

(See "Continuing Disclosure of Information" herein)

Dated March 26, 2007

NEW ISSUE - Book-Entry-Only

In the opinion of Special Tax Counsel, interest on the Obligations (defined below) is excludable from gross income for federal income tax purposes under existing law, subject to the matters described under "Tax Matters" herein, and is not includable in the alternative minimum taxable income of individuals. See "TAX MATTERS" for a discussion of the opinion of Special Tax Counsel, including the alternative minimum tax on corporations.

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

\$24,300,000
CITY OF LANCASTER, TEXAS
(Dallas County)
GENERAL OBLIGATION REFUNDING AND IMPROVEMENT BONDS, SERIES 2007

Dated Date: March 15, 2007

Due: February 15, as shown below

PAYMENT TERMS . . . Interest on the \$24,300,000 City of Lancaster, Texas General Obligation Refunding and Improvement Bonds, Series 2007 (the "Bonds") will accrue from March 15, 2007 (the "Dated Date"), will be payable February 15 and August 15 of each year, commencing February 15, 2008, until maturity or prior redemption, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The definitive Bonds will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company ("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 within a maturity. **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 and Certificates - Book-Entry-Only System" herein. The initial Paying Agent/Registrar is The Bank of New York Trust Company, N.A., Dallas, Texas (see "The Bonds and Certificates - 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 particularly Vernon's Texas Codes Annotated ("V.T.C.A."), Government Code, Chapters 1207 and 1331, as amended, and an election held in the City of Lancaster, Texas on November 8, 2005, and are direct obligations of the City of Lancaster, Texas (the "City"), payable from a continuing ad valorem tax levied on all taxable property within the City, within the limits prescribed by law, as provided in the ordinance authorizing the Bonds (the "Bond Ordinance") (see "The Bonds and Certificates - Authority for Issuance").

PURPOSE . . . Proceeds from the sale of the Bonds will be used for (i) constructing and equipping a new public safety building, (ii) constructing and equipping fire stations, (iii) constructing and equipping a new senior citizens center, (iv) to refund a portion of the City's outstanding debt described in Schedule I attached to this Official Statement (the "Refunded Bonds") to lower the overall debt service requirements of such debt, and (v) to pay the costs associated with the issuance of the Bonds.



The scheduled payment of principal of and interest on the Bonds when due will be insured by a financial guaranty insurance policy to be issued concurrently with the delivery of the Bonds by Ambac Assurance Corporation.

MATURITY SCHEDULE

CUSIP Prefix ⁽¹⁾: 514444

Amount	Feb 15 Maturity	Interest Rate	Yield	CUSIP Suffix ⁽¹⁾	Amount	Feb 15 Maturity	Interest Rate	Yield	CUSIP Suffix ⁽¹⁾
\$ 120,000	2008	4.000%	3.620%	VJ4	\$ 1,245,000	2016	5.000%	3.870%	VS4
645,000	2009	4.000%	3.630%	VK1	1,210,000	2017	5.000%	3.900%	VT2
745,000	2010	4.000%	3.640%	VL9	1,325,000	2018	5.000%	3.990%	VU9
845,000	2011	4.000%	3.650%	VM7	650,000	2019	4.000%	4.180%	VV7
885,000	2012	4.000%	3.680%	VN5	725,000	2020	4.125%	4.270%	VW5
970,000	2013	4.000%	3.730%	VP0	800,000	2021	4.125%	4.330%	VX3
1,050,000	2014	5.000%	3.770%	VQ8	850,000	2022	4.250%	4.390%	VY1
1,135,000	2015	5.000%	3.820%	VR6	885,000	2023	4.250%	4.420%	VZ8

\$1,900,000 5.00% TERM BONDS DUE FEBRUARY 15, 2025 PRICED TO YIELD 4.19% - CUSIP #514444WA2
\$2,100,000 5.00% TERM BONDS DUE FEBRUARY 15, 2027 PRICED TO YIELD 4.21% - CUSIP #514444WB0
\$6,215,000 4.60% TERM BONDS DUE FEBRUARY 15, 2032 PRICED TO YIELD 4.60% - CUSIP #514444WC8

(Accrued Interest from March 15, 2007 to be added)

(1) CUSIP is a registered trademark of the American Bankers Association. CUSIP data herein is provided by Standard and Poor's CUSIP Service Bureau, a division of the McGraw-Hill Companies, Inc. This data is not intended to create a database and does not serve in any way as a substitute for the CUSIP Services. Neither the City, the Financial Advisor nor the Underwriters shall be responsible for the selection or correctness of the CUSIP numbers set forth herein.

REDEMPTION . . . The City reserves the right, at its option, to redeem Bonds having stated maturities on and after February 15, 2018, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2017, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption (see "The Bonds and Certificates - Optional Redemption"). The Bonds maturing on February 15 in each of the years 2025, 2027 and 2032 (the "Term Bonds") are also subject to mandatory sinking fund redemption prior to maturity (see "The Bonds and Certificates - Mandatory Redemption").

SEPARATE ISSUES . . . The Bonds are being offered by the City concurrently with the "City of Lancaster, Texas, Tax and Waterworks and Sewer System Surplus Revenue Certificates of Obligation, Series 2007" (the "Certificates"), under a common Official Statement, and such Bonds and Certificates are hereinafter sometimes referred to collectively as the "Obligations." The Bonds and Certificates are separate and distinct securities offerings being issued and sold independently except for the common Official Statement, and, while the Obligations share certain common attributes, each issue is separate from the other and should be reviewed and analyzed independently, including the type of obligation being offered, its terms for payment, the security for its payment, the rights of the holders, and other features.

LEGALITY . . . The Bonds are offered for delivery when, as and if issued and received by the Underwriters of the Bonds and subject to the approving opinion of the Attorney General of Texas and the opinion of West & Associates, L.L.P., Bond Counsel, Dallas, Texas, and Andrews Kurth, LLP, Special Tax Counsel, Houston Texas (see Appendix C, "Form of Bond and Special Tax Counsel's Opinions"). Certain legal matters will be passed upon for the Underwriters by Fulbright & Jaworski L.L.P., Dallas, Texas, Counsel for the Underwriters.

DELIVERY . . . It is expected that the Bonds will be available for delivery through The Depository Trust Company on May 1, 2007.

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(See "Continuing Disclosure of Information" herein)

Dated March 26, 2007

NEW ISSUE - Book-Entry-Only

In the opinion of Special Tax Counsel, interest on the Obligations (defined below) is excludable from gross income for federal income tax purposes under existing law, subject to the matters described under "Tax Matters" herein, and is not includable in the alternative minimum taxable income of individuals. See "TAX MATTERS" for a discussion of the opinion of Special Tax Counsel, including the alternative minimum tax on corporations.

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

\$14,565,000
CITY OF LANCASTER, TEXAS
(Dallas County)

TAX AND WATERWORKS AND SEWER SYSTEM SURPLUS REVENUE CERTIFICATES OF OBLIGATION, SERIES 2007

Dated Date: March 15, 2007

Due: February 15, as shown below

PAYMENT TERMS . . . Interest on the \$14,565,000 City of Lancaster, Texas Tax and Waterworks and Sewer System Surplus Revenue Certificates of Obligation, Series 2007 (the "Certificates") will accrue from March 15, 2007 (the "Dated Date"), will be payable February 15 and August 15 of each year, commencing February 15, 2008, until maturity or prior redemption, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The definitive Certificates will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company ("DTC") pursuant to the Book-Entry-Only System described herein. Beneficial ownership of the Certificates may be acquired in denominations of \$5,000 or integral multiples thereof within a maturity. **No physical delivery of the Certificates will be made to the beneficial owners thereof.** Principal of, premium, if any, and interest on the Certificates will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Certificates. See "The Bonds and Certificates - Book-Entry-Only System" herein. The initial Paying Agent/Registrar is The Bank of New York Trust Company, N.A., Dallas, Texas (see "The Bonds and Certificates - Paying Agent/Registrar").

AUTHORITY FOR ISSUANCE . . . The Certificates are issued pursuant to the Constitution and general laws of the State of Texas (the "State"), particularly Subchapter C of Chapter 271, Texas Local Government Code, as amended, and constitute direct obligations of the City of Lancaster, Texas (the "City"), payable from a combination of (i) the levy and collection of an annual ad valorem tax, within the limits prescribed by law, on all taxable property within the City, and (ii) a limited (not to exceed \$1,000) junior and subordinate pledge of the surplus Net Revenues of the City's Waterworks and Sewer System as provided in the ordinance authorizing the Certificates (the "Certificate Ordinance") (see "The Bonds and Certificates - Authority for Issuance").

PURPOSE . . . Proceeds from the sale of the Certificates will be used for: (a) certain improvements to the Airport; (b) certain City-wide park design, renovations, improvements, construction, and equipping of such parks; (c) certain bridge, street and alley design, construction, improvements and the equipping thereof, including drainage improvements incidental thereto; (d) certain design, renovation and improvements to Historic Town Square, certain municipal buildings, including the Visitor's Center, City Hall, the new Senior Center, the Animal Shelter, the Community Development building, the new Public Safety Building, Municipal Court Old Library; and the Lancaster Countryview Golf Course, including the beautification improvements, landscaping, and equipping thereof; (e) certain storm water and water and sewer design, renovation, and improvements within the City, and the equipping thereof; (f) certain renovations and improvements to City Fire and Police Stations; (g) purchase of fire and safety equipment and vehicles; (h) purchase of technology, communications equipment, and software for the city and police and fire departments; and (i) payment for professional services rendered in connection with the above listed projects.



The scheduled payment of principal of and interest on the Certificates when due will be insured by a financial guaranty insurance policy to be issued concurrently with the delivery of the Certificates by Ambac Assurance Corporation.

MATURITY SCHEDULE

CUSIP Prefix⁽¹⁾: 514444

Amount	Feb 15 Maturity	Interest Rate	Yield	CUSIP Suffix ⁽¹⁾	Amount	Feb 15 Maturity	Interest Rate	Yield	CUSIP Suffix ⁽¹⁾
\$ 200,000	2008	4.000%	3.620%	UM8	\$ 595,000	2018	4.000%	3.990%	UX4
420,000	2009	4.000%	3.630%	UN6	620,000	2019	4.000%	4.180%	UY2
430,000	2010	4.000%	3.640%	UP1	645,000	2020	4.125%	4.270%	UZ9
450,000	2011	4.000%	3.650%	UQ9	665,000	2021	4.125%	4.330%	VA3
515,000	2012	4.000%	3.680%	UR7	700,000	2022	4.250%	4.390%	VB1
555,000	2013	4.000%	3.730%	US5	735,000	2023	4.250%	4.420%	VC9
600,000	2014	4.000%	3.770%	UT3	765,000	2024	4.250%	4.450%	VD7
530,000	2015	4.000%	3.820%	UU0	800,000	2025	4.375%	4.480%	VE5
550,000	2016	4.000%	3.870%	UV8	835,000	2026	4.375%	4.500%	VF2
570,000	2017	4.000%	3.900%	UW6	875,000	2027	4.375%	4.520%	VG0

\$2,510,000 4.60% TERM CERTIFICATE DUE FEBRUARY 15, 2032 PRICED TO YIELD 4.60% CUSIP #514444VH8

(Accrued Interest from March 15, 2007 to be added)

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REDEMPTION . . . The City reserves the right, at its option, to redeem Certificates having stated maturities on and after February 15, 2018, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2017, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption (see "The Bonds and Certificates - Optional Redemption"). The Certificates maturing on February 15, 2032 (the "Term Certificates") are also subject to mandatory sinking fund redemption prior to maturity (see "The Bonds and Certificates - Mandatory Redemption").

SEPARATE ISSUES . . . The Certificates are being offered by the City concurrently with the "City of Lancaster, Texas, General Obligation Refunding and Improvement Bonds, Series 2007" (the "Bonds"), and such Certificates and Bonds are hereinafter sometimes referred to collectively as the "Obligations." The Certificates and Bonds are separate and distinct securities offerings being issued and sold independently except for the common Official Statement, and, while the Obligations share certain common attributes, each issue is separate from the other and should be reviewed and analyzed independently, including the type of obligation being offered, its terms for payment, the security for its payment, the rights of the holders, and other features.

LEGALITY . . . The Certificates are offered for delivery when, as and if issued and received by the Underwriters of the Certificates and subject to the approving opinion of the Attorney General of Texas and the opinion of West & Associates, L.L.P., Bond Counsel, Dallas, Texas, and Andrews Kurth, LLP, Special Tax Counsel, Houston Texas (see Appendix C, "Form of Bond and Special Tax Counsels' Opinions"). Certain legal matters will be passed upon for the Underwriters Fulbright & Jaworski L.L.P., Dallas, Texas, Counsel for the Underwriters.

DELIVERY . . . It is expected that the Certificates will be available for delivery through The Depository Trust Company on May 1, 2007.

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This Official Statement, which includes the cover page and the Appendices hereto, does not constitute an offer to sell or the solicitation of an offer to buy in any jurisdiction to any person to whom it is unlawful to make such offer, solicitation, or sale.

No dealer, broker, salesperson, or other person has been authorized to give information or to make any representation other than those contained in this Official Statement, and, if given or made, such other information or representations must not be relied upon.

The information set forth herein has been obtained from the City and other sources believed to be reliable, but such information is not guaranteed as to accuracy or completeness and is not to be construed as the representation, promise, or guarantee of the Financial Advisor. This Official Statement contains, in part, estimates and matters of opinion which are not intended as statements of fact, and no representation is made as to the correctness of such estimates and opinions, or that they will be realized. 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 City or other matters described herein since the date hereof. See "Continuing Disclosure of Information" for a description of the City's undertaking to provide certain information on a continuing basis.

Neither the City nor its Financial Advisor make any representation as to the accuracy, completeness, or adequacy of the information supplied by The Depository Trust Company for use in this Official Statement.

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 hereto, to obtain information essential to making an informed investment decision.

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

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

The agreements of the City and others related to the Obligations are contained solely in the contracts described herein. Neither this Official Statement nor any other statement made in connection with the offer or sale of the Obligations is to be construed as constituting an agreement with the purchaser of the Obligations. INVESTORS SHOULD READ THE ENTIRE OFFICIAL STATEMENT, INCLUDING ALL SCHEDULES AND APPENDICES ATTACHED HERETO, TO OBTAIN INFORMATION ESSENTIAL TO MAKING AN INFORMED INVESTMENT DECISION.

This Official Statement contains "Forward-Looking" statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. Such statements may involve known and unknown risks, uncertainties, and other factors which may cause the actual results, performance, and achievements to be different from future results, performance, and achievements expressed or implied by such forward-looking statements. Investors are cautioned that the actual results could differ materially from those set forth in the forward-looking statements.

The Bonds and Certificates 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 and Certificates in accordance with applicable securities law provisions of the jurisdiction in which these securities 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 and Certificates 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 CITY**..... The City of Lancaster is a political subdivision and municipal corporation of the State located in Dallas County, Texas. The City was incorporated in 1952, and first adopted its Home Rule Charter in 1956. The City operates under a Council/Manager form of government with a City Council comprised of the Mayor and seven Councilmembers. The City Manager is the chief administrative officer. The City covers approximately 29 square miles (see "Introduction - Description of the City").

- THE BONDS**..... The \$24,300,000 General Obligation Refunding and Improvement Bonds, Series 2007 are issued as Serial Bonds maturing on February 15 in the years 2008 through 2023, and as Term Bonds maturing February 15, 2025, February 15, 2027, and February 15, 2032 (see "The Bonds and Certificates - Description of the Bonds and Certificates").

- THE CERTIFICATES**..... The \$14,565,000 Tax and Waterworks and Sewer System Surplus Revenue Certificates of Obligation, Series 2007 are issued as Serial Certificates maturing on February 15 in the years 2008 through 2027, and as a Term Certificate maturing February 15, 2032 (see "The Bonds and Certificates - Description of the Bonds and Certificates").

- PAYMENT OF INTEREST**..... Interest on the Bonds and Certificates accrues from March 15, 2007, and is payable February 15, 2008, and each August 15 and February 15 thereafter until maturity or prior redemption (see "The Bonds and Certificates - Description of the Bonds and Certificates," "The Bonds and Certificates - Optional Redemption," and "The Bonds and Certificates - Mandatory Redemption").

- AUTHORITY FOR ISSUANCE**..... The Bonds are issued pursuant to the Constitution and general laws of the State, including particularly Chapters 1207 and 1331, Texas Government Code, as amended, an election held in the City on November 8, 2005, and the Bond Ordinance passed by the City Council of the City (see "The Bonds and Certificates- Authority for Issuance").

The Certificates are issued pursuant to the general laws of the State, particularly Subchapter C of Chapter 271, Texas Local Government Code, as amended, and the Certificate Ordinance passed by the City Council of the City (see "The Bonds and Certificates - Authority for Issuance").

- SECURITY FOR THE BONDS**..... The Bonds constitute direct and voted obligations of the City, payable from an annual ad valorem tax levied, within the limits prescribed by law, on all taxable property located within the City (see "The Bonds and Certificates - Security and Source of Payment").

- SECURITY FOR THE CERTIFICATES**..... The Certificates constitute direct obligations of the City payable from (i) a continuing annual ad valorem tax levied, within the limits prescribed by law, on all taxable property within the City and (ii) a limited (not to exceed \$1,000) junior and subordinate pledge of the surplus Net Revenues (as defined in the Certificate Ordinance) of the City's Waterworks and Sewer System (see "The Bonds and Certificates - Security and Source of Payment").

- REDEMPTION**..... The City reserves the right, at its option, to redeem Bonds or Certificates, as the case may be, having stated maturities on and after February 15, 2018, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2017, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption (see "The Bonds and Certificates - Optional Redemption"). The Bonds maturing on February 15, 2025, February 15, 2027, and February 15, 2032 (the "Term Bonds") are also subject to mandatory redemption in part prior to maturity at the price of par plus accrued interest to the redemption date. The Certificates maturing on February 15, 2032 (the "Term Certificates") are also subject to mandatory sinking fund redemption prior to maturity. See "The Bonds and Certificates – Mandatory Redemption".

- TAX EXEMPTION**..... In the opinion of Bond and Special Tax Counsel, the interest on the Bonds and Certificates will be excludable from gross income for federal income tax purposes under existing law subject to the matters described under "Tax Matters " herein including the alternative minimum tax on corporations.

USE OF PROCEEDS Proceeds from the sale of the Bonds will be used for (i) constructing and equipping a new public safety building, (ii) constructing and equipping fire stations, (iii) constructing and equipping a new senior citizens center, (iv) to refund a portion of the City's outstanding debt described in Schedule I attached to this Official Statement (the "Refunded Bonds") to lower the overall debt service requirements of such debt, and (v) to pay the costs associated with the issuance of the Bonds.

Proceeds from the sale of the Certificates will be used for: (a) certain improvements to the Airport; (b) certain City-wide park design, renovations, improvements, construction, and equipping of such parks; (c) certain bridge, street and alley design, construction, improvements and the equipping thereof, including drainage improvements incidental thereto; (d) certain design, renovation and improvements to Historic Town Square; certain municipal buildings, including the Visitor's Center, City Hall, the new Senior Center, the Animal Shelter, the Community Development building, the new Public Safety Building, Municipal Court Old Library; and the Lancaster Countryview Golf Course, including the beautification improvements, landscaping, and equipping thereof; (e) certain storm water and water and sewer design, renovation, and improvements within the City, and the equipping thereof; (f) certain renovations and improvements to City Fire and Police Stations; (g) purchase of fire and safety equipment and vehicles; (h) purchase of technology, communications equipment, and software for the city and police and fire departments; and (i) payment for professional services rendered in connection with the above listed projects.

RATINGS The Bonds and Certificates are rated "Aaa" by Moody's Investors Service, Inc. ("Moody's") and "AAA" by Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("S&P") through an insurance policy to be issued by AMBAC Assurance Corporation concurrently with the delivery of the Bonds and Certificates. The presently outstanding general obligation debt of the City is rated "A2" by Moody's and "A" by S&P. The City also has issues outstanding which are rated "Aaa" by Moody's and "AAA" by S&P through credit enhancement in the form of municipal bond insurance policies (see "Other Information - Ratings").

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

LEGAL OPINIONS West and Associates L.L.P., Dallas, Texas, Bond Counsel, and Andrews Kurth LLP, Houston, Texas, Special Tax Counsel.

PAYMENT RECORD The City has never defaulted on the payment of its tax supported indebtedness.

SELECTED FINANCIAL INFORMATION

Fiscal Year Ended 9/30	Estimated City Population ⁽¹⁾	Taxable Assessed Valuation	Per Capita Taxable Assessed Valuation	Tax-Supported Debt	Per Capita Tax-Supported Debt	Ratio Tax-Supported	% of Total Tax Collections
						to Taxable Assessed Valuation	
2003	26,796	\$ 1,027,361,750	\$ 38,340	\$ 30,280,000	\$ 1,130	2.95%	102.61%
2004	28,700	1,125,115,094	39,203	28,955,000	1,009	2.57%	100.88%
2005	30,000	1,255,946,124	41,865	27,655,000	922	2.20%	101.43%
2006	33,550	1,380,239,526	41,140	26,915,000	802	1.95%	99.36%
2007	35,000	1,551,066,943	44,316	56,635,000 ⁽²⁾	1,618	3.65%	34.19% ⁽³⁾

(1) Source: North Central Texas Council of Governments.

(2) Projected; includes the Bonds and Certificates. Includes self-supporting debt. See Tables 1 and 10 herein and the footnotes related thereto.

(3) Collections for part year only, through January 1, 2007.

CITY OFFICIALS, STAFF, AND CONSULTANTS

ELECTED OFFICIALS

<u>City Council</u>	<u>Length of Service</u>	<u>Term Expires</u>	<u>Occupation</u>
Joe Tillotson Mayor	8 Years	May, 2008	Retired
Carol Strain-Burk Councilmember, District 1	7 Years	May, 2007	Consultant
C.R. Dick Headen Councilmember, District 2	2 Years	May, 2008	Public Education School District
Susan Anderson Councilmember, District 3	8 Years	May, 2007	Pharmaceuticals
James Daniels Councilmember, District 4	2 Years	May, 2008	Retired
Clyde Hairston Councilmember, District 5	3 Years	May, 2007	Minister
Kimberly Lankford Councilmember, District 6	4 Years	May, 2008	Consultant

SELECTED ADMINISTRATIVE STAFF

<u>Name</u>	<u>Position</u>	<u>Length of Service with City</u>
Jan Belcher	Acting City Manager	4 Years
Maria Joyner	Director of Finance	10 1/2 Years
Dolle Shane	City Secretary	3 1/2 Years
Bob Hager	City Attorney	29 Years

CONSULTANTS AND ADVISORS

Certified Public Accountants Weaver & Tidwell L.L.P.
Dallas, Texas

Bond Counsel West & Associates, L.L.P.
Dallas, Texas

Special Tax Counsel..... Andrews Kurth LLP
Houston, Texas

Financial Advisor First Southwest Company
Fort Worth, Texas

For additional information regarding the City, please contact:

Jan Belcher		David K. Medanich
Maria Joyner		Laura Alexander
City of Lancaster	or	First Southwest Company
211 North Henry Street		777 Main Street, Suite 1200
Lancaster, Texas 75146		Fort Worth, Texas 76102-3123
(972) 218-1110		(817) 332-9710

OFFICIAL STATEMENT

RELATING TO

\$24,300,000
CITY OF LANCASTER, TEXAS
GENERAL OBLIGATION REFUNDING
AND IMPROVEMENT BONDS, SERIES 2007

\$14,565,000
CITY OF LANCASTER, TEXAS
TAX AND WATERWORKS AND SEWER SYSTEM SURPLUS
REVENUE CERTIFICATES OF OBLIGATION, SERIES 2007

INTRODUCTION

This Official Statement, which includes the Appendices hereto, provides certain information regarding the issuance of \$24,300,000 City of Lancaster, Texas, General Obligation Refunding and Improvement Bonds, Series 2007 (the "Bonds") and \$14,565,000 City of Lancaster, Texas, Tax and Waterworks and Sewer System Surplus Revenue Certificates of Obligation, Series 2007 (the "Certificates") (collectively, the "Obligations"). The Bonds and the Certificates are separate and distinct securities offerings being authorized for issuance under separate ordinances (the "Bond Ordinance" and the "Certificate Ordinance", respectively) adopted by the City Council of the City, but are being offered and sold pursuant to a common Official Statement, and while the Bonds and Certificates share certain common attributes, each issue is separate and apart from the other and should be reviewed and analyzed independently, including the kind and type of obligation being issued, its terms of payment, the security for its payment, the rights of the holders and the covenants and agreements made with respect thereto. Capitalized terms used in this Official Statement have the same meanings assigned to such terms in the Bond Ordinance and Certificate Ordinance to be adopted on the date of sale of the Bonds and Certificates (collectively, "the Ordinances"), except as otherwise indicated herein.

This Official Statement contains descriptions of the Bonds and Certificates and certain information regarding the City and its finances. All descriptions of documents contained herein are only summaries and are qualified in their entirety by reference to each such document. Copies of such documents may be obtained from the City's Financial Advisor, First Southwest Company, Dallas, Texas.

DESCRIPTION OF THE CITY . . . The City is a political subdivision and municipal corporation of the State, duly organized and existing under the laws of the State, including the City's Home Rule Charter. The City was incorporated in 1952, and first adopted its Home Rule Charter in 1956. The City operates under a Council/Manager form of government with a City Council comprised of the Mayor and six Councilmembers. The term of office is two years with the terms of the Mayor and two of the Councilmembers' terms expiring in even-numbered years and the other terms of the four remaining Councilmembers expiring in odd-numbered years. The City Manager is the chief administrative officer for the City. Some of the services that the City provides are: public safety (police and fire protection), municipal court, streets, engineering, traffic and transportation, water distribution, sewer treatment, sanitation, health, recreation, public improvements, planning and zoning, and general administrative services. The 2000 Census population for the City was 25,894, while the estimated 2007 population is 35,000. The City covers approximately 10.9 square miles.

PLAN OF FINANCING

PURPOSE . . . Proceeds from the sale of the Bonds will be used for (i) constructing and equipping a new public safety building, (ii) constructing and equipping fire stations, (iii) constructing and equipping a new senior citizens center, (iv) to refund a portion of the City's outstanding debt described in Schedule I attached to this Official Statement (the "Refunded Bonds") to lower the overall debt service requirements of such debt, and (v) to pay the costs associated with the issuance of the Bonds.

Proceeds from the sale of the Certificates will be used for: (a) certain improvements to the Airport; (b) certain City-wide park design, renovations, improvements, construction, and equipping of such parks; (c) certain bridge, street and alley design, construction, improvements and the equipping thereof, including drainage improvements incidental thereto; (d) certain design, renovation and improvements to Historic Town Square; certain municipal buildings, including the Visitor's Center, City Hall, the new Senior Center, the Animal Shelter, the Community Development building, the new Public Safety Building, Municipal Court Old Library; and the Lancaster Countryview Golf Course, including the beautification improvements, landscaping, and equipping thereof; (e) certain storm water and water and sewer design, renovation, and improvements within the City, and the equipping thereof; (f) certain renovations and improvements to City Fire and Police Stations; (g) purchase of fire and safety equipment and vehicles; (h) purchase of technology, communications equipment, and software for the city and police and fire departments; and (i) payment for professional services rendered in connection with the above listed projects.

REFUNDED BONDS . . . The principal and interest due on the Refunded Bonds are to be paid on the scheduled interest payment dates and the respective redemption dates of such Refunded Bonds, from funds to be deposited pursuant to a certain Escrow Agreement (the "Escrow Agreement") between the City and The Bank of New York Trust Company, National Association, Dallas, TX (the "Escrow Agent"). The Bond Ordinance provides that from the proceeds of the sale of the Bonds received from the Underwriters, the City will deposit with the Escrow Agent the amount necessary to accomplish the discharge and final payment of the Refunded Bonds on their respective redemption dates. Such funds will be held by the Escrow Agent in a special escrow account (the "Escrow Fund") and used to purchase direct obligations of the United States of America (the "Federal Securities"). Under the Escrow Agreement, the Escrow Fund is irrevocably pledged to the payment of the principal of and interest on the Refunded Bonds.

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

By deposit of the Federal Securities and cash, if necessary, with the Escrow Agent pursuant to the Escrow Agreement, the City will have effected the defeasance of all the Refunded Bonds in accordance with the law. It is the opinion of Bond Counsel that as a result of such defeasance and in reliance upon the report of Grant Thornton LLP, certified public accountants, the Refunded Bonds will be outstanding only for the purpose of receiving payments from the Federal Securities and any cash held for such purpose by the Escrow Agent and such Refunded Bonds will not be deemed as being outstanding bonds of the City payable from taxes nor for the purpose of applying any limitation on the issuance of debt.

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

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

	<u>The Bonds</u>	<u>The Certificates</u>
<u>Sources of Funds</u>		
Par Amount of Obligations	\$ 24,300,000.00	\$ 14,565,000.00
Original Issue Premium	786,615.25	52,424.30
Transfer from Prior Issue Debt Service Fund	192,287.15	-
Accrued Interest	142,495.70	78,482.39
Total Sources of Funds	<u>\$ 25,421,398.10</u>	<u>\$ 14,695,906.69</u>
<u>Uses of Funds</u>		
Deposit to Escrow Fund	\$ 8,023,495.97	\$ -
Deposit to Construction Fund	16,800,000.00	14,262,261.00
Deposit to Interest and Sinking Fund	145,167.54	78,482.39
Original Issue Discount	68,024.65	116,375.65
Costs of Issuance ⁽¹⁾	384,709.94	238,787.65
Total Uses of Funds	<u>\$ 25,421,398.10</u>	<u>\$ 14,695,906.69</u>

(1) Includes Underwriters' Discount and Insurance Premium.

THE BONDS AND CERTIFICATES

DESCRIPTION OF THE BONDS AND CERTIFICATES . . . The Bonds and Certificates are dated March 15, 2007, and mature on February 15 in each of the years and in the amounts shown on the cover page and page 3 hereof. Interest will be computed on the basis of a 360-day year of twelve 30-day months, and will be payable on August 15 and February 15 of each year, commencing February 15, 2008, until maturity or prior redemption. The definitive Bonds and Certificates 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 and Certificates will be made to the beneficial owners thereof.** Principal of, premium, if any, and interest on the Bonds and Certificates will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Bonds and Certificates. See "The Bonds and Certificates - Book-Entry-Only System" herein.

AUTHORITY FOR ISSUANCE . . . The Bonds are being issued pursuant to the Constitution and general laws of the State of Texas, particularly Chapters 1207 and 1331, Texas Government Code, as amended; an election held and passed by a majority of the participating voters on November 8, 2005; and the Bond Ordinance. See "Table 11 – Authorized But Unissued General Obligation Bonds."

The Certificates are being issued pursuant to the Constitution and general laws of the State of Texas, particularly Subchapter C of Chapter 271, Texas Local Government Code (the Certificate of Obligation Act of 1971), as amended, and the Certificate Ordinance passed by the City Council.

SECURITY AND SOURCE OF PAYMENT . . .

The Bonds . . . The Bonds constitute direct obligations of the City and the principal thereof and interest thereon are payable from an annual ad valorem tax levied by the City, within the limits prescribed by law, upon all taxable property in the City, as provided in the Bond Ordinance.

The Certificates . . . The Certificates constitute direct obligations of the City and the principal thereof and interest thereon are payable from an annual ad valorem tax levied by the City, within the limits prescribed by law, upon all taxable property in the City, and are additionally secured by and payable from a limited (not to exceed \$1,000) junior and subordinate pledge of the surplus net revenues of the City's waterworks and sewer system remaining after payment of all operation and maintenance expenses thereof, and all debt service, reserve and other requirements in connection with all of the City's revenue obligations (now or hereafter outstanding) that are payable from all or part of said revenues, all as provided in the Certificate Ordinance.

TAX RATE LIMITATION . . . All taxable property within the City is subject to the assessment, levy and collection by the City of a continuing, direct annual ad valorem tax within the limits prescribed by law sufficient to provide for the payment of principal of and interest on all ad valorem tax debt. Article XI, Section 5 of the Texas Constitution is applicable to the City, and provides for a maximum ad valorem tax rate of \$2.50 per \$100 Taxable Assessed Valuation for all City purposes. The Home Rule Charter of the City adopts the constitutional maximum tax rate of \$2.50 per \$100 Assessed Valuation for all City purposes. Administratively, the Texas Attorney General will permit allocation of \$1.50 of the \$2.50 maximum tax rate for all general obligation debt service. The issuance of the Bonds and Certificates does not violate this constitutional provision, the City's Home Rule Charter, or the Texas Attorney General's administrative policy.

OPTIONAL REDEMPTION . . . The City reserves the right, at its option, to redeem the Bonds or Certificates, or both, having stated maturities on and after February 15, 2018 in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2017 or any date thereafter, at the par value thereof plus accrued interest to the date of redemption or if less than all of the Bonds or Certificates are to be redeemed, the City may select the maturities of Bonds or Certificates, as the case may be, to be redeemed. If less than all the Bonds or Certificates of any maturity are to be redeemed, the Paying Agent/Registrar (or DTC while the Bonds and Certificates are in Book-Entry-Only form) shall determine by lot the Bonds and Certificates, or portions thereof, within such maturity to be redeemed. If a Bond or Certificate (or any portion of the principal sum thereof) shall have been called for redemption and notice of such redemption shall have been given, such Bond or Certificate (or the principal amount thereof to be redeemed) shall become due and payable on such redemption date and interest thereon shall cease to accrue from and after the redemption date, provided funds for the payment of the redemption price and accrued interest thereon are held by the Paying Agent/Registrar on the redemption date.

MANDATORY REDEMPTION . . . The Bonds maturing on February 15, 2025, February 15, 2027 and February 15, 2032 (the "Term Bonds"), are subject to mandatory redemption in part at a price of par, plus accrued interest to the dates of redemption, on the dates and in the principal amounts as follows:

Term Bonds Maturing					
February 15, 2025		February 15, 2027		February 15, 2032	
Redemption Date	Principal Amount	Redemption Date	Principal Amount	Redemption Date	Principal Amount
February 15, 2024	\$ 925,000	February 15, 2026	\$ 1,025,000	February 15, 2028	\$ 1,130,000
February 15, 2025*	975,000	February 15, 2027*	1,075,000	February 15, 2029	1,185,000
				February 15, 2030	1,240,000
				February 15, 2031	1,300,000
				February 15, 2032*	1,360,000

* Maturity.

The Certificates maturing on February 15, 2032 (the "Term Certificates"), are subject to mandatory redemption in part at a price of par, plus accrued interest to the dates of redemption, on the dates and in the principal amounts as follows:

Term Certificates Maturing	
February 15, 2032	
Redemption Date	Principal Amount
February 15, 2028	\$ 455,000
February 15, 2029	480,000
February 15, 2030	500,000
February 15, 2031	525,000
February 15, 2032*	550,000

* Maturity.

The Paying Agent/Registrar shall select by lot, or other customary method, the numbers of the Term Bonds and Term Certificates to be redeemed. Any Term Bonds or Term Certificates not selected for prior redemption shall be paid on the date of their Stated Maturity.

The principal amount of the Term Bonds and Term Certificates to be redeemed on each mandatory redemption date may be reduced, at the option of the City, by the principal amount of the Term Bonds and Term Certificates which, at least 45 days prior to the mandatory redemption date, (1) shall have been acquired by the City at a price not exceeding the principal amount of such Term Bonds and Term Certificates 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 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 Obligations, the City shall cause a notice of redemption to be sent by United States mail, first class, postage prepaid, to the registered owners of the Obligations 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 NOTWITHSTANDING WHETHER ONE OR MORE REGISTERED OWNERS MAY HAVE FAILED TO RECEIVE SUCH NOTICE. If an Obligation (or any portion of its principal sum) shall have been duly called for redemption and notice of such redemption duly given, then upon the redemption date such Obligation (or the portion of its principal sum to be redeemed) shall become due and payable, and, if monies for the payment of the redemption price and the interest accrued on the principal amount to be redeemed to the date of redemption are held for the purpose of such payment by the Paying Agent/Registrar, interest shall cease to accrue and be payable from and after the redemption date on the principal amount redeemed.

BOOK-ENTRY-ONLY SYSTEM . . . *This section describes how ownership of the Obligations is to be transferred and how the principal of, premium, if any, and interest on the Obligations are to be paid to and credited by The Depository Trust Company ("DTC"), New York, New York, while the Obligations, as applicable, 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 City believes the source of such information to be reliable, but takes no responsibility for the accuracy or completeness thereof.*

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

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

DTC, the world's largest 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 2.2 million issues of U.S. and non-U.S. equity, 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, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Fixed Income Clearing Corporation, and Emerging Markets Clearing Corporation (NSCC, FICC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. 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 Standard & Poor's highest rating: AAA. 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 and www.dtc.org.

Purchases of Obligations under the DTC system must be made by or through Direct Participants, which will receive a credit for the Obligations on DTC's records. The ownership interest of each actual purchaser of each Obligation ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Obligations are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive

certificates representing their ownership interests in Obligations, except in the event that use of the book-entry system for the Obligations is discontinued.

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

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

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

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

Payment of redemption proceeds and principal and interest payments on the Obligations will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or 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 securities 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 nor its nominee, Paying Agent/Registrar, or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds and principal and interest payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or Paying Agent/Registrar, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

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

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

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

Information concerning DTC and the Book-Entry-Only System has been obtained from DTC and is not guaranteed as to accuracy or completeness by, and is not to be construed as a representation by the City or the Underwriters.

Effect of Termination of Book-Entry-Only System. In the event the Book-Entry-Only System with respect to the Obligations is discontinued by DTC, or the use of the Book-Entry-Only System with respect to the Obligations is discontinued by the City, printed securities certificates will be issued to the respective holders of the Obligations, as the case may be, and the respective Obligations will be subject to transfer, exchange, and registration provisions as set forth in the Ordinances, summarized under "The Bonds and Certificates - Transfer, Exchange, and Registration" below.

PAYING AGENT/REGISTRAR . . . The initial Paying Agent/Registrar for the Obligations is The Bank of New York Trust Company, N.A., Dallas, Texas. In the Ordinances, the City retains the right to replace the Paying Agent/Registrar. The City covenants to maintain and provide a Paying Agent/Registrar at all times until the Bonds or Certificates, as the case may be, are duly paid and any successor Paying Agent/Registrar shall be a commercial bank or trust company organized under the laws of the State of Texas or other entity duly qualified and legally authorized to serve as and perform the duties and services of Paying Agent/Registrar for the Bonds and Certificates. Upon any change in the Paying Agent/Registrar for the Bonds or Certificates, the City agrees to promptly cause a written notice thereof to be sent to each registered owner of the Bonds and Certificates

affected by the changes 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 Obligations shall 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 shall 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 Obligations will be paid to the registered owner at their stated maturity or earlier redemption upon presentation to designated payment/transfer office of the Paying Agent/Registrar. If the date for the payment of the principal of or interest on the Obligations shall be 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 shall be the next succeeding day which is not such a day, and payment on such date shall 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, the Bonds and Certificates may be transferred and exchanged on the registration books of the Paying Agent/Registrar only upon presentation and surrender to the Paying Agent/Registrar and such transfer or exchange shall be without expense or service charge to the registered owner, except for any tax or other governmental charges required to be paid with respect to such registration, exchange and transfer. Bonds and Certificates may be assigned by the execution of an assignment form on the respective Bonds and Certificates or by other instrument of transfer and assignment acceptable to the Paying Agent/Registrar. New Bonds and Certificates will be delivered by the Paying Agent/Registrar, in lieu of the Bonds and Certificates 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 and Certificates issued in an exchange or transfer of Bonds and Certificates 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 and Certificates 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 and Certificates 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 and Certificates surrendered for exchange or transfer. See "Book-Entry-Only System" herein for a description of the system to be utilized initially in regard to ownership and transferability of the Bonds and Certificates. Neither the City nor the Paying Agent/Registrar shall be required to transfer or exchange any Bond or Certificate (i) during the period commencing with the close of business on any Record Date and ending with the opening of business on the next following principal or interest payment date, or (ii) with respect to any Bond or Certificate called for redemption, in whole or in part, within 45 days of the date fixed for redemption; provided, however, such limitation of transfer shall not be applicable to an exchange by the registered owner of the uncalled balance of a Bond or Certificate.

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

In the event of a non-payment of interest on a scheduled payment date, and for 30 days thereafter, a new record date for such interest payment (a "Special Record Date") will be established by the Paying Agent/Registrar, if and when funds for the payment of such interest have been received from the City. Notice of the Special Record Date and of the scheduled payment date of the past due interest ("Special Payment Date", which shall be 15 days after the Special Record Date) shall be sent at least five business days prior to the Special Record Date by United States mail, first class postage prepaid, to the address of each registered owner of a Bond or Certificate to be paid on the Special Payment Date that appears 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.

REPLACEMENT OBLIGATIONS . . . If any Obligation is mutilated, destroyed, stolen or lost, a new Obligation in the same principal amount as the Obligation so mutilated, destroyed, stolen or lost will be issued. In the case of a mutilated Obligation, such new Obligation will be delivered only upon surrender and cancellation of such mutilated Obligation. In the case of any Obligation issued in lieu of and substitution for an Obligation which has been destroyed, stolen or lost, such new Obligation will be delivered only (a) upon filing with the City and the Paying Agent/Registrar a certificate to the effect that such Obligation has been destroyed, stolen or lost and proof of ownership thereof, and (b) upon furnishing the City and the Paying Agent/Registrar with indemnity satisfactory to them. The person requesting the authentication and delivery of a new Obligation must pay such expenses as the Paying Agent/Registrar may incur in connection therewith.

REMEDIES . . . Each Ordinance establishes specific events of default with respect to the respective series of Obligations. If the City defaults in the payment of the principal of or interest on the Bonds or Certificates when due or the City defaults in the observance or performance of any of the covenants, conditions, or obligations of the City, the failure to perform which materially, adversely affects the rights of the owners thereof, including but not limited to, their prospect or ability to be repaid in accordance with the respective Ordinance, and the continuation thereof for a period of 60 days after notice of such default is given by any owner to the City, each Ordinance provides that any registered owner of an Obligation is entitled to seek a writ of mandamus from a court of proper jurisdiction requiring the City to make such payment or observe and perform such covenants, obligations, or conditions. The issuance of a writ of mandamus may be sought if there is no other available remedy at law to compel performance of the respective Obligations or Ordinances and the City's obligations are not uncertain or disputed. The remedy of mandamus is controlled by equitable principles, so rests with the discretion of the court, but may not be arbitrarily refused. There is no acceleration of maturity of the Obligations in the event of default and, consequently, the remedy of

mandamus may have to be relied upon from year to year. The Ordinances do not provide for the appointment of a trustee to represent the interest of the owners of the Obligations upon any failure of the City to perform in accordance with the terms of the Ordinances, or upon any other condition and accordingly all legal actions to enforce such remedies would have to be undertaken at the initiative of, and be financed by, the registered owners. On June 30, 2006, the Texas Supreme Court ruled in *Tooke v. City of Mexia*, 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 City's sovereign immunity from a suit for money damages, owners of Obligations may not be able to bring such a suit against the City for breach of the Obligations or Ordinance covenants. Even if a judgment against the City could be obtained, it could not be enforced by direct levy and execution against the City's property. Further, the registered owners cannot themselves foreclose on property within the City or sell property within the City to enforce the tax lien on taxable property to pay the principal of and interest on the Bonds. Furthermore, the City is eligible to seek relief from its creditors under Chapter 9 of the U.S. Bankruptcy Code ("Chapter 9"). Although Chapter 9 provides for the recognition of a security interest represented by a specifically pledged source of revenues, the pledge of ad valorem taxes in support of a general obligation of a bankrupt entity is not specifically recognized as a security interest under Chapter 9. Chapter 9 also includes an automatic stay provision that would prohibit, without Bankruptcy Court approval, the prosecution of any other legal action by creditors or Bondholders of an entity which has sought protection under Chapter 9. Therefore, should the City avail itself of Chapter 9 protection from creditors, the ability to enforce would be subject to the approval of the Bankruptcy Court (which could require that the action be heard in Bankruptcy Court instead of other federal or state court); and the Bankruptcy Code provides for broad discretionary powers of a Bankruptcy Court in administering any proceeding brought before it. The opinions of Bond Counsel will note that all opinions relative to the enforceability of the Obligations are qualified with respect to the customary rights of debtors relative to their creditors.

DEFEASANCE . . . The respective Ordinances provide for the defeasance of the Bonds or Certificates when the payment of the principal of and premium, if any, on the Bonds or Certificates, as the case may be, 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 entity, in trust (1) money sufficient to make such payment or (2) Government Securities, certified by an independent public accounting firm of national reputation to mature as to principal and interest in such amounts and at such times to insure the availability, without reinvestment, of sufficient money to make such payment, and all necessary and proper fees, compensation, and expenses of the paying agent for the Bonds or Certificates being defeased. The respective Ordinances provide 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 are rated as to investment quality by a nationally recognized investment rating firm not less than AAA or its equivalent, and (c) noncallable obligations of a state or an agency or a county, municipality, or other political subdivision of a state that have been refunded and that are rated as to investment quality by a nationally recognized investment rating firm not less than AAA or its equivalent. The City has additionally reserved 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 City moneys in excess of the amount required for such defeasance.

Upon such deposit as described above, such Obligations shall no longer be regarded to be outstanding or unpaid. After firm banking and financial arrangements for the discharge and final payment or redemption of such Obligations have been made as described above, all rights of the City to initiate proceedings to call such Obligations for redemption or take any other action amending the terms of such Obligations are extinguished; provided, however, that the right to call the Obligations for redemption is not extinguished if the City: (i) in the proceedings providing for the firm banking and financial arrangements, expressly reserves the right to call such Obligations for redemption; (ii) gives notice of the reservation of that right to the owners of such Obligations 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 authorize.

AMENDMENTS . . . In each Ordinance, the City has reserved the right to amend the Ordinance without the consent of any holder for the purpose of amending or supplementing the Ordinance to (i) cure any ambiguity, defect or omission therein that does not materially adversely affect the interests of the holders, (ii) grant additional rights or security for the benefit of the holders, (iii) add events of default as shall not be inconsistent with the provisions of the Ordinance that do not materially adversely affect the interests of the holders, (iv) qualify the Ordinance under the Trust Indenture Act of 1939, as amended, or corresponding provisions of federal laws from time to time in effect or (v) make such other provisions in regard to matters or questions arising under the Ordinance that are not inconsistent with the provisions thereof and which, in the opinion of Bond Counsel for the City, do not materially adversely affect the interests of the holders.

Each Ordinance further provides that the holders of the Bonds or Certificates, as applicable, aggregating in principal amount 51% of the outstanding Bonds or Certificates, as the case may be, shall have the right from time to time to approve any amendment not described above to the Ordinance if it is deemed necessary or desirable by the City; provided, however, that without the consent of 100% of the holders in original principal amount of the then outstanding Bonds or Certificates so affected, no amendment may be made for the purpose of: (i) making any change in the maturity of any of the outstanding Bonds or Certificates; (ii) reducing the rate of interest borne by any of the outstanding Bonds Certificates; (iii) reducing the amount of the principal of, or redemption premium, if any, payable on any outstanding Bonds or Certificates; (iv) modifying the terms of payment of principal or of interest or redemption premium on outstanding Bonds or Certificates, or imposing any condition with respect to such payment; or (v) changing the minimum percentage of the principal amount of the Bonds or Certificates necessary for consent to such amendment. Reference is made to the Ordinances for further provisions relating to the amendment thereof.

OBLIGATION INSURANCE

PAYMENT PURSUANT TO FINANCIAL GUARANTY INSURANCE POLICY

Ambac Assurance Corporation ("Ambac Assurance") has made a commitment to issue a financial guaranty insurance policy (the "Financial Guaranty Insurance Policy") relating to the Obligations, effective as of the date of issuance of the Obligations. Under the terms of the Financial Guaranty Insurance Policy, Ambac Assurance will pay to The Bank of New York, in New York, New York, or any successor thereto (the "Insurance Trustee"), that portion of the principal of and interest on the Obligations that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor (as such terms are defined in the Financial Guaranty Insurance Policy). Ambac Assurance will make such payments to the Insurance Trustee on the later of the date on which such principal and/or interest becomes Due for Payment or within one business day following the date on which Ambac Assurance shall have received notice of Nonpayment from the Trustee/Paying Agent/Bond Registrar. The insurance will extend for the term of the Obligations and, once issued, cannot be canceled by Ambac Assurance.

The Financial Guaranty Insurance Policy will insure payment only on stated maturity dates and on mandatory sinking fund installment dates, in the case of principal, and on stated dates for payment, in the case of interest. If the Obligations become subject to mandatory redemption and insufficient funds are available for redemption of all outstanding Obligations, Ambac Assurance will remain obligated to pay the principal of and interest on outstanding Obligations on the originally scheduled interest and principal payment dates, including mandatory sinking fund redemption dates. In the event of any acceleration of the principal of the Obligations, the insured payments will be made at such times and in such amounts as would have been made had there not been an acceleration, except to the extent that Ambac Assurance elects, in its sole discretion, to pay all or a portion of the accelerated principal and interest accrued thereon to the date of acceleration (to the extent unpaid by the Obligor). Upon payment of all such accelerated principal and interest accrued to the acceleration date, Ambac Assurance's obligations under the Financial Guaranty Insurance Policy shall be fully discharged.

In the event the Trustee/Paying Agent/Bond Registrar has notice that any payment of principal of or interest on an Obligation that has become Due for Payment and that is made to a holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from its registered owner pursuant to the United States Bankruptcy Code in accordance with a final, non-appealable order of a court of competent jurisdiction, such registered owner will be entitled to payment from Ambac Assurance to the extent of such recovery if sufficient funds are not otherwise available.

The Financial Guaranty Insurance Policy does **not** insure any risk other than Nonpayment (as set forth in the Financial Guaranty Insurance Policy). Specifically, the Financial Guaranty Insurance Policy does **not** cover:

1. payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity;
2. payment of any redemption, prepayment or acceleration premium; and
3. nonpayment of principal or interest caused by the insolvency or negligence of the Trustee, Paying Agent or Bond Registrar, if any.

If it becomes necessary to call upon the Financial Guaranty Insurance Policy, payment of principal requires surrender of the Obligations to the Insurance Trustee together with an appropriate instrument of assignment so as to permit ownership of such Obligations to be registered in the name of Ambac Assurance to the extent of the payment under the Financial Guaranty Insurance Policy. Payment of interest pursuant to the Financial Guaranty Insurance Policy requires proof of holder entitlement to interest payments and an appropriate assignment of the holder's right to payment to Ambac Assurance.

Upon payment of the insurance benefits, Ambac Assurance will become the owner of the Obligation, appurtenant coupon, if any, or right to payment of the principal of or interest on such Obligation and will be fully subrogated to the surrendering holder's rights to payment.

AMBAC ASSURANCE CORPORATION

Ambac Assurance is a Wisconsin-domiciled stock insurance corporation regulated by the Office of the Commissioner of Insurance of the State of Wisconsin, and is licensed to do business in 50 states, the District of Columbia, the Territory of Guam, the Commonwealth of Puerto Rico and the U.S. Virgin Islands, with admitted assets of approximately **\$10,015,000,000** (unaudited) and statutory capital of approximately **\$6,371,000,000** (unaudited) as of **December 31, 2006**. Statutory capital consists of Ambac Assurance's policyholders' surplus and statutory contingency reserve. Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc., Moody's Investors Service, Inc. and Fitch Ratings have each assigned a triple-A financial strength rating to Ambac Assurance.

Ambac Assurance has obtained a ruling from the Internal Revenue Service to the effect that the insuring of an obligation by Ambac Assurance will not affect the treatment for federal income tax purposes of interest on such obligation and that insurance proceeds representing maturing interest paid by Ambac Assurance under policy provisions substantially identical to those contained in the

Financial Guaranty Insurance Policy shall be treated for federal income tax purposes in the same manner as if such payments were made by the Obligor.

Ambac Assurance makes no representation regarding the Obligations or the advisability of investing in the Obligations and makes no representation regarding, nor has it participated in the preparation of, this Official Statement other than the information supplied by Ambac Assurance and presented under the heading "Insert Title of Bond Insurance Section".

Available Information

The parent company of Ambac Assurance, Ambac Financial Group, Inc. (the "Company"), is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and in accordance therewith files reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). These reports, proxy statements and other information can be read and copied at the SEC's public reference room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. The SEC maintains an internet site at <http://www.sec.gov> that contains reports, proxy and information statements and other information regarding companies that file electronically with the SEC, including the Company. These reports, proxy statements and other information can also be read at the offices of the New York Stock Exchange, Inc., 20 Broad Street, New York, New York 10005.

Copies of Ambac Assurance's financial statements prepared in accordance with statutory accounting standards are available from Ambac Assurance. The address of Ambac Assurance's administrative offices is One State Street Plaza, 19th Floor, New York, New York 10004, and its telephone number is (212) 668-0340.

Incorporation of Certain Documents by Reference

The following document filed by the Company with the SEC (File No. 1-10777) is incorporated by reference in this Official Statement:

The Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and filed on March 1, 2007.

All documents subsequently filed by the Company pursuant to the requirements of the Exchange Act after the date of this Official Statement will be available for inspection in the same manner as described above in "**Available Information**".

TAX INFORMATION

AD VALOREM TAX LAW . . . The appraisal of property within the City is the responsibility of the Dallas Central Appraisal District (the "Appraisal District"). Excluding agricultural and open-space land, which may be taxed on the basis of productive capacity, the Appraisal District is required under the Title I of the Texas Tax Code (referred to herein as 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 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. State law further limits the appraised value of a residence homestead for a tax year to an amount not to exceed the lesser of (1) the market value of the property, or (2) the sum of (a) 10% of the appraised value of the property for the last year in which the property was appraised for taxation times the number of years since the property was last appraised, plus (b) the appraised value of the property for the last year in which the property was appraised plus (c) the market value of all new improvements to the property. The value placed upon property within the Appraisal District is subject to review by an Appraisal Review Board, consisting of three members appointed by the Board of Directors of the Appraisal District. The Appraisal District is required to review the value of property within the Appraisal District at least every three years. The City may require annual review at its own expense, and is entitled to challenge the determination of appraised value of property within the City by petition filed with the Appraisal Review Board.

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

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

Under 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: (1) An exemption of not less than \$3,000 of the market value of the residence homestead of persons 65 years of age or older and the disabled from all ad valorem taxes thereafter levied by the political subdivision; (2) An exemption of up to 20% of the market value of residence homesteads. The minimum exemption under this provision is \$5,000.

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.

As of January 1, 2004, under Article VIII and State law, the governing body of a county, municipality or junior college district may provide for a freeze on total amount of ad valorem levied on the residence homestead of a disabled person or persons 65 years of age or older above the amount of tax imposed in the year such residence qualified for such exemption. Also, upon receipt of a petition signed by five percent of the registered voters of the county, municipality or junior college district, an election must be held to determine by majority vote whether to establish such a limitation on taxes paid on residence homesteads of persons 65 years of age or who are disabled. Upon providing for such exemption, the total amount of taxes imposed on such homestead cannot be increased except for maintenance, repairs or improvements required to comply with governmental requirements and such freeze is transferable to a different residence homestead and to the surviving spouse living in such homestead who is disabled or is at least 55 years of age. Once established such freeze cannot be repealed or rescinded.

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.

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 Sections 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, 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.

The City may create one or more tax increment financing districts ("TIF") within the City and freeze the taxable values of property in the TIF at the value at the time of its creation. Other overlapping taxing units levying taxes in the TIF may agree to contribute all or part of future ad valorem taxes levied and collected against the value of property in the TIF in excess of the "frozen values" to pay or finance the costs of certain public improvements in the TIF. Taxes levied by the City against the values of real property in the TIF in excess of the "frozen" value are not available for general city use but are restricted to paying or financing "project costs" within the TIF. The City also may enter into tax abatement agreements to encourage economic development. Under the agreements, a property owner agrees to construct certain improvements on its property. The City 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.

EFFECTIVE TAX RATE AND ROLLBACK TAX RATE . . . Section 26.05 of the Property Tax Code provides that the governing body of a taxing unit is required to adopt the annual tax rate for the unit before the later of September 30 or the 60th day after the date the certified appraisal roll is received by the taxing unit, and a failure to adopt a tax rate by such required date will result in the tax rate for the taxing unit for the tax year to be the lower of the effective tax rate calculated for that tax year or the tax rate adopted by the taxing unit for the preceding tax year. Furthermore, Section 26.05 provides the City Council may not adopt a tax rate that exceeds the lower of the rollback tax rate or the effective tax rate until two public hearings are held on the proposed tax rate following a notice of such public hearings (including the requirement that notice be posted on the City's website if the City owns, operates or controls an internet website and public notice be given by television if the City has free access to a television channel) and the City Council has otherwise complied with the legal requirements for the adoption of such tax rate. The tax rate consists of two components: (1) a rate for funding of maintenance and operation expenditures for the next year, and (2) a rate to fund debt service in the next year.

Under the Property Tax Code, the City must annually calculate and publicize its "effective tax rate" and "rollback tax rate". If the adopted tax rate exceeds the rollback tax rate the qualified voters of the City by petition may require that an election be held to determine whether or not to reduce the tax rate adopted for the current year to the rollback tax rate.

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

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

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

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

PROPERTY ASSESSMENT AND TAX PAYMENT . . . Property within the City is generally assessed as of January 1 of each year. Business inventory may, at the option of the taxpayer, be assessed as of September 1. Oil and gas reserves are assessed on the basis of a valuation process which uses an average of the daily price of oil and gas for the prior 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 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	Cumulative Interest	Total
February	6%	1%	7%
March	7	2	9
April	8	3	11
May	9	4	13
June	10	5	15
July	12	6	18

After July, penalty remains at 12%, and interest increases at the rate of 1% each month. In addition the taxing unit may contact with an attorney for the collection of delinquent taxes and the amount of compensation as set forth in such contract may not provide for a fee that exceeds 20% of the amount of delinquent tax, penalty, and interest collected. Under certain circumstances, taxes which become delinquent on the homestead of a taxpayer 65 years old or older incur a penalty of 8% per annum with no additional penalties or interest assessed. In general, property subject to the City's lien may be sold, in whole or in parcels, pursuant to court order to collect the amounts due. Federal law does not allow for the collection of penalty and interest against

an estate in bankruptcy. Federal bankruptcy law provides that an automatic stay of action by creditors and other entities, including governmental units, goes into effect with the filing of any petition in bankruptcy. The automatic stay prevents governmental units from foreclosing on property and prevents liens for post-petition taxes from attaching to property and obtaining secured creditor status unless, in either case, an order lifting the stay is obtained from the bankruptcy court. In many cases post-petition taxes are paid as an administrative expense of the estate in bankruptcy or by order of the bankruptcy court.

CITY APPLICATION OF TAX CODE . . . The City grants an exemption to the market value of the residence homestead of persons 65 years of age or older of \$30,000; the disabled are also granted an exemption of \$30,000.

The City has not granted any part of the additional exemption of up to 20% of the market value of residence homesteads; minimum exemption of \$5,000.

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

The City has not adopted the tax freeze for citizens who are disabled or are 65 years of age or older, which became a local option and subject to local referendum on January 1, 2004.

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

The City does not tax nonbusiness personal property. Dallas County collects taxes for the City.

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

The City does tax freeport property.

The City does collect the additional one-quarter cent sales tax for reduction of ad valorem taxes.

The City has adopted a tax abatement policy and currently grants abatements to four companies for 50% of the value of improvements for periods ranging from 5 to 10 years.

TABLE 1 - VALUATION, EXEMPTIONS AND GENERAL OBLIGATION DEBT

2006/07 Market Valuation Established by Dallas Central Appraisal District		\$ 1,663,734,690
Less Exemptions/Reductions at 100% Market Value:		
Over 65/Disabled Persons Exemptions	\$ 41,595,340	
Disabled Veterans Exemptions	1,909,236	
Freeport Exemption	18,878,955	
Capped Value Loss	5,180,038	
Pollution Control Exemption	436,151	
Abatements	6,180,383	
Agricultural and Other Exemptions	<u>38,487,644</u>	<u>112,667,747</u>
2006/07 Taxable Assessed Valuation		\$ 1,551,066,943
City Funded Debt Payable from Ad Valorem Taxes (as of 1-1-07) ⁽¹⁾		
General Obligation Bonds	\$ 15,095,000 ⁽²⁾	
Certificates of Obligation	2,910,000	
Trinity River Authority Contract Revenue Debt	1,000,000	
The Certificates	14,565,000	
The Bonds	<u>24,300,000</u>	
Funded Debt Payable from Ad Valorem Taxes		\$ 57,870,000
Less Self-Supporting Debt: ⁽³⁾		
Water and Sewer System General Obligation Debt	\$ 10,409,307 ⁽⁴⁾	
Stormwater System General Obligation Debt	650,000 ⁽⁵⁾	
Airport System General Obligation Debt	172,280 ⁽⁶⁾	
Economic Development Corporation General Obligation Debt	3,035,000 ⁽⁵⁾	
Recreational Development Corporation General Obligation Debt	11,075,000 ⁽⁶⁾	
Trinity River Authority Contract Revenue Debt	<u>1,000,000</u>	<u>26,341,587</u>
General Purpose Funded Debt Payable from Ad Valorem Taxes		\$ 31,528,414
Interest and Sinking Fund as of 1-1-07		\$ 165,018
Ratio Total Funded Debt to Taxable Assessed Valuation		3.73%
Ratio Net Funded Debt to Taxable Assessed Valuation		2.03%

2007 Estimated Population - 35,000
Per Capita Taxable Assessed Valuation - \$44,316
Per Capita Total Funded Debt - \$1,653
Per Capita Net Funded Debt - \$901

- (1) The above statement of indebtedness does not include currently outstanding \$735,000 Waterworks and Sewer System Revenue Bonds, as these bonds are payable solely from the net revenues of the Waterworks and Sewer System (the "System"), as defined in the ordinances authorizing the bonds.
- (2) Excludes the Refunded Bonds.
- (3) General obligation debt in the amounts shown for which repayment is provided from revenues of the respective revenue systems. The amount of self supporting debt is based on the percentages of revenue support as shown in Table 10. It is the City's current policy to provide these payments from respective system revenues. This policy is subject to change in the future. To the extent such policy is changed and such self-supporting debt is not paid from the respective system revenues, such debt will be paid from ad valorem taxes.
- (4) Includes a portion of the Bonds and Certificates.
- (5) Includes a portion of the Certificates.
- (6) Includes a portion of the Bonds.

TABLE 2 - TAXABLE ASSESSED VALUATIONS BY CATEGORY

Category	Taxable Appraised Value for Fiscal Year Ended September 30,					
	2007		2006		2005	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Real, Residential, Single-Family	\$ 955,596,970	57.44%	\$ 858,404,500	58.05%	\$ 767,615,380	56.36%
Real, Residential, Multi-Family	71,836,850	4.32%	71,632,880	4.84%	71,982,440	5.29%
Real, Vacant Lots/Tracts	62,744,480	3.77%	40,772,260	2.76%	36,041,310	2.65%
Real, Acreage (Land Only)	60,090,789	3.61%	43,825,128	2.96%	39,250,840	2.88%
Real, Farm and Ranch Improvements	8,174,461	0.49%	6,869,222	0.46%	7,511,330	0.55%
Real, Commercial	224,332,650	13.48%	201,270,070	13.61%	179,864,190	13.21%
Real, Industrial	16,842,450	1.01%	17,655,160	1.19%	17,931,750	1.32%
Oil, Gas and Mineral Reserves	-	0.00%	-	0.00%	-	0.00%
Real and Tangible Personal, Utilities	103,585,990	6.23%	89,064,210	6.02%	112,289,720	8.24%
Tangible Personal, Commercial	102,457,380	6.16%	97,211,300	6.57%	83,341,240	6.12%
Tangible Personal, Industrial	54,394,700	3.27%	49,548,240	3.35%	43,594,480	3.20%
Tangible Personal, Other	-	0.00%	-	0.00%	-	0.00%
Tangible Personal, Mobile Homes	2,070,190	0.12%	931,210	0.06%	874,810	0.06%
Special Inventory	1,607,780	0.10%	1,519,010	0.10%	1,643,540	0.12%
Total Appraised Value Before Exemptions	\$ 1,663,734,690	100.00%	\$ 1,478,703,190	100.00%	\$ 1,361,941,030	100.00%
Totally Exempt Property/Adjustments	-		-		-	
Total Exemptions/Reductions	(112,667,747)		(98,463,664)		(105,994,906)	
Taxable Assessed Value	\$ 1,551,066,943		\$ 1,380,239,526		\$ 1,255,946,124	

Category	Taxable Appraised Value for Fiscal Year Ended September 30,			
	2004		2003	
	Amount	% of Total	Amount	% of Total
Real, Residential, Single-Family	\$ 677,853,100	53.27%	\$ 591,801,570	51.38%
Real, Residential, Multi-Family	73,049,560	5.74%	65,924,770	5.72%
Real, Vacant Lots/Tracts	40,062,265	3.15%	32,349,070	2.81%
Real, Acreage (Land Only)	31,107,760	2.44%	40,427,810	3.51%
Real, Farm and Ranch Improvements	15,110,860	1.19%	7,167,310	0.62%
Real, Commercial	178,648,060	14.04%	175,292,820	15.22%
Real, Industrial	15,711,230	1.23%	14,991,770	1.30%
Real and Tangible Personal, Utilities	460	0.00%	460	0.00%
Real and Tangible Personal, Utilities	106,447,080	8.37%	92,472,990	8.03%
Tangible Personal, Commercial	88,324,260	6.94%	85,126,540	7.39%
Tangible Personal, Industrial	43,304,660	3.40%	43,987,090	3.82%
Tangible Personal, Other	279,860	0.02%	1,423,930	0.12%
Tangible Personal, Mobile Homes	981,910	0.08%	948,190	0.08%
	1,515,900	0.12%	-	0.00%
Total Appraised Value Before Exemptions	\$ 1,272,396,965	100.00%	\$ 1,151,914,320	100.00%
Adjustments	(38,190,540)		(36,444,920)	
Total Exemptions/Reductions	(109,091,331)		(88,107,650)	
Taxable Assessed Value	\$ 1,125,115,094		\$ 1,027,361,750	

NOTE: Valuations shown are certified taxable assessed values reported by the Dallas Central 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 GENERAL OBLIGATION DEBT HISTORY

Fiscal Year Ended 9/30	Estimated Population ⁽¹⁾	Taxable Assessed Valuation	Taxable Assessed Valuation Per Capita	Tax Debt Outstanding at End of Year	Ratio Tax Debt to Taxable Assessed Valuation	Funded Debt Per Capita
2003	26,796	\$ 1,027,361,750	\$ 38,340	\$ 30,280,000	2.95%	\$ 1,130
2004	28,700	1,125,115,094	39,203	28,955,000	2.57%	1,009
2005	30,000	1,255,946,124	41,865	27,655,000	2.20%	922
2006	33,550	1,380,239,526	41,140	26,915,000	1.95%	802
2007	35,000	1,551,066,943	44,316	56,635,000 ⁽²⁾	3.65%	1,618

(1) Source: North Central Texas Council of Governments.

(2) Projected, includes the Bonds and Certificate. Includes self-supporting debt. See Tables 1 and 10 herein and accompanying footnotes. Excludes the Refunded Bonds.

TABLE 4 - TAX RATE, LEVY AND COLLECTION HISTORY

Fiscal Year Ended 9/30	Tax Rate	Distribution		Tax Levy	% of Current Tax Collections to Tax Levy	% of Total Tax Collections to Tax Levy
		General Fund	Interest and Sinking Fund			
2003	\$ 0.6717	\$ 0.5468	\$ 0.1249	\$ 6,900,789	98.03%	102.61%
2004	0.6717	0.6276	0.0441	7,247,329	96.02%	100.88%
2005	0.6717	0.5830	0.0887	8,436,190	96.42%	101.43%
2006	0.6717	0.6055	0.0662	9,271,069	95.25%	99.36%
2007	0.6717	0.6091	0.0626	10,251,831	32.57%	34.19% ⁽¹⁾

(1) Collections through January 1, 2007.

TABLE 5 - TEN LARGEST TAXPAYERS

Name of Taxpayer	Nature of Property	2006/07 Taxable Assessed Valuation	% of Total Taxable Assessed Valuation
Southwestern Bell	Telephone Utility	\$ 51,145,324	3.30%
Texas Utilities Electric Co.	Electric Utility	48,472,059	3.13%
Brasscraft Manufacturing	Plumbing Products	13,807,932	0.89%
Swift Transporting Inc.	Transporting	12,370,750	0.80%
Ecanae LP	Real Estate	11,658,875	0.75%
Frankel, Edward B. Trustee	Real Estate	11,500,000	0.74%
Pleasant Run Courtyard	Apartments	11,500,000	0.74%
Brenntag Southwest, Inc.	Industrial Chemicals	10,542,840	0.68%
Wal Mart	Retail	10,450,000	0.67%
HD Development Prop LP	Retail Store	9,239,630	0.60%
		<u>\$ 190,687,410</u>	<u>12.29%</u>

GENERAL OBLIGATION DEBT LIMITATION . . . No general obligation debt limitation is imposed on the City under current State law or the City's Home Rule Charter (see "The Bonds and Certificates – Tax Rate Limitation").

TABLE 6 - TAX ADEQUACY ⁽¹⁾

2007 Principal and Interest Requirements	\$ 966,543
\$0.0630 Tax Rate at 99.00% Collection Produces	\$ 967,400
Average Annual Principal and Interest Requirements, 2007 - 2032	\$ 2,062,956
\$0.1344 Tax Rate at 99.00% Collection Produces	\$ 2,063,788
Maximum Principal and Interest Requirements, 2023	\$ 2,506,170
\$0.1633 Tax Rate at 99.00% Collection Produces	\$ 2,507,563

(1) Includes the Bonds and Certificates, less self-supporting debt. Excludes the Refunded Bonds.

TABLE 7 - ESTIMATED OVERLAPPING DEBT

Expenditures of the various taxing entities within the territory of the City are paid out of ad valorem taxes levied by such entities on properties within the City. Such entities are independent of the City and may incur borrowings to finance their expenditures. This statement of direct and estimated overlapping ad valorem tax bonds ("Tax Debt") was developed from information contained in "Texas Municipal Reports" published by the Municipal Advisory Council of Texas. Except for the amounts relating to the City, the City has not independently verified the accuracy or completeness of such information, and no person should rely upon such information as being accurate or complete. Furthermore, certain of the entities listed may have issued additional 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 City.

Taxing Jurisdiction	2006/07 Taxable Assessed Value	2006/07 Tax Rate	Total G.O. Debt	Estimated % Applicable	City's Overlapping G.O. Debt As of 1-1-07	Authorized But Unissued Debt as of 1/1/2007
City of Lancaster	\$ 1,551,066,943	\$ 0.6717	\$ 31,528,414 ⁽¹⁾	100.00%	\$ 31,528,414	\$ -
Lancaster Independent School District	1,505,507,570	1.7260	114,366,755	95.09%	108,751,348	-
Dallas County	146,317,744,795	0.2139	213,606,039	0.80%	1,708,848	6,200,000
Dallas County Community College	151,810,313,601	0.0810	100,380,000	0.80%	803,040	380,000,000
Dallas County Hospital District	146,317,744,795	0.2540	-	0.80%	-	-
Total Direct and Overlapping G.O. Debt					\$ 142,791,650	
Ratio of Direct and Overlapping G.O. Debt to Taxable Assessed Valuation					9.21%	
Per Capita Overlapping G.O. Debt					\$ 4,079.76	

(1) Includes the Bonds and Certificates, less self-supporting debt. Excludes Refunded Bonds.

TABLE 8 - PRO-FORMA GENERAL OBLIGATION DEBT SERVICE REQUIREMENTS

Fiscal Year Ended 9/30	Outstanding Debt ⁽¹⁾		The Bonds ⁽²⁾		The Certificates ⁽³⁾		Total Outstanding Debt	Less:	Less:	Less:	Less:	Less:	Total Debt Less Self-Supporting Requirements	% of Principal Retired
	Principal	Interest	Principal	Interest	Principal	Interest		W&S Self-Supporting Requirements ⁽⁴⁾	Stormwater Self-Supporting Requirements ⁽⁵⁾	EDC Self-Supporting Requirements ⁽⁵⁾	LRDC Self-Supporting Requirements	Airport Self-Supporting Requirements ⁽⁶⁾		
2007	\$ 1,235,000	\$ 970,460	\$ -	\$ -	\$ -	\$ -	\$ 2,205,460	\$ 834,832	\$ -	\$ -	\$ 397,846	\$ 6,238	\$ 966,543	
2008	1,190,000	718,146	120,000	1,577,444	200,000	866,131	4,671,721	1,375,207	47,926	227,004	906,373	14,268	2,100,943	
2009	810,000	680,480	645,000	1,097,484	420,000	597,810	4,250,774	1,315,415	51,013	226,550	906,958	17,218	1,733,620	
2010	845,000	650,064	745,000	1,069,684	430,000	580,810	4,320,558	1,302,644	50,013	227,250	906,350	16,818	1,817,483	
2011	875,000	616,854	845,000	1,037,884	450,000	563,210	4,387,948	1,308,223	49,013	227,750	909,299	16,418	1,877,245	15.22%
2012	680,000	587,033	885,000	1,003,284	515,000	543,910	4,214,226	1,082,723	48,013	228,050	906,140	16,018	1,933,283	
2013	715,000	561,056	970,000	966,184	555,000	522,510	4,289,750	1,086,423	47,013	228,150	916,645	15,618	1,995,902	
2014	745,000	533,387	1,050,000	920,534	600,000	499,410	4,348,331	1,085,748	50,913	228,050	920,310	15,168	2,048,143	
2015	775,000	504,035	1,135,000	865,909	530,000	476,810	4,286,754	938,448	49,713	227,750	917,398	19,543	2,133,903	
2016	925,000	469,963	1,245,000	806,409	550,000	455,210	4,451,581	1,039,723	48,513	227,250	917,685	18,793	2,199,618	35.74%
2017	1,110,000	428,010	1,210,000	745,034	570,000	432,810	4,495,854	1,017,720	47,313	226,550	916,179	11,644	2,276,449	
2018	1,165,000	380,224	1,325,000	681,659	595,000	409,510	4,556,393	1,015,594	46,113	230,550	918,031	11,702	2,334,403	
2019	1,220,000	328,980	650,000	635,534	620,000	385,210	3,839,724	219,901	49,813	229,250	927,706	11,323	2,401,731	
2020	1,270,000	274,290	725,000	607,581	645,000	359,507	3,881,378	220,456	48,391	227,647	925,139	11,345	2,448,400	
2021	1,325,000	215,768	800,000	576,128	665,000	332,488	3,914,383	220,111	46,947	225,738	925,170	11,337	2,485,080	59.75%
2022	1,390,000	154,125	850,000	541,565	700,000	303,898	3,939,588	219,856	50,375	228,406	928,325	11,309	2,501,317	
2023	1,460,000	90,000	885,000	504,696	735,000	273,404	3,948,100	225,848	48,675	230,544	925,188	11,676	2,506,170	
2024	1,270,000	28,575	925,000	462,765	765,000	241,529	3,692,869	224,151	46,975	227,363	925,363	11,595	2,257,422	
2025	-	-	975,000	415,265	800,000	207,773	2,398,038	167,281	50,141	228,734	-	-	1,951,881	
2026	-	-	1,025,000	365,265	835,000	172,007	2,397,272	165,609	48,172	229,547	-	-	1,953,944	81.55%
2027	-	-	1,075,000	312,765	875,000	134,601	2,397,366	168,609	51,094	229,922	-	-	1,947,741	
2028	-	-	1,130,000	259,900	455,000	104,995	1,949,895	-	-	-	-	-	1,949,895	
2029	-	-	1,185,000	206,655	480,000	83,490	1,955,145	-	-	-	-	-	1,955,145	
2030	-	-	1,240,000	150,880	500,000	60,950	1,951,830	-	-	-	-	-	1,951,830	
2031	-	-	1,300,000	92,460	525,000	37,375	1,954,835	-	-	-	-	-	1,954,835	96.70%
2032	-	-	1,360,000	31,280	550,000	12,650	1,953,930	-	-	-	-	-	1,953,930	100.00%
	<u>\$ 19,005,000</u>	<u>\$ 8,191,449</u>	<u>\$ 24,300,000</u>	<u>\$ 15,934,244</u>	<u>\$ 14,565,000</u>	<u>\$ 8,658,006</u>	<u>\$ 90,653,699</u>	<u>\$ 15,234,524</u>	<u>\$ 976,132</u>	<u>\$ 4,562,054</u>	<u>\$ 15,996,102</u>	<u>\$ 248,031</u>	<u>\$ 53,636,856</u>	

DEBT INFORMATION

- (1) "Outstanding Debt" does not include lease/purchase obligations, includes self-supporting debt. Excludes the Refunded Bonds.
- (2) Average life of the issue - 14.101 years. Interest on the Bonds has been calculated at the rates illustrated on the cover page hereof.
- (3) Average life of the issue - 13.772 years. Interest on the Certificates has been calculated at the rates illustrated on page 3 hereof
- (4) Includes a portion of the Bonds and Certificates.
- (5) Includes a portion of the Certificates.
- (6) Includes a portion of the Bonds.

TABLE 9 - INTEREST AND SINKING FUND BUDGET PROJECTION

Tax-Supported Debt Service Requirements, Fiscal Year Ending 9/30/07		\$ 966,543
Interest and Sinking Fund, 9/30/06	\$ 177,000	
Interest and Sinking Fund Tax Levy	962,794	
Estimated Investment Earnings	<u>10,000</u>	<u>1,149,794</u>
Estimated Balance, 9/30/07		\$ 183,251

TABLE 10 - COMPUTATION OF SELF-SUPPORTING DEBT

Revenue Available for Debt Service from Waterworks and Sewer System, Fiscal Year Ended 9-30-06	\$ 4,171,433
Less: Revenue Bonds Requirements, 2007 Fiscal Year	<u>104,475</u>
Balance Available for Other Purposes	\$ 4,066,958
System General Obligation Bond Requirements, 2007 Fiscal Year	<u>834,832</u>
Balance	\$ 3,232,126
Percentage of System General Obligation Bonds, Self-Supporting	100.00%
Revenue Available for Debt Service from Airport Fund, Fiscal Year Ended 9-30-06	\$ 142,715 ⁽¹⁾
Airport General Obligation Bond Requirements, 2007 Fiscal Year	<u>6,238</u>
Balance	\$ 136,477
Percentage of Airport General Obligation Bonds, Self-Supporting	100.00%
Fund Balances Available for Debt Service from LRDC, Fiscal Year Ended 9-30-06	\$ 3,086,342 ⁽²⁾
LRDC General Obligation Bond Requirements, 2008 Fiscal Year	<u>906,373</u> ⁽³⁾
Balance	\$ 2,179,970
Percentage of LRDC General Obligation Bonds, Self-Supporting	100.00%

(1) Includes transfer from airport operating fund.

(2) Represents the fund balance available to pay debt service on debt that is considered self-supported debt payable from the proceeds of the ½ cent sales and use tax levied on behalf of the Lancaster Recreational Development Corporation ("LRDC"). See Table 14 for a description of sales and use taxes.

(3) The City budgeted to the fiscal year end 2007 debt service requirements for the LRDC. It is anticipated that the LRDC will continue to make payments for debt service in fiscal year 2008.

TABLE 11 - AUTHORIZED BUT UNISSUED GENERAL OBLIGATION BONDS

Purpose	Date Authorized	Amount Authorized	Amount Heretofore Issued	Amount Being Issued	Unissued Balance
Public Safety Improvements	11/8/2005	\$ 13,100,000	\$ -	\$ 13,100,000	\$ -
Senior Citizen Center	11/8/2005	2,600,000	-	2,600,000	-
Fire Station	11/8/2005	<u>1,100,000</u>	-	<u>1,100,000</u>	-
		\$ 16,800,000	\$ -	\$ 16,800,000	\$ -

ANTICIPATED ISSUANCE OF GENERAL OBLIGATION DEBT . . . The City does not anticipate the issuance of additional general obligation debt within the next twelve months.

TABLE 12 - OTHER OBLIGATIONS

The City has a lease purchase agreement in the original principal amount of \$1,885,000, now outstanding in the principal amount of \$1,000,000 and due in monthly installments through March 1, 2011, at interest rates ranging from 4.35% - 5.00%. The City has a second lease purchase agreement in the original principal amount of \$717,492, now outstanding in the principal amount of \$167,275 and due in monthly installments through March 1, 2009, at interest rates ranging from 4.20% - 5.95% (see Appendix B, "Excerpts from the City's Annual Financial Report", page 35).

PENSION FUND . . . The City provides pension benefits for all of its full-time employees through the Texas Municipal Retirement System ("TMRS"), a State-wide administered pension plan. The City makes annual contributions to the plan equal to the amounts accrued for pension expense. The City's annual pension cost for fiscal year 2005 was \$1,315,139 (see Appendix B, "Excerpts from the City's Annual Financial Report", page 37).

The City is one of 774 municipalities having their benefit plan administered by TMRS. Each of the 774 municipalities have an annual individual actuarial valuation performed. As of December 31, 2004, the City had an unfunded actuarial accrued liability of \$6,607,949, or 64.7% of the City's annual covered payroll (see Appendix B, "Excerpts from the City's Annual Financial Report", page 42).

FINANCIAL INFORMATION

TABLE 13 - CHANGES IN NET ASSETS ⁽¹⁾

	Fiscal Year Ended September 30,			
	2006 ⁽²⁾	2005	2004	2003
<u>Revenues:</u>				
Program Revenues:				
Charges for Services	\$ 4,878,000	\$ 3,999,858	\$ 4,717,140	\$ 4,067,615
Operating Grants & Contributions	8,664,990	8,446,446	9,089,160	7,835,926
Capital Grants & Contributions	7,492,241	7,419,015	3,006,303	5,733,943
General Revenues:				
Taxes & Fees	14,648,706	13,181,344	11,901,736	11,285,821
Other	675,882	639,182	273,875	300,336
Total Revenues	<u>\$ 36,359,819</u>	<u>\$ 33,685,845</u>	<u>\$ 28,988,214</u>	<u>\$ 29,223,641</u>
<u>Expenses:</u>				
Program Expenses:				
General Government	\$ 3,161,510	\$ 3,217,556	\$ 2,284,857	\$ 1,746,530
Public Safety	11,195,259	11,165,686	10,225,692	9,569,667
Public Works	237,742	224,314	836,319	879,456
Community Development and Recreation	3,008,994	3,134,112	3,237,048	2,816,807
Community Services	12,006	11,023	16,053	130,639
Social and Welfare	7,887,551	8,162,741	8,286,134	7,124,781
Non Departmental	1,766,007	1,954,663	1,695,639	1,375,077
Interest and Fiscal Charges	346,888	349,191	377,322	297,241
Total Expenses	<u>\$ 27,615,957</u>	<u>\$ 28,219,286</u>	<u>\$ 26,959,064</u>	<u>\$ 23,940,198</u>
Increase (Decrease in Net Assets Before Transfers)	\$ 8,743,862	\$ 5,466,559	\$ 2,029,150	\$ 5,283,443
Transfers	872,212	460,012	734,219	669,394
Change in Net Assets	\$ 9,616,074	\$ 5,926,571	\$ 2,763,369	\$ 5,952,837
Net Assets - Beginning	59,398,617	53,472,046	50,708,677	44,755,840
Net Assets - Ending	<u>\$ 69,014,691</u>	<u>\$ 59,398,617 ⁽³⁾</u>	<u>\$ 53,472,046</u>	<u>\$ 50,708,677</u>

(1) Beginning with fiscal year ended September 30, 2003, the City implemented Government Accounting Standards Board Statement No. 34 ("GASB 34"). In accordance with GASB 34, the City's financial statements for the fiscal year ended September 30, 2005, which are attached hereto as Appendix B, include a management discussion and analysis of the operating results of such fiscal year. Reference is made to Appendix B for such information.

(2) Preliminary unaudited information provided by City Staff, subject to change.

(3) Approximately eighty four percent (84%) of total net assets represent resources that are subject to restrictions on how they may be used. The unrestricted sixteen percent (16%) is available to be used to meet the City's ongoing obligations to citizens and creditors (see Appendix B, "Excerpts from the City's Annual Financial Report", page 6).

TABLE 13A - GENERAL FUND REVENUES AND EXPENDITURES HISTORY

Revenues	Fiscal Year Ended September 30,				
	2006 ⁽¹⁾	2005	2004	2003	2002
Taxes and Fees	\$ 12,755,193	\$ 12,128,645	\$ 11,344,027	\$ 9,900,401	\$ 9,303,951
Licenses and Permits	1,116,470	1,034,360	1,093,896	1,240,337	791,124
Intergovernmental	70,582	105,565	780,291	841,777	304,867
Charges for Services	502,104	910,666	806,673	675,221	501,769
Fines and Forfeitures	1,646,572	1,582,851	1,553,561	1,228,941	768,461
Interest	147,247	143,569	68,022	84,222	132,092
Miscellaneous	285,955	551,304	290,774	376,530	259,944
Total Revenues	\$ 16,524,122	\$ 16,456,960	\$ 15,937,244	\$ 14,347,429	\$ 12,062,208
Expenditures					
General Government	\$ 1,755,852	\$ 1,819,146	\$ 1,586,656	\$ 1,287,538	\$ 1,182,543
Public Safety	10,388,966	10,146,958	8,759,453	8,296,300	7,791,052
Public Works	897,569	798,671	753,240	778,688	940,990
Cultural and Recreational	3,445,990	3,731,559	3,104,373	2,733,247	562,007
Community Service	12,075	11,023	16,053	376,217	1,199,493
Non Departmental	15,077	1,726,818	1,628,633	1,294,030	1,050,842
Total Expenditures	\$ 16,515,529	\$ 18,234,175	\$ 15,848,408	\$ 14,766,020	\$ 12,726,927
Excess (Deficiency) of Revenues Over Expenditures	\$ 8,593	\$ (1,777,215)	\$ 88,836	\$ (418,591)	\$ (664,719)
Transfers In	\$ 872,212	\$ 833,845	\$ 817,471	\$ 818,278	\$ 632,881
Transfers Out	(675,000)	-	(153,319)	(344,500)	(235,600)
Proceeds from Capital Lease	-	-	-	-	560,692
Transfer from Component Unit	-	-	-	-	27,294
Total Sources (Uses)	\$ 197,212	\$ 833,845	\$ 664,152	\$ 473,778	\$ 985,267
Net Increase (Decrease)	\$ 205,805	\$ (943,370)	\$ 752,988	\$ 55,187	\$ 320,548
Beginning Fund Balance	5,926,881	6,870,251	6,117,263	6,062,076	5,741,528
Prior Period Adjustments	-	-	-	-	-
Residual Equity Transfer	-	-	-	-	-
Ending Fund Balance	\$ 6,132,686	\$ 5,926,881	\$ 6,870,251	\$ 6,117,263	\$ 6,062,076

(1) Preliminary unaudited information provided by City Staff, subject to change.

TABLE 14 - MUNICIPAL SALES TAX HISTORY

In addition to the sales and use tax levied by the State of Texas, the City levies the following local sales and use taxes for the purposes described: (i) a one percent (1%) sales and use tax the proceeds of which are credited to the General Fund of the City and are not pledged to the payment of debt; (ii) a voter-authorized one-half of one percent (1/2 of 1%) sales and use tax collected on behalf of LRDC for park and recreational development; (iii) a voter-authorized one-quarter of one percent (1/4 of 1%) sales and use tax collected on behalf of Lancaster Economic Development Corporation ("LEDC") for economic development and which may be pledged to the payment of debt issued by the LEDC; and (iv) a voter-authorized one-quarter of one percent (1/4 of 1%) sales and use tax for property tax reduction. Collection and enforcement of the sales and use taxes are effected through the Comptroller of Public Accounts, State of Texas, who remits the proceeds of the tax, after deduction of a 2% service fee, to the City monthly.

DISTRIBUTION OF SALES AND USE TAXES

Property Tax Relief	0.25¢
Economic and Community Development	0.25¢
Recreational Development Corporation	0.50¢
City Sales & Use Tax	1.00¢
State Sales & Use Tax	<u>6.25¢</u>
Total	8.25¢

GENERAL FUND SALES AND USE TAX

Fiscal Year Ended 9/30	Total Collected	% of Ad Valorem Tax Levy	Equivalent of Ad Valorem Tax Rate	Per Capita
2002	\$ 2,266,213	34.37%	\$ 0.2309	\$ 86
2003	2,232,759	32.36%	0.2173	83
2004	2,241,529	30.93%	0.1992	78
2005	2,460,672	29.17%	0.1959	82
2006 ⁽¹⁾	2,903,018	31.31%	0.2103	87

(1) Unaudited, preliminary, subject to change.

ECONOMIC DEVELOPMENT, RECREATION DEVELOPMENT AND PROPERTY REDUCTION SALES AND USE TAXES

Fiscal Year Ended Collected	1/4% Economic Development Tax Collected	1/2% Recreational Development Tax Collected	1/4% Property Reduction Tax Collected
2002	\$ 566,553	\$ 1,133,107	\$ 566,553
2003	558,190	1,116,380	558,190
2004	560,382	1,120,765	560,382
2005	615,168	1,230,336	615,168
2006 ⁽¹⁾	725,754	1,451,509	725,754

(1) Unaudited, preliminary, subject to change.

FINANCIAL POLICIES

Basis of Accounting . . . The City's accounting records of the governmental fund revenues and expenditures are recognized on the modified accrual basis. Revenues are recognized in the accounting period in which they are available and measurable. Expenditures are recognized in the accounting period in which the fund liability occurred, if measurable, except for unmatured interest on general long-term debt.

Proprietary Fund revenues and expenses are recognized on the full accrual basis. Revenues are recognized in the accounting period in which they are earned and become measurable. Expenses are recognized in the accounting period in which they are incurred.

Fund Balances . . . It is the City's policy regarding the General Fund and Enterprise Funds that working capital resources should be maintained at a minimum of 15% of the Fund's operating expenditure budget. The City maintains its various debt service funds in accordance with the covenants of the bond ordinances.

Use of Bond Proceeds . . . The City's policy is to use bond proceeds for capital expenditures only. Such revenues are never to be used to fund normal City operations.

Budgetary Procedures . . . The City Charter establishes the fiscal year as the twelve-month period beginning each October 1. Each year between May and July, the City Manager analyzes, and then after review, submits a budget of estimated revenues and expenditures to the City Council. Subsequently, the City Council will hold work sessions to discuss and amend the budget to coincide with their direction of the City. Various public hearings may be held to comply with applicable law. The City Council will adopt a budget prior to September 30. If the Council fails to adopt a budget then the budget presented to the Council by the City Manager becomes the adopted budget.

During the fiscal year, budgetary control is maintained by the monthly review of departmental appropriation balances. Actual operations are compared to the amounts set forth in the budget. Departmental appropriations that have not been expended lapse at the end of the fiscal year. Therefore, funds that were budgeted and not used by the departments during the fiscal year are not available for their use unless appropriated in the ensuing fiscal year's budget.

INVESTMENTS

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

LEGAL INVESTMENTS . . . Under Texas law, the City 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 of Texas or its agencies and instrumentalities, (3) collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States, (4) other obligations, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, the State of Texas or the United States or their respective agencies and instrumentalities, (5) obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent, (6) bonds issued, assumed, or guaranteed by the State of Israel, (7) effective September 1, 2005, certificates of deposit (i) issued by a depository institution that has its main office or a branch office in the State of Texas, that are guaranteed or insured by the Federal Deposit Insurance Corporation or the National Credit Union Share Insurance Fund, or are secured as to principal by Bonds described in clauses (1) through (6) or in any other manner and amount provided by law for County deposits, or (ii) where; (a) the funds are invested by the County through a depository institution that has a main office or branch office in this state and that is selected by the County; (b) the depository institution selected by the County arranges for the deposit of funds in one or more federally insured depository institutions, wherever located; (c) the certificates of deposit are insured by the United States or an instrumentality of the United States; (d) the depository institution acts as a custodian for the County with respect to the certificates of deposit; and (e) at the same time that the certificates of deposit are issued, the depository institution selected by the County receives deposits from customers of other federally insured depository institutions, wherever located, that is equal to or greater than the funds invested by the County through the depository institution selected under clause (ii)(a) above, (8) fully collateralized repurchase agreements that have a defined termination date, are fully secured by obligations described in clause (1), and are placed through a primary government securities dealer or a financial institution doing business in the State of Texas, (9) bankers' acceptances with a stated maturity of 270 days or less from the date of its issuance, if the short-term obligations of the accepting bank or its parent are rated at least A-1 or P-1 or the equivalent by at least one nationally recognized credit rating agency, (10) commercial paper that is rated at least A-1 or P-1 or the equivalent by either (a) two nationally recognized credit rating agencies or (b) one nationally recognized credit rating agency if the paper is fully secured by an irrevocable letter of credit issued by a U.S. or state bank, (11) no-load money market mutual funds registered with and regulated by the Securities and Exchange Commission that have a dollar weighted average stated maturity of 90 days or less and include in their investment objectives the maintenance of a stable net asset value of \$1 for each share, (12) no-load mutual funds registered with the Securities and Exchange Commission that have an average weighted maturity of less than two years, invest exclusively in obligations described in the preceding clauses, and are continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than AAA or its equivalent, and (13) public funds investment pools that have an advisory board which includes participants in the pool and are continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than AAA or its equivalent or no lower than investment grade with a weighted average maturity no greater than 90 days. Texas law also permits the City to invest bond proceeds in a guaranteed investment contract, subject to limitations as set forth in the Public Funds Investment Act, Texas Government Code, Chapter 2256 (the "PFIA").

A political subdivision such as the City may enter into securities lending programs if (i) the securities loaned under the program are 100% collateralized, a loan made under the program allows for termination at any time and a loan made under the program is either secured by (a) obligations that are described in clauses (1) through (6) above, (b) irrevocable letters of credit issued by a state or national bank that is continuously rated by a nationally recognized investment rating firm at not less than A or its equivalent or (c)

cash invested in obligations described in clauses (1) through (6) above, clauses (10) through (12) above, or an authorized investment pool; (ii) securities held as collateral under a loan are pledged to the City, held in the City's name and deposited at the time the investment is made with the City or a third party designated by the City; (iii) a loan made under the program through either a primary government securities dealer or a financial institution doing business in the State of Texas; and (iv) the agreement to lend securities has a term of one year or less.

The City may invest in such obligations directly or through government investment pools that invest solely in such obligations provided that the pools are rated no lower than AAA or AAAM or an equivalent by at least one nationally recognized rating service or no lower than investment grade by at least one nationally recognized rating service and has or which has a weighted average maturity no greater than 90 days. The City is specifically prohibited from investing in (1) obligations whose payment represents the coupon payments on the outstanding principal balance of the underlying mortgage-backed security collateral and pays no principal (2) obligations whose payment represents the principal stream of cash flow from the underlying mortgage-backed security and bears no interest (3) collateralized mortgage obligations that have a stated final maturity of greater than 10 years and (4) collateralized mortgage obligations the interest rate of which is determined by an index that adjusts opposite to the changes in a market index.

INVESTMENT POLICIES . . . Under Texas law, the City is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity; that address investment diversification, yield, maturity, and the quality and capability of investment management; and that includes a list of authorized investments for City funds, maximum allowable stated maturity of any individual investment, and the maximum average dollar-weighted maturity allowed for pooled fund groups. All City funds must be invested consistent with a formally adopted "Investment Strategy Statement" that specifically addresses each fund's investment. Each Investment Strategy Statement will describe its objectives concerning: (1) suitability of investment type, (2) preservation and safety of principal, (3) liquidity, (4) marketability of each investment, (5) diversification of the portfolio, and (6) yield.

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

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

TABLE 15 - CURRENT INVESTMENTS

As of January 1, 2007, the City's investable funds were invested in the following categories:

<u>Description</u>	<u>Percent</u>	<u>Market Value</u>
TexPool	100.00%	\$ 19,308,278

TAX MATTERS

In the opinion of Andrews Kurth LLP, Texas, Special Tax Counsel, interest on the Obligations is (1) excludable under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), from gross income of the owners thereof for federal income tax purposes and (2) is not includable in the alternative minimum taxable income of individuals or corporations, except as described below.

The foregoing opinions of Special Tax Counsel are based on the Code and the regulations, rulings and court decisions thereunder in existence on the date of issue of the Obligations. Such authorities are subject to change and any such change could prospectively or retroactively result in the inclusion of the interest on the Obligations in gross income of the owners thereof or change the treatment of such interest for purposes of computing alternative minimum taxable income.

In rendering its opinions, Special Tax Counsel has assumed continuing compliance by the City with certain covenants of the Ordinances authorizing the issuance of the Obligations and has relied on representations by the City with respect to matters solely within the knowledge of the City, which Special Tax Counsel has not independently verified. The covenants and representations relate to, among other things, the use of Obligation proceeds and any facilities financed therewith, the source of repayment of the Obligations, the investment of Obligation proceeds and certain other amounts prior to expenditure, and requirements that excess arbitrage earned on the investment of Obligation proceeds and certain other amounts be paid periodically to the United States and that the City file an information report with the Internal Revenue Service (the "Service"). If the City should fail to comply with the covenants in the Ordinances, or if its representations relating to the Obligations that are contained in the Ordinances should be determined to be inaccurate or incomplete, interest on the Obligations could become taxable from the date of delivery of the Obligations, regardless of the date on which the event causing such taxability occurs.

Interest on all tax-exempt obligations, such as the Obligations, owned by a corporation (other than an S corporation, a regulated investment company, a real estate investment trust (REIT), a real estate mortgage investment conduit (REMIC) or a financial asset securitization investment trust (FASIT)) will be included in such corporation's adjusted current earnings for purposes of calculating such corporation's alternative minimum taxable income. A corporation's alternative minimum taxable income is the basis on which the alternative minimum tax imposed by the Code is computed.

Except as stated above, Special Tax Counsel will express no opinion as to any federal, state or local tax consequences resulting from the ownership of, receipt or accrual of interest on or acquisition or disposition of the Obligations.

Special Tax 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 City described above. No ruling has been sought from the Service with respect to the matters addressed in the opinion of Special Tax Counsel, and Special Tax Counsel's opinion is not binding on the Service. The Service has an ongoing program of auditing the tax-exempt status of the interest on municipal obligations. If an audit of the Obligations is commenced, under current procedures the Service is likely to treat the City as the "taxpayer," and the owners of the Obligations may 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 Obligations, the City may have different or conflicting interests from the owners of the Obligations. Public awareness of any future audit of the Obligations could adversely affect the value and liquidity of the Obligations during the pendency of the audit, regardless of its ultimate outcome.

Under the Code, taxpayers are required to provide information on their returns regarding the amount of tax-exempt interest, such as interest on the Obligations, received or accrued during the year.

Prospective purchasers of the Obligations should be aware that the ownership of tax-exempt obligations, such as the Obligations, may result in collateral federal income tax consequences to, among others, financial institutions, life insurance companies, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain S corporations with Subchapter C earnings and profits, individual recipients of Social Security or Railroad Retirement benefits, taxpayers who are deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, taxpayers owning an interest in a FASIT that holds tax-exempt obligations, and individuals otherwise eligible for the earned income tax credit. Such prospective purchasers should consult their tax advisors as to the consequences of investing in the Obligations.

If a tax-exempt obligation, such as the Obligations, was acquired at a "market discount" and if the fixed maturity of such obligation is equal to, or exceeds, one year from the date of issue, the Code provides ordinary income tax treatment of gain recognized upon the disposition of such "market discount bond." A "market discount bond" is one which is acquired by the holder at a purchase price which is less than the stated redemption price at maturity or, in the case of a bond issued at an original issue discount, the "revised issue price" (*i.e.*, a market discount). Such treatment applies to "market discount bonds" to the extent the gain from the disposition thereof exceeds the accrued market discount of such bonds unless a statutory *de minimis* rule applies. The "accrued market discount" is the amount which bears the same ratio to the market discount as the number of days during which the holder holds the obligation bears to the number of days between the acquisition date and the final maturity date. The applicability of the market discount rules may adversely affect the liquidity or secondary market price of the Obligations. Purchasers should consult their own tax advisors regarding the potential implications of market discount with respect to the Obligations.

FEDERAL INCOME TAX ACCOUNTING TREATMENT OF ORIGINAL ISSUE DISCOUNT AND PREMIUM OBLIGATIONS

DISCOUNT OBLIGATIONS . . . Some of the Obligations may be offered at initial offering prices which are less than the stated redemption prices at maturity of such Obligations. If the initial offering prices of the Obligations are lower than the stated redemption price payable at maturity, the Obligations of that maturity (the "Discount Obligations") will be considered to have "original issue discount" for federal income tax purposes. An initial owner who purchases a Discount Obligation in the initial public offering of the Obligation at such an initial offering price will acquire such Discount Obligation with original issue discount equal to the difference between (a) the stated redemption price payable at the maturity of such Discount Obligation and (b) the initial offering price to the public of such Discount Obligation. Under existing law, such original issue discount will be treated for federal income tax purposes as additional interest on an Obligation and such initial owner will be entitled to exclude from gross income for federal income tax purposes that portion of such original issue discount deemed to be earned (as discussed below) during the period while such Discount Obligation continues to be owned by such initial owner. Except as otherwise provided herein, the discussion regarding interest on the Obligations under the caption "TAX MATTERS" generally applies to original issue discount deemed to be earned on a Discount Obligations while held by an owner who has purchased such Obligations at the initial offering price in the initial public offering of the Obligations and that discussion should be considered in connection with this portion of the Official Statement.

In the event of a redemption, sale, or other taxable disposition of a Discount Obligation prior to its stated maturity, however, any amount realized by such initial owner in excess of the basis of such Discount Obligations in the hands of such owner (increased to reflect the portion of the original issue discount deemed to have been earned while such Discount Obligation continues to be held by such initial owner) will be includable in gross income for federal income tax purposes.

Because original issue discount on a Discount Obligation will be treated for federal income tax purposes as interest on an Obligation, such original issue discount must be taken into account for certain federal income tax purposes as it is deemed to be earned even though there will not be a corresponding cash payment. Corporations that purchase Discount Obligations must take into account original issue discount as it is deemed to be earned for purposes of determining alternative minimum tax. Other owners of a Discount Obligation may be required to take into account such original issue discount as it is deemed to be earned for purposes of determining certain collateral federal tax consequences of owning an Obligation. See "TAX MATTERS" for a discussion regarding the alternative minimum taxable income consequences for corporations and for a reference to collateral federal tax consequences for certain other owners.

The characterization of original issue discount as interest is for federal income tax purposes only and does not otherwise affect the rights or obligations of the owner of a Discount Obligation or of the City. The portion of the principal of a Discount Obligation representing original issue discount is payable upon the maturity or earlier redemption of such Obligation to the registered owner of the Discount Obligation at that time.

Under special tax accounting rules prescribed by existing law, a portion of the original issue discount on each Discount Obligation is deemed to be earned each day. The portion of the original issue discount deemed to be earned each day is determined under an actuarial method of accrual, using the yield to maturity as the constant interest rate and semi-annual compounding.

The federal income tax consequences of the purchase, ownership, redemption, sale or other disposition of Discount Obligation by an owner that did not purchase such Obligation in the initial public offering and at the initial offering price may be determined according to rules which differ from those described above. All prospective purchasers of Discount Obligation should consult their tax advisors with respect to the determination for federal, state and local income tax purposes of interest and original issue discount accrued upon redemption, sale or other disposition of such Discount Obligations and with respect to the federal, state, local and foreign tax consequences of the purchase, ownership, redemption, sale or other disposition of such Discount Obligations.

PREMIUM OBLIGATIONS . . . Some of the Obligations may be offered at initial offering prices which exceed the stated redemption prices payable at the maturity of such Obligations. If any of the Obligations of such maturities are sold to members of the public (which for this purpose excludes bond houses, brokers and similar persons or organizations acting in the capacity of wholesalers or underwriters) at such initial offering prices, each of the Obligations of such maturities ("Premium Obligations") will be considered for federal income tax purposes to have "bond premium" equal to the amount of such excess. The basis for federal income tax purposes of a Premium in the hands of an initial purchaser who purchases such Obligation in the initial offering must be reduced each year and upon the sale or other taxable disposition of the Obligation by the amount of amortizable bond premium. This reduction in basis will increase the amount of any gain (or decrease the amount of any loss) recognized for federal income tax purposes upon the sale or other taxable disposition of a Premium Obligation by the initial purchaser. Generally, no corresponding deduction is allowed for federal income tax purposes, for the reduction in basis resulting from amortizable bond premium. The amount of bond premium on a Premium Obligation which is amortizable each year (or shorter period in the event of a sale or disposition of a Premium Obligation) is determined under special tax accounting rules which use a constant yield throughout the term of the Premium Obligation based on the initial purchaser's original basis in such Obligation. The federal income tax consequences of the purchase, ownership, redemption, sale or other disposition by an owner of Obligations that are not purchased in the initial offering or which are purchased at an amount representing a price other than the initial offering prices for the Obligations of the same maturity may be determined according to rules which differ from those described above. Moreover, all prospective purchasers of Obligations should consult their tax advisors with respect to the federal, state, local and foreign tax consequences of the purchase, ownership, redemption, sale or other disposition of Premium Obligations.

CONTINUING DISCLOSURE OF INFORMATION

In each of the respective Ordinances, the City has made the following agreement for the benefit of the holders and beneficial owners of the Obligations. The City is required to observe the agreement for so long as it remains obligated to advance funds to pay the Obligations. Under the agreement, the City will be obligated to provide certain updated financial information and operating data annually, and timely notice of specified material events, to certain information vendors. This information will be available to securities brokers and others who subscribe to receive the information from the vendors.

ANNUAL REPORTS . . . The City will provide certain updated financial information and operating data to certain information vendors annually. The information to be updated includes all quantitative financial information and operating data with respect to the City of the general type included in this Official Statement under Tables numbered 1 through 6 and 8 through 15 and in Appendix B. The City will update and provide this information within six months after the end of each fiscal year ending in or after 2007. The City will provide the updated information to each nationally recognized municipal securities information repository ("NRMSIR") and to any state information depository ("SID") that is designated by the State of Texas and approved by the State of Texas and approved by the staff of the United States Securities and Exchange Commission (the "SEC").

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

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

The Municipal Advisory Council of Texas (the "MAC") has been designated by the State of Texas and approved by the SEC staff as a qualified SID. The address of the MAC is 600 West 8th Street, P.O. Box 2177, Austin, Texas 78768-2177, and its telephone number is 512/476-6947. The MAC has also received SEC approval to operate, and has begun to operate, a "central post office" for information filings made by municipal issuers, such as the City. A municipal issuer may submit its information filings with the central post office, which then transmits such information to the NRMSIRs and the appropriate SID for filing. This central post office can be accessed and utilized at www.DisclosureUSA.org ("DisclosureUSA"). The City may utilize DisclosureUSA for the filing of information relating to the Obligations, unless the SEC has withdrawn the interpretive advice stated in its letter to the MAC dated September 7, 2004.

MATERIAL EVENT NOTICES . . . The City will also provide timely notices of certain events to certain information vendors. The City will provide notice of any of the following events with respect to the Obligations, if such event is material to a decision to purchase or sell Obligations: (1) principal and interest payment delinquencies; (2) non-payment related defaults; (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 or events affecting the tax-exempt status of the Obligations; (7) modifications to rights of holders of the Obligations; (8) Obligation calls; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the Obligations; and (11) rating changes. In addition, the City will provide timely notice of any failure by the City to provide information, data, or financial statements in accordance with its agreement described above under "Annual Reports." The City will provide each notice described in this paragraph to the SID and to either each NRMSIR or the Municipal Securities Rulemaking Board ("MSRB").

AVAILABILITY OF INFORMATION FROM NRMSIRS AND SID . . . The City has agreed to provide the foregoing information only to NRMSIRs and the SID. The information will be available to holders of Obligations only if the holders comply with the procedures and pay the charges established by such information vendors or obtain the information through securities brokers who do so.

AMENDMENTS . . . The City may amend its continuing disclosure agreement from time to time to adapt to changed circumstances that arise from a change in legal requirements, a change in law, or a change in the identity, nature, status, or type of operations of the City, if (i) the agreement, as amended, would have permitted an underwriter to purchase or sell Obligations in the offering described herein in compliance with the Rule, taking into account any amendments or interpretations of the Rule to the date of such amendment, as well as such changed circumstances, and (ii) either (a) the holders of a majority in aggregate principal amount of the outstanding Obligations consent to the amendment or (b) any person unaffiliated with the City (such as nationally recognized bond counsel) determines that the amendment will not materially impair the interests of the holders and beneficial owners of the Obligations. The City may also amend or repeal the provisions of this continuing disclosure agreement if the SEC amends or repeals the applicable provisions of the Rule or a court of final jurisdiction enters judgment that such provisions of the Rule are invalid, but only if and to the extent that the provisions of this sentence would not prevent an underwriter from lawfully purchasing or selling Obligations in the primary offering of the Obligations. If the City so amends the agreement, it has agreed to include with the next financial information and operating data provided in accordance with its agreement described above under "Annual Reports" an explanation, in narrative form, of the reasons for the amendment and of the impact of any change in the type of financial information and operating data so provided.

COMPLIANCE WITH PRIOR UNDERTAKINGS . . . The City became obligated to file annual reports with the state information depository ("SID") and each nationally recognized municipal securities information repository ("NRMSIR") beginning in 1997. The City filed all of the required reports, but the financial statements for fiscal years 2003-2005 were filed late. The City has filed a notice of late filing, and the City and its financial advisor have implemented procedures to ensure timely filing in the future.

OTHER INFORMATION

RATINGS

The Bonds and Certificates have been rated "Aaa" by Moody's and "AAA" by S&P by virtue of a municipal bond insurance policy to be issued by AMBAC Assurance Corporation. The presently outstanding tax supported debt of the City is rated "A2" by Moody's and "A" by S&P. The City also has issues outstanding which are rated "Aaa" by Moody's and "AAA" by S&P through insurance by various commercial insurance companies. An explanation of the significance of such ratings may be obtained from the companies furnishing the ratings. The ratings reflect only the respective views of such organizations and the City 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 or both of such rating companies, if in the judgment of either or both 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 and Certificates.

LITIGATION

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

REGISTRATION AND QUALIFICATION OF BONDS AND CERTIFICATES FOR SALE

The sale of the Bonds and Certificates 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 and Certificates have not been qualified under the Securities Act of Texas in reliance upon various exemptions contained therein; nor have the Bonds or Certificates been qualified under the securities acts of any jurisdiction. The City assumes no responsibility for qualification of the Bonds or Certificates under the securities laws of any jurisdiction in which the Bonds and Certificates may be sold, assigned, pledged, hypothecated, or otherwise transferred. This disclaimer of responsibility for qualification for sale or other disposition of the Bonds and Certificates 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

The Obligations. Section 1201.041 of the Public Security Procedures Act (Chapter 1201, Texas Government Code) provides that the Obligations are negotiable instruments 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 prudence standard, the Obligations are legal investments for state banks, savings banks, trust companies with at least \$1 million of capital, and savings and loan associations.

The Certificates. Section 271.051, Texas Local Government Code, provides that the Certificates are legal and authorized investments for banks, savings banks, trust companies, building and loan associations, savings and loan associations, insurance companies, fiduciaries, trustees and guardians, and for the sinking funds of municipalities, school districts, and other political subdivisions or public agencies of the State of Texas. The Certificates are eligible to secure deposits of any public funds of the state, municipalities, school districts, and other political subdivisions of the state, and are legal security for those deposits to the extent of their market value.

General Considerations. For political subdivisions in Texas that have adopted investment policies and guidelines in accordance with the Public Funds Investment Act (V.T.C.A., Government Code, Chapter 2256), the Obligations may have to be assigned a rating of "A" or its equivalent as to investment quality by a national rating agency before such obligations are eligible investments for sinking funds and other public funds. The City has made no investigation of other laws, rules, regulations, or investment criteria which might apply to such institutions or entities or which might limit the suitability of the Obligations for any of the foregoing purposes or limit the authority of such institutions or entities to purchase or invest in the Obligations for such purposes. The City has made no review of laws in other states to determine whether the Obligations are legal investments for various institutions in those states.

LEGAL OPINIONS

The City will furnish complete transcripts of proceedings had incident to the authorization and issuance of the Obligations, including the unqualified approving legal opinions of the Attorney General of Texas approving the Initial Bond and Initial Certificate and to the effect that the Obligations are valid and legally binding obligations of the City, and based upon examination of such transcripts of proceedings, the approving legal opinion of Bond Counsel, to like effect. The City will also furnish an opinion of Special Tax Counsel to the effect that the interest on the Obligations will be excludable from gross income for federal income tax purposes under Section 103(a) of the Code, subject to the matters described under "Tax Matters" herein, including the alternative minimum tax on corporations. 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 captions "Plan of Financing" (exclusive of the information under the subcaption "Sources and Uses of Proceeds"), "The Bonds and Certificates" (exclusive of the information under the subcaptions "Book-Entry-Only System" and "Remedies"), and "Continuing Disclosure of Information" (exclusive of the information under the subsection "Compliance with Prior Undertakings") and the subcaptions "Legal Opinions" (except for the last two sentences of the first paragraph thereof), "Registration and Qualification of Bonds and Certificates for Sale" and "Legal Investments and Eligibility to Secure Public Funds in Texas" under the caption "Other Information" in the Official Statement and such firm is of the opinion that the information relating to the Obligations 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 Obligations, such information conforms to the respective Ordinances. The legal fees to be paid to Bond Counsel for services rendered in connection with the issuance of the Obligations is contingent on the sale and delivery of the Obligations. The legal opinions will accompany the Obligations deposited with DTC or will be printed on the Obligations in the event of the discontinuance of the Book-Entry-Only System. Certain legal matters will be passed upon for the Underwriters Fulbright & Jaworski L.L.P., Counsel to the Underwriters. The legal fee of such firm is contingent on the sale and delivery of the Obligations.

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

AUTHENTICITY OF FINANCIAL DATA AND OTHER INFORMATION

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

FINANCIAL ADVISOR

First Southwest Company is employed as Financial Advisor to the City in connection with the issuance of the Obligations. The Financial Advisor's fee for services rendered with respect to the sale of the Obligations is contingent upon the issuance and delivery of the Obligations. First Southwest Company, in its capacity as Financial Advisor, has relied on the opinions of Bond Counsel and Special Tax Counsel and has not verified and does not assume any responsibility for the information, covenants and representations contained in any of the legal documents with respect to the federal income tax status of the Obligations, or the possible impact of any present, pending or future actions taken by any legislative or judicial bodies.

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

VERIFICATION OF ARITHMETICAL AND MATHEMATICAL COMPUTATIONS

The arithmetical accuracy of certain computations included in the schedules provided by First Southwest Company on behalf of the City relating to (a) computation of forecasted receipts of principal and interest on the Federal Securities and the forecasted payments of principal and interest to redeem the Refunded Obligations and (b) computation of the yields of the Refunding Bonds and the restricted Federal Securities were verified by Grant Thornton LLP, certified public accountants. Such computations were based solely on assumptions and information supplied by First Southwest Company on behalf of the City. Grant Thornton LLP has restricted its procedures to verifying the arithmetical accuracy of certain computations and has not made any study or evaluation of the assumptions and information on which the computations are based and, accordingly, has not expressed an opinion on the data used, the reasonableness of the assumptions, or the achievability of the forecasted outcome. Such verification will be relied upon by Bond Counsel in rendering its opinions with respect to the exclusion from gross income of interest on the Bonds for federal income tax purposes and with respect to defeasance of the Refunded Bonds.

UNDERWRITING

The Underwriters have agreed, subject to certain conditions, to purchase the Bonds from the City, at an underwriting discount of \$143,596.50. The Underwriters have agreed, subject to certain conditions, to purchase the Certificates from the City, at an underwriting discount of \$87,027.95. The Underwriters will be obligated to purchase all of the respective Obligations if any respective Obligations are purchased. The Obligations to be offered to the public may be offered and sold to certain dealers (including the Underwriters and other dealers depositing Obligations into investment trusts) at prices lower than the public offering prices of such Obligations and such public offering prices may be changed, from time to time, by the Underwriters.

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

FORWARD-LOOKING STATEMENTS DISCLAIMER

The statements contained in this Official Statement, and in any other information provided by the City, that are not purely historical, are forward-looking statements, including statements regarding the City's expectations, hopes, intentions, or strategies regarding the future. Readers should not place undue reliance on forward-looking statements. All forward-looking statements included in this Official Statement are based on information available to the City on the date hereof, and the City assumes no obligation to update any such forward-looking statements. The City'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 City. 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 Ordinances authorizing the issuance of the Obligations approved the form and content of this Official Statement, and any addenda, supplement or amendment thereto, and authorized its further use in the reoffering of the Obligations by the Underwriters.

/s/ JOE TILLOTSON
Mayor
City of Lancaster, Texas

ATTEST:

/s/ DOLLE SHANE
City Secretary

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SCHEDULE OF REFUNDED OBLIGATIONS**General Obligation Refunding and Improvement Bonds, Series 1995**

<u>Original Dated Date</u>	<u>Maturity Date</u>	<u>Interest Rate</u>	<u>Principal Amount Outstanding</u>	<u>Principal Amount Refunded</u>
5/15/1995	2/15/2008	5.100%	\$ 85,000	\$ 85,000
	2/15/2009	5.200%	90,000	90,000
	2/15/2010	5.300%	95,000	95,000
	2/15/2011	5.400%	100,000	100,000
	2/15/2012	5.450%	105,000	105,000
	2/15/2013	5.500%	115,000	115,000
	2/15/2014	5.550%	120,000	120,000
	2/15/2015	5.600%	130,000	130,000
			<u>\$ 840,000</u>	<u>\$ 840,000</u>

The 2008 - 2015 maturities will be redeemed prior to original maturity on June 1, 2007 at par.

General Obligation Refunding and Improvement Bonds, Series 1996

<u>Original Dated Date</u>	<u>Maturity Date</u>	<u>Interest Rate</u>	<u>Principal Amount Outstanding</u>	<u>Principal Amount Refunded</u>
6/1/1996	2/15/2008	5.500%	\$ 100,000	\$ 100,000
	2/15/2009	5.500%	110,000	110,000
	2/15/2010	5.600%	115,000	115,000
	2/15/2011	5.650%	120,000	120,000
	2/15/2012	5.700%	130,000	130,000
	2/15/2013	5.750%	135,000	135,000
	2/15/2014	5.800%	145,000	145,000
	2/15/2015	5.850%	155,000	155,000
	2/15/2016	5.900%	165,000	165,000
			<u>\$ 1,175,000</u>	<u>\$ 1,175,000</u>

The 2008 - 2016 maturities will be redeemed prior to original maturity on June 1, 2007 at par.

General Obligation Bonds, Series 1998

<u>Original Dated Date</u>	<u>Maturity Date</u>	<u>Interest Rate</u>	<u>Principal Amount Outstanding</u>	<u>Principal Amount Refunded</u>
4/1/1998	2/15/2009	4.700%	\$ 440,000	\$ 440,000
	2/15/2010	4.700%	455,000	455,000
	2/15/2011	4.800%	485,000	485,000
	2/15/2012	4.900%	510,000	510,000
	2/15/2013	5.000%	535,000	535,000
	2/15/2014	5.000%	560,000	560,000
	2/15/2015	5.000%	590,000	590,000
	2/15/2018 ⁽¹⁾	5.000%	2,320,000	2,320,000
			<u>\$ 5,895,000</u>	<u>\$ 5,895,000</u>

The 2009 - 2018 maturities will be redeemed prior to original maturity on February 15, 2008 at par.

(1) The 2018 maturity is a term bond with scheduled annual mandatory sinking fund redemptions on February 15 of each year commencing February 15, 2016.

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APPENDIX A

GENERAL INFORMATION REGARDING THE CITY

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LOCATION . . . The City of Lancaster is a growing community located in south central Dallas County approximately twelve miles south of the downtown Dallas business district. The City is located near the major intersections of Interstate Highways 35, 635 and 45, providing ready access to all parts of the Dallas-Fort Worth Metroplex.

POPULATION . . . The City has grown steadily since the mid-1970's, when it was a small bedroom community.

Population history is as follows:

<u>Year</u>	<u>Population</u>	<u>Year</u>	<u>Population</u>
1970 Census	10,612	1994	22,300
1980 Census	14,807	1995	22,300
1982	15,700	1996	23,000
1983	16,200	1997	23,400
1984	17,700	1998	23,300
1985	18,750	1999	24,300
1986	20,750	2000 Census	25,894
1987	20,850	2001	26,350
1988	23,000	2002	26,400
1989	23,000	2003	26,796
1990 Census	22,117	2004	28,700
1991	22,189	2005	30,000
1992	22,877	2006	33,550
1993	22,877	2007	35,000

EDUCATION . . . Educational facilities are primarily provided by the Lancaster Independent School District. The District is comprised of a Developmental Center, five elementary, one intermediate, one junior high and one high school. All campuses in the District are accredited by the Southern Association of Colleges and Schools and the Texas Education Agency. The high school curriculum offers sound basics for college preparation with college credit available in senior-level honors courses and features a strong vocational training program. Lancaster boasts a student-to-computer ratio of four-to-one, the lowest in the Dallas area and one of the lowest nationwide. The District has been recognized nationally for its commitment to instructional technology.

Higher education facilities located within a 35-mile radius of the City include Southern Methodist University, the University of Texas at Arlington, Texas Christian University and Cedar Valley Junior College.

TRANSPORTATION . . . The City is bounded in the west by Interstate Highway 35 East, in the east by Interstate Highway 45, and in the north by Interstate Highway 635 South, and is traversed by State Highway 342. The City is served by the Lancaster Municipal Airport, M-K-T Railroad, Southern Pacific Railroad, two bus lines and five freight lines. The City is approximately 25 miles southeast of the Dallas-Fort Worth International Airport and 18 miles from Dallas Love Field.

RECREATION . . . Recreational facilities in the City are provided by four City parks covering 165 acres of land, one swimming pool, four lighted tennis courts, seven lighted ball diamonds, one youth center and several movie theaters. Country View Golf Course offers a 175-acre public golf course.

GROWTH INDICES

<u>Fiscal Year</u>	<u>Population</u>	<u>Building Permits⁽¹⁾</u>		<u>Water Customers</u>
		<u>Number</u>	<u>Value</u>	
2002	26,400	556	\$ 56,865,869	8,311
2003	28,700	744	131,531,322	8,425
2004	29,850	573	83,094,656	8,700
2005	31,044	507	74,120,638	8,923
2006	33,550	830	119,006,275	10,655

Sources: City of Lancaster, Planning Department.

ECONOMY . . . The City has eight major industrial or commercial sites totaling over 5,300 acres available for marketing to new business and industry with all utilities available. There are four industrial parks totaling over 300 acres with all utilities in place. Lancaster Municipal Airport has undergone major changes by adding to its capacity for general aviation and offering a natural opportunity for freight-related industries. Additions include a new 5,000 foot runway, taxiway, lighting and navigational directional beacon to existing facilities.

The City is primarily a suburban residential area with industry and manufacturing becoming increasingly important to the local economy.

Some of the primary employers in the City are listed below.

<u>Company</u>	<u>Type of Business</u>	<u>Estimated Number of Employees</u>
Lancaster Independent School District	Public education	689
Wal-Mart Stores, Inc.	Retail store	450
Brass Craft Western	Plumbing products	390
Medical Center at Lancaster	Medical facility	340
Oak Creek Homes	Manufactured housing production and distribution	280
City of Lancaster	Local government	263
Cedar Valley College	Education	225
Swift Transportation	Truckload Carrier	200
Lasco Bathware, Tomkins, Inc.	Fiberglass bath fixtures, tubs, shower stalls	200
AT&T Material Distribution Center	Telephone equipment, cables and supplies	200
WNA Comet South	Plastic food and beverage containers	185
Bentwood Companies	Wood kitchen and bathroom cabinets	185
Communications Test Designs, Inc.	Telecommunication repair and distribution	153
FFE Transportation Services	Trucking	150
TXU Electric Delivery	Transformer reconditioning and related services	135
Home Depot	Retail store	130
Consolidated Mail Outpatient Pharmacy	Pharmaceutical distribution	110
Continental Cabinets, Inc.	Cabinet components	106
LGS Technologies, Inc.	Gaskets, shims	100
Dart Transit	Transportation, general commodities	90
Amrep, Inc.	Chemicals and allied products	85
Swivl-Eze Marine	Boat hardware	65
Bilco Corporation	Residential and commercial brick	65

APPENDIX B

EXCERPTS FROM THE
CITY OF LANCASTER, TEXAS
ANNUAL FINANCIAL REPORT
For the Year Ended September 30, 2005

The information contained in this Appendix consists of excerpts from the City of Lancaster, Texas Annual Financial Report for the Year Ended September 30, 2005, and is not intended to be a complete statement of the City's financial condition. Reference is made to the complete Report for further information.

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**WEAVER
AND
TIDWELL**

L L P.

CERTIFIED PUBLIC
ACCOUNTANTS
AND CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

To Members of the City Council
and City Manager
City of Lancaster, Texas

We have audited the accompanying basic financial statements of the governmental activities, the business-type activities, the discretely presented component units, each major fund and the aggregate remaining fund information of the City of Lancaster, Texas (the "City") as of and for the year ended September 30, 2005, which collectively comprise the City's basic financial statements, as listed in the table of contents. These basic financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these basic financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards and *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 basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Lancaster, Texas at September 30, 2005, and the respective changes in financial position and cash flows, where applicable, thereof, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 16, 2007, on our consideration of the City's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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AN INDEPENDENT MEMBER OF
BAKER TILLY
INTERNATIONAL

The accompanying management's discussion and analysis, schedule of funding progress, and budgetary comparison schedules on pages 3 through 10 and 42, 43, and 44, respectively, are not a required part of the basic financial statements but are supplementary information required by the GASB. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The combining, individual non-major fund financial statements, and discretely presented component units listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements of the City. The combining and individual non-major and discretely presented component unit fund financial statements have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Weaver and Tidwell, L.L.P.

WEAVER AND TIDWELL, L.L.P.

Dallas, Texas
January 16, 2007

Management's Discussion and Analysis City of Lancaster, Texas September 30, 2005

The Management's Discussion and Analysis (MD&A) section presents a narrative overview and analysis of the financial activities of the City for the fiscal year ended September 30, 2005. We encourage readers to consider the information presented here in conjunction with the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The assets of the City exceeded its liabilities at the end of the fiscal year 2005, resulting in \$103,591,392 of net assets. Net assets associated with governmental activities are approximately \$59.3 million, or 57% of the total net assets of the City. Net assets associated with business-type activities are approximately \$44 million, or 43% of the total net assets of the City. The largest portion of net assets consists of investment in capital assets, net of related debt, which is \$86.3 million.
- Unrestricted net assets, which may be used to meet the City's future obligations, consist of \$16.6 million, or 16% of the City's total net assets. Unrestricted net assets for governmental activities are approximately \$4.0 million, or 7% of total net assets for governmental activities; unrestricted net assets for business activities are approximately \$12.6 million, or 20% of total net assets for business-type activities.
- As of the close of fiscal year 2005, the City of Lancaster's governmental funds reported a combined ending fund balance of \$5,231,033 a decrease of \$3,092,110 from the prior year.
- At the end of the current fiscal year, total fund balance for the general fund was \$5,926,881. This represents over 31% of general fund expenditures which exceeds the 15% required by the City's adopted fund balance policy. Of this amount, 97% is available for spending at the government's discretion (unreserved fund balance).
- The City's total capital assets net of accumulated depreciation increased by \$20.3 million which is primarily attributed to additions to the City's Governmental Funds and Water/Sewer Fund infrastructure.
- The City's long-term liabilities decreased \$967,076 due to scheduled repayment of existing debt.

OVERVIEW OF THE FINANCIAL STATEMENTS

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

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

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

The statement of activities presents information showing how the City's net assets changed during the most recent fiscal year. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods; for example uncollected taxes and earned, but not used, vacation leave.

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City include general administration, public safety, library, non departmental, human resources and finance. The business-type activities of the City include water and sewer, drainage systems, and airport operations.

The government-wide financial statements include the Economic Development Corporation and the Recreational Development Corporation as part of its reporting entity as discretely presented component units. Discrete presentation entails reporting component unit financial data in columns separate from the financial data of the primary government. The Lancaster Economic Development Corporation and the Lancaster Recreational Development Corporation are legally separate entities.

The government-wide financial statements can be found on pages 12 through 14 of this report.

Fund Financial Statements The fund financial statements provide detailed information about the most significant funds – not the City as a whole. Some funds are required to be established by state law and by bond covenants. However, the City Council establishes many other funds to help it control and manage money for particular purposes or to show that it is meeting legal responsibilities when using certain taxes, grants, or other money. The City's two kinds of funds – Governmental and Proprietary – utilize different accounting approaches.

Governmental Funds The majority of the City's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method identified as the modified accrual basis of accounting, which measures cash and all other financial assets that can be readily converted to cash. The governmental fund statements provide a detailed short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs.

By comparing information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements, readers may better understand the long-term impact of the government's near-term financing decisions. The relationships or differences between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is detailed in a reconciliation following the fund financial statements.

Information is presented separately in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures, and changes in fund balances for the General fund, Capital Project Fund, and HUD Fund, all of which are considered to be major funds. Data from the other governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of combining statements elsewhere in this report.

Proprietary Funds The City charges customers for the services it provides, whether to outside customers or to other units within the City. These services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Activities. In fact, the City's enterprise funds (a component of proprietary funds) are identical to the business-type activities that are reported in the governmental-wide statements but provide more detail and additional information, such as cash flows, for proprietary funds.

The City of Lancaster maintains an Enterprise Fund to account for water and sewer services provided to the City's retail and wholesale customers. All activities associated with providing such services are accounted for in this fund, including administration, operation, maintenance, debt service, capital improvements, billing and collection. The City's intent is that costs of providing the services to the general public on a continuing basis is financed through user charges in a manner similar to a private business enterprise.

The proprietary fund financial statements can be found on pages 21 through 40 of this report.

Notes to the Financial Statements The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 22 through 43 of this report.

Other Information In addition to the basic financial statement and accompanying notes, this report also presents certain required supplementary information concerning the City's progress in funding its obligations. Required supplementary information immediately follows the notes to the financial statement. Combining statements for non-major governmental funds and component unit fund financial statements follow the section of required supplementary information.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. As of September 30, 2005, the City of Lancaster assets exceeded its liabilities by \$103,591,392.

The largest portion of the City's net assets, 83.41%, reflects its investment in capital assets (e.g., land, building, equipment, improvements, construction in progress, and infrastructure), less any debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; consequently these assets are not available for future spending. Although the City's investments in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

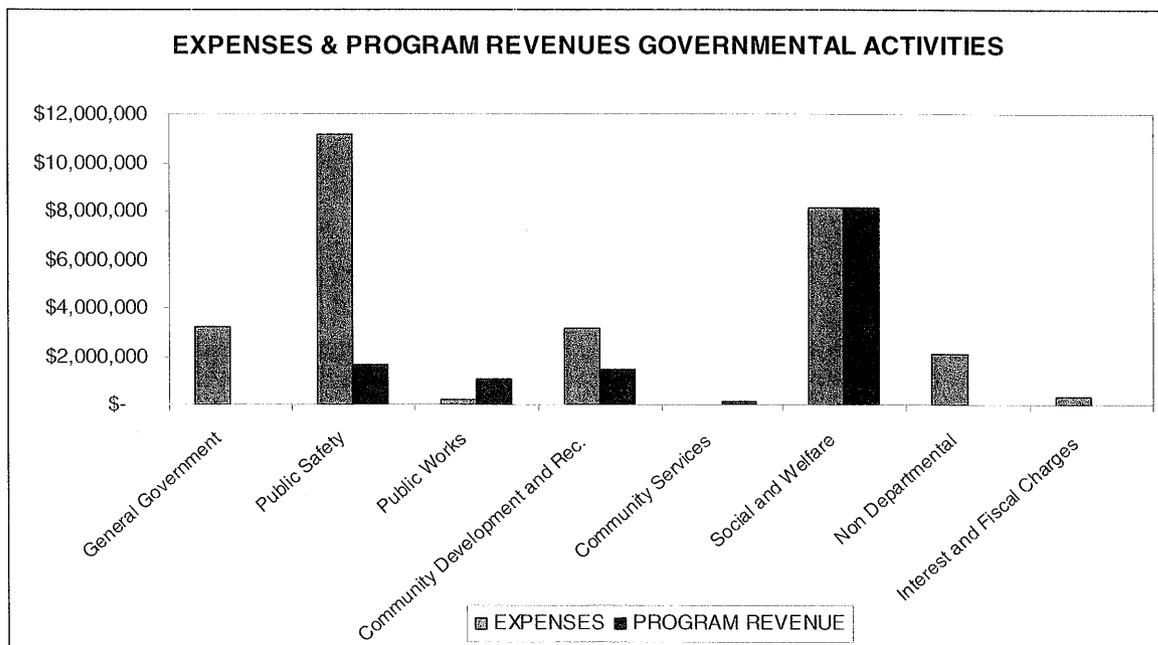
An additional portion of the City's net assets, .67%, represents resources that are subject to external restriction on how they may be used. The remaining balance of unrestricted net assets, \$16,606,148 or 15.58%, may be used to meet the City's ongoing obligations to citizens and creditors.

As of September 30, 2005, the City is able to report positive balances in all three categories of net assets, for the government as a whole, as well as for its separate governmental and business-type activities.

	<u>City of Lancaster Net Assets</u>					
	Governmental Activities 2005	Business-type Activities 2005	Total 2005	Governmental Activities 2004	Business-type Activities 2004	Total 2004
Current and Other Assets	\$ 8,870,107	\$ 14,223,654	\$ 23,093,761	\$ 12,965,154	\$ 13,779,452	\$ 23,093,761
Capital Assets	61,959,363	40,909,441	102,868,804	52,950,990	38,492,635	91,443,625
Total Assets	<u>\$ 70,829,470</u>	<u>\$ 55,133,095</u>	<u>\$ 125,962,565</u>	<u>\$ 65,916,144</u>	<u>\$ 52,272,087</u>	<u>\$ 118,188,231</u>
Long-Term Liabilities	\$ 8,235,864	\$ 9,371,785	\$ 17,607,649	\$ 8,230,546	\$ 9,958,249	\$ 18,188,795
Other Liabilities	3,194,989	1,652,633	4,847,622	4,213,552	2,307,593	6,521,145
Total Liabilities	<u>\$ 11,430,853</u>	<u>\$ 11,024,418</u>	<u>\$ 22,455,271</u>	<u>\$ 12,444,098</u>	<u>\$ 12,265,842</u>	<u>\$ 24,709,940</u>
Net Assets:						
Invested in Capital assets, net of Related Debt	\$ 55,125,562	\$ 31,169,977	\$ 86,295,539	\$ 46,133,536	\$ 30,857,399	\$ 76,990,935
Restricted	220,705	469,000	689,705	230,583	1,326,281	1,556,864
Unrestricted	4,052,350	12,553,798	16,606,148	7,107,927	7,822,565	14,930,492
Total Net Assets	<u>\$ 59,398,617</u>	<u>\$ 44,192,775</u>	<u>\$ 103,591,392</u>	<u>\$ 53,472,046</u>	<u>\$ 40,006,245</u>	<u>\$ 93,478,291</u>

Analysis of City's Operations The following table provides a summary of the City's operations for the year ended September 30, 2005. Overall, the City had an increase in net assets of \$9,788,850.

	Governmental Activities 2005	Business-type Activities 2005	Total 2005	Governmental Activities 2004	Business-type Activities 2004	Total 2005
REVENUES:						
Program Revenues:						
Charges for Services	\$ 3,999,858	\$ 8,438,791	\$ 12,438,649	\$ 4,717,140	\$ 8,524,433	\$ 13,241,573
Operating Grant & Contribution	8,446,446	209,269	8,655,715	9,089,160	29,530	9,118,690
Capital Grants & Contributions	7,419,015	3,497,830	10,916,845	3,006,303	1,035,645	4,041,948
General Revenue						
Taxes & Fees	13,181,344	-	13,181,344	11,901,736	-	11,901,736
Others	639,182	353,014	992,196	273,875	139,886	413,761
Total Revenues	33,685,845	12,498,904	46,184,749	28,988,214	9,729,494	38,717,708
Program Expenses						
General Government	3,217,556	-	3,217,556	2,284,857	-	2,284,857
Public Safety	11,165,686	-	11,165,686	10,225,692	-	10,225,692
Public Works	224,314	-	224,314	836,319	-	836,319
Community Development and Community Services	3,134,112	-	3,134,112	3,237,048	-	3,237,048
Social and Welfare	11,023	-	11,023	16,053	-	16,053
8,162,741	-	8,162,741	8,286,134	-	8,286,134	
Non Departmental	1,954,663	-	1,954,663	1,695,639	-	1,695,639
Interest and Fiscal Charges	349,191	-	349,191	377,322	-	377,322
Water & Sewer	-	7,705,662	7,705,662	-	7,675,269	7,675,269
Airport	-	298,127	298,127	-	305,881	305,881
Golf Course	-	172,824	172,824	-	166,563	166,563
Total Expenses	28,219,286	8,176,613	36,395,899	26,959,064	8,147,713	35,106,777
Increase (decrease in net assets before transfers)						
	5,466,559	4,322,291	9,788,850	2,029,150	1,581,781	3,610,931
Transfers	460,012	(460,012)	-	734,219	(734,219)	-
Changing in Net Assets	5,926,571	3,862,279	9,788,850	2,763,369	847,562	3,610,931
Net Assets - Beginning	53,472,046	40,006,245	93,478,291	50,708,677	39,158,683	89,867,360
Prior Period adjustment	-	324,251	324,251	-	-	-
Net Assets - Ending	\$ 59,398,617	\$ 44,192,775	\$ 103,591,392	\$ 53,472,046	\$ 40,006,245	\$ 93,478,291



Financial Analysis of the Government's Funds

Governmental Funds

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

As of the end of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$5,231,033, a decrease of \$3,092,110 (approximately 39%) in comparison with the prior year. Of this amount, 96% constitutes unreserved fund balance, which is available for spending at the City's discretion.

In the General Fund, the original budget projected a \$2,894,619 decrease in fund balance this fiscal year. There were no differences between the original and final amended budget. Key factors in this decline are as follows:

- A long range plan approved by City Council to reduce high fund balances to target amounts and to transfer amounts above the target to the Capital Project Fund in future years.
- A long range plan approved by City Council to gradually increase required services as revenues continued to increase.
- An increase in capital expenditures prior to implementing the annual capital improvement program.
- Also, this budget came together in an environment of declining local and national economic conditions while providing increased City services without a property tax increase.

The HUD Fund has a total fund balance of \$94,392, a decrease of \$79,331 from the prior year. The budget included a planned increase in housing assistance based on an increase in revenues from HUD and utilizing past excess revenues received from HUD that increased prior year fund balance.

Proprietary Funds The City's proprietary fund statements provide detail on the City's individual business-like activities and additionally report the financial results of the internal service funds which have been consolidated in the government-wide statements.

Unrestricted net assets of the proprietary funds at the end of the year were \$12,553,798. The total increase was \$4.1 million from the prior year. This increase is mostly related to an increase in Capital Assets and a decrease in long-term liabilities. Due to scheduled repayments of existing debt. Please note, there has been no rate increases by the City for water since 1998 and for sewer since 1993.

Capital Assets The City's investment in capital assets for its governmental and business-type activities as of September 30, 2005, amount to \$102,868,804 (net of accumulated depreciation). This investment in capital assets includes land, building, park facilities, roads, bridges and water and sewer lines.

	Governmental Activities		Business-Type Activities		Totals	
	2004	2005	2004	2005	2004	2005
Land	\$ 11,674,352	\$ 11,821,072	\$ 3,596,261	\$ 3,596,261	\$ 15,270,613	\$ 15,417,333
Buildings	4,808,692	4,797,506	4,658,605	3,753,530	9,467,297	8,551,036
Equipment	9,633,762	11,392,217	1,739,716	2,037,829	11,373,478	13,430,046
Construction in Progress	3,173,699	5,741,883	12,994,777	531,986	16,168,476	6,273,869
Other Structures	-	-	30,664,115	47,815,796	30,664,115	47,815,796
Park Improvements	1,623,024	1,623,024	3,093,109	3,093,109	4,716,133	4,716,133
Streets and Bridges	51,587,063	56,519,677	-	-	51,587,063	56,519,677
Drainage	1,683,845	3,999,333	-	-	1,683,845	3,999,333
Runways & taxiways	-	-	2,264,101	2,264,101	2,264,101	2,264,101
Depreciations	(31,233,447)	(33,935,349)	(20,518,049)	(22,183,171)	(51,751,496)	(56,118,520)
Total	\$ 52,950,990	\$ 61,959,363	\$ 38,492,635	\$ 40,909,441	\$ 91,443,625	\$ 102,868,804

Long-term Debt At the end of the current fiscal year, the City had total bonds outstanding of \$15,749,999 excluding Components Units. Of this amount \$6,817,225 is tax supported debt. The remainder of the City's debt represents bonds secured solely by specified revenue sources (i.e., revenue bonds).

	Governmental Activities		Business-Type Activities		Totals	
	2004	2005	2004	2005	2004	2005
General Obligation Bonds	\$ 4,460,063	\$ 3,792,225	\$ 8,494,936	\$ 8,137,774	\$ 12,954,999	\$ 11,929,999
Certificates of Obligation	3,135,000	3,025,000	-	-	3,135,000	3,025,000
Revenue Bonds	-	-	855,000	795,000	855,000	795,000
Capital Leases	260,361	214,275	1,335,000	1,170,000	1,595,361	1,384,275
Total	\$ 7,855,424	\$ 7,031,500	\$ 10,684,936	\$ 10,102,774	\$ 18,540,360	\$ 17,134,274

The City's total debt decreased by \$1,406,086 during the current fiscal year. The key factor in this decrease was the due to scheduled repayment of existing debt.

- o The City has an A2 rating from Moody's Investors Service and an A rating from Standard and Poor's.

On May 9, 2005, the City Council approved a Reimbursement Resolution to fund amounts previously advanced for certain expenditures, including preliminary expenditures, for the acquisition, design and construction of certain capital projects and to finance these eligible projects by the issuance of certificates of obligations.

Pursuant to this resolution the City Council preliminarily authorizes financing for the eligible projects. The Council expects that the financing for the projects will not exceed the maximum aggregate principal amount of \$15,682,661.

Economic Factor and Next Year's Budgets and Rates

In the fiscal year 2005-06 budget, general fund revenues are budgeted to increase by 9.48% from the 2004-05 budget year. This increase is mostly attributed to property taxes, which benefited from increases in assessed valuations. The City's total tax base increased by \$128 million of which 67% of this increase was in new growth. Based on the Certified Tax Roll, the City's tax base increased to \$1.364 billion (from \$1.237 billion). New construction increased from \$83 million to \$86 million or 2.819%. Certified assessed valuations increased 10% over the preceding year while the City tax rate was set at the same rate for the six year in a row, \$0.6717 per \$100 of valuation

Property taxes make up about 49% of budgeted revenues and sales tax make up about 18.7% of budgeted revenues. Several new developments will have a very positive effect in 2006.

One very important component of the General Fund budget is to ensure that our compensation structure is aligned with our overall objective to improve organization performance and service delivery. The city set out to address issues of competitiveness in recruiting and retaining employees in order to allow for more cost effective service delivery, by developing a more effective and more qualified workforce. On April 1, 2005, the City implemented a step system, with nine steps per pay grade and all employees were placed on the nearest higher step. The compensation program is based on an incremental approach. This approach will be successful if the City continues to grow.

The adopted budget maintained the step system with an overall market adjustment for the non-uniformed employees of 3% on October 1, 2005. Additionally, on April 1, 2006 the City will continue in its second year of the step system that allows employees to advance in the payroll system based on performance. The total estimated cost relating to the market adjustment and the step plan is approximately \$520,000.

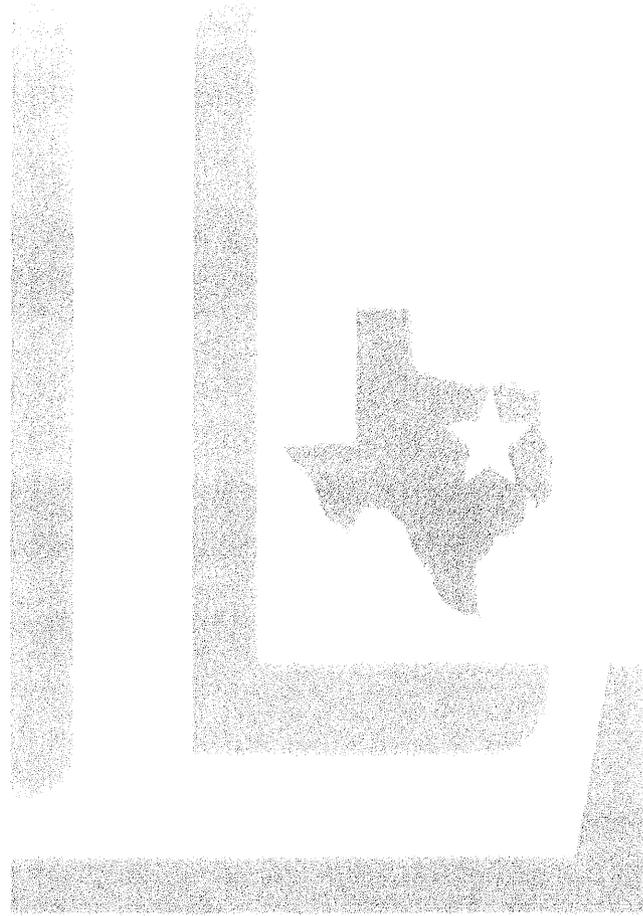
The adopted budget continues the practice of setting aside a reserve equal to 15 percent of the General Fund operating budget to ensure the City can provide basic services in the event of major emergencies.

Request for Information

For additional information please contact Maria Joyner at 972-218-1333 Finance Department, City of Lancaster, Texas, P.O. BOX 940 Lancaster, TX 75146 Email mjoyner@lancaster-tx.com.

BASIC FINANCIAL STATEMENTS

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Lancaster

**CITY OF LANCASTER
STATEMENT OF NET ASSETS
SEPTEMBER 30, 2005**

	Primary Government			Component Units	
	Governmental Activities	Business-type Activities	Total	Lancaster Economic Corporation	Lancaster Recreational Corporation
ASSETS					
Cash and Cash Equivalents	\$ 1,518,605	\$ -	\$ 1,518,605	\$ 163,342	\$ 48,710
Investments	4,951,274	10,895,452	15,846,726	1,155,579	2,891,261
Receivables (net of allowance)					
Delinquent Taxes	836,847	-	836,847	-	-
Accounts	406,247	913,462	1,319,709	-	-
Sales Tax	596,631	-	596,631	119,326	238,653
Fines	488,101	-	488,101	-	-
Miscellaneous	-	-	-	-	484
Internal Balances	(135,669)	135,669	-	-	-
Due from other governments	22,320	-	22,320	-	-
Prepaid Items	41,580	400	41,980	-	-
Inventory	27,309	-	27,309	-	-
Debt Issue Costs	116,862	244,442	361,304	-	290,930
Restricted Assets:					
Cash and Cash Equivalents	-	1,558,904	1,558,904	-	-
Investments	-	475,325	475,325	-	-
Capital Assets:					
Land and Construction in Progress	17,562,955	4,128,247	21,691,202	1,331,165	989,118
Other Capital Assets, Net of Accumulated Depreciation	44,396,408	36,781,194	81,177,602	-	16,842,815
Total Assets and Other Debits	70,829,470	55,133,095	125,962,565	2,769,412	21,301,971
LIABILITIES AND NET ASSETS					
Liabilities:					
Accounts and Contracts Payable	1,297,955	443,392	1,741,347	3,232	4,723
Accrued Liabilities	534,198	90,613	624,811	8,127	1,034
Accrued Interest	38,546	61,962	100,508	-	57,750
Deposits	293,769	405,026	698,795	-	-
Deferred Revenue	71,089	-	71,089	-	-
Noncurrent liabilities:					
Due within one year	959,432	651,640	1,611,072	-	-
Due in more than one year	8,235,864	9,371,785	17,607,649	-	10,490,575
Total Liabilities	11,430,853	11,024,418	22,455,271	11,359	10,554,082
Net Assets:					
Invested in Capital Assets, Net of Related Debt	55,125,562	31,169,977	86,295,539	1,331,165	7,644,097
Restricted for Debt Service	220,705	469,000	689,705	-	140,064
Unrestricted	4,052,350	12,553,798	16,606,148	1,426,888	2,963,728
Total Net Assets	\$ 59,398,617	\$ 44,192,775	\$ 103,591,392	\$ 2,758,053	\$ 10,747,889

The Notes to Financial Statements are an integral part of these statements.

**CITY OF LANCASTER
STATEMENT OF ACTIVITIES
SEPTEMBER 30, 2005**

Functions/Programs	Expenses	Program Revenues	
		Charges for Services	Operating Grants and Contributions
Primary government:			
Governmental Activities:			
General Government	\$ 3,217,556	\$ -	\$ -
Public Safety	11,165,686	1,635,711	28,144
Public Works	224,314	795,537	265,449
Community Development and Recreatic	3,134,112	1,434,639	14,257
Community Services	11,023	133,971	-
Social and Welfare	8,162,741	-	8,138,596
Non-departmental	1,954,663	-	-
Interest and fiscal charges	349,191	-	-
Total governmental activities	28,219,286	3,999,858	8,446,446
Business-type activities:			
Water & Sewer	7,705,662	8,250,721	-
Airport	298,127	129,722	209,269
Golf Course	172,824	58,348	-
Total business-type activities	8,176,613	8,438,791	209,269
Total primary government	\$ 36,395,899	\$ 12,438,649	\$ 8,655,715
Component units:			
Lancaster Economic Corporation	\$ 844,444	\$ -	\$ -
Lancaster Recreational Corporation	1,967,057	-	255,000
	\$ 2,811,501	\$ -	\$ 255,000

GENERAL REVENUES:

Taxes:
Property Taxes
Sales Taxes
Franchise Taxes
Other Local Taxes
Interest on Investments
Miscellaneous
Transfers

Total general revenues and transfers

Change in Net Assets

NET ASSETS, beginning of year

PRIOR PERIOD ADJUSTMENT

NET ASSETS, end of year

The Notes to Financial Statements are an integral part of these statements.

Capital Grants and Contributions	Changes in Net Assets				
	Primary Government			Component Units	
	Governmental Activities	Business - Type Activities	Total	Lancaster Economic Corporation	Lancaster Recreational Corporation
\$ -	\$ (3,217,556)	\$ -	\$ (3,217,556)	\$ -	\$ -
46,417	(9,455,414)	-	(9,455,414)	-	-
7,372,598	8,209,270	-	8,209,270	-	-
-	(1,685,216)	-	(1,685,216)	-	-
-	122,948	-	122,948	-	-
-	(24,145)	-	(24,145)	-	-
-	(1,954,663)	-	(1,954,663)	-	-
-	(349,191)	-	(349,191)	-	-
<u>7,419,015</u>	<u>(8,353,967)</u>	<u>-</u>	<u>(8,353,967)</u>	<u>-</u>	<u>-</u>
3,497,830	-	4,042,889	4,042,889	-	-
-	-	40,864	40,864	-	-
-	-	(114,476)	(114,476)	-	-
<u>3,497,830</u>	<u>-</u>	<u>3,969,277</u>	<u>3,969,277</u>	<u>-</u>	<u>-</u>
<u>\$ 10,916,845</u>	<u>\$ (8,353,967)</u>	<u>\$ 3,969,277</u>	<u>\$ (4,384,690)</u>	<u>\$ -</u>	<u>\$ -</u>
\$ -	\$ -	\$ -	\$ -	\$ (844,444)	\$ -
-	-	-	-	-	(1,712,057)
<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (844,444)</u>	<u>\$ (1,712,057)</u>
	8,606,773	-	8,606,773	-	-
	3,075,840	-	3,075,840	615,168	1,230,336
	1,465,012	-	1,465,012	-	-
	33,719	-	33,719	-	-
	190,921	347,978	538,899	47,690	75,630
	448,261	5,036	453,297	3,094	-
	460,012	(460,012)	-	-	-
	<u>14,280,538</u>	<u>(106,998)</u>	<u>14,173,540</u>	<u>665,952</u>	<u>1,305,966</u>
	5,926,571	3,862,279	9,788,850	(178,492)	(406,091)
	53,472,046	40,006,245	93,478,291	2,936,545	11,153,980
	-	324,251	324,251	-	-
	<u>\$ 59,398,617</u>	<u>\$ 44,192,775</u>	<u>\$ 103,591,392</u>	<u>\$ 2,758,053</u>	<u>\$ 10,747,889</u>

The Notes to Financial Statements are an integral part of these statements.

**CITY OF LANCASTER
BALANCE SHEET – GOVERNMENT FUNDS
SEPTEMBER 30, 2005**

ASSETS	General Fund	HUD Fund	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
Cash and cash equivalents	\$ 1,309,599	\$ 117,416	\$ -	\$ 91,590	\$ 1,518,605
Investments	3,385,036	25,322	873,710	667,206	4,951,274
Receivables (net of allowance for uncollectibles):					
Delinquent taxes	614,744	-	-	222,103	836,847
Accounts	247,719	-	-	158,528	406,247
Sales tax	596,631	-	-	-	596,631
Fines	488,101	-	-	-	488,101
Due from:					
Other funds	2,308,438	-	-	-	2,308,438
Other governments	-	21,521	-	799	22,320
Inventory, at cost	27,309	-	-	-	27,309
Prepaid Items	36,807	4,773	-	-	41,580
Total assets and other debits	\$ 9,014,384	\$ 169,032	\$ 873,710	\$ 1,140,226	\$ 11,197,352
LIABILITIES AND FUND BALANCES					
Liabilities:					
Accounts and contracts payable	\$ 895,114	\$ 74,640	\$ 268,972	\$ 59,229	\$ 1,297,955
Accrued liabilities	523,247	-	-	10,951	534,198
Deposits	293,769	-	-	-	293,769
Due to:					
Other funds	201,186	-	2,112,618	130,303	2,444,107
Deferred revenue	1,174,187	-	-	222,103	1,396,290
Total liabilities	3,087,503	74,640	2,381,590	422,586	5,966,319
Fund Balances (Deficit):					
Reserved for:					
Debt service	-	-	-	37,212	37,212
Inventory and prepaid items	64,116	-	-	-	64,116
Unreserved:					
Designated for equipment replacement	202,817	-	-	-	202,817
Unreserved and undesignated	5,659,948	94,392	(1,507,880)	680,428	4,926,888
Total fund balances (deficit)	5,926,881	94,392	(1,507,880)	717,640	5,231,033
Total liabilities and fund balances	\$ 9,014,384	\$ 169,032	\$ 873,710	\$ 1,140,226	\$ 11,197,352

The Notes to Financial Statements are an integral part of these statements.

**CITY OF LANCASTER
RECONCILIATION OF THE BALANCE SHEET OF GOVERNMENTAL
FUNDS TO THE STATEMENT OF NET ASSETS
AS OF SEPTEMBER 30, 2005**

Total fund balance-governmental funds.	\$ 5,231,033
Amounts reported for governmental activities in the statement of net assets are different because:	
Costs associated with the issuance of governmental long term debt are expenses when incurred in the fund statements and are capitalized and amortized over the life of the debt in the government-wide statements.	116,862
Capital assets used in governmental activities are not financial resources and therefore are not reported as assets in governmental funds. Capital assets are reported in the government-wide financial statements, net of accumulated depreciation.	61,959,363
Interest payable on long term debt does not require current financial resources, therefore interest payable is not reported as a liability in the governmental funds balance sheet.	(38,546)
Revenues earned but not available within sixty days of the year end are not recognized as revenue on the fund financial statements.	1,325,201
Long-term liabilities, including bonds, payable, are not due and payable in the current period and therefore are not reported in the fund financial statements. Long-term liabilities at year-end consist of:	
General obligation bonds	(3,792,225)
Certificates of obligation bonds	(3,025,000)
Capital lease	(214,275)
Compensated absences	(2,244,633)
Deferred loss on refunding	80,837
Total net assets - governmental activities	\$ 59,398,617

The Notes to Financial Statements are an integral part of these statements.

CITY OF LANCASTER
STATEMENTS OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES – GOVERNMENTAL FUNDS
YEAR ENDED SEPTEMBER 30, 2005

	General Fund	HUD Fund	Capital Projects Fund	Non-major Governmental Funds	Total Governmental Funds
REVENUES:					
Taxes and fees	\$ 12,128,645	\$ -	\$ -	\$ 1,916,995	\$ 14,045,640
Licenses and permits	1,034,360	-	-	-	1,034,360
Intergovernmental	105,565	8,065,958	-	-	8,171,523
Charges for services	910,666	-	-	-	910,666
Fines and forfeits	1,582,851	-	181,787	-	1,764,638
Interest	143,569	2,739	23,765	20,848	190,921
Miscellaneous	551,304	72,638	163,851	-	787,793
Total revenues	16,456,960	8,141,335	369,403	1,937,843	26,905,541
EXPENDITURES:					
Current:					
General government	1,819,146	-	-	478,031	2,297,177
Public safety	10,146,958	-	-	-	10,146,958
Public works	798,671	-	-	-	798,671
Community development and recreation	3,731,559	-	-	-	3,731,559
Community services	11,023	-	-	-	11,023
Non departmental	1,726,818	-	-	-	1,726,818
Social and welfare	-	8,162,741	-	-	8,162,741
Capital outlay	-	-	2,418,131	-	2,418,131
Debt service:					
Principal retirement	-	-	-	823,919	823,919
Interest and fiscal charges	-	-	-	340,666	340,666
Total expenditures	18,234,175	8,162,741	2,418,131	1,642,616	30,457,663
Excess (deficiency) of revenues over expenditures	(1,777,215)	(21,406)	(2,048,728)	295,227	(3,552,122)
Other financing sources (uses):					
Operating transfers in	833,845	-	-	-	833,845
Operating transfers out	-	(57,925)	(288,891)	(27,017)	(373,833)
Total other financing sources (uses)	833,845	(57,925)	(288,891)	(27,017)	460,012
Excess (deficiency) of revenues over expenditures and other sources (uses)	(943,370)	(79,331)	(2,337,619)	268,210	(3,092,110)
Fund balances, beginning of year	6,870,251	173,723	829,739	449,430	8,323,143
Fund balances (deficits), end of year	\$ 5,926,881	\$ 94,392	\$ (1,507,880)	\$ 717,640	\$ 5,231,033

The Notes to Financial Statements are an integral part of these statements.

**CITY OF LANCASTER
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES OF GOVERNMENTAL
FUNDS TO THE STATEMENT OF ACTIVITIES
YEAR ENDED SEPTEMBER 30, 2005**

Net change in fund balances- total governmental funds	\$ (3,092,110)
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets are allocated over their estimated useful lives and reported as depreciation expense. (Additions of \$4,541,064 net of disposals of \$21,600).	4,519,464
Governmental funds do not recognize assets contributed by developers. However, in the statement of activities the fair market value of those assets are recognized as revenue, then allocated over their estimated useful lives and reported as depreciation expense.	7,190,811
Depreciation expense on capital assets is reported in the government-wide statement of activities and changes in net assets, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in the governmental funds.	(2,701,902)
Current year principal payments of long-term liabilities are shown as expenditures in the fund financial statements, but shown as reductions in long-term liabilities in the government-wide financial statements as follows:	
General obligation bonds	\$ 777,838
Capital leases	<u>46,086</u>
	823,924
Current year changes in the long term liability for compensated absences do not require the use of current financial resources; therefore, are not reported as expenditures in governmental funds.	(394,579)
Current year changes in accrued interest payable do not require the use of current financial resources; therefore, are not reported as expenditures in governmental funds.	1,749
Certain revenues in the government-wide statement of activities that do not provide current financial resources are not reported as revenue in the governmental funds.	(410,255)
Amortization of bond issue costs and the deferred loss on refunding are not recognized on the fund financial statements.	<u>(10,531)</u>
Change in net assets of governmental activities	<u>\$ 5,926,571</u>

The Notes to Financial Statements are an integral part of these statements.

**CITY OF LANCASTER
STATEMENT OF NET ASSETS – PROPRIETARY FUNDS
SEPTEMBER 30, 2005**

ASSETS	<u>Water and Sewer</u>	<u>Non-major Enterprise Funds</u>	<u>Total Proprietary Funds</u>
Current assets:			
Cash and cash equivalents	\$ -	\$ -	\$ -
Investments	10,636,341	259,111	10,895,452
Receivables (net of allowance for uncollectibles):			
Accounts	548,929	15,060	563,989
Unbilled	349,473	-	349,473
Due from other funds	2,313,804	-	2,313,804
Prepaid items	400	-	400
Total current assets	<u>13,848,947</u>	<u>274,171</u>	<u>14,123,118</u>
Restricted assets:			
Cash	1,558,904	-	1,558,904
Investments	475,325	-	475,325
Total restricted assets	<u>2,034,229</u>	<u>-</u>	<u>2,034,229</u>
Deferred bond issuance costs	241,807	2,635	244,442
Capital assets:			
Non-depreciable	85,561	4,042,686	4,128,247
Depreciable (net)	33,920,910	2,860,284	36,781,194
Total assets	<u>50,131,454</u>	<u>7,179,776</u>	<u>57,311,230</u>
LIABILITIES			
Current Liabilities:			
Accounts and contracts payable	434,755	8,637	443,392
Accrued Liabilities	90,401	212	90,613
Accrued Interest	60,828	1,134	61,962
Due to other funds	1,953,783	224,352	2,178,135
Deposits	405,026	-	405,026
Total current liabilities	<u>2,944,793</u>	<u>234,335</u>	<u>3,179,128</u>
Non-current liabilities:			
Due within one year	651,640	-	651,640
Due in more than one year	9,199,251	172,534	9,371,785
Total non-current liabilities	<u>9,850,891</u>	<u>172,534</u>	<u>10,023,425</u>
Total liabilities	<u>12,795,684</u>	<u>406,869</u>	<u>13,202,553</u>
NET ASSETS			
Invested in capital assets, net of related debt	24,436,906	6,733,071	31,169,977
Restricted for revenue bond retirement	469,000	-	469,000
Unrestricted	12,429,864	123,934	12,553,798
Total net assets	<u>\$ 37,335,770</u>	<u>\$ 6,857,005</u>	<u>\$ 44,192,775</u>

The Notes to Financial Statements are an integral part of these statements.

**CITY OF LANCASTER
STATEMENT OF REVENUES, EXPENSES, AND
CHANGES IN NET ASSETS – PROPRIETARY FUNDS
YEAR ENDED SEPTEMBER 30, 2005**

	Water and Sewer Fund	Non-major Enterprise Funds	Total
OPERATING REVENUES:			
Charges for services	\$ 7,610,812	\$ 188,070	\$ 7,798,882
Miscellaneous	92,481	-	92,481
Total operating revenues	<u>7,703,293</u>	<u>188,070</u>	<u>7,891,363</u>
OPERATING EXPENSES:			
Personnel services	977,343	1,800	979,143
Maintenance	111,883	22,905	134,788
Purchase of water	1,184,632	-	1,184,632
Materials and supplies	136,902	174	137,076
Heat, light and power	122,242	8,113	130,355
Depreciation	1,357,003	342,280	1,699,283
Bad debts	89,136	-	89,136
Benefit payments	288,157	-	288,157
Sewage treatment	2,710,897	-	2,710,897
Special services	131,192	75,640	206,832
Miscellaneous	37,883	9,414	47,297
Insurance	20,000	1,505	21,505
Equipment rental	8,388	-	8,388
Total operating expenses	<u>7,175,658</u>	<u>461,831</u>	<u>7,637,489</u>
OPERATING INCOME (LOSS)	<u>527,635</u>	<u>(273,761)</u>	<u>253,874</u>
NONOPERATING REVENUES (EXPENSES)			
Interest revenue	341,310	6,667	347,977
Interest and fiscal charges	(530,004)	(9,120)	(539,124)
Intergovernmental	-	209,269	209,269
Contributions	3,497,830	-	3,497,830
Other nonoperating revenues	547,428	5,037	552,465
Total nonoperating revenues (expenses)	<u>3,856,564</u>	<u>211,853</u>	<u>4,068,417</u>
INCOME (LOSS) BEFORE TRANSFERS	<u>4,384,199</u>	<u>(61,908)</u>	<u>4,322,291</u>
TRANSFERS:			
Operating transfers in	288,891	-	288,891
Operating transfers out	(748,903)	-	(748,903)
Total transfers	<u>(460,012)</u>	<u>-</u>	<u>(460,012)</u>
NET INCOME (LOSS)	3,924,187	(61,908)	3,862,279
NET ASSETS, BEGINNING OF YEAR	33,087,332	6,918,913	40,006,245
PRIOR PERIOD ADJUSTMENT	324,251	-	324,251
NET ASSETS, END OF YEAR	<u>\$ 37,335,770</u>	<u>\$ 6,857,005</u>	<u>\$ 44,192,775</u>

The Notes to Financial Statements are an integral part of these statements.

**CITY OF LANCASTER
STATEMENT OF CASH FLOWS
ALL PROPRIETARY FUNDS
YEAR ENDED SEPTEMBER 30, 2005**

	Water and Sewer Fund	Non-major Enterprise Funds	Total
CASH FLOWS FROM OPERATING ACTIVITIES:			
Receipts from customers and users	\$ 7,915,770	\$ 215,870	\$ 8,131,640
Payments to other funds	(825,594)	-	(825,594)
Payments to employees	(1,259,346)	-	(1,259,346)
Payments to suppliers	(4,831,355)	(113,088)	(4,944,443)
Net cash provided by operating activities	<u>999,475</u>	<u>102,782</u>	<u>1,102,257</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:			
Acquisition and construction of capital assets	(395,607)	(9,222)	(404,829)
Principal payments on debt	(417,162)	-	(417,162)
Interest payments on debt	(461,850)	(9,120)	(470,970)
Principal payments on capital leases	(165,000)	-	(165,000)
Interest payments on capital leases	(51,570)	-	(51,570)
Impact fees collected	547,428	-	547,428
Net cash used in capital and related financing activities	<u>(943,761)</u>	<u>(18,342)</u>	<u>(962,103)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:			
Operating transfers in from other funds	288,891	-	288,891
Operating transfers out to other funds	(748,903)	-	(748,903)
Proceeds from other nonoperating revenue	-	5,037	5,037
Proceeds from intergovernmental grant	-	30,000	30,000
Net cash used in noncapital financing activities	<u>(460,012)</u>	<u>35,037</u>	<u>(424,975)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:			
Interest on investments	341,310	6,667	347,977
Net cash provided by investing activities	<u>341,310</u>	<u>6,667</u>	<u>347,977</u>
Net increase in cash and cash equivalents	(62,988)	126,144	63,156
Cash and cash equivalents, beginning of year	12,733,558	217,204	12,950,762
Cash and cash equivalents, end of year	<u>\$ 12,670,570</u>	<u>\$ 343,348</u>	<u>\$ 13,013,918</u>
RECONCILIATION OF CASH AND CASH EQUIVALENTS			
Unrestricted cash	\$ -	\$ -	\$ -
Unrestricted investments	10,636,341	259,111	10,895,452
Restricted cash	1,558,904	-	1,558,904
Restricted investments	475,325	-	475,325
Total Cash and cash equivalents	<u>\$ 12,670,570</u>	<u>\$ 259,111</u>	<u>\$ 12,929,681</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES:			
Operating income (loss)	\$ 527,635	\$ (273,761)	\$ 253,874
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:			
Depreciation and amortization	1,357,003	342,419	1,699,422
Provision for bad debts	34,579	-	34,579
Change in assets and liabilities:			
Increase in accounts receivable	160,328	27,800	188,128
Increase in due to/ from other funds	(825,594)	-	(825,594)
Decrease in prepaid items	117,754	-	117,754
Increase (decrease) in accounts and contracts payable	(428,029)	6,284	(421,745)
Increase in accrued liabilities	32,075	40	32,115
Increase in deposits	17,570	-	17,570
Increase (decrease) in compensated absences	6,154	-	6,154
Net cash provided by operating activities	<u>\$ 999,475</u>	<u>\$ 102,782</u>	<u>\$ 1,102,257</u>
SUPPLEMENTAL DISCLOSURE OF NONCASH TRANSACTIONS:			
Contribution of capital assets	<u>\$ 3,497,830</u>	<u>\$ 179,269</u>	<u>\$ 3,677,099</u>

The Notes to Combined Financial Statements are an integral part of these statements.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the City of Lancaster are presented in accordance with generally accepted accounting principles applicable to state and local governmental units as set forth by the Governmental Accounting Standards Board ("GASB"). The following is a summary of the more significant accounting policies:

A. Reporting Entity

The City of Lancaster ("City") was incorporated in 1853. The City operates as a home-rule city, under a Council-Manager form of government and provides the following services as authorized by its charter: public safety (police and fire), highways and streets, water and sewer utilities, sanitation, health and social services, parks and recreation, public improvements, airport, golf course, planning and zoning, and general administrative services.

The City of Lancaster's basic financial statements include the separate governmental entities that are controlled by or are dependent on the City. The determination to include separate governmental entities is based on the criteria of GASB Statement 14, "The Financial Reporting Entity" as amended by GASB 39, "Determining Whether Certain Organizations Are Component Units". GASB Statement 14 defines the reporting entity as the primary government and those component units for which the primary government is financially accountable. To be financially accountable, a voting majority of the component unit's board must be appointed by the primary government, and either (A) the primary government must be able to impose its will, or (B) the primary government may potentially benefit financially or be financially responsible for the component unit.

The Lancaster Economic Development Corporation ("Economic") and the Lancaster Recreational Development Corporation ("Recreational") are nonprofit industrial development corporations formed in July and October, 1995; respectively, under the Development Corporation Act of 1979. Both Economic and Recreational are organized exclusively for the purposes of benefiting and accomplishing public purposes, and to act on behalf of the City. This includes the construction and renovation of municipal buildings, the acquisition, improvement and operation of parks as well as other economic development purposes. The affairs of these corporations are managed by two separate boards of directors, which are appointed by the City Council. The City Council approves annual budgets and issuances of debt. The Lancaster Economic Development Corporation and the Lancaster Recreational Development Corporation have been discretely presented in the accompanying financial statements. Separate financial statements of the individual component units are not available.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

B. Basis of Presentation

Government-wide Financial Statements

The government-wide financial statements (the statement of net assets and the statement of activities) report information on all of the activities of the City. The effect of interfund activity, within the governmental and business-type activities columns, has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

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

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

Fund Financial Statements

The City segregates transactions related to certain functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. Separate statements are presented for governmental funds and proprietary funds. These statements present each major fund as a separate column on the fund financial statements; all non-major funds are aggregated and presented in a single column.

Governmental funds are those funds through which most governmental functions typically are financed. The measurement focus of governmental funds is on the sources, uses and balances of current financial resources. The City has presented the following major governmental funds:

General Fund - The General Fund is the main operating fund of the City. This fund is used to account for all financial resources not accounted for in other funds. All general tax revenues and other receipts that are not restricted by law or contractual agreement to some other fund are accounted for in this fund. General operating expenditures, fixed charges and capital improvement costs that are not paid through other funds are paid from the General Fund.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

B. Basis of Presentation – continued

Capital Projects Fund - The Capital Projects Fund is utilized to account for financial resources to be used for the acquisition or construction of major capital facilities.

HUD Fund - The HUD Fund is used to account for funds from grants received from the U.S. Department of Housing and Urban Development and transactions relating to the Lancaster Housing Agency.

Proprietary Funds are accounted for using the economic resources measurement focus and the accrual basis of accounting. The accounting objectives are determinations of net income, financial position and cash flow. All assets and liabilities are included on the Statement of Net Assets. The City has presented the following major proprietary fund:

Water and Sewer Fund - The Water and Sewer Fund is used to account for the acquisition, operation and maintenance of a municipal water and sewer utility, supported primarily by user charges to the public.

Proprietary funds distinguish operating revenues and expenses from non-operating 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. Operating expenses for the proprietary funds include the cost of personnel and contractual services, supplies and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

C. Measurement Focus

Measurement focus is the accounting convention, which determines which assets, and liabilities are included on the balance sheet of a fund type and whether a fund type's operating statement presents "financial flow" or capital maintenance information per fund.

The government-wide statements and fund financial statements for proprietary funds are reported using the economic resources measurement focus, which means all assets and liabilities (whether current or non-current) are included on the statement of net assets and the operating statements present increases (revenues) and decreases (expenses) in net total assets.

Governmental fund financial statements are reported using the current financial resources measurement focus, which means only current assets and current liabilities are generally included on their balance sheets.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

C. Measurement Focus

Their reported fund balance (net current assets) is considered a measure of "available spendable resources." Governmental fund operating statements present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets. Accordingly, they are said to present a summary of sources and uses of "available spendable resources" during a period.

Proprietary funds are accounted for on a "net income and capital maintenance" measurement focus. This means that all assets, liabilities, equity, revenues, expenses and transfers relating to the activity of a proprietary fund are accounted for through the proprietary fund. The measurement focus is upon the determination of net income, financial position and cash flows.

D. 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. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The government-wide statements and fund financial statements for proprietary funds are accounted for using the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, including unbilled water and sewer services which are accrued. Expenses are recognized at the time the liability is incurred.

Governmental fund financial statements are reported using the modified accrual basis for accounting. Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual; i.e., when they become both measurable and available. "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough, thereafter, to be used to pay liabilities of the current period.

Ad valorem, franchise and sales tax revenues recorded in the General Fund are considered to be susceptible-to-accrual. Licenses and permits, charges for services (except for sanitation services), fines and forfeits and rents and concessions are recorded as revenues when received in cash because they are generally not measurable until actually received. Investment earnings and intergovernmental revenue are recorded as earned since they are measurable and available.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

E. Cash Flows Statement

For purposes of the statement of cash flows, the City considers cash and cash equivalents to be all unrestricted cash and certificates of deposit with an original maturity date of three months or less.

F. Investments

Substantially all operating cash, deposits, and short-term investments are maintained in consolidated cash and investment accounts. Related interest income is allocated to the various funds based primarily on ownership by each fund of specific investments. Cash equivalents consist of highly liquid investments with original maturities of three months or less.

Investments in U.S. Treasury and agency obligations with maturities of one year or less when purchased are reported at amortized cost. Nonparticipating contracts are reported at cost. All other investments are reported at fair value.

State statutes authorize the City to invest in obligations of the U.S. Government or its agencies; obligations of the State of Texas or its agencies; and certain other obligations, repurchase agreements, money market mutual funds and certificates of deposits within established criterion.

G. Allowance for Uncollectible Accounts

An allowance for uncollectible taxes including penalties and interest and water and sewer billed receivables is provided based on an analysis of historical trends. The allowances for uncollectible taxes and water and sewer billings at September 30, 2005 and 2004 were \$137,128 and \$342,631, respectively.

H. Inventory

Inventories, which are recognized as expenditures as they are consumed, are stated at cost (first-in, first-out) for governmental funds. Inventories in the General Fund consist of expendable supplies.

I. Prepaid Items

Prepaid balances are for payments made by the City in the current year to provide services occurring in the subsequent year.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

J. Interfund Receivables and Payables

Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances".

K. Transactions Between Funds

Quasi-external transactions are accounted for as revenues, expenditures or expenses. Transactions that constitute reimbursements to a fund for expenditures/expenses initially made from it that are properly applicable to another fund, are recorded as expenditures/expenses in the reimbursing fund and as a reduction of expenditures/expenses in the fund reimbursed. All other interfund transactions, except quasi-external transactions and reimbursements, are recorded as transfers.

L. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets, are reported in the applicable governmental or business-type activities columns in the government-wide financial statements and in the fund financial statements for proprietary funds. All capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Donated assets are valued at fair market value on the date donated. Repairs and maintenance are recorded as expenses. Renewals and betterments are capitalized. Interest is capitalized on Proprietary Fund Type assets acquired with tax-exempt debt. The amount of interest to be capitalized is calculated by offsetting interest expenses incurred from the date of the borrowing unit until completion of the project with interest earned on invested proceeds over the same period.

Assets capitalized have a useful life of over one year. Depreciation is recorded on each class of depreciable property utilizing the straight-line method over the estimated useful lives of the assets. Estimated useful lives of major categories of property are

Plants and buildings	25 years
Other structures	10-50 years
Machinery and equipment	6-10 years

M. Accumulated Unpaid Vacations, Sick Leave and Other Employee Benefit Amounts

Sick leave is recorded when paid because employees are not compensated for unused sick leave. Vacation is earned in varying amounts up to a maximum of 20 days per year for employees with 10 or more years of service. Unused vacation leave carried forward from one year to the next is limited to 260 hours.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

M. Accumulated Unpaid Vacations, Sick Leave and Other Employee Benefit Amounts - continued

The liability for unused vested vacation leave as of September 30, 2005, is shown as a liability for compensated absences in the applicable governmental or business-type activities columns in the government-wide statements and in the fund financial statements for the proprietary funds. The amount to be paid from current available financial resources is not considered significant.

NOTE 2. CASH AND INVESTMENTS

At year-end, the carrying amount of the City's bank deposits was \$3,373,659 (composed of \$3,161,607 related to the primary government and \$212,052 related to discretely presented component units) and the bank balances were \$3,895,012. The bank balances on September 30, 2005 were entirely covered by federal depository insurance or by collateral held by the City's agent in the City's name.

Statutes authorize the City to invest in obligations of the U.S. Treasury and U.S. agencies and repurchase agreements and municipal pools. During the year ended September 30, 2005, the City did not own any types of securities other than those permitted by the statute.

Governmental investments are categorized as either (1) insured or registered for which securities are held by the City or its agent in the City's name, (2) uninsured and unregistered for which securities are held by the counterparty's trust department or agent in the City's name, or (3) uninsured and unregistered for which the securities are held by the counterparty or its trust department or agent, but not in the City's name.

During the year ended September 30, 2005 the City invested in the Texpool fund, which is an investment fund authorized by the Texas Legislature and administered by the Texas State Treasury. The Texas Treasury Safekeeping Trust Company is the trustee and is a limited purpose trust company authorized pursuant to Texas Government Code. The purpose of the Texpool fund is to allow for the pooling of public funds to provide a higher yield on the pooled investment than would be possible with the investment of the individual public entity's funds. Texpool investments are subject to the same investment policies maintained by the State Treasury for all state funds. The legislature has authorized only certain investment instruments for public funds, including repurchase agreements, U.S. Treasury bills and bonds, securities of other U.S. government agencies, commercial paper and other safe instruments. The investment in Texpool and any accrued interest may be redeemed at the City's discretion. TexPool operates in a manner consistent with the SEC's Rule 2a7 of the Investment Company Act of 1940. TexPool uses amortized cost rather than market value to report net assets to compute share prices. Accordingly the fair value of the position in TexPool is the same as the value of TexPool shares.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 2. CASH AND INVESTMENTS

Investments at year end are shown below:

	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Category</u>
Primary Government	<u>\$ 16,322,051</u>	<u>\$ 16,322,051</u>	N/A
Texpool	<u>16,322,051</u>	<u>16,322,051</u>	
Total Primary Government			
Component Units			
Texpool	<u>4,046,480</u>	<u>4,046,480</u>	N/A
Total Component Units	<u>4,046,480</u>	<u>4,046,480</u>	
Total	<u>\$ 20,368,891</u>	<u>\$ 20,368,891</u>	

NOTE 3. PROPERTY TAXES

Property taxes attach as an enforceable lien on property as of October 1. Taxes are levied on October 1 and are due and payable on or before January 31 of the following year. All unpaid taxes become delinquent February 1 of the following year. Tax collections for the year ended September 30, 2005, were 96.7% of the levy. Dallas County bills and collects property taxes for the City. Any uncollected property taxes at September 30 which are not expected to be collected within 60 days are recorded as taxes receivable and deferred revenues. Anticipated refunds of such taxes are recorded as liabilities and reductions of revenue when they are measurable and their validity seems certain.

The statutes of the State of Texas do not prescribe a legal debt limit, nor does the City's charter provide for a debt limit. However, Article XI, Section 5 of the Texas Constitution applicable to cities of more than 5,000 population limits ad valorem tax rate to \$2.50 per \$100 assessed valuation. However, as a city, which operates under a Home Rule Charter, Lancaster has a debt limit of \$1.50 per \$100 assessed valuation. For the year ended September 30, 2005, the City had a tax rate of \$.67170 per \$100 assessed valuation, of which \$.58301 was allocated for general government and \$.08869 was allocated for the payment of principal and interest on general obligation debt.

In Texas, countywide central appraisal districts are required to assess all property within the appraisal district on the basis of 100% of its appraised value and are prohibited from applying any assessment ratios. The value of property within the appraisal district must be reviewed every three years; however, the City may, at its own expense, require annual reviews of appraised values. The City may challenge appraised values established by the appraisal district through various appeals and, if necessary, legal action. Under this legislation, the City continues to set tax rates on City property.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 3. PROPERTY TAXES - CONTINUED

However, if the effective tax rate, excluding tax rates for bonds and other contractual obligations, adjusted for new improvements, exceeds the tax rate for the previous year by more than 8%, qualified voters of the City may petition for an election to determine whether to limit the tax rate to no more than 8% above the tax rate of the previous year. This legislation provides that, if approved by the qualified voters in the City, both the appraisal and collection functions may be placed with the appraisal district. In addition, the City may obtain approval from its governing body to place these functions with the appraisal district.

NOTE 4. INTERFUND TRANSACTIONS

At September 30, 2005, interfund balances and transactions, excluding discretely presented component units were as follows:

	Interfund Receivables	Interfund Payables	Transfers In	Transfers Out
General Fund	\$ 2,308,438	\$ 201,186	\$ 833,845	\$ -
HUD Special Revenue Fund	-	-	-	57,925
Capital Projects Fund	-	2,112,618	-	288,891
Other Governmental Funds	-	130,303	-	27,017
Water and Sewer Fund	2,313,804	1,953,783	288,891	748,903
Other Enterprise Funds	-	224,352	-	-
	<u>\$ 4,622,242</u>	<u>\$ 4,622,242</u>	<u>\$ 1,122,736</u>	<u>\$ 1,122,736</u>

The General Fund interfund receivable is for a temporary cash overdraft for the Other Governmental, Water and Sewer, and Other Enterprise Funds. The Water and Sewer Fund interfund receivable from the General Fund is for an interfund loan to purchase Bear Creek Nature Park approved by City Council and for a temporary loan made to provide financing resources for capital projects approved by City Council which will be repaid subject to the various loan terms. The Capital Projects Fund transfers out is for the purchase of Water/Sewer capital assets. The interfund transfer to the General Fund from the HUD Special Revenue, Other Governmental, and Water and Sewer Funds is for indirect services provided by central service departments accounted for in the General Fund. The interfund transfer from the HUD Special Revenue to the General Fund is for indirect services provided by central services departments accounted for in the General Fund. The interfund transfer to Other Enterprise Funds from Other Governmental Funds supports debt service expenditures for the Municipal Golf Course.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 5. FIXED ASSETS

Governmental Funds

Capital assets of the Governmental Funds are as follows:

	Balance September 30, 2004	Increases	Decreases	Adjustments/ Transfers	Balance September 30, 2005
Capital assets not being depreciated:					
Land	\$ 11,674,352	\$ 146,720	\$ -	\$ -	\$ 11,821,072
Construction in progress	3,173,699	2,568,184	-	-	5,741,883
Total capital assets not being depreciated	<u>\$ 14,848,051</u>	<u>\$ 2,714,904</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 17,562,955</u>
Capital assets being depreciated:					
Buildings	\$ 4,808,692	\$ 10,414	\$ (21,600)	\$ -	\$ 4,797,506
Streets	51,587,063	4,932,614	-	-	56,519,677
Park structures	1,623,024	-	-	-	1,623,024
Equipment and furniture	9,633,762	1,758,455	-	-	11,392,217
Drainage	1,683,845	2,315,488	-	-	3,999,333
Total capital assets being depreciated	69,336,386	9,016,971	(21,600)	-	78,331,757
Less accumulated depreciation	31,233,447	2,701,902	-	-	33,935,349
Total capital assets being depreciated, net	<u>\$ 38,102,939</u>	<u>\$ 6,315,069</u>	<u>\$ (21,600)</u>	<u>\$ -</u>	<u>\$ 44,396,408</u>

Enterprise Funds

Fixed assets of the Enterprise Funds are as follows:

	Balance September 30, 2004	Increases	Decreases	Adjustments/ Transfers	Balance September 30, 2005
Water and Sewer System:					
Capital assets not being depreciated					
Land	\$ 85,561	\$ -	\$ -	\$ -	\$ 85,561
Construction in progress	12,642,060	-	-	(12,642,060)	-
Total capital assets not being depreciated	<u>\$ 12,727,621</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (12,642,060)</u>	<u>\$ 85,561</u>
Capital assets being depreciated					
Plants and buildings	\$ 2,472,998	\$ -	\$ -	\$ -	\$ 2,472,998
Other structures	30,664,115	3,604,546	-	12,642,060	46,910,721
Machinery and equipment	1,039,438	288,891	-	-	1,328,329
Total capital assets being depreciated	34,176,551	3,893,437	-	12,642,060	50,712,048
Less accumulated depreciation	15,468,157	1,322,981	-	-	16,791,138
Total capital assets being depreciated, net	<u>\$ 18,708,394</u>	<u>\$ 2,570,456</u>	<u>\$ -</u>	<u>\$ 12,642,060</u>	<u>\$ 33,920,910</u>

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 5. FIXED ASSETS - CONTINUED

Enterprise Funds – continued

	Balance September 30, 2004	Increases	Decreases	Adjustments/ Transfers	Balance September 30, 2005
Regional Airport:					
Capital assets not being depreciated					
Land	\$ 3,161,146	\$ -	\$ -	\$ -	\$ 3,161,146
Construction in progress	352,717	179,269	-	-	531,986
Total capital assets not being depreciated	<u>\$ 3,513,863</u>	<u>\$ 179,269</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,693,132</u>
Capital assets being depreciated					
Runways and taxiways	\$ 2,264,101	\$ -	\$ -	\$ -	\$ 2,264,101
Buildings	1,280,532	-	-	-	1,280,532
Other equipment	143,425	-	-	-	143,425
Total capital assets being depreciated	3,688,058	-	-	-	3,688,058
Less accumulated depreciation	<u>3,195,350</u>	<u>176,385</u>	<u>-</u>	<u>-</u>	<u>3,371,735</u>
Total capital assets being depreciated, net	<u>\$ 492,708</u>	<u>\$ (176,385)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 316,323</u>
Municipal Golf Course:					
Capital assets not being depreciated					
Land	\$ 349,554	\$ -	\$ -	\$ -	\$ 349,554
Total capital assets not being depreciated	<u>\$ 349,554</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 349,554</u>
Capital assets being depreciated					
Plants and buildings	\$ 3,093,109	\$ -	\$ -	\$ -	\$ 3,093,109
Other structures	905,075	-	-	-	905,075
Machinery and equipment	556,853	9,222	-	-	566,075
Total capital assets being depreciated	4,555,037	9,222	-	-	4,564,259
Less accumulated depreciation	<u>1,854,542</u>	<u>165,756</u>	<u>-</u>	<u>-</u>	<u>2,020,298</u>
Total capital assets being depreciated, net	<u>\$ 2,700,495</u>	<u>\$ (156,534)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,543,961</u>

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 5. FIXED ASSETS - CONTINUED

Discretely Presented Component Units

Capital assets of the Lancaster Economic Development Corporation are as follows:

	Balance September 30, 2004	Increases	Decreases	Adjustments/ Transfers	Balance September 30, 2005
Capital assets not being depreciated					
Land	\$ 100,378	\$ -	\$ -	\$ -	\$ 100,378
Construction in progress	220,532	1,010,255	-	-	1,230,787
Total capital assets not being depreciated	<u>\$ 320,910</u>	<u>\$ 1,010,255</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,331,165</u>

Capital assets of the Lancaster Recreational Development Corporation are as follows:

	Balance September 30, 2004	Increases	Decreases	Adjustments/ Transfers	Balance September 30, 2005
Capital assets not being depreciated					
Land	\$ 989,118	\$ -	\$ -	\$ -	\$ 989,118
Total capital assets not being depreciated	<u>\$ 989,118</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 989,118</u>
Capital assets being depreciated					
Buildings	\$ 157,797,360	\$ -	\$ -	\$ -	\$ 157,797,360
Park structures	3,965,809	-	-	-	3,965,809
Equipment and furniture	379,259	-	-	-	379,259
Total capital assets being depreciated	162,142,428	-	-	-	162,142,428
Less accumulated depreciation	2,468,651	830,962	-	-	3,299,613
Total capital assets being depreciated, net	<u>\$ 159,673,777</u>	<u>\$ (830,962)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 158,842,815</u>

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

Governmental activities:

General and administrative	\$ 258,865
Public safety	2,022,382
Public works	97,074
Community development and recreation	242,686
Non-departmental	80,895
Total depreciation expense - governmental activities	<u>\$ 2,701,902</u>

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 6. LONG-TERM LIABILITIES

The following is a summary of changes in long-term liabilities:

	Balance October 1, 2004	Additions	Retirements	Balance September 30, 2005	Due Within One Year
Governmental activities					
General obligation bonds	\$ 4,460,063	\$ -	\$ (667,838)	\$ 3,792,225	\$ 72,360
Certificates of obligation	3,135,000	-	(110,000)	3,025,000	115,000
Deferred loss on refunding	(85,092)	-	4,255	(80,837)	-
Compensated absences	1,850,054	1,028,354	(633,775)	2,244,633	710,070
Capital leases	260,361	-	(46,086)	214,275	62,002
Total governmental activities	\$ 9,620,386	\$ 1,028,354	\$ (1,453,444)	\$ 9,195,296	\$ 959,432
Business-type activities					
General obligation bonds	\$ 8,494,936	\$ -	\$ (357,162)	\$ 8,137,774	\$ 382,640
Deferred loss on refunding	(152,890)	-	34,022	(118,868)	-
Revenue bonds	855,000	-	(60,000)	795,000	60,000
Compensated absences	33,365	39,196	(33,042)	39,519	39,000
Capital leases	1,335,000	-	(165,000)	1,170,000	170,000
Total business-type activities	\$ 10,565,411	\$ 39,196	\$ (581,182)	\$ 10,023,425	\$ 651,640
Discretely presented component units					
General obligation bonds	\$ 11,530,000	\$ -	\$ -	\$ 11,530,000	\$ -
Deferred loss on refunding	(1,088,921)	-	49,496	(1,039,425)	-
Total discretely presented component units	\$ 10,441,079	\$ -	\$ 49,496	\$ 10,490,575	\$ -

General long-term debt consists of capital leases, liabilities for accrued vacation leave, and general obligation bonds and certificates of obligation, which are direct obligations, issued on the full faith and credit of the City. Principal and interest payments on the general obligation bonds and certificates of obligation are secured by ad valorem taxes levied on all taxable property within the City and surplus revenues of the Water and Sewer Fund and Airport Fund. A portion of the general obligation bonds has been issued on behalf of the Water and Sewer Fund. Although these bonds are secured by the full faith and credit of the City and have no specific claim against Water and Sewer Fund assets, debt service requirements are provided by the Water and Sewer Fund. Accordingly, this debt is reflected as an obligation of the Water and Sewer Fund.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 6. LONG-TERM LIABILITIES - CONTINUED

General obligation bonds, revenue bonds, certificates of obligation and capital leases outstanding at September 30, 2005, consist of the following individual issues:

	<u>Governmental Activities</u>	<u>Water and Sewer</u>	<u>Airport</u>	<u>Total Primary Government</u>	<u>Discretely Presented Component Units</u>
<u>General Obligation Bonds</u>					
\$4,145,000 1995 General Obligation Refunding Bonds, due in annual installments through February 15, 2015, 3.90% - 5.60%	\$ 908,863	\$ 96,053	\$ -	\$ 1,004,916	\$ -
\$4,100,000 1996 General Obligation Refunding and Improvement Bonds, due in annual installments through August 15, 2016, 5.40% - 5.90%	661,831	414,342	98,910	1,175,083	-
\$8,070,000 1998 General Obligation bonds, due in annual installments through February 15, 2018, 4.60% - 6.50%	-	7,080,000	-	7,080,000	-
\$14,200,000 2002 General Obligation Refunding Bonds, due in annual installments through February 15, 2005, 3.00% - 4.50%	<u>2,221,531</u>	<u>371,189</u>	<u>77,280</u>	<u>2,670,000</u>	<u>11,530,000</u>
	<u>\$ 3,792,225</u>	<u>\$ 7,961,584</u>	<u>\$ 176,190</u>	<u>\$ 11,929,999</u>	<u>\$ 11,530,000</u>
<u>Revenue Bonds</u>					
\$2,905,000 1995 Waterworks and Sewer System Revenue Refunding and Improvement Bonds, due in annual installments through September 1, 2015, 3.90% - 5.60%	<u>\$ -</u>	<u>\$ 795,000</u>	<u>\$ -</u>	<u>\$ 795,000</u>	<u>\$ -</u>
<u>Certificates of Obligation</u>					
\$3,210,000 2003 Certificate of Obligation Bonds, due in annual installments through February 15, 2023, 3.25% - 4.50%	<u>\$ 3,025,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,025,000</u>	<u>\$ -</u>

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 6. LONG-TERM LIABILITIES - CONTINUED

	Governmental Activities	Water and Sewer	Total Primary Government
<u>Capital Leases</u>			
\$1,885,000 Lease Purchase Agreement, due in monthly installments through March 1, 2011, 4.35% - 5.00%	\$ -	\$ 1,170,000	\$ 1,170,000
\$717,492 Lease Purchase Agreement, due in monthly installments through March 1, 2009, 4.20% - 5.95%	214,275	-	214,275
	\$ 214,275	\$ 1,170,000	\$ 1,384,275

In prior years, the City defeased certain General Obligation Bonds, Revenue Bonds and Certificates of Obligation by placing the proceeds of the new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the City's financial statements. On September 30, 2005, \$9,720,000 of bonds outstanding are considered defeased.

The annual requirements to amortize the long-term debt as of September 30, 2005 are as follows:

Fiscal Year	General Obligation Bonds				Revenue Bond	
	Governmental Activities	Water and Sewer Fund	Airport Fund	Recreational Component Unit	Total	Water and Sewer Fund
2006	\$ 254,175	\$ 774,810	\$ 9,072	\$ 461,997	\$ 1,500,054	\$ 102,415
2007	254,998	770,370	9,072	910,173	1,944,613	104,475
2008	305,907	802,343	17,261	906,373	2,031,884	106,225
2009	308,729	808,997	17,617	906,957	2,042,300	102,655
2010	308,156	802,540	17,512	906,350	2,034,558	109,015
2011-2015	1,549,066	4,049,568	87,634	4,569,791	10,256,059	527,525
2016-2020	1,568,181	2,795,434	63,735	4,604,740	9,032,090	-
2021-2024	1,241,637	220,406	45,915	3,704,045	5,212,003	-
	5,790,849	11,024,468	267,818	16,970,426	34,053,561	1,052,310
Less Interest	1,998,624	3,062,884	91,628	5,440,426	10,593,562	257,310
Total principal	\$ 3,792,225	\$ 7,961,584	\$ 176,190	\$ 11,530,000	\$ 23,459,999	\$ 795,000

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 6. LONG-TERM LIABILITIES - CONTINUED

Fiscal Year	Certificates of Obligation Governmental Activities	Capital Leases		Total
		Governmental Activities	Business-type Activities	
2006	\$ 237,188	\$ 62,002	\$ 222,543	\$ 284,545
2007	238,075	62,002	224,360	286,362
2008	238,788	62,002	220,736	282,738
2009	239,325	62,001	226,493	288,494
2010	239,688	-	231,321	231,321
2011-2015	1,208,550	-	225,500	225,500
2016-2020	1,207,246	-	-	-
2021-2024	721,457	-	-	-
	<u>4,330,317</u>	<u>248,007</u>	<u>1,350,953</u>	<u>1,598,960</u>
Less Interest	<u>1,305,317</u>	<u>33,732</u>	<u>180,953</u>	<u>214,685</u>
Total principal	<u>\$ 3,025,000</u>	<u>\$ 214,275</u>	<u>\$ 1,170,000</u>	<u>\$ 1,384,275</u>

NOTE 7. RETIREMENT PLAN

Plan Description

The City provides pension benefits for all of its full-time employees through a nontraditional, joint contributory, hybrid defined benefit plan in the state-wide Texas Municipal Retirement System (TMRS), one of over 774 administered by TMRS, an agent multiple-employer public employee retirement system.

Benefits depend upon the sum of the employee's contributions to the plan, with interest, and the City-financed monetary credits, with interest. At the date the plan began, the City granted monetary credits for service rendered before the plan began of a theoretical amount equal to two times what would have been contributed by the employee, with interest, prior to establishment of the plan. Monetary credits for service since the plan began are a percent (100%, 150%, or 200%) of the employee's accumulated contributions. In addition, the City can grant, as often as annually, another type of monetary credit referred to as an updated service credit which is a theoretical amount; which, when added to the employee's accumulated contributions and the monetary credits for service since the plan began would be the total monetary credits and employee contributions accumulated with interest if the current employee contribution rate and city matching percent had always been in existence and if the employee's salary had always been the average of his salary in the last three years that are one year before the effective date. At retirement, the benefit is calculated as if the sum of the employee's accumulated contributions with interest and the employer-financed monetary credits with interest were used to purchase an annuity.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 7. RETIREMENT PLAN - CONTINUED

Members can retire at ages 60 and above with 5 or more years of service or with 25 years of service regardless of age. The plan also provides death and disability benefits. A member is vested after 5 years, but he must leave his accumulated contributions in the plan. If a member withdraws his own money, he is not entitled to the employer-financed monetary credits, even if he was vested. The plan provisions are adopted by the governing body of the City, within the options available in the state statutes governing TMRS and within the actuarial constraints also in the statutes.

TMRS issues a publicly available annual financial report that includes financial statements and required supplementary information. The report may be obtained by writing to TMRS, P.O. Box 149133, Austin, Texas 78714-9153.

Contributions

The contribution rate for the employees is 7%, and the City's matching percent is currently 2 to 1, both as adopted by the governing body of the City. Under the state law governing TMRS, the actuary annually determines the City contribution rate. This rate consists of the normal cost contribution rate and the prior service contribution rate, both of which are calculated to be a level percent of payroll from year to year. The normal cost contribution rate finances the currently accruing monetary credits due to the City matching percent, which are the obligation of the City as of an employee's retirement date, not at the time the employee's contributions are made. The normal cost contribution rate is the actuarially determined percent of payroll necessary to satisfy the obligation of the City to each employee at the time his/her retirement becomes effective. The prior service contribution rate amortizes the unfunded (overfunded) actuarial liability (asset) over the remainder of the plan's 25-year amortization period. The unit credit actuarial cost method is used for determining the City contribution rate. Both the employees and the City make contributions monthly. Since the City needs to know its contribution rate in advance for budgetary purposes, there is a one-year delay between the actuarial valuation that serves as the basis for the rate and the calendar year when the rate goes into effect. (i.e. December 31, 2004 valuation is effective for rates beginning January 2006.)

The annual pension cost for 2005 was \$1,315,139. The City's annual pension cost was equal to the required and actual contributions for the years ended December 31, 2004, 2003 and 2002.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 7. RETIREMENT PLAN - CONTINUED

Schedule of Actuarial Liabilities and Funding Progress:

	FY 2005-04	FY 2004-03	FY 2003-02	FY 2002-01	FY 2000-01	FY 1999-00
Actuarial Valuation Date	12/31/2004	12/31/2003	12/31/2002	12/31/2001	12/23/2000	12/31/1999
Actuarial Valuation of Assets	\$ 21,655,578	\$ 19,287,766	\$ 17,961,871	\$ 16,672,228	\$ 15,081,238	\$ 13,384,251
Actuarial Accrued Liability	28,263,527	25,747,040	23,228,811	21,734,002	19,739,569	17,568,441
Percentage Funded	76.60%	74.90%	77.30%	76.70%	76.40%	76.20%
Unfunded (Over-funded)						
Actuarial Accrued Liability U(UAAL)	6,607,949	6,459,274	5,266,940	5,061,774	4,658,331	4,184,190
Annual Covered Payroll	10,219,681	8,406,699	7,826,294	7,078,232	7,368,692	7,433,991
UAAL as a Percentage of Covered Payroll	64.70%	76.80%	67.30%	71.50%	63.20%	56.30%
Net Pension Obligation (NPO) at Beginning of Period						
Annual Pension cost:						
Annual Required Contribution (ARC)	1,315,139	1,103,135	978,227	919,560	857,296	995,918
Interest on NPO Adjusted to the ARC						
Contributions Made	1,315,139	1,103,135	978,227	919,560	857,296	995,918
Increase in NPA						
NPO at End of Period	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

Actuarial Assumptions

The City of Lancaster is one of 774 municipalities having their benefit plan administered by TMRS. Each of the 774 municipalities have an annual individual actuarial valuation performed. All assumptions for the December 31, 2004 valuations are contained in the 2004 TMRS Comprehensive Annual Financial Report, a copy of which may be obtained by writing to P.O. Box 149153, Austin, Texas 78714-9153.

Actuarial Assumptions: (a) Actuarial Cost method-United Credit (b) Amortization method-Level Percent of payroll (c) remaining Amortization Period-25 years-open period (d) Asset Valuation Method-Amortized Cost (to accurately reflect the requirements of GASB Statement No. 25, paragraphs 36e and 138)(e) Investment Rate of Return-8% (f) Projected Salary Increases-None (g) Includes Inflation at-None and (h) Costs-of-Living Adjustments-None.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 8. DEFERRED COMPENSATION PLAN

The City participates in a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all permanent City employees, permits them to defer, until future years, up to 25% of annual gross earnings not to exceed \$8,000 a year. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

The City has amended plan documents to conform with the requirements of subsection (g) of IRC Section 457. Accordingly, all amounts of compensation deferred under the plans, all property and rights purchased with those amounts and all income attributable to those amounts, property or rights are held in trust for the exclusive benefit of the participants and beneficiaries.

It is the opinion of the City's legal counsel that the City has no liability for losses and provides limited administrative duties.

Investments are managed by the plans' trustees under one of 28 investment options or a combination thereof. The choice of the investment options(s) is made by the participants.

In accordance with GASB No. 32, the deferred compensation plans are no longer included in the financial statements of the City.

NOTE 9. COMMITMENTS AND CONTINGENCIES

Risk Management

The City is exposed to various risks of loss related to torts, theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City is part of the Texas Municipal League Intergovernmental Risk Pool. Premiums are paid to the Pool, which retain a limit of loss. Reinsurance companies insure the risks beyond those limits. The City retains, as a risk, only the deductible amount of each policy. There were no significant reduction in coverage in the past fiscal year and there were no settlements exceeding insurance coverage in each of the past three fiscal years.

Trinity River Authority of Texas

The City contracts with Trinity River Authority of Texas ("TRA"), a conservation and reclamation district, whereby the Authority finances, constructs, operates and maintains sewage transportation and treatment facilities for the benefit of the City. The current contract is extended through the date until which all bonds have been paid. The City makes payments monthly, which are based on an estimate of its share of costs. The City's share of costs for the fiscal year ended September 30, 2005 was \$2,710,897. This estimate is calculated by TRA who makes adjustments for over/under charges in the City's next fiscal year. There were no adjustments to the amounts as calculated by the TRA for the year ended September 30, 2005.

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 9. COMMITMENTS AND CONTINGENCIES

Federal and State Programs

The City participates in several state and federal grant programs, which are governed by various rules and regulations of the grantor agencies. Costs charged to the respective grant programs are subject to audit and adjustment by the grantor agencies; therefore, to the extent that the City has not complied with the rules and regulations governing the grants, refunds of any money received may be required and the collectibility of any related receivable at September 30, 2005 may be impaired. In the opinion of the City, there are no significant contingent liabilities relating to compliance with the rules and regulations governing the respective grants; therefore, no provision has been recorded in the accompanying financial statements for such contingencies.

Other Contingencies

There are other claims and pending actions incidental to normal operations of the City. In the opinion of the City administration, the City's potential liability in these matters will not have a material impact on the financial statements.

NOTE 10. RESERVATIONS AND DESIGNATIONS OF FUND BALANCE/RETAINED EARNINGS

Designations of fund balance reflect City management's intended use of resources. As of September 30, 2005, the City designated unreserved fund balance was for equipment replacement \$202,817. The equipment replacement designation is for the replacement of the City's vehicle and large equipment fleet.

Reserves represent those portions of fund balance not appropriable for expenditure or legally segregated for a specific use. Reserves of retained earnings consist of resources accumulated for the retirement of debt (reserve for debt service) and the unexpended portion of impact fees which are restricted for water and sewer improvements (reserve for capital improvements).

**CITY OF LANCASTER
NOTES TO BASIC FINANCIAL STATEMENTS**

NOTE 11. EXCESS OF EXPENDITURES OVER APPROPRIATIONS

The following funds and expenditure categories had excesses of expenditures over appropriations at the legal level of control (fund level):

<u>Fund</u>	<u>Department</u>	<u>Excess Expenditures over Appropriations</u>
General Fund	Community Services	\$ 11,023
General Fund	Non-departmental	31,339
HUD Special Revenue Fund	Social and Welfare	596,128
Stormwater Drainage Fund	General Government	33,853

NOTE 12. PRIOR PERIOD ADJUSTMENT

During the year ended September 30, 2004 expenses were accrued related to the Water and Sewer Fund that should have been recognized as expense during the year ended September 30, 2005 for \$324,251.

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APPENDIX C

FORM OF BOND COUNSEL'S OPINIONS

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West & Associates L.L.P.

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May 1, 2007

WE HAVE ACTED as Bond Counsel for the City of Lancaster, Texas (the "City") in connection with an issue of bonds (the "Bonds") described as follows:

CITY OF LANCASTER, TEXAS, GENERAL OBLIGATION REFUNDING AND IMPROVEMENT BONDS, SERIES 2007, dated March 15, 2007, in the aggregate principal amount of \$24,300,000, maturing on February 15 in the years 2008 through and including 2023, and as Term Bonds maturing February 15, 2025, February 15, 2027, and February 15, 2032. The Bonds are issuable in fully registered form only, in denominations of \$5,000 or integral multiples thereof, and bear interest, and may be transferred and exchanged as set out in the Bonds and in the ordinance (the "Ordinance") adopted by the City Council of the City authorizing their issuance.

WE HAVE ACTED as Bond Counsel for the sole purpose of rendering an opinion with respect to the legality and validity of the Bonds under the Constitution and laws of the State of Texas. In such capacity we have examined the Constitution and laws of the State of Texas, federal income tax law, and a transcript of certain certified proceedings pertaining to the issuance of the Bonds and the obligations that are being refunded (the "Refunded Obligations") with the proceeds of the Bonds, as described in the Ordinance. The transcript contains certified copies of certain proceedings of the City, The Bank of New York Trust Company, N.A. (the "Escrow Agent") and the report (the "Report") of Grant Thornton LLP, which verifies the sufficiency of the deposits made with the Escrow Agent for the defeasance of the Refunded Obligations and the mathematical accuracy of certain computations of the yield on the Bonds and the obligations acquired with the proceeds of the Bonds, certain certifications and representations and other material facts within the knowledge and control of the City, upon which we rely, and certain other customary documents and instruments authorizing and relating to the issuance of the Bonds and the firm banking and financial arrangements for the discharge and final payment of the Refunded Obligations. We have also examined executed Bond No. R-1 of this issue.

WE HAVE NOT BEEN REQUESTED to examine, and have not investigated or verified, any original proceedings, records, data or other material, but have relied upon the transcript of certified proceedings. We have not assumed any responsibility with respect to the financial condition or capabilities of the City or the disclosure thereof in connection with the sale of the Bonds. Our role in connection with the City's Official Statement prepared for use in connection with the sale of the Bonds has been limited as described therein.

BASED ON SUCH EXAMINATION, it is our opinion as follows:

- (1) The transcript of certified proceedings evidences complete legal authority for the issuance of the Bonds in full compliance with the Constitution and laws of the State of Texas presently in effect; the Bonds constitute valid and legally binding obligations of the City enforceable in accordance with the terms and conditions thereof, except to the extent that the rights and remedies of the owners of the Bonds may be limited by laws heretofore or hereafter enacted relating to bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting the rights of creditors of political subdivisions and the exercise of judicial discretion in appropriate cases; and the Bonds have been authorized and delivered in accordance with law;
- (2) The Bonds are payable, both as to principal and interest, from the receipts of an annual ad valorem tax levied, within the limits prescribed by law, upon taxable property located within the City, which taxes have been pledged irrevocably to pay the principal of and interest on the Bonds; and
- (3) The escrow agreement between the City and the Escrow Agent (the "Escrow Agreement") has been duly executed and delivered and constitutes a binding and enforceable agreement in accordance with its terms; the establishment of the Escrow Fund pursuant to the Escrow Agreement and the deposit made therein constitute the making of firm banking and financial arrangements for the discharge and final payment of the Refunded Obligations; the Refunded Obligations, having been discharged and paid, are no longer outstanding, and the lien on and pledge of ad valorem taxes and other revenues as set forth in the ordinances authorizing their issuance will be appropriately and legally defeased; the holders of the Refunded Obligations may obtain payment of the principal of, redemption premium, if any, and interest on the Refunded Obligations only out of the funds provided therefor now held for that purpose by the Escrow Agent pursuant to the terms of the Escrow Agreement; and therefore the Refunded Obligations are deemed to be fully paid and no longer outstanding, except for the purpose of being paid from the funds provided therefor in such Escrow Agreement.

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

West & Associates L.L.P.

320 S. R.L. Thornton Freeway, Suite 300
Dallas, Texas 75203
214.941.1881 Phone
214.941.1399 Fax
westllp.com

May 1, 2007

WE HAVE ACTED as Bond Counsel for the CITY OF LANCASTER, TEXAS, a municipal corporation of the State of Texas (the "City") in connection with an issue of certificates of obligation (the "Certificates") described as follows:

CITY OF LANCASTER, TEXAS TAX AND WATERWORKS AND SEWER SYSTEM SURPLUS REVENUE CERTIFICATES OF OBLIGATION, SERIES 2007, dated March 15, 2007, in the aggregate principal amount of \$14,565,000, maturing on February 15 in the years 2008 through and including 2027, and as a Term Certificate maturing February 15, 2032. The Certificates are issuable in fully registered form only, in denominations of \$5,000 or integral multiples thereof, bear interest and may be transferred and exchanged as set out in the Certificates and in the ordinance (the "Ordinance") adopted by the City Council of the City (the "City Council") authorizing their issuance.

WE HAVE ACTED as Bond Counsel for the sole purpose of rendering an opinion with respect to the legality and validity of the Certificates under the Constitution and laws of the State of Texas. In such capacity we have examined the Constitution and laws of the State of Texas and a transcript of certain certified proceedings pertaining to the issuance of the Certificates, as described in the Ordinance. The transcript contains certified copies of certain proceedings of the City; certain certifications and representations and other material facts within the knowledge and control of the City, upon which we rely; and certain other customary documents and instruments authorizing and relating to the issuance of the Certificates. We have also examined executed Certificate No. R-1.

WE HAVE NOT BEEN REQUESTED to examine, and have not investigated or verified, any original proceedings, records, data or other material, but have relied upon the transcript of certified proceedings. We have not assumed any responsibility with respect to the financial condition or capabilities of the City or the disclosure thereof in connection with the sale of the Certificates. Our role in connection with the City's Official Statement prepared for use in connection with the sale of the Certificates has been limited as described therein.

BASED ON SUCH EXAMINATION, it is our opinion as follows:

(1) The transcript of certified proceedings evidences complete legal authority for the issuance of the Certificates in full compliance with the Constitution and laws of the State of Texas presently in effect; the Certificates constitute valid and legally binding obligations of the City enforceable in accordance with the terms and conditions thereof, except to the extent that the rights and remedies of the owners of the Certificates may be limited by laws heretofore or hereafter enacted relating to bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting the rights of creditors of political subdivisions and the exercise of judicial discretion in appropriate cases; and the Certificates have been authorized and delivered in accordance with law;

(2) The Certificates are payable, both as to principal and interest, from the receipts of an annual ad valorem tax levied, within the limits prescribed by law, upon taxable property located within the City, which taxes have been pledged irrevocably to pay the principal of and interest on the Certificates; and

(3) The surplus revenues (limited in an amount not to exceed \$1,000) of the City's combined Waterworks and Sewer System, after the payment of all operation and maintenance expenses thereof (the "Net Revenues"), are pledged to the payment of the principal of and interest on the Certificates; provided, however, that such pledge is junior and subordinate in all respects to the pledge of Net Revenues to the payment of any obligation of the City, whether authorized heretofore or hereafter, which the City designates as having a pledge senior to the pledge of Net Revenues to the payment of the Certificates.

The City has reserved the right to issue, for any lawful purpose at any time, in one or more installments, bonds, certificates of obligation and other obligations of any kind secured by a pledge of the Net Revenues that may be prior and superior in right to, on a parity with, or junior and subordinate to the pledge of Net Revenues securing the Certificates.

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

APPENDIX D

FORM OF SPECIAL TAX COUNSEL'S OPINIONS

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May 1, 2007

WE HAVE ACTED as Special Tax Counsel for City of Lancaster, Texas (the "City"), in connection with an issue of bonds (the "Bonds") described as follows:

CITY OF LANCASTER, GENERAL OBLIGATION REFUNDING AND IMPROVEMENT BONDS, SERIES 2007, dated March 15, 2007, in initial denominations equal to the entire principal amount of each scheduled maturity of the Bonds, aggregating \$24,300,000.

The Bonds mature, bear interest and may be transferred and exchanged as set out in the Bonds and in the ordinance of the City's City Council authorizing the Bonds (the "Bond Ordinance"). The Bonds are subject to optional redemption prior to maturity as set out in the Bonds and in the Bond Ordinance.

WE HAVE ACTED as Special Tax Counsel for the sole purpose of rendering an opinion with respect to the exclusion of interest on the Bonds from gross income under federal income tax law. In such capacity we have examined the federal income tax law and a transcript of certain certified proceedings pertaining to the issuance of the Bonds, as described in the Bond Ordinance. The transcript contains certified copies of certain proceedings of the City; certain certifications and representations and other material facts within the knowledge and control of the City, upon which we rely; and certain other customary documents and instruments authorizing and relating to the issuance of the Bonds.

WE HAVE NOT BEEN REQUESTED to examine, and have not investigated or verified, any original proceedings, records, data or other material, but have relied upon the transcript of certified proceedings. We have not assumed any responsibility with respect to the financial condition or capabilities of the City or the disclosure thereof in connection with the sale of the Bonds.

BASED ON OUR EXAMINATION AS DESCRIBED ABOVE, it is our opinion that, subject to the restrictions hereinafter described, interest on the Bonds is excludable from gross income of the owners thereof for federal income tax purposes under existing law and is not subject to the alternative minimum tax on individuals or, except as hereinafter described, corporations. The opinion set forth in the first sentence of this paragraph is subject to the condition that the City comply with all requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the issuance of the Bonds in order that interest thereon be, or continue to be, excluded from gross income for federal income tax purposes. The City has covenanted in the Bond Ordinance to comply with each such requirement. Failure to comply with certain of such requirements may cause the inclusion of interest on the Bonds in gross income for federal income tax purposes to be retroactive to the date of issuance of the Bonds. The Code and the existing regulations, rulings and court decisions thereunder, upon which the foregoing opinions of Special Tax Counsel are based, are subject to

May 1, 2007

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change, which could prospectively or retroactively result in the inclusion of the interest on the Bonds in gross income of the owners thereof for federal income tax purposes.

INTEREST ON all tax-exempt obligations, including the Bonds, owned by a corporation (other than an S corporation, a regulated investment company, a real estate investment trust (REIT), a real estate mortgage investment conduit (REMIC) or a financial asset securitization investment trust (FASIT)) will be included in such corporation's adjusted current earnings for purposes of calculating such corporation's alternative minimum taxable income. A corporation's alternative minimum taxable income is the basis on which the alternative minimum tax imposed by the Code is computed.

EXCEPT AS DESCRIBED HEREIN, we express no opinions as to any other matters except with respect to the excludability of the interest on the Bonds from gross income from the owners thereof for federal income tax purposes.

IN PROVIDING THE FOREGOING OPINIONS, we have relied upon representations of the City with respect to matters solely within the knowledge of the City, which we have not independently verified, and have assumed the accuracy and completeness thereof.

IN ADDITION, EXCEPT AS DESCRIBED ABOVE, we express no opinion as to any federal, state or local tax consequences under present law, or future legislation, resulting from the ownership of, receipt or accrual of interest on, or the acquisition or disposition of, the City. Prospective purchasers of the Bonds should be aware that the ownership of tax-exempt obligations, such as the Bonds, may result in collateral federal income tax consequences to, among others, financial institutions, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain S corporations with Subchapter C earnings and profits, individual recipients of Social Security or Railroad Retirement benefits, taxpayers who are deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, taxpayers owning an interest in a FASIT that holds tax-exempt obligations and individuals otherwise qualified for the earned income credit. For the foregoing reasons, prospective purchasers should consult their tax advisors as to the consequences of investing in the Bonds.

May 1, 2007

WE HAVE ACTED as Special Tax Counsel for City of Lancaster, Texas (the "City"), in connection with an issue of certificates of obligation (the "Certificates") described as follows:

CITY OF LANCASTER, TEXAS TAX AND WATERWORKS AND SEWER SYSTEM SURPLUS REVENUE CERTIFICATES OF OBLIGATION, SERIES 2007, dated March 15, 2007, in initial denominations equal to the entire principal amount of each scheduled maturity of the Certificates, aggregating \$14,565,000.

The Certificates mature, bear interest and may be transferred and exchanged as set out in the Certificates and in the ordinance of the City's City Council authorizing the Certificates (the "Certificate Ordinance"). The Certificates are subject to optional redemption prior to maturity as set out in the Certificates and in the Certificate Ordinance.

WE HAVE ACTED as Special Tax Counsel for the sole purpose of rendering an opinion with respect to the exclusion of interest on the Certificates from gross income under federal income tax law. In such capacity we have examined the federal income tax law and a transcript of certain certified proceedings pertaining to the issuance of the Certificates, as described in the Certificate Ordinance. The transcript contains certified copies of certain proceedings of the City; certain certifications and representations and other material facts within the knowledge and control of the City, upon which we rely; and certain other customary documents and instruments authorizing and relating to the issuance of the Certificates.

WE HAVE NOT BEEN REQUESTED to examine, and have not investigated or verified, any original proceedings, records, data or other material, but have relied upon the transcript of certified proceedings. We have not assumed any responsibility with respect to the financial condition or capabilities of the City or the disclosure thereof in connection with the sale of the Certificates.

BASED ON OUR EXAMINATION AS DESCRIBED ABOVE, it is our opinion that, subject to the restrictions hereinafter described, interest on the Certificates is excludable from gross income of the owners thereof for federal income tax purposes under existing law and is not subject to the alternative minimum tax on individuals or, except as hereinafter described, corporations. The opinion set forth in the first sentence of this paragraph is subject to the condition that the City comply with all requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the issuance of the Certificates in order that interest thereon be, or continue to be, excluded from gross income for federal income tax purposes. The City has covenanted in the Certificate Ordinance to comply with each such requirement. Failure to comply with certain of such requirements may cause the inclusion of interest on the Certificates in gross income for federal income tax purposes to be retroactive to the date of issuance of the Certificates. The Code and the existing regulations, rulings and court

May 1, 2007

Page 2

decisions thereunder, upon which the foregoing opinions of Special Tax Counsel are based, are subject to change, which could prospectively or retroactively result in the inclusion of the interest on the Certificates in gross income of the owners thereof for federal income tax purposes.

INTEREST ON all tax-exempt obligations, including the Certificates, owned by a corporation (other than an S corporation, a regulated investment company, a real estate investment trust (REIT), a real estate mortgage investment conduit (REMIC) or a financial asset securitization investment trust (FASIT)) will be included in such corporation's adjusted current earnings for purposes of calculating such corporation's alternative minimum taxable income. A corporation's alternative minimum taxable income is the basis on which the alternative minimum tax imposed by the Code is computed.

EXCEPT AS DESCRIBED HEREIN, we express no opinions as to any other matters except with respect to the excludability of the interest on the Certificates from gross income from the owners thereof for federal income tax purposes.

IN PROVIDING THE FOREGOING OPINIONS, we have relied upon representations of the City with respect to matters solely within the knowledge of the City, which we have not independently verified, and have assumed the accuracy and completeness thereof.

IN ADDITION, EXCEPT AS DESCRIBED ABOVE, we express no opinion as to any federal, state or local tax consequences under present law, or future legislation, resulting from the ownership of, receipt or accrual of interest on, or the acquisition or disposition of, the City. Prospective purchasers of the Certificates should be aware that the ownership of tax-exempt obligations, such as the Certificates, may result in collateral federal income tax consequences to, among others, financial institutions, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain S corporations with Subchapter C earnings and profits, individual recipients of Social Security or Railroad Retirement benefits, taxpayers who are deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, taxpayers owning an interest in a FASIT that holds tax-exempt obligations and individuals otherwise qualified for the earned income credit. For the foregoing reasons, prospective purchasers should consult their tax advisors as to the consequences of investing in the Certificates.

APPENDIX E

SPECIMEN BOND INSURANCE POLICY

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Financial Guaranty Insurance Policy

Obligor:

Policy Number:

Obligations:

Premium:

Ambac Assurance Corporation (Ambac), a Wisconsin stock insurance corporation, in consideration of the payment of the premium and subject to the terms of this Policy, hereby agrees to pay to The Bank of New York, as trustee, or its successor (the "Insurance Trustee"), for the benefit of the Holders, that portion of the principal of and interest on the above-described obligations (the "Obligations") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor.

Ambac will make such payments to the Insurance Trustee within one (1) business day following written notification to Ambac of Nonpayment. Upon a Holder's presentation and surrender to the Insurance Trustee of such unpaid Obligations or related coupons, uncanceled and in bearer form and free of any adverse claim, the Insurance Trustee will disburse to the Holder the amount of principal and interest which is then Due for Payment but is unpaid. Upon such disbursement, Ambac shall become the owner of the surrendered Obligations and/or coupons and shall be fully subrogated to all of the Holder's rights to payment thereon.

In cases where the Obligations are issued in registered form, the Insurance Trustee shall disburse principal to a Holder only upon presentation and surrender to the Insurance Trustee of the unpaid Obligation, uncanceled and free of any adverse claim, together with an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee duly executed by the Holder or such Holder's duly authorized representative, so as to permit ownership of such Obligation to be registered in the name of Ambac or its nominee. The Insurance Trustee shall disburse interest to a Holder of a registered Obligation only upon presentation to the Insurance Trustee of proof that the claimant is the person entitled to the payment of interest on the Obligation and delivery to the Insurance Trustee of an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee, duly executed by the Holder or such Holder's duly authorized representative, transferring to Ambac all rights under such Obligation to receive the interest in respect of which the insurance disbursement was made. Ambac shall be subrogated to all of the Holders' rights to payment on registered Obligations to the extent of any insurance disbursements so made.

In the event that a trustee or paying agent for the Obligations has notice that any payment of principal of or interest on an Obligation which has become Due for Payment and which is made to a Holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from the Holder pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such Holder will be entitled to payment from Ambac to the extent of such recovery if sufficient funds are not otherwise available.

As used herein, the term "Holder" means any person other than (i) the Obligor or (ii) any person whose obligations constitute the underlying security or source of payment for the Obligations who, at the time of Nonpayment, is the owner of an Obligation or of a coupon relating to an Obligation. As used herein, "Due for Payment", when referring to the principal of Obligations, is when the scheduled maturity date or mandatory redemption date for the application of a required sinking fund installment has been reached and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by application of required sinking fund installments), acceleration or other advancement of maturity; and, when referring to interest on the Obligations, is when the scheduled date for payment of interest has been reached. As used herein, "Nonpayment" means the failure of the Obligor to have provided sufficient funds to the trustee or paying agent for payment in full of all principal of and interest on the Obligations which are Due for Payment.

This Policy is noncancelable. The premium on this Policy is not refundable for any reason, including payment of the Obligations prior to maturity. This Policy does not insure against loss of any prepayment or other acceleration payment which at any time may become due in respect of any Obligation, other than at the sole option of Ambac, nor against any risk other than Nonpayment.

In witness whereof, Ambac has caused this Policy to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.



President



Secretary

Effective Date:

Authorized Representative

THE BANK OF NEW YORK acknowledges that it has agreed to perform the duties of Insurance Trustee under this Policy.

Form No.: 2B-0012 (1/01)



Authorized Officer of Insurance Trustee

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Financial Advisory Services
Provided By

