for each major asset class included in the systems target asset allocation as of August 31, 2016 are summarized below:

Asset Class	Target Allocation	Long-Term Expected Geometric Real Rate of Return	Expected Contribution to Long-Term Portfolio Returns
Global Equity			
U.S.	18%	4.6%	1.0%
Non-U.S. Developed	13%	5.1%	0.8%
Emerging Markets	9%	5.9%	0.7%
Directional Hedge Funds	4%	3.2%	0.1%
Private Equity	13%	7.0%	1.1%
Stable Value			
U.S. Treasuries	11%	0.7%	0.1%
Absolute Return	0%	1.8%	0.0%
Stable Value Hedge Funds	4%	3.0%	0.1%
Cash	1%	-0.2%	0.0%
Real Return			
Global Inflation Linked Bonds	3%	0.9%	0.0%
Real Assets	16%	5.1%	1.1%
Energy and Natural Resources	3%	6.6%	0.2%
Commodities	0%	1.2%	0.0%
Risk Parity			
Risk Parity	5%	6.7%	0.3%
Inflation Expectations			2.2%
Alpha			1.0%
Total	<u>100%</u>		<u>8.7%</u>

*Discount Rate Sensitivity Analysis*

The following schedule shows the impact of the Net Pension Liability if the discount rate used was 1% less or 1% greater than the discount rate that was used (8%) in measuring the 2016 Net Pension Liability.

	1% Decrease in Discount Rate (7.0%)	Discount Rate 8.0%	1% Increase in Discount Rate (9.0%)
District's Proportionate Share of the Net Pension Liability:	\$ 13,422,943	\$ 8,673,039	\$ 4,644,161

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*Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions*

At August 31, 2017, Cleveland Independent School District reported a liability of \$8,673,039 for its proportionate share of the TRS net pension liability. This liability reflects a reduction for State pension support provided to Cleveland Independent School District. The amount recognized by Cleveland Independent School District as its proportionate share of the net pension liability, the related State support, and the total portion of the net pension liability that was associated with Cleveland Independent School District were as follows:

District's Proportionate Share of the Collective Net Pension Liability	\$	8,673,039
State's Proportionate Share that is Associated with the District		12,662,136
Total		\$ 21,335,175

The net pension liability last was measured as of August 31, 2016 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The employer's proportion of the net pension liability was based on the employer's contributions to the pension plan relative to the contributions of all employers to the plan for the period September 1, 2015 through August 31, 2016.

At August 31, 2016 the employer's proportion of the collective net pension liability was .0229515% which was an increase of .0027471% from its proportion measured as of the previous measurement date of August 31, 2015.

There were no changes of assumptions or other inputs that affected measurement of the total pension liability during the measurement period. In addition, there were no changes of benefit terms that affected measurement of the total pension liability during the measurement period.

For the year ended August 31, 2017, Cleveland Independent School District recognized pension expense of \$777,058 and revenue of \$1,066,748 for support provided by the State.

At August 31, 2017, Cleveland Independent School District reported its proportionate share of the TRS's deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences Between Expected and Actual Economic Experience	\$ 135,992	\$ 258,972
Changes in Actuarial Assumptions	264,339	240,405
Difference Between Projected and Actual Investment Earnings	1,671,307	936,891
Changes in Proportion and Difference Between the Employer's Contributions and the Proportionate Share of Contributions	2,574,234	574
Contributions Paid to TRS Subsequent to the Measurement Date	760,469	-
Total	\$ 5,406,341	\$ 1,436,842

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The net amounts of the employer’s balances of deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year Ended 8/31:	Pension Expense Amount
2017	\$ 559,763
2018	559,763
2019	1,028,209
2020	523,766
2021	382,942
Thereafter	154,585

**9. EMPLOYEE HEALTH CARE COVERAGE**

During the year ended August 31, 2017, employees of the District were covered by the state-wide health insurance plan, TRS Active Care. The District contributed between \$239 and \$869 per month per employee to the Plan, and employees, at their option, authorized payroll withholdings to pay additional contributions or premiums for employee and/or dependents. TRS manages TRS Active Care. The Plan is administered by Aetna while Caremark was assigned the prescription drug plan.

**10. RETIREE HEALTH CARE PLAN**

*Plan Description*

The District contributes to the Texas Public School Retired Employees Group Insurance Program (TRS-Care), a cost-sharing multiple-employer defined benefit postemployment health care plan administered by TRS. TRS-Care provides health care coverage for certain persons (and their dependents) who retired under TRS. The statutory authority for the program is Texas Insurance Code (TIC), Chapter 1575. Section 1575.052 grants the TRS Board of Trustees the authority to establish and amend basic and optional group insurance coverage for participants. TRS issues a publicly available financial report that includes financial statements and required supplementary information for TRS-Care. That report may be obtained by visiting the TRS website at [www.trs.state.tx.us](http://www.trs.state.tx.us) under the TRS Publications heading, by writing to the Communications Department of the Teacher Retirement System of Texas at 1000 Red River Street, Austin, Texas 78701, or by calling the TRS Communications Department at 1-800-223-8778.

*Funding Policy*

Contribution requirements are not actuarially determined but are legally established each biennium by the Texas Legislature. TIC, Sections 1575.202, 203 and 204 establish state, active employee and public school contributions, respectively. Funding for free basic coverage is provided by the program based upon public school district payroll. Per TIC, Chapter 1575, the public school contribution may not be less than 0.25% or greater than 0.75% of the salary of each active employee of the public school. Funding for optional coverage is provided by those participants selecting the optional coverage. The State of Texas and active public school employee contribution rates were 1.0% and 0.65% of the public school payroll, respectively, with school districts contributing a percentage of payrolls set at 0.55% for fiscal years 2016 and 2017.

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*Medicare Part-D Subsidies*

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003, which was effective January 1, 2006, established prescription drug coverage for Medicare beneficiaries known as Medicare Part-D. One of the provisions of Medicare Part-D allows for the Texas Public School Retired Employee Group Insurance Program (TRS-Care) to receive retiree drug subsidy payments from the federal government to offset certain prescription drug expenditures for eligible TRS-Care participants.

A summary of the subsidy payments received by TRS-Care on behalf of the District for the last two fiscal years is as follows:

Fiscal Year	Medicare Part-D State On-Behalf Payments
2017	\$ 110,528
2016	81,985

**11. FUND BALANCES**

The District complies with GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds. Those fund balance classifications are described below.

Nonspendable - Amounts that cannot be spent because they are either not in a spendable form or are legally or contractually required to be maintained intact.

Restricted - Amounts that can be spent only for specific purposes because of constraints imposed by external providers, or imposed by constitutional provisions or enabling legislation.

Committed - Amounts that can only be used for specific purposes pursuant to approval by formal action by the Board.

Assigned - For the General Fund, the Board, or an official or body that has been delegated authority by the Board, may appropriate amounts that are to be used for a specific purpose. For all other governmental funds, any remaining positive amounts not previously classified as nonspendable, restricted or committed.

Unassigned - Amounts that are available for any purpose; these amounts can be reported only in the District's General Fund.

A detail of the fund balance amounts within each category is included on the governmental funds balance sheet.

Fund balance of the District may be committed for a specific purpose by formal action of the Board, the District's highest level of decision-making authority. Commitments may be established, modified, or rescinded only through a resolution approved by the Board. The Board has delegated authority to the Superintendent to assign fund balance for a specific purpose. In circumstances where an expenditure is to be made for a purpose for which amounts are available in multiple fund balance classifications, the order in which resources will be expended is as follows: restricted fund balance, committed fund balance, assigned fund balance, and unassigned fund balance.

CLEVELAND INDEPENDENT SCHOOL DISTRICT  
 NOTES TO THE FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED AUGUST 31, 2017

**12. REVENUE FROM LOCAL AND INTERMEDIATE SOURCES**

During the current year, revenues from local and intermediate sources consisted of the following:

Type	General Fund	Debt Service Fund	Capital Projects Fund	Non-Major			Trust Funds	Total
				Governmental Funds	Proprietary Funds			
Property Taxes	\$11,057,082	\$ 3,516,199	\$ -	\$ -	\$ -	\$ -	\$ -	\$14,573,281
Investment Income	93,301	33,571	98,224	4,330	321		11	229,758
Rent	9,063	-	-	-	-	-	-	9,063
Gifts	19,565	-	-	1,435	-		2,000	23,000
Insurance Recovery	503	-	-	-	-	-	-	503
Food Sales	-	-	-	311,997	-	-	-	311,997
Athletics	36,590	-	-	-	-	-	-	36,590
Enterprising Revenues	3,347	-	-	-	-	-	-	3,347
Misc. Local Revenue	252,607	-	-	28,402	140,800		-	421,809
<b>Total</b>	<b>\$11,472,058</b>	<b>\$ 3,549,770</b>	<b>\$ 98,224</b>	<b>\$ 346,164</b>	<b>\$ 141,121</b>		<b>\$ 2,011</b>	<b>\$15,609,348</b>

**13. UNEARNED REVENUE**

Unearned revenue at August 31, 2017 consisted of the following amounts:

Fund	State Grants	Federal Grants	Total
Non-Major Governmental Funds	\$ 9,549	\$ 6,766	\$ 16,315
<b>Total</b>	<b>\$ 9,549</b>	<b>\$ 6,766</b>	<b>\$ 16,315</b>

**14. RISK MANAGEMENT**

The District's risk management program includes coverages through third party insurance providers for property, automobile liability, school professional liability, crime, workers' compensation, and other miscellaneous bonds. During the year ended August 31, 2017, there were no significant reductions in insurance coverage from coverage in the prior year. Losses in excess of the various deductible levels are covered through traditional indemnity coverage for buildings and contents, and vehicle liability with various insurance firms. Settled claims have not exceeded insurance limits for the past three years.

**15. COMMITMENTS AND CONTINGENCIES**

The District participates in a number of federal financial assistance programs. Although the District's grant programs have been audited in accordance with the provisions of *Government Auditing Standards* and when applicable, the Uniform Guidance, for the year ended August 31, 2017, these programs are subject to financial and compliance audits performed by the specific grantors. These audits, if performed, could result in amounts of expenditures being disallowed by the granting agencies and subject to repayment. The District however expects that such amounts, if any, would be immaterial.

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CLEVELAND INDEPENDENT SCHOOL DISTRICT  
 NOTES TO THE FINANCIAL STATEMENTS  
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**16. SELF-INSURANCE FUND**

The District participates in a workers' compensation plan through a Fixed Cost/Loss Fund Program administered by Claims Administrative Services, Inc (CAS). The District's ultimate liability is the ending liability in its loss fund. CAS has excess insurance for the pool and the current self-insured retention is \$1 million.

A reconciliation of the estimated claim liability is as follows:

Year Ended August 31,	Beginning Liability	Estimated Current Year Claims	Claim Payments	Ending Liability
2015	\$ 223,435	\$ 118,823	\$ 122,753	\$ 219,505
2016	219,505	82,982	99,622	202,865
2017	202,865	218,450	113,505	307,810

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**APPENDIX C**

FORM OF BOND COUNSEL'S OPINION

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[Closing Date]

IN REGARD to the authorization and issuance of the "Cleveland Independent School District Unlimited Tax School Building Bonds, Series 2018A", dated December 1, 2018, in the aggregate principal amount of \$37,160,000 (the "Bonds"), we have examined into their issuance by the Cleveland Independent School District (the "District") solely to express legal opinions as to the validity of the Bonds and the exclusion of the interest on the Bonds from gross income for federal income tax purposes, and for no other purpose. We have not been requested to investigate or verify, and we neither expressly nor by implication render herein any opinion concerning, the financial condition or capabilities of the District, the disclosure of any financial or statistical information or data pertaining to the District and used in the sale of the Bonds, or the sufficiency of the security for or the value or marketability of the Bonds.

THE BONDS are issued in fully registered form only and in denominations of \$5,000 or any integral multiple thereof (within a maturity). The Bonds mature on February 15 in each of the years specified in the pricing certificate (the "Pricing Certificate") executed pursuant to an order adopted by the Board of Trustees of the District authorizing the issuance of the Bonds (the "Order" and, jointly with the Pricing Certificate, the "Bond Order"), without right of prior redemption. The Bonds accrue interest from the date, at the rates, and in the manner and interest is payable on the dates, all as provided in the Bond Order.

IN RENDERING THE OPINIONS herein we have examined and rely upon (i) original or certified copies of the proceedings relating to the issuance of the Bonds, including the Bond Order and an examination of the initial Bond executed and delivered by the District (which we found to be in due form and properly executed); (ii) certifications of officers of the District relating to the expected use and investment of proceeds of the sale of the Bonds and certain other funds of the District and (iii) other documentation and such matters of law as we deem relevant. In the examination of the proceedings relating to the issuance of the Bonds, we have assumed the authenticity of all documents submitted to us as originals, the conformity to original copies of all documents submitted to us as certified copies, and the accuracy of the statements contained in such documents and certifications.

BASED ON OUR EXAMINATION, we are of the opinion that, under applicable laws of the United States of America and the State of Texas in force and effect on the date hereof:

Page 2 of Legal Opinion of Norton Rose Fulbright US LLP

Re: \$37,160,000 "Cleveland Independent School District Unlimited Tax School Building Bonds, Series 2018A", dated December 1, 2018

1. The Bonds have been duly authorized by the District and, when issued in compliance with the provisions of the Bond Order, are valid, legally binding, and enforceable obligations of the District, payable from the proceeds of an ad valorem tax levied, without legal limit as to rate or amount, upon all taxable property within the District, except to the extent that the enforceability thereof may be affected by bankruptcy, insolvency, reorganization, moratorium, or other similar laws affecting creditors' rights or the exercise of judicial discretion in accordance with general principles of equity.

2. Pursuant to section 103 of the Internal Revenue Code of 1986, as amended to the date hereof (the "Code"), and existing regulations, published rulings, and court decisions thereunder, and assuming continuing compliance after the date hereof by the District with the provisions of the Bond Order relating to sections 141 through 150 of the Code, interest on the Bonds for federal income tax purposes (a) will be excludable from the gross income, as defined in section 61 of the Code, of the owners thereof, and (b) will not be included in computing the alternative minimum taxable income of the owners thereof.

WE EXPRESS NO OTHER OPINION with respect to any other federal, state, or local tax consequences under present law or any proposed legislation resulting from the receipt or accrual of interest on, or the acquisition or disposition of, the Bonds. Ownership of tax-exempt obligations such as the Bonds may result in collateral federal tax consequences to, among others, financial institutions, life insurance companies, property and casualty insurance companies, certain foreign corporations doing business in the United States, "S" corporations with subchapter "C" earnings and profits, owners of interests in a financial asset securitization investment trust, individual recipients of Social Security or Railroad Retirement benefits, individuals otherwise qualifying for the earned income tax credit and taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry, or who have paid or incurred certain expenses allocable to, tax-exempt obligations.

OUR OPINIONS ARE BASED on existing law, which is subject to change. Such opinions are further based on our knowledge of facts as of the date hereof. We assume no duty to update or supplement our opinions to reflect any facts or circumstances that may thereafter come to our attention or to reflect any changes in any law that may thereafter occur or become effective. Moreover, our opinions are not a guarantee of result and are not binding on the Internal Revenue Service; rather, such opinions represent our legal judgment based upon our review of existing law that we deem relevant to such opinions and in reliance upon the representations and covenants referenced above.



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