

**CITY OF THE COLONY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2008**

Pursuant to Generally Accepted Accounting Principles, the City of The Colony is providing this narrative overview and analysis of its financial activities for the fiscal year ended September 30, 2008. This Management's Discussion and Analysis (MD&A) provides additional information that was not contained in the Letter of Transmittal. Readers are advised to read both in order to gain understanding of the financial picture of the City. This discussion and analysis includes prior year data for comparison purposes.

Financial Highlights

- The City's total assets exceeded the City's total liabilities at the close of the fiscal year by \$165,754,764. Of this amount \$16,734,033 (unrestricted net assets) may be used to meet the government's ongoing obligations to citizens and creditors.
- The government's total net assets increased by \$9,361,793, due mainly to increases in net assets of \$6,546,627 in governmental activities and \$2,815,166 in business-type activities.
- As of the close of the current fiscal year, The Colony's governmental funds reported combined ending fund balances of \$16,491,979, a decrease of \$3,449,807. \$10,199,487 is capital expenditures for streets, storm drainage, and municipal building renovations. The general fund has an increase in fund balance of \$673,642. The other special revenue, debt service and capital projects comprised of the differences in the governmental fund balances. Out of the \$16,491,979 fund balances in the governmental funds, \$6,252,576 is available for spending at the government's discretion (unreserved and undesignated fund balance).
- At the end of the current fiscal year, unreserved and undesignated fund balance for the general fund was also \$6,252,576 or 31.10 percent of total general fund expenditures.
- The City's total long-term debt decreased by \$3,243,665 (3.2 percent) during the current fiscal year. The key factor in this increase was the annual retirement of long-term debts and debt issuance of \$1,700,000. There were two refundings in the fiscal year to take advantage of the low interest environment.

Overview of the Financial Statements

The MD&A serves as an introduction to The Colony's basic financial statements. The Colony's basic financial statements comprise three components:

1. Government-wide financial statements,
2. Fund financial statements, and
3. Notes to the financial statements.

The report also contains other supplementary information in addition to the basic financial statements.

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Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of The Colony's finances, in a manner similar to a private-sector business.

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

The statement of activities presents information showing how the City's net assets changed during the most recent fiscal year. All changes in net assets are reported as incurred regardless of when cash is received or paid. Thus, revenues and expenses are reported on accrual basis even though cash flows occur in the future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the City of The Colony 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 of The Colony include general government, public safety, streets, sanitation, and culture and recreation. The business-type activities of the City of The Colony include water and sewerage operation.

The government-wide financial statements include not only the City of The Colony itself (known as the primary government), but also a legally separate Economic Development Corporation and a legally separate Community Development Corporation for which the City of The Colony is financially accountable. Financial information for these component units is reported separately from the financial information presented for the primary government itself.

The government-wide financial statements can be found on pages 15 to 17 of this report.

In the Statement of Net Assets and the Statement of Activities, the City is divided into three kinds of activities:

- Governmental Activities – Most of the City's basic services are reported as governmental activities, including the general government, public safety, municipal court, public works, culture and recreation, planning and zoning, public improvements, and code enforcement. Taxes and intergovernmental revenues principally support these services.
- Business-type Activities – Functions that are intended to recover all or a significant portion of their costs through user fees and charges are considered as business-type activities. The business-type activity of The Colony includes Water and Wastewater Utility.
- Component Units – The City includes two separate legal entities, The Economic Development Corporation and the Community Development Corporation in its report. Although they are legally separate, they are included as the component units because the City is accountable for them. Financial information for these component units is reported separately from the financial information presented for the primary government.

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Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Colony, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of The Colony can be divided into three categories:

1. Governmental funds – Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements.

However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

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

The City of The Colony maintains 15 individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the general fund, the debt service fund, and the capital projects fund, which are considered to be major funds. Non-major governmental funds are aggregated in total.

The City of The Colony adopts annual appropriated budgets for its General fund, Debt Service fund, Stewart Creek Park fund, Environmental fund, Hidden Cove Park fund, Special Events fund, and Hotel/Motel Taxes fund. The budgeted comparison statement has been provided for the general fund to demonstrate compliance with the budget.

2. Proprietary funds – The City of The Colony maintains two different types of proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City of The Colony uses enterprise funds to account for its water and sewer operation. Internal service funds are an accounting device used to accumulate and allocate costs internally among the City of The Colony's various functions. The Colony uses an internal service fund to account for its fleet maintenance services. Because the fleet maintenance services predominantly benefit governmental rather than business-type functions, they have been included within the governmental activities in the government-wide financial statements.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The water sewer utility fund is considered to be a major fund of The Colony.

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3. Fiduciary funds – Fiduciary funds are used to account for resources held for the benefit of parties outside the government. The city does not have a fiduciary fund.

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 31 to 57 of this report.

Other information

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the City of The Colony. This Management's Discussions and Analysis is part of the 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 the close of the 2007-2008 fiscal year, The Colony's net assets (assets exceeding liabilities) totaled \$165,754,764.

The largest portion of The Colony's net assets (88.1 percent) reflects its investment in capital assets (e.g., land, buildings, machinery, and equipment); less any related debt used to acquire those assets that is still outstanding. The City of The Colony uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City of The Colony's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot generate revenues to liquidate these liabilities.

An additional portion of the City's net assets (1.75 percent) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets (\$16,734,033) may be used to meet the government's ongoing obligations to citizens and creditors.

	Governmental Activities		Business-type Activities		Total	
	2008	2007	2008	2007	2008	2007
Current and other assets	\$ 21,522,999	\$ 23,635,943	\$ 16,991,223	\$ 20,362,680	\$ 38,514,222	\$ 43,998,623
Capital assets	156,652,907	148,877,679	73,145,859	68,532,835	229,798,766	217,410,514
Total assets	178,175,906	172,513,622	90,137,082	88,895,515	268,312,988	261,409,137
Long-term liabilities outstanding	47,373,234	48,701,870	49,170,400	51,085,429	96,543,634	99,787,299
Other liabilities	3,452,463	3,008,170	2,562,127	2,220,697	6,014,590	5,228,867
Total liabilities	50,825,697	51,710,040	51,732,527	53,306,126	102,558,224	105,016,166
Net assets:						
Invested in capital assets, net of related debt	114,835,815	110,759,032	31,288,426	30,497,405	146,124,241	141,256,437
Restricted	969,106	275,435	1,927,384	1,987,616	2,896,490	2,263,051
Unrestricted	11,545,288	9,769,115	5,188,745	3,104,368	16,734,033	12,873,483
Total net assets	\$ 127,350,209	\$ 120,803,582	\$ 38,404,555	\$ 35,589,389	\$ 165,754,764	\$ 156,392,971

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At the end of the current fiscal year, the City has positive balances in all three categories of net assets, for the government as a whole, as well as for its separate governmental and business activities.

The City's net assets increased by \$9,361,793 during the current fiscal year. About all of this increase represents increases in ongoing revenues outstripping similar increases in ongoing expenses.

CHANGES IN NET ASSETS

	Governmental Activities		Business-type Activities		Total	
	2008	2007	2008	2007	2008	2007
Revenues:						
Program revenues:						
Charges for services	\$ 4,788,732	\$ 3,917,649	\$ 12,989,227	\$ 11,340,679	\$ 17,777,959	\$ 15,258,328
Operating grants and contributions	2,866,700	3,426,207	170,058	170,058	3,036,758	3,596,265
Capital grants and contributions	6,706,427	8,226,536	1,018,773	3,404,723	7,725,200	11,631,259
General revenues:						
Property taxes	14,305,445	12,774,611	23,758	764,062	14,329,203	13,538,673
Sales taxes	3,055,468	2,880,852	-	-	3,055,468	2,880,852
Franchise taxes	1,807,584	1,939,565	-	-	1,807,584	1,939,565
Other taxes	125,573	141,496	-	-	125,573	141,496
Interest	725,623	843,217	552,763	864,807	1,278,386	1,708,024
Miscellaneous	479,157	806,175	464,046	155,429	943,203	961,604
Total revenues	\$ 34,860,709	\$ 34,956,308	\$ 15,218,625	\$ 16,699,758	\$ 50,079,334	\$ 51,656,066
Expenses:						
General government	5,457,879	5,174,718	-	-	5,457,879	5,174,718
Public safety	10,724,686	9,615,093	-	-	10,724,686	9,615,093
Public works	6,787,684	7,138,705	-	-	6,787,684	7,138,705
Culture and recreation	3,828,479	3,869,375	-	-	3,828,479	3,869,375
Interest on long-term debt	1,797,601	2,113,208	2,183,417	1,950,634	3,981,018	4,063,842
Water and sewer			9,937,795	8,259,668	9,937,795	8,259,668
Total expenses	\$ 28,596,329	\$ 27,911,099	\$ 12,121,212	\$ 10,210,302	\$ 40,717,541	\$ 38,121,401
Increase in net assets before transfers	6,264,380	7,045,209	3,097,413	6,489,456	9,361,793	13,534,665
Transfers	282,247	2,456,591	(282,247)	(2,456,591)	-	-
Increase in net assets	6,546,627	9,501,800	2,815,166	4,032,865	9,361,793	13,534,665
Beginning net assets (October 1)	120,803,582	111,301,752	35,589,389	31,556,524	156,392,971	142,858,306
Ending net assets (September 30)	\$ 127,350,209	\$ 120,803,552	\$ 38,404,555	\$ 35,589,389	\$ 165,754,764	\$ 156,392,971

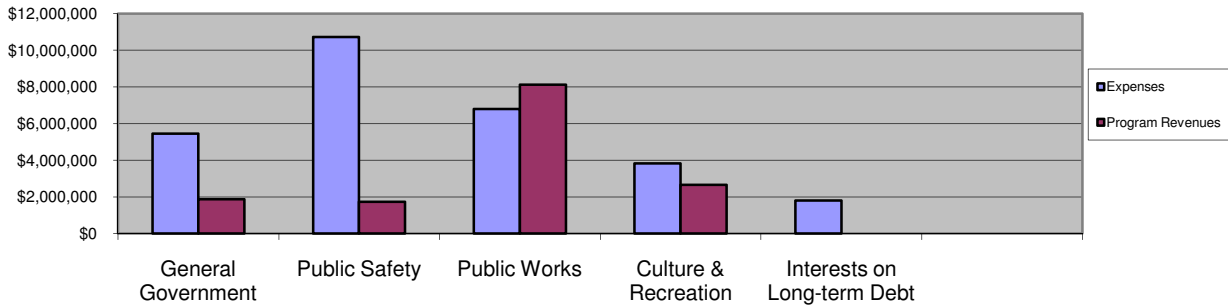
Governmental Activities. Governmental activities increased the City's net assets by \$6,546,627, thereby accounting for 69.93 percent of the total growth in the net assets of The Colony. Key elements of this increase are as follows:

Total Property taxes (including collections in the Utility Tax Supported Debt) increased by \$782,981 during the year. This increase was due to commercial and residential new development. The certified roll for 2007-2008 went up by \$128,373,684 or 6.84%. General Fund sales tax collection has increased by \$174,616, licenses and permits increased by \$842,860 due to increase in development activities. Sales in The Colony and at Edward Don & Company's regional distributing center at Austin Ranch are strong resulting in the increase in sales tax collection. There are slight decreases in Franchise Taxes, Hotel/Motel Taxes, interest earnings, impact fees, and miscellaneous revenues. These decreases are the result of the local economy affected by the financial crisis.

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For the most part, increases in expenses closely paralleled inflation and growth in the demand for services. The Fire Department has hired three firefighters/paramedics to adequately staff the new fire station opened at the end of 2007. There were eight new positions in other departments added in fiscal year 2007-2008, with one code enforcement officer; one trail maintenance worker, two patrol officers, two traffic officers, one warrant officer and one electronic resources librarian. A part-time position in the Municipal Court Department was upgraded to full-time. A part-time lifeguard and a part-time athletic coordinator completed new hires. Debt service payments have increased by \$740,226 or 16.48 percent to pay for the principal and interest. Multiple capital projects in streets, parks and recreations and others are underway. The projects were financed by prior and current debt issuances. In August 2008, \$1.7 million of Certificates of Obligation was issued to finance equipment enhancements.

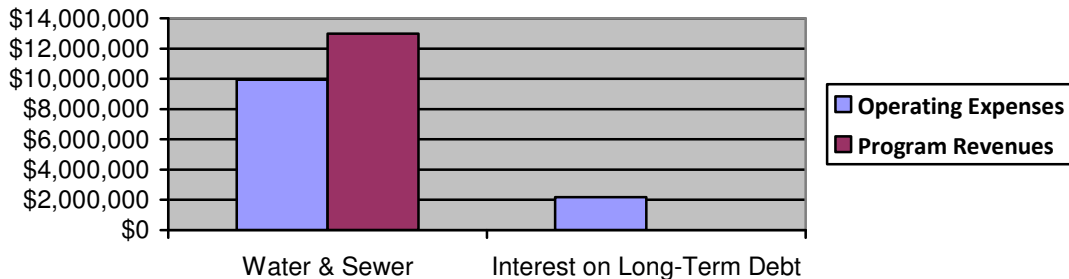
EXPENSE AND PROGRAM REVENUES - GOVERNMENTAL ACTIVITIES



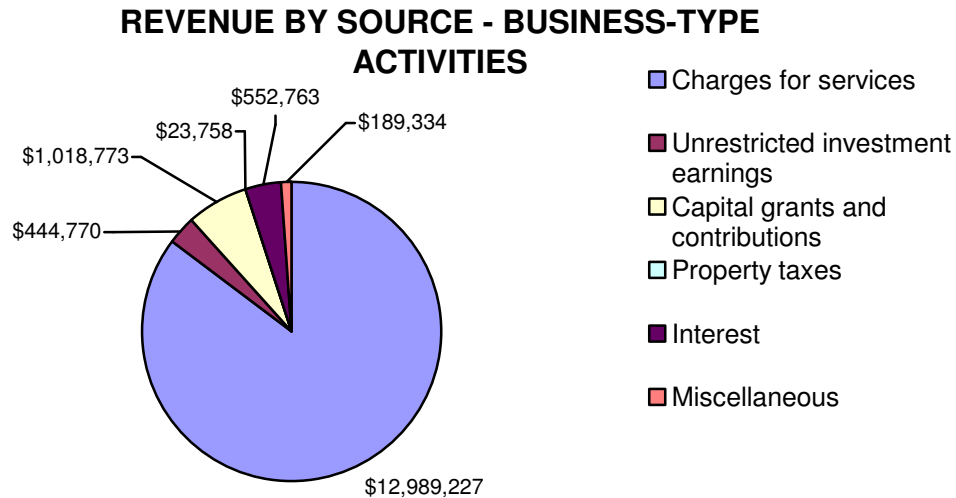
Business-type activities. Business-type activities increased the City's net assets by \$2,815,166 accounting for 30.07 percent of the total growth in the government's net assets. Key elements of this increase are as follows:

A majority of the increase is due to the \$1,018,773 capital contributions to the Utility Fund which represents water mains and sanitation sewers built by developers at the new development. Revenues also increased by \$1,648,548 due to the weather and increased consumption.

**Operating Expense and Program Revenues
Business-type Activities**



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Financial Analysis of the Government's Funds

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

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 a government's net resources available for spending at the end of the fiscal year.

At the end of the current fiscal year, the City's governmental funds reported combined ending fund balances of \$16,491,979 a decrease of \$3,449,807 in comparison with the prior year. Approximately 37.91 percent of this total amount (\$6,252,576) constitutes the unreserved and undesignated fund balance, which is available for spending at the City's discretion. The remainder of the fund balance is reserved and designated to indicate that it is not available for new spending because it has already been committed to:

1. Liquidate contracts and purchase orders of the prior period (\$444,594),
2. Reserve for capital projects (\$7,437,260),
3. Pay debt service (\$1,123,924), or
4. Reserved for court security and technology (\$352,660)
5. Designated to liquidate deficit at Hidden Cove Park (\$140,000).
6. Restricted for Special Revenue Funds (\$740,965)

The general fund is the chief operating fund of The Colony. At the end of the current fiscal year, unreserved and undesignated fund balance of the general fund was \$6,252,576, while total fund balance reached \$6,695,977. As a measure of the general fund's liquidity, it may be useful to compare both unreserved and undesignated fund balance and total fund balance to total fund expenditures. Unreserved and undesignated fund balance represents 31.10 percent of total general fund expenditures (excluding operating transfers to other funds), while total fund balance represents 33.3 percent of that same amount.

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The fund balance of the City's general fund increased by \$673,642 during the current fiscal year. Key factors in this growth are as follows:

- An increase in property tax revenues of \$735,292 is due to increase in assessed values because of growth and decrease in allocation to General Debt Service Fund.
- Sales tax increased by \$174,616 due to growth in local economy and Edward Don & Co.'s regional distributing center.
- Increase in transfers from other funds by \$531,800.
- Expenditures in the general fund increased by \$1,515,080 due to the addition of eleven new full-time, two part-time and an upgrade from part-time to full-time positions, increase in energy, utility costs, and health insurance, and inflation factors.

The debt service fund has a total fund balance of \$1,123,924, all of which is reserved for the payment of debt service. The net increase in fund balance during the current year in the debt service fund was \$157,927. The City has a dedicated property tax for general debt service. The property tax produced revenues of \$4,286,610 in the current fiscal year. Debt service payments have increased by \$740,226.

The capital projects fund has a total fund balance of \$7,437,260 which is reserved for capital projects. The fund balance decreased from prior year by \$4,750,736 due to acquisition and construction costs spent in current year on debt proceeds received in past years.

There was a \$1.7 million debt issuance in fiscal year 2007-2008 to finance equipment and enhancements.

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

Increase in unrestricted net assets of the Utility Fund at the end of the year amounted to \$2,074,956. The increase was mainly due to revenues exceeding expenditures. Other factors concerning the finances of this fund have already been addressed in the discussion of the City's business-type activities.

General Fund Budgetary Highlights

During the year, there was a \$479,585 increase in appropriations between the original and final amended budget. Following are the main components of the increase:

- | | |
|--|-------------|
| • Prior Year Encumbrance roll forward | \$151,818 |
| • Increase in transfers to other funds | \$593,384 |
| • Miscellaneous decreases | (\$265,617) |

The increase in revenues of \$618,970 between final budget and actual was due to better projections of anticipated revenues in mid-year. Revenues from licenses and permit increased by \$767,303 due to new developments in various parts of the city.

In the original budget, salary increases were included in the non-departmental budget. The budget for these salary adjustments was reallocated to individual departments in the final amended budget. During the year, revenues exceeded budgetary estimates and expenditures were less than budgetary estimates resulting in an increase in the general fund fund balance of \$515,059.

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Capital Asset and Debt Administration

Capital assets. The City's investment in capital assets for its governmental and business-type activities as of September 30, 2008, amounts to \$229,798,766 (net of accumulated depreciation). This investment in capital assets includes land, buildings and system, water and sewer system infrastructure improvements, machinery and equipment, park facilities, and roads. The City's investment in capital assets for the current fiscal year increased by 5.7 percent (a 5.2 percent increase for governmental activities and a 6.7 percent increase for business-type activities).

Major capital asset events during the current fiscal year included the following:

- **Phase IIIB Streets Reconstruction** – This project includes the reconstruction of nine residential streets with 6" thick concrete reinforced paving, sidewalk and driveway returns and street right-of-ways. Drainage will be improved as needed and new water and wastewater lines will be installed within the right-of-ways. This project should be complete in February 2009, with an estimated cost of \$6.5M.
- **Phase IIIC Streets Reconstruction** – This project includes the reconstruction of Aztec Drive from Blair Oaks Drive to Clover Valley Drive and Branch Hollow Drive from Arbor Glen Drive to South Colony Blvd. The streets will be re-constructed to the same width as existing with 6" thick concrete reinforced with paving. Sidewalk and driveway returns within street right-of-ways will also be reconstructed and new water and sanitary sewer lines will be installed within the street right-of-way. This project is in the construction phase with an estimated cost of \$1.4M.
- **Interlocal Agreements with Denton County**
 - **Paige Road** – improve and widen Paige Road from South Colony to North Colony as a six lane divided roadway, including drainage, utility improvements, signs, street lights, and landscaping. This project should be complete in March 2009 with an estimated cost \$6.7M.
 - **Memorial Drive** – improve and widen Memorial Drive from Blair Oaks to Paige Road, including drainage, utility improvements, signs, street lights and landscaping. This project should be complete in March 2009 with an estimated cost \$1.5M.
- **Police and Courts Facility** – The design and expansion of the existing police and courts building. This project is in the architectural phase with an estimated cost of \$695K.
- **Austin Ranch Fire Station** – Design for a new fire station at Austin Ranch. This project is in the architectural phase with an estimated cost of \$233K.
- **Public Service Station** – Design and construction for a new Public Services Station. This project is in the architectural phase with an estimated cost of \$482K.
- **Park Improvements**
 - **Hike & Bike** – Design and construction of a shoreline trail. This project is in construction with an estimated cost of \$2.9M.
 - **Miscellaneous Parks Improvements** – includes playground equipment, right-of-way/handicap accessible sidewalks, estimated cost \$100K.
- **Well Site #3** – Construction of a new water well at well site #3. This project is currently in the construction phase with an estimated cost \$2.1M.
- **Interlocal Agreement with the City of Carrollton & Lewisville** – Construct a waterline from Dallas Water Utilities Elm Fork Water Treatment Plant near Keller Springs and Old

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Denton Road to Carrollton's North side Pump Station near Parker and Josey. This project is near completion. Estimated cost \$8.4M.

- **Expansion of Master Lift Station #1** – Expansion from the existing 4.5 million gallons per day (MGD) to 10.0 MGD. The lift station will include instrumentation and controls, Supervisory Control and Data Acquisition (SCADA), odor control, site security and accessibility. Construction began in July 2008 and has an estimated cost \$2.9M.
- **Northwest Trunk Sewer Line Replacement** – A portion of the northwest trunk sewer line failed and required emergency repair. The video inspections revealed the line was corroded and in need of replacement from Main Street east to the influent lift station at the wastewater treatment plant. Construction began in August 2008 and has an estimated cost of \$640K.

**CAPITAL ASSETS
(Net of Depreciation)**

	Governmental Activities		Business-type Activities		Totals	
	2008	2007	2008	2007	2008	2007
<u>Capital Assets Being Depreciated:</u>						
Water systems	\$ -	\$ -	\$ 26,833,538	\$ 24,310,382	\$ 26,833,538	\$ 24,310,382
Sanitary sewer systems	-	-	26,327,827	25,221,013	26,327,827	25,221,013
Drainage system	-	-	445,573	486,174	445,573	486,174
Buildings	9,241,604	6,333,542	123,854	57,676	9,365,458	6,391,218
Improvements other than buildings	7,434,189	7,465,140	-	-	7,434,189	7,465,140
Aquatic Park	1,041,220	1,068,798	-	-	1,041,220	1,068,798
Machinery and equipment	3,631,321	3,573,344	159,707	194,914	3,791,028	3,768,258
Organization costs	-	-	-	-	-	-
Infrastructure	96,203,167	94,095,317	2,407,073	2,605,281	98,610,240	96,700,598
Total	<u>\$ 117,551,501</u>	<u>\$ 112,536,141</u>	<u>\$ 56,297,572</u>	<u>\$ 52,875,440</u>	<u>\$ 173,849,073</u>	<u>\$ 165,411,581</u>
<u>Capital Assets Not Being Depreciated:</u>						
Land & Land Improvements	\$ 4,358,020	\$ 4,358,020	\$ 2,891,887	\$ 1,749,366	\$ 7,249,907	\$ 6,107,386
Right-of-Ways	24,682,941	24,682,941	-	-	24,682,941	24,682,941
Construction in Progress	10,060,445	7,300,577	13,956,400	13,908,029	24,016,845	21,208,606
Total	<u>\$ 39,101,406</u>	<u>\$ 36,341,538</u>	<u>\$ 16,848,287</u>	<u>\$ 15,657,395</u>	<u>\$ 55,949,693</u>	<u>\$ 51,998,933</u>

Additional information on the City's capital assets can be found in note 4 on pages 44 – 45 to the basic financial statements.

**OUTSTANDING DEBT
GENERAL OBLIGATION AND REVENUE BONDS**

	Governmental Activities		Business-type Activities		Totals	
	2008	2007	2008	2007	2008	2007
General Obligation Bonds	\$ 15,040,000	\$ 15,103,742	\$ -	\$ -	\$ 15,040,000	\$ 15,103,742
Certificates of Obligation	31,269,761	31,889,682	26,544,760	26,903,660	57,814,521	58,793,342
Tax Notes	-	-	-	-	-	-
Revenue Bonds	-	-	21,445,000	22,875,000	21,445,000	22,875,000
Total	<u>\$ 46,309,761</u>	<u>\$ 46,993,424</u>	<u>\$ 47,989,760</u>	<u>\$ 49,778,660</u>	<u>\$ 94,299,521</u>	<u>\$ 96,772,084</u>

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Long-term debt. At the end of the current fiscal year, the City had total bonded debt outstanding of \$94,299,521. Of this amount, \$72,854,521 comprises debt backed by the full faith and credit of the government. The remainder of the City's debt (\$21,445,000) represents bonds secured solely by specified revenue sources (i.e. revenue bonds).

The City's total debt decreased by \$2,472,563 during the current fiscal year. The key factor in this decrease was due to retirement and refunding of debts and the issuance of Certificate of Obligations to finance equipment enhancements (\$1,700,000). Additional information on the City's long-term debt can be found in note 5 to the basic financial statements.

The City's general and revenue obligations maintain an AA- and A- rating respectively from Standard & Poor's and an A2 and A3 rating respectively from Moody's Investors Service. The recent upgrade of the City's general obligation bonds by Standard & Poor's boasts well for The Colony. It speaks well of the City's proactive approach to economic development and financial management.

State Statutes limit the amount of general obligation debt, a governmental entity may issue to \$2.50 per \$100 of its total assessed valuation. The current debt limitation for the City is \$50,156,188, which is in excess of the City's outstanding general obligation debt. The revenue supported debt in the Utility Fund is limited to the net revenues equaling to at least 1.10 times the maximum annual principal and interest requirements and 1.25 times the average annual principal and interest requirements of all parity bonds to be outstanding. The net revenues in the Utility Fund are higher than the required limitations and are monitored each year for appropriate coverage.

Economic Factors and Next Year's Budgets and Rates

- As of December 2008, the unemployment rate for the City is at 5.3 percent, which is an increase from a rate of 3.8 percent a year ago. The City's unemployment rate is better than the state's average unemployment rate at 5.6 percent and the national average rate at 7.1 percent.
- Ad valorem tax base also increased by \$127,504,764 for 2008-2009.
- Total sales tax is projected to increase by \$187,616 due to the growth of retail sales.
- Franchise fees are budgeted to grow by \$182,616 because of increase in households and commercial establishments.
- Fines and forfeitures will increase by \$180,505 due to increase in citations with more patrol officers on the street.
- Licenses and Permits in the General Fund were projected to decrease by \$631,514 due to the global and regional downturn of the economy.
- Transfers from other funds to General Fund are budgeted at \$211,458 higher than 2007-2008.

The state of Texas and The Colony fare better than the national economy. The recession was started by the housing and financial crisis and has spread globally. The City is monitoring its revenues and expenditures carefully to avoid a significant reduction in fund balances. All of these factors were considered in preparing the City's budget for the 2008-2009 fiscal year.

**CITY OF THE COLONY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED SEPTEMBER 30, 2008**

During the current fiscal year, unreserved and undesignated fund balance in the general fund increased to \$6,252,576. There is a designation of \$140,000 to cover the Hidden Cove Park deficit. The City has also appropriated \$303,401 in encumbrances for spending in the 2008-2009 fiscal year budget. Due to the growth in revenues, tax rate for 2008-2009 was reduced by .75 cents.

The Council approved a 6.75 percent increase in the water and sewer rates for all customers effective October 1, 2008. The rate increase is necessary to finance debt service on new debts to improve the aging water and sewer infrastructure and to provide enough revenues to meet increasing costs. Such improvements to the City's water and wastewater infrastructure will position the city to meet its population growth.

Requests for Information

This financial report is designed to provide a general overview of the City's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Finance Director, The City of The Colony, 6800 Main Street, The Colony, Texas 75056.