
AUDIT REPORT

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

MONTGOMERY COUNTY, TEXAS

DECEMBER 31, 2012

CONTENTS

INDEPENDENT AUDITORS' REPORT

MANAGEMENT'S DISCUSSION AND ANALYSIS

STATEMENT OF NET POSITION AND GOVERNMENTAL FUNDS BALANCE SHEET Page 1

RECONCILIATION OF THE BALANCE SHEET TO THE STATEMENT OF NET POSITION GOVERNMENTAL FUNDS Page 2

STATEMENT OF ACTIVITIES AND GOVERNMENTAL FUNDS REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE Page 3

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES GOVERNMENTAL FUNDS Page 4

NOTES TO FINANCIAL STATEMENTS INCLUDING NOTES REQUIRED BY TEXAS COMMISSION ON ENVIRONMENTAL QUALITY Pages 5-18

REQUIRED SUPPLEMENTARY INFORMATION

BUDGETARY COMPARISON SCHEDULE – GENERAL FUND Page 19

TEXAS SUPPLEMENTARY INFORMATION

SERVICES AND RATES Pages 20-20b

SCHEDULE OF GENERAL FUND EXPENDITURES Page 21

SCHEDULE OF TEMPORARY INVESTMENTS Page 22

TAXES LEVIED AND RECEIVABLE Pages 23-23a

GENERAL LONG-TERM DEBT SERVICE REQUIREMENTS - BY YEARS Pages 24-24a

ANALYSIS OF CHANGES IN GENERAL LONG-TERM DEBT Page 25

COMPARATIVE STATEMENT OF REVENUES AND EXPENDITURES - GENERAL AND DEBT SERVICE FUNDS Page 26

BOARD MEMBERS, KEY ADMINISTRATIVE PERSONNEL AND CONSULTANTS Pages 27-27a

April 24, 2013

INDEPENDENT AUDITOR'S REPORT

Board of Directors
Montgomery County Utility District No. 4
Montgomery County, Texas

We have audited the financial statements of the governmental activities, the General Fund, the Debt Service Fund, the Capital Projects Fund and remaining fund information, which collectively comprise the basic financial statements of the Montgomery County Utility District No. 4, Montgomery County, Texas, as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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



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

Opinion

In our opinion, the financial statements referred to above, present fairly, in all material respects, the respective financial position of the governmental activities, the General Fund, the Debt Service Fund, the Capital Projects Fund and remaining fund information of Montgomery County Utility District No. 4 as of December 31, 2012, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplemental Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the District's basic financial statements. The accompanying supplemental information as listed in the table of contents is presented for purposes of additional analysis and is required by the Texas Commission on Environmental Quality and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied by us in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects, in relation to the basic financial statements taken as a whole.


DAVID L. MERRITT, P.C.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Using this Annual Report

Within this section of the Montgomery County Utility District No. 4 (the "District") annual report, the District's Board of Directors provides narrative discussion and analysis of the financial activities of the District for the year ended December 31, 2012.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements are comprised of three components: 1) Government-Wide Financial Statements; 2) Fund Financial Statements, and 3) Notes to Financial Statements. This report also contains supplementary information required by the Governmental Accounting Standards Board and other supplementary information required by the District's state oversight agency, the Texas Commission on Environmental Quality.

In accordance with required reporting standards, the District reports its financial activities as a special-purpose government. Special-purpose governments are governmental entities which engage in a single governmental program, such as the provision of water, sanitary sewer, and drainage services. The financial statements of special-purpose governments combine two types of financial statements into one statement. These two types of financial statements are the government-wide financial statements and the fund financial statements. The fund financial statements are presented on the left side of the statements, a column for adjustments is to the right of the fund financial statements, and the government-wide financial statements are presented to the right side of the adjustments column. The following sections describe the measurement focus of the two types of statements and the significant differences in the information they provide.

Government-Wide Financial Statements

The focus of government-wide financial statements is on the overall financial position and activities of the District. The District's government-wide financial statements include the statement of net position and statement of activities, which are prepared using accounting principles that are similar to commercial enterprises. The purpose of the statement of net position is to attempt to report all of the assets owned by and liabilities of the District. The District reports all of its assets when it acquires or begins to maintain the assets and reports all of its liabilities when they are incurred.

The difference between the District's total assets and total liabilities is labeled as net position and this difference is similar to the total owner's equity presented by a commercial enterprise.

The purpose of the statement of activities is to present the revenues and expenses of the District. Again, the items presented on the statement of activities are measured in a manner similar to the approach used by a commercial enterprise in that revenues are recognized when earned or established criteria are satisfied and expenses are reported when incurred by the District. All changes in net position are reported when the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues are reported even when they may not be collected for several months or years after the end of the accounting period and expenses are recorded even though they may not have used cash during the current period.

Although the statement of activities looks different from a commercial enterprise's income statement, the financial statement is different only in format, not substance. Whereas the bottom line in a commercial enterprise is its net income, the District reports an amount described as change in net position.

Fund Financial Statements

Unlike government-wide financial statements, the focus of fund financial statements is directed to specific activities of the District rather than the District as a whole. Except for the general fund, a specific fund is established to satisfy managerial control over resources or to satisfy finance-related legal requirements established by external parties or governmental statutes or regulations.

Governmental Fund financial statements consist of a balance sheet and statement of revenues, expenditures and changes in fund balances and are prepared on an accounting basis that is significantly different from that used to prepare the government-wide financial statements.

In general, these financial statements have a short-term emphasis and, for the most part, measure and account for cash and other assets that can easily be converted into cash. For example, amounts reported on the balance sheet include items such as cash and receivables collectible within a very short period of time, but do not include capital assets such as land utility systems. Fund liabilities include amounts that are to be paid within a very short period after the end of the fiscal year. The difference between a fund's total assets and total liabilities is labeled the fund balance, and generally indicates the amount that can be used to finance the next fiscal year's activities. Likewise, the operating statement for governmental funds reports only those revenues and expenditures that were collected in cash or paid with cash, respectively, during the current period or very shortly after the end of the fiscal year.

Because the focus of the government-wide and fund financial statements are different, there are significant differences between the totals presented in these financial statements. For this reason, there is an analysis in the financial statements that reconciles the total fund balances to the amount of net position presented in the governmental activities column on the statement of net position. Also, there is an analysis in the financial statements that reconciles the total change in fund balances for all governmental funds to the change in net position as reported in the governmental activities column in the statement of activities.

Notes to Financial Statements

The notes to financial statements provide additional information that is essential to a full understanding of the data found in the government-wide and fund financial statements.

Financial Analysis of the District as a Whole

The District's overall financial position and operations for the past year is summarized as follows based on the information included in the government-wide financial statements.

Summary of Net Position

	<u>2012</u>	<u>2011</u>
<i>Current and other assets</i>	\$ 8,524,279	\$ 10,563,125
<i>Capital assets</i>	<u>6,144,433</u>	<u>4,054,799</u>
<i>Total assets</i>	<u>14,668,712</u>	<u>14,617,924</u>
<i>Long-term liabilities</i>	5,755,000	6,550,000
<i>Other liabilities</i>	<u>986,278</u>	<u>409,390</u>
<i>Total liabilities</i>	<u>6,741,278</u>	<u>6,959,390</u>
<i>Net position:</i>		
<i>Invested in capital assets, net of related debt</i>	2,909,194	1,849,080
<i>Restricted</i>	1,072,336	1,990,739
<i>Unrestricted</i>	<u>3,945,904</u>	<u>3,818,715</u>
<i>Total net position</i>	<u>\$ 7,927,434</u>	<u>\$ 7,658,534</u>

The total net position of the District increased by \$591,633. Although the District'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 be used to liquidate these liabilities.

Summary of Changes in Net Position

Revenues:	<u>2012</u>	<u>2011</u>
<i>Property taxes</i>	\$ 1,517,213	\$ 3,603,103
<i>Charges for services</i>	1,216,322	1,889,876
<i>Other revenues</i>	<u>115,696</u>	<u>125,741</u>
<i>Total revenues</i>	2,849,231	5,618,720
<i>Expenses for services</i>	<u>2,364,180</u>	<u>2,841,078</u>
<i>Change in net position before extraordinary items</i>	485,051	2,777,642
<i>Property Settlement</i>	109,653	
<i>Capital Contributions</i>		90,000
<i>Voided Checks for Prior Years Expenditures</i>	19,102	
<i>Refund of Prior Years Taxes</i>	<u>(22,173)</u>	<u>(7,139)</u>
<i>Net position, beginning of year</i>	7,658,534	4,798,031
<i>Prior period adjustment</i>	<u>(322,733)</u>	
<i>Net position, end of year</i>	<u>\$ 7,927,434</u>	<u>\$ 7,658,534</u>

Financial Analysis of the District's Funds

The District's combined fund balances as of December 31, 2012 were \$5,656,291 a decrease of \$2,327,862 from prior years.

The General Fund balance decreased by \$103,708, as a result of capital outlay expenditures.

The Debt Service Fund balance decreased by \$425,175.

The Capital Projects Fund decreased by \$1,798,979, as a result of capital outlay expenditures.

General Fund Budgetary Highlights

The Board of Directors did not amend the budget during the fiscal year. The original budget adopted by the Board of Directors anticipated an increase in the fund balance during the year ended December 31, 2012 of \$347,742. There were several differences between the budgeted and actual amounts. The major difference was between budgeted expenditures of \$2,012,118 and the actual amount of \$2,342,411. The anticipated budgetary fund balance as of December 31, 2012 was expected to be \$3,421,886 and the actual year ended fund balance was \$2,970,436.

Capital Assets and Related Debt

Capital Assets

Capital assets held by the District at the end of the current and previous fiscal year are summarized as follows:

Capital Assets (Net of Accumulated Depreciation)

	<u>2012</u>	<u>2011</u>
Land and easements	\$ 41,572	\$ 41,572
Water facilities	3,016,555	2,725,825
Sewer facilities	<u>3,086,306</u>	<u>1,287,402</u>
Totals	<u>\$ 6,144,433</u>	<u>\$ 4,054,799</u>

During the current year, the additions to capital assets were as follows:

Water improvements paid for with General Fund resources	\$ 524,648
Sewer improvements paid for with Series 2011 bond proceeds	<u>1,757,437</u>
Total additions to capital assets	<u>\$ 2,282,085</u>

Debt

The changes in the debt position of the District during the year ended December 31, 2012 are summarized as follows:

Bonded debt payable, January 1, 2012	\$ 6,550,000
Bond principal paid	<u>(795,000)</u>
Bonded debt payable, December 31, 2012	<u>\$ 5,755,000</u>

At December 31, 2012, the District has \$21,000,000 unlimited revenue and tax bonds authorized but unissued for the purposes of acquiring, constructing and improving the water, sanitary sewer and drainage system within the District and \$5,228,683 refunding purpose only bonds authorized but unissued.

The District's Series 2004 or refunding purposes bonds were sold with an insured rating of "AAA" by virtue of bond insurance issued by Ambac Assurance Corporation ("AMBAC"). As of November 10, 2010, S&P withdrew its rating of AMBAC. Once AMBAC's rating was reduced to below the District's underlying rating, the bond rating became the underlying rating of "A+". The Series 2011 bonds were sold with an insured rating by Assured Guaranty Municipal Corp. (AGMC) of "AA+". On November 30, 2011, AGMC's rating was downgraded to "AA-".

OTHER RELEVANT FACTORS

Relationship to the City of Conroe

Under existing Texas law, since the District lies wholly within the extraterritorial jurisdiction of the City of Conroe, the District must conform to a City of Conroe ordinance consenting to the creation of the District. In addition, the District may be annexed by the City of Conroe without the District's consent. If the District is annexed, the City will assume the District's assets and obligations (including the bonded indebtedness) and dissolve the District within ninety (90) days.

The District received the City of Conroe's notice regarding annexation on February 20, 2012. On February 22, 2013, the District entered into a Strategic Partnership Agreement ("SPA") with the City of Conroe, Texas (the "City") pursuant to Texas Local Government Code, Section 43.0751, which SPA provides for: (1) annexation of the territory of the District by the City for full purposes effective December 31, 2014; (2) continuation of the District, after annexation, as a "limited district" with powers and functions provided by law, including water, wastewater, storm sewer, and solid waste services, and also including the power to levy taxes and collect user fees; (3) provision of fire, police, and other municipal services by the City; (4) payments by the City to the District, including payments to defray debt service related to the Bonds; (5) binding each owner and future owners of land included within the territory of the District; and (6) other matters.

OTHER

The District does not foresee any significant changes in the property tax base during the year ending December 31, 2013.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide a general overview of the Montgomery County Utility District No. 4's finances for anyone with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to Montgomery County Utility District No. 4, c/o Coats, Rose, Yale, Ryman & Lee, P.C., 3 E. Greenway Plaza, Suite 2000, Houston, Tx 77046.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**STATEMENT OF NET POSITION AND GOVERNMENTAL FUNDS BALANCE SHEET
DECEMBER 31, 2012**

ASSETS

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Capital Projects Fund</u>	<u>Total</u>
Cash & Investments (Note 3)	\$ 1,664,808	\$ 853,126	\$ 3,783,110	\$ 6,301,044
Taxes Receivable	462,014	341,643		803,657
Other Receivables (Note 4)	222,389			222,389
Joint Venture Investment (Note 10)	11,570			11,570
Prepayments	21,747		47,810	69,557
Internal Receivables	1,482,032			1,482,032
Accrued Interest Receivable	4,752			4,752
Deferred Charges				
Capital Assets (net of accumulated depreciation): (Note 8)				
Land				
Infrastructure				
TOTAL ASSETS	<u>\$ 3,869,312</u>	<u>\$ 1,194,769</u>	<u>\$ 3,830,920</u>	<u>\$ 8,895,001</u>

LIABILITIES

Accounts Payable (Note 4)	\$ 219,738	\$	\$ 516,159	\$ 735,897
Customer Deposits	117,563			117,563
Accrued Interest Payable				
Deferred Revenues	561,575	341,643		903,218
Internal Payables		1,357,302	124,730	1,482,032
Long-term Liabilities: (Note 5)				
Due within one year				
Due after one year				
Total Liabilities	<u>898,876</u>	<u>1,698,945</u>	<u>640,889</u>	<u>3,238,710</u>

FUND BALANCE/NET POSITION

Fund Balances:				
Nonspendable	21,747			21,747
Committed	337,301			337,301
Restricted		853,126	3,190,031	4,043,157
Unassigned	2,611,388	(1,357,302)		1,254,086
Total Fund Balances	<u>2,970,436</u>	<u>(504,176)</u>	<u>3,190,031</u>	<u>5,656,291</u>
TOTAL LIABILITIES AND FUND EQUITY	<u>\$ 3,869,312</u>	<u>\$ 1,194,769</u>	<u>\$ 3,830,920</u>	<u>\$ 8,895,001</u>

Net Position:

Invested in Capital Assets, net of related debt	
Restricted for Debt Service	
Unrestricted	
Total Net Position	

<u>Adjust- ments</u>	<u>Statement of Net Position</u>
\$	\$
	6,301,044
10,385	814,042
	222,389
1,100,925	1,112,495
	69,557
(1,482,032)	-
	4,752
	-
41,572	41,572
6,102,861	6,102,861
<u>5,773,711</u>	<u>14,668,712</u>
	735,897
	117,563
132,818	132,818
(903,218)	-
(1,482,032)	-
200,000	200,000
5,555,000	5,555,000
<u>3,502,568</u>	<u>6,741,278</u>
(21,747)	-
(337,301)	-
(4,043,157)	-
(1,254,086)	-
<u>(5,656,291)</u>	<u>-</u>
2,909,194	2,909,194
1,072,336	1,072,336
3,945,904	3,945,904
<u>\$ 7,927,434</u>	<u>\$ 7,927,434</u>

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

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

RECONCILIATION OF THE BALANCE SHEET
TO THE STATEMENT OF NET POSITION
GOVERNMENTAL FUNDS
AS OF DECEMBER 31, 2012

Fund balances - total governmental funds \$ 5,656,291

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

Capital assets used in governmental activities are not financial resources and therefore are not reported in the governmental funds.

Joint Venture Investment	\$ 1,100,925	
Governmental capital assets	8,791,118	
Less accumulated depreciation	<u>(2,646,685)</u>	7,245,358

Long-term liabilities, including bonds payable are not due and payable in the current period and therefore are not reported in the governmental funds.

Governmental bonds payable	(5,755,000)	
Interest Payable	<u>(132,818)</u>	(5,887,818)

Deferred revenue and penalty and interest in governmental funds are susceptible to full accrual on the entity-wide statements.

Penalty and Interest Receivable	10,385	
Deferred Revenue	<u>903,218</u>	<u>913,603</u>

Net position of governmental activities \$ 7,927,434

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**STATEMENT OF ACTIVITIES AND GOVERNMENTAL FUNDS REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCES
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Capital Projects Fund</u>	<u>Total</u>
Revenues:				
Charges for Water Service	\$ 611,419	\$	\$	\$ 611,419
Charges for Sewer Service	604,903			604,903
Property Taxes (Note 5)	850,818	681,073		1,531,891
Tap Connection and Inspection Fees	44,070			44,070
Covenant Revenue (Note 12)	5,210			5,210
Investment Earnings	8,157	394	9,288	17,839
Penalties and Interest	11,893	4,074		15,967
Other	14,753			14,753
TOTAL REVENUES	<u>2,151,223</u>	<u>685,541</u>	<u>9,288</u>	<u>2,846,052</u>
Expenditures/Expenses:				
Service Operations:				
Water Service	365,773			365,773
Sewer Service	584,901			584,901
Purchased Services	192,536			192,536
Contracted Services	119,454	12,527		131,981
Professional Fees	305,602			305,602
Director Fees	22,800			22,800
Other	226,697	1,335	50,830	278,862
Capital Outlay	524,648		1,757,437	2,282,085
Debt Service:				
Principal		795,000		795,000
Interest		320,956		320,956
Depreciation (Note 8)				
Total Expenditures/Expenses	<u>2,342,411</u>	<u>1,129,818</u>	<u>1,808,267</u>	<u>5,280,496</u>
Deficiency of Revenues Over Expenditures	(191,188)	(444,277)	(1,798,979)	(2,434,444)
Other Financing Sources/Uses:				
Refund of Prior Years Taxes	(22,173)			(22,173)
Voided Checks for Prior Years Expenditures		19,102		19,102
Property Settlement	109,653			109,653
Deficiency of Revenues and Other Financing Sources/Uses Over Expenditures	(103,708)	(425,175)	(1,798,979)	(2,327,862)
Change in Net Position				
Fund Balance/Net Position:				
January 1, 2012	3,074,144	(79,001)	4,989,010	7,984,153
Prior Period Adjustment (Note 17)				
December 31, 2012	<u>\$ 2,970,436</u>	<u>\$ (504,176)</u>	<u>\$ 3,190,031</u>	<u>\$ 5,656,291</u>

<u>Adjust- ments</u>	<u>Statement of Activities</u>
\$	\$
	611,419
	604,903
(14,678)	1,517,213
	44,070
8,470	13,680
	17,839
9,387	25,354
	14,753
<u>3,179</u>	<u>2,849,231</u>
	365,773
	584,901
	192,536
	131,981
	305,602
	22,800
	278,862
(2,282,085)	-
(795,000)	-
(31,682)	289,274
192,451	192,451
<u>(2,916,316)</u>	<u>2,364,180</u>
2,919,495	
22,173	(22,173)
(19,102)	19,102
(109,653)	109,653
2,327,862	
485,051	485,051
(325,619)	7,658,534
	(322,733)
<u>\$ 2,271,143</u>	<u>\$ 7,927,434</u>

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

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012

Net change in fund balances - total governmental funds \$ (2,327,862)

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 is depreciated over their estimated useful lives.

Expenditures for capital assets	\$ 2,282,085	
Less current year depreciation	<u>(192,451)</u>	2,089,634

Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net position. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net position. This is the amount by which proceeds exceeded repayments.

Principal Payments		795,000
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Some revenues reported in the statement of activities do not provide current financial resources and therefore are not reported as revenues in governmental funds.

Voided Checks for Prior Years Expenditures	(19,102)	
Property Settlement	(109,653)	
Standby Revenue	8,470	
Tax Revenue	7,495	
Penalty and Interest	<u>9,387</u>	(103,403)

Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds.

Interest Expense		<u>31,682</u>
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Change in net position of governmental activities		\$ <u><u>485,051</u></u>
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The accompanying notes are an integral part of the financial statements.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2012

NOTE 1. CREATION OF DISTRICT

Montgomery County Utility District No. 4 (the "District") was created by an Act of the 62nd Legislature of the State of Texas, Regular Session, 1971, in accordance with the Texas Water Code, Chapter 54. The District consolidated with Montgomery County Utility District No. 23 pursuant to a consolidation agreement effective February 27, 1978. The Board of Directors held its first meeting on June 6, 1972, and the first bonds were sold on September 7, 1978. The District is empowered, among other things, to purchase, to construct, to operate, and to maintain all works, improvements and facilities necessary for the supply of water, for the collection and processing of wastewater, and for the control and diversion of storm water. The District also contracts for garbage service.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The District's financial statements are prepared in accordance with generally accepted accounting principles generally accepted in the United States of America. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements. In addition, the accounting records of the District are maintained generally in accordance with the Water District Financial Management Guide published by the Commission. The more significant accounting policies established in GAAP and used by the District are discussed below.

GASB Statement No. 34 established standards for external financial reporting for all state and local government entities, which include a requirement for a Statement of Net Position and a Statement of Activities. It requires the classification of net position into three components: Invested in Capital Assets, Net of Related Debt; Restricted; and Unrestricted. These classifications are defined as follows:

Invested in Capital Assets, Net of Related Debt – This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvements of those assets.

Restricted Assets – This component of net position consists of external constraints placed on the use of net position imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulation of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted Net Position – This component of net position consists of net position that do not meet the definition of "Restricted" or "Invested in Capital Assets, Net of Related Debt."

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

When both restricted and unrestricted (i.e., Committed, Assigned and Unassigned) resources are available for use, generally it is the District's policy to use restricted resources first.

Reporting Entity

In evaluating how to define the District, for financial reporting purposes, the Board of Directors has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the criteria set forth in GAAP. The basic, but not the only, criterion for including a potential component unit within the reporting entity is the governing body's ability to exercise oversight responsibility. The most significant manifestation of this ability is financial interdependency. Other manifestations of the ability to exercise oversight responsibility include, but are not limited to, the selection of governing authority, the designation of management, the ability to significantly influence operations and accountability for fiscal matters. The other criterion used to evaluate potential component units for inclusion or exclusion from the reporting entity is the existence of special financing relationships, regardless of whether the District is able to exercise oversight responsibilities. The District is a participant in a joint venture as more fully described in Note 10. No other entities exist that should be considered for inclusion as a component unit. Complete financial statements for the Plant may be obtained from BKD, LLP, 2800 Post Oak Blvd #2600, Houston, Texas 77056.

Basic Financial Statements – Government-Wide Statements

The District's basic financial statements include both government-wide (reporting the District as a whole) and fund financial statements (reporting the District's major funds). The District's water and sewer services are classified as governmental-type activities.

In the government-wide Statement of Net Position, the governmental activities columns are presented on a consolidated basis by column and are reported on a full accrual, economic resource basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations. The District's net position is reported in three parts – invested in capital assets, net of related debt; restricted net position; and unrestricted net position.

The government-wide Statement of Activities reports each of the District's general government revenues. The Statement of Activities reduces gross revenues by direct function expenses.

The District does not allocate indirect costs.

This government-wide focus is more on the sustainability of the District as an entity and the change in the District's net position resulting from the current year's activities.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Basic Financial Statements – Fund Financial Statements

The financial transactions of the District are reported in individual funds in the fund financial statements. Each fund is accounted for by providing a separate set of self-balancing accounts that comprises its assets, liabilities, reserves, fund equity, revenues and expenditures/expenses. The various funds are reported by generic classification within the financial statements.

The following types are used by the District:

Governmental Funds

The focus of the governmental funds' measurement is upon determination of financial position and changes in financial position rather than upon net income. The following is a description of the governmental funds of the District:

General Funds should be used to account for and report all financial resources not accounted for and reported in another fund.

Debt Service Funds are used to account for and report financial resources that are restricted, committed, or assigned to expenditure for general government debt principal and interest.

Capital Project Funds are used to account for and report financial resources that are restricted, committed, or assigned to expenditure for capital outlays, including acquisition or construction of capital assets.

Basis of Accounting

Basis of accounting refers to the point at which revenues or expenditures/expenses are recognized in the accounts and reported in the financial statements. It relates to the timing of the measurements made regardless of the measurement focus applied.

Accrual

The governmental activities in the government-wide financial statements are presented on the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred.

Modified Accrual

The governmental funds financial statements are presented on the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recorded when susceptible to accrual; i.e., both measurable and

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012**

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Basis of Accounting (continued)

Modified Accrual (continued)

available. "Available" means collectible within the current period or within 60 days after year end. Expenditures are generally recognized under the modified accrual basis of accounting when the related liability is incurred. The exception to this general rule is that principal and interest on general obligation long-term debt, if any, is recognized when due.

Measurement Focus

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

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

Fund Balance Classifications

GASB Statement 54, Fund Balance Reporting and Governmental Fund – Type Definitions, requires the classification of fund balances in governmental funds using the following hierarchy:

Nonspendable Fund Balance includes portion of net resources that cannot be spent because of their form or because they must be maintained intact. Resources not in spendable form include supplies, inventories, prepaid items, long-term advances to other funds, net of deferred interest revenue, long-term receivable, net of deferred interest revenue, nonfinancial assets held for resale, and unrealized change in the fair value of investments.

Restricted Fund Balance includes net resources that can be spent only for the specific purposes stipulated by constitution, external resource provides (creditors, grantors, contributors), laws and regulations of other governments, or through enabling legislation.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Basis of Accounting (continued)

Fund Balance Classifications (continued)

Committed Fund Balance includes spendable net resources that can only be used for specific purposes pursuant to constraints imposed by formal Council actions, no later than the close of the fiscal year. Those constraints remain binding unless removed or changed in the same manner employed to previously commit those resources.

Unassigned Fund Balance represents spendable net resources that have not been restricted, committed, or assigned to specific purposes.

Capital Assets

Capital assets purchased or acquired with an original cost of \$5,000 or more are reported at historical cost or estimated historical cost. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. Depreciation on all assets is provided on the straight-line basis over the following estimated useful lives:

Buildings	40 Years
Water and sewer system	10-45 Years
Machinery and equipment	5-20 Years

Revenues

Substantially all governmental fund revenues are accrued. Property tax revenues are recognized in the year for which they are levied.

Expenditures

Expenditures are recognized when the related fund liability is incurred.

Internal Activity

Amounts transferred from one fund to another fund are reported as other financing sources or uses. Loans by one fund to another fund and amounts paid by one fund for another fund are reported as interfund receivables and payables in the Governmental Funds Balance Sheet if there is intent to repay the amount and if the debtor fund has the ability to repay the advance on a timely basis. In general, the amounts shown are unremitted Maintenance Tax collections, overpaid Maintenance Tax collections and/or Capital Outlay expenditures.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Budget

The Board of Directors adopts an annual nonappropriated budget for the General Fund in accordance with the accounting principles applicable to that Fund. During the current year, the budget was not amended.

Pension Plan

The District has no employees, therefore, it has no current year contribution obligations. Effective January 1, 2000, the Internal Revenue Service determined that directors are considered to be "employees" for federal payroll purposes only.

Subsequent Events

In preparing these financial statements, management has evaluated and disclosed all material subsequent events through April 24, 2013; which is the date these statements were available to be issued.

Accounting Estimates

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

NOTE 3. CASH AND INVESTMENTS

Texas statutes include specifications for and limitations applicable to the District and its authority to purchase investments as defined in the Public Funds Investment Act. Authorized investments are summarized as follows: (1) obligations of the United States or its instrumentalities, (2) direct obligations of the State of Texas or its agencies, (3) certain collateralized mortgage obligations (4) other obligations, the principal of and interest on which are unconditionally guaranteed or insured by the State of Texas or the United States or its agencies and instrumentalities, (5) certain A rated or higher obligations of states, agencies, counties, cities, and other political subdivisions of any state, (6) bonds insured, assumed or guaranteed by the State of Israel, (7) insured or collateralized certificates of deposit, (8) certain fully collateralized repurchase agreements secured by delivery, (9) certain banker's acceptances with limitations, (10) commercial paper rated A-1 or P-1 or higher and a maturity of 270 days or less, (11) no load money market mutual funds and no-load mutual funds with limitations, (12) certain guaranteed investment contracts, (13) certain qualified governmental investment pools and (14) a qualified securities lending program.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 3. CASH AND INVESTMENTS (continued)

Under Texas law, the District is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity and that address investment diversification, yield, maturity, and the quality and capability of investment management, and all District funds must be invested in accordance with the following investment objectives: understanding the suitability of the investment to the District's financial requirements, first; preservation and safety of principal, second; liquidity, third; marketability of the investments if the need arises to liquidate the investment before maturity, fourth; diversification of the investment portfolio, fifth; and yield, sixth. The District's investments must be made "with judgment and care, under prevailing circumstances, that a person of prudence, discretion, and intelligence would exercise in the management of the person's own affairs, not for speculation, but for investment, considering the probable safety of capital and the probable income to be derived." No person may invest District funds without express written authority from the Board of Directors.

The Public Funds Investment Act, Chapter 2256, Government Code includes a requirement for the District's auditor to perform a compliance audit of the District's compliance with its adopted investment policy. Based upon a test for compliance, the District's auditor acknowledges that the District has substantially complied with the provisions of the investment policy.

	<u>ASSETS AT COST</u>		<u>FAIR VALUE</u>
	<u>Cash and Cash</u>		<u>Combined</u>
	<u>Equivalents</u>	<u>Investments</u>	
GENERAL FUND			
Demand Deposits, Money Market Deposit Accounts and Savings Account	\$ 70,061	\$	\$ 70,061
TexPool		54,747	54,747
Certificates of Deposit		1,540,000	1,540,000
DEBT SERVICE FUND			
(Restricted for Servicing of Bonded Debt)			
Demand Deposits, Money Market Deposit Accounts and Savings Account	658,073		658,073
TexPool		195,053	195,053
CAPITAL PROJECTS FUND			
(Restricted for Purchasing of Fixed Assets)			
Demand Deposits, Money Market Deposit Accounts and Savings Account	3,783,110		3,783,110
TOTALS	<u>\$ 4,511,244</u>	<u>\$ 1,789,800</u>	<u>\$ 6,301,044</u>

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 3. CASH AND INVESTMENTS (continued)

Investments are reflected at cost, which the District considers to be fair value. The District invests in TexPool, an external investment pool that is not SEC-registered. The State Comptroller of Public Accounts of the State of Texas has oversight of TexPool. Federated Investors manage the daily operations of this pool under a contract with the Controller. TexPool has a rating of AAAM by Standard & Poors. The fair value of the District's position in the pool is the same as the value of pool shares.

The District's Investment Policy requires risk assessment in compliance with the provisions of Texas Statutes.

The District invests short-term to avoid any interest rate risks and there is no credit risk based upon the Standard & Poors rating.

Texas statutes require that any cash balance in any fund shall to the extent not insured by the Federal Deposit Insurance Corporation or its successor be continuously secured by a valid pledge to the District of securities eligible under the laws of Texas to secure the funds of municipal utility districts, having an aggregate market value, including accrued interest, at all times equal to the uninsured cash balance in the fund to which such securities are pledged. At the fiscal year end the carrying amount of the District's bank deposits was \$4,511,244 and the bank balances were \$4,405,154. Of the bank balances, \$568,346 were covered by federal depository insurance and the balance was covered by pledged securities held by a third party.

The District's policy is to require depositories to pledge adequate collateral to secure the District's deposits at all times to the extent that the District's depository balances exceed the limits of federal depository insurance. As of the highest cash balance date of each depository exceeding federal depository insurance, each depository did pledge adequate collateral to secure the deposits of the District. The entities pledging the collateral provided the information concerning market value.

NOTE 4. DISAGGREGATION OF RECEIVABLES AND PAYABLE BALANCES

Receivables

Receivables at December 31, 2012, were as follows:

	<u>Accounts</u>	<u>Standby</u>	<u>Total Receivables</u>
Governmental activities:			
General	\$ 122,828	\$ 99,561	\$ 222,389
Total – governmental activities	\$ 122,828	\$ 99,561	\$ 222,389

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 4. DISAGGREGATION OF RECEIVABLES AND PAYABLE BALANCES
(continued)

Payables

Payables at December 31, 2012, were as follows:

	<u>Vendors</u>	<u>Total Payables</u>
Governmental activities:		
General	\$ 219,738	\$ 219,738
Capital Projects	<u>516,159</u>	<u>516,159</u>
Total-governmental activities	\$ <u>735,897</u>	\$ <u>735,897</u>

NOTE 5. BONDS PAYABLE

Bonded debt activity for the current year is as follows:

	<u>Balance January 1, 2012</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance December 31, 2012</u>	<u>Amounts Due within One Year</u>
Governmental Activities:					
Bonds Payable:					
Series 2004	\$ 795,000	\$ -	\$ 795,000	\$ -	\$ -
Series 2011	<u>5,755,000</u>	<u>-</u>	<u>-</u>	<u>5,755,000</u>	<u>200,000</u>
Total Bonds Payable	\$ <u>6,550,000</u>	\$ <u>-</u>	\$ <u>795,000</u>	\$ <u>5,755,000</u>	\$ <u>200,000</u>

The outstanding bonds of Montgomery County Utility District No. 4, Montgomery County, Texas, are callable for redemption prior to maturity at the option of the District. The bonds may be called in whole or in part for the purpose of retirement or refunding, or both, at par in addition to unpaid accrued interest. Series 2011 bonds may be called on March 1, 2019, or any date thereafter at a price equal to the par value thereof, plus accrued interest to date of redemption.

Bonds Voted	\$56,160,000	Refunding Bonds Approved	\$14,160,000
Bonds Approved For Sale	14,160,000	Refunding Bonds Sold	8,931,317
Bonds Sold	14,160,000		

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012**

NOTE 5. BONDS PAYABLE (continued)

Bonds outstanding as of December 31, 2012 are as follows:

	<u>Interest Rate</u>	<u>Amount</u>	<u>Amount Outstanding January 1, 2012</u>	<u>Issued</u>	<u>Retired</u>	<u>Amount Outstanding December 31, 2012</u>
Unlimited Tax Refunding Bonds:						
	2.00% to					
Series 2004	3.50%	\$ 5,745,000	\$ 795,000	\$ -	\$ 795,000	\$ -
Unlimited Tax Bonds:						
	3.00% to					
Series 2011	5.50%	5,755,000	<u>5,755,000</u>	<u>-</u>	<u>-</u>	<u>5,755,000</u>
			<u>\$ 6,550,000</u>	<u>\$ -</u>	<u>\$ 795,000</u>	<u>\$ 5,755,000</u>

As of December 31, 2012, the Debt Service Requirements on bonds outstanding are as follows:

<u>Years</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 200,000	\$ 240,135	\$ 440,135
2014	210,000	228,860	438,860
2015	220,000	217,035	437,035
2016	230,000	204,660	434,660
2017	245,000	191,597	436,597
2018	255,000	177,848	432,848
2019	270,000	163,410	433,410
2020	285,000	151,710	436,710
2021	300,000	142,748	442,748
2022	315,000	132,941	447,941
2023	335,000	121,960	456,960
2024	350,000	109,754	459,754
2025	370,000	96,241	466,241
2026	390,000	81,516	471,516
2027	410,000	65,658	475,658
2028	435,000	48,546	483,546
2029	455,000	30,069	485,069
2030	480,000	10,200	490,200
	<u>\$ 5,755,000</u>	<u>\$ 2,414,888</u>	<u>\$ 8,169,888</u>

The bonds are payable from the proceeds of an ad valorem tax levied upon all property within the District subject to taxation without limitation as to rate or amount, and are further payable from and secured by a lien on and pledge of the net revenues to be received from the operation of the District's waterworks and sanitary sewer system.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012**

NOTE 5. BONDS PAYABLE (continued)

The District appears to be in compliance with the provisions of the Bond Order for each respective Series. At December 31, 2012, the Debt Service Fund had coverage of 1.94.

During the year ended December 31, 2012, the District levied an ad valorem Debt Service Tax at the rate of \$0.2375 per \$100 of assessed valuation, which resulted in a tax levy of \$638,337 of the taxable valuation of \$367,991,295 for the 2012 tax year. The Bond Resolution for the Series 2011 bonds require that the District levy and collect an ad valorem Debt Service Tax sufficient to pay interest and principal on bonds when due and the cost of assessing and collecting taxes.

The District's tax calendar is as follows:

- Lien Date - January 1
- Levy Date - Before the later of September 30 or the 60th day after the receipt of certified appraisal roll
- Due Date - Upon receipt, not later than January 31
- Delinquent Date - February 1, at which time the taxpayer is liable for penalty and interest.

NOTE 6. RESTRICTED CASH AND TEMPORARY INVESTMENTS

The following balances were restricted by the Bond Order as of December 31, 2012:

	<u>Restricted For</u>	
	<u>Servicing of Bonded Debt</u>	<u>Purchasing of Fixed Assets</u>
Cash	\$ 658,073	\$ 3,783,110
Investments	195,054	-
Total	<u>\$ 853,127</u>	<u>\$ 3,783,110</u>

NOTE 7. INSURANCE

In accordance with the Bond Resolution for the Series 2011 Bonds, the District agrees it will at all times keep insured such parts of the System as are usually insured by municipal corporations and political subdivisions in Texas operating like properties in similar locations under the same circumstances with a reasonable insurance company or companies against risk, accidents or casualties against which and to the extent insurance is usually carried by such entities; provided, however, that at any time while any contractor engaged in construction work shall be fully responsible, therefore, the District shall not be required to carry such insurance. At the Balance Sheet date, the facilities were insured for \$4,240,000 with no co-insurance clause.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012**

NOTE 8. CAPITAL ASSETS

Capital asset activity for the current year is as follows:

	<u>Balances January 1, 2012</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balances December 31, 2012</u>
Governmental activities:				
Capital assets not being depreciated				
Land	\$ 41,572	\$ -	\$ -	\$ 41,572
Total capital assets not being depreciated	<u>41,572</u>	<u>-</u>	<u>-</u>	<u>41,572</u>
Capital assets, being depreciated				
Water	4,394,704	524,648		4,919,352
Sewer	<u>2,072,757</u>	<u>1,757,437</u>		<u>3,830,194</u>
Total capital assets being depreciated	<u>6,467,461</u>	<u>2,282,085</u>	<u>-</u>	<u>8,749,546</u>
Less accumulated depreciation for:				
Water and Sewer	<u>(2,454,234)</u>	<u>(192,451)</u>		<u>(2,646,685)</u>
Total accumulated depreciation	<u>(2,454,234)</u>	<u>(192,451)</u>	<u>-</u>	<u>(2,646,685)</u>
Total capital assets, being depreciated, net	<u>4,013,227</u>	<u>2,089,634</u>	<u>-</u>	<u>6,102,861</u>
Governmental activities capital assets, net	\$ <u>4,054,799</u>	\$ <u>2,089,634</u>	\$ <u>-</u>	\$ <u>6,144,433</u>

NOTE 9. MAINTENANCE TAXES

An election held April 1, 1978, authorized a Maintenance Tax not to exceed \$1.00 per \$100 valuation on all property subject to taxation within the District. During the twelve months ended December 31, 2012, the District has levied an ad valorem Maintenance Tax of \$0.1725 per \$100 valuation for the 2012 tax year. This Maintenance Tax was used by the General Fund to pay expenditures of operating the District's waterworks and sanitary sewer system.

NOTE 10. CONTRACT WITH OTHER DISTRICT

On October 22, 1979, the District amended the water supply and sanitary sewer service contract with Montgomery County Utility District No. 3. This contract is for the term of forty years unless either party gives eighteen months notice of termination. The contract calls for a monthly service charge per service connection, subject to yearly modifications for increased operating costs. Effective July 1989, the District's new water well was completed and placed in service, and the monthly purchase of water from District No. 3 was discontinued. In May 1991, the sewage treatment plant expansion was completed and the districts began sharing operating costs. On April 18, 2011, the Districts agreed to commence construction of a new wastewater treatment plant at the shared expense of the Districts.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012**

NOTE 10. CONTRACT WITH OTHER DISTRICT (continued)

The districts jointly own the 700,000 gallons-per-day plant. (As of February 1, 2002, the plant has been expanded to 950,000 gallons-per-day) District No. 3 operates the plant on behalf of the districts. Operating costs are shared based on costs per equivalent connection times the number of equivalent connections in each district. During the current period, the District was billed \$348,466 for its share of operating costs, of which \$56,449 is payable to District No. 3 at December 31, 2012. On April 18, 2011, the District authorized construction of a new plant.

NOTE 11. CONTRACT TO LEASE PREMISES

On September 7, 1995, the District entered into a contract with Rural Fire Prevention District No. 3. This contract is for a term of forty years. Under its terms, the lessee shall use a lot leased from the District as a firefighting and emergency medical services dispatch facility.

NOTE 12. COVENANT FEES

The District is the beneficiary of covenants included in the subdivision's deed restrictions for substantially all subdivided property in the District. These covenants include the imposition of a contractual service availability fee ("Covenant Fee") payable to the District and is secured by a subordinate lien on the subdivided property as provided in the deed restrictions. The District does not assess standby fees as defined in Section 50.056 of the Texas Water Code. These Covenant Fees and associate liens are enforceable in accordance with the terms of the deed restrictions and applicable general law and are not subject to review or approval by the Texas Commission on Environmental Quality. Covenant fees are recorded in revenue as collected.

NOTE 13. RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters for which the District carries commercial insurance. The District has not significantly reduced insurance coverage or had settlements which exceeded coverage amounts for the past three fiscal years.

NOTE 14. CHANGE OF FISCAL YEAR-END

The District was granted the authority to change its year-end from June 30 to December 31 effective July 1, 2010.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012**

NOTE 15. FUND DEFICIT

The \$504,176 deficit in the Debt Service Fund is the result of a reduced tax levy which may require transfers of funds from the General Fund.

NOTE 16. SUBSEQUENT EVENT

On February 22, 2013, the District entered into a Strategic Partnership Agreement (“SPA”) with the City of Conroe, Texas (the “City”) pursuant to Texas Local Government Code, Section 43.0751, which SPA provides for: (1) annexation of the territory of the District by the City for full purposes effective December 31, 2014; (2) continuation of the District, after annexation, as a “limited district” with powers and functions provided by law, including water, wastewater, storm sewer, and solid waste services, and also including the power to levy taxes and collect user fees; (3) provision of fire, police, and other municipal services by the City; (4) payments by the City to the District, including payments to defray debt service related to the Bonds; (5) binding each owner and future owners of land included within the territory of the District; and (6) other matters.

NOTE 17. PRIOR PERIOD ADJUSTMENT

Net Position, December 31, 2011	\$ 7,658,534
GASB 65 Adjustment of Deferred Charges	<u>(322,733)</u>
Net Position, December 31, 2011	<u>\$ 7,335,801</u>

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

REQUIRED SUPPLEMENTARY INFORMATION

DECEMBER 31, 2012

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Actual</u>	<u>Original Budget</u>	<u>Variance - Positive (Negative)</u>
REVENUES:			
Charges for Water Service	\$ 611,419	\$ 714,000	\$ (102,581)
Charges for Sewer Service	604,903	608,040	(3,137)
Property Taxes	850,818	970,000	(119,182)
Tap Connection and Inspection Fees	44,070	17,900	26,170
Covenant Revenue	5,210	6,000	(790)
Investment Earnings	8,157	16,120	(7,963)
Penalties and Interest	11,893	12,300	(407)
Other	14,753	15,500	(747)
Total Revenues	<u>2,151,223</u>	<u>2,359,860</u>	<u>(208,637)</u>
EXPENDITURES/EXPENSES:			
Service Operations:			
Water Service	365,773	347,000	(18,773)
Sewer Service	584,901	408,000	(176,901)
Purchased Services	192,536	192,360	(176)
Contracted Services	119,454	106,200	(13,254)
Professional Fees	305,602	109,200	(196,402)
Director Fees	22,800	24,000	1,200
Other	226,697	310,308	83,611
Capital Outlay	524,648	515,050	(9,598)
Total Expenditures Expenses	<u>2,342,411</u>	<u>2,012,118</u>	<u>(330,293)</u>
Excess (Deficiency) of Revenues over Expenditures	(191,188)	347,742	(538,930)
Other Financing Sources/Uses:			
Refund of Prior Years Taxes	(22,173)		
Property Settlement	109,653		
Net Change in Fund Balance	(103,708)	347,742	(538,930)
Fund Balance:			
January 1, 2012	3,074,144	3,074,144	
December 31, 2012	<u>\$ 2,970,436</u>	<u>\$ 3,421,886</u>	<u>\$ (538,930)</u>

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4
SUPPLEMENTAL INFORMATION REQUIRED BY THE
WATER DISTRICT FINANCIAL MANAGEMENT GUIDE
DECEMBER 31, 2012

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**SERVICES AND RATES
FOR THE YEAR ENDED DECEMBER 31, 2012**

1. Services Provided by the District during the Fiscal Year:

Retail Water Wholesale Water Drainage
 Retail Wastewater Wholesale Wastewater Irrigation
 Parks/Recreation Fire Protection Security
 Solid Waste/Garbage Flood Control Roads
 Participates in joint venture, regional system and/or wastewater service
 (Other than emergency interconnect)
 Other (specify) _____

2. Retail Service Providers

a. Retail Rates Based on 5/8" Meter (or equivalent):

	<u>Minimum Charge</u>	<u>Minimum Usage</u>	<u>Flat Rate Y/N</u>	<u>Rate per 1,000 Gallons Over Minimum</u>	<u>Usage Levels</u>
Water:	\$ <u>11.00</u>	<u>4,000</u>	<u>N</u>	\$ <u>1.35</u>	<u>4,001-10,000</u>
				\$ <u>1.80</u>	<u>10,001-15,000</u>
				\$ <u>2.25</u>	<u>15,001-20,000</u>
				\$ <u>2.75</u>	<u>20,001-25,000</u>
				\$ <u>3.50</u>	<u>25,001-30,000</u>
				\$ <u>5.00</u>	<u>30,001 and over</u>
Waste-Water:	\$ <u>30.00</u>	<u>-</u>	<u>Y</u>	\$ _____	_____
				\$ _____	_____
Surcharge:	\$ <u>.07</u>	<u>1,000</u>	_____	\$ _____	_____

District employs winter averaging for wastewater usage? Yes ___ No X

Total charges per 10,000 gallons usage: Water: \$ 19.80 Wastewater: \$ 30.00

See accompanying auditor's report.

2. Retail Service Providers (continued)

b. Water and Wastewater Retail Connections:

<u>Meter Size</u>	<u>Total Connections</u>	<u>Active Connections</u>
Unmetered		
≤ ¾"	1,419	1,389
1"	56	55
1 ½"	2	2
2"	10	10
3"	2	2
4"	1	1
6"		
8"		
10"		
Total Water	1,490	1,459
Total Wastewater	1,467	1,436

3. Total Water Consumption during the Fiscal Year (rounded to the nearest thousand):

Gallons pumped into system:	<u>337,227</u>	Water Accountability Ratio: (Gallons billed/Gallons pumped)
Gallons billed to customers:	<u>322,072</u>	<u>95.5%</u>

4. Standby Fees: (authorized only under TWC Section 49.231):

Does the District have Debt Service standby fees? Yes ___ No X

If yes, Date of the most recent Commission Order: _____

Does the District have Operation and Maintenance standby fees? Yes ___ No X

If yes, Date of the most recent Commission Order: _____

See accompanying auditor's report.

5. **Location of District:**

County(ies) in which district is located. Montgomery

Is the District located entirely within one county? Yes X No ___

Is the District located within a city? Entirely___ Partly___ Not at all X

City(ies) in which district is located. _____

Is the District located within a city's extra territorial jurisdiction (ETJ)?

Entirely X Partly___ Not at all___

ETJ's in which district is located. Conroe, Tx

Are Board members appointed by an office outside the district? Yes ___ No X

If Yes, by whom? _____

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**SCHEDULE OF GENERAL FUND EXPENDITURES
FOR THE YEAR ENDED DECEMBER 31, 2012**

Professional Fees:	
Audit	\$ 14,300
Legal	236,005
Engineering	55,297
	<u>305,602</u>
Purchased Services for Resale:	
Purchased Water & Sewer Service	175,491
Tap Connection Expenses	17,045
Total Purchased Services for Resale	<u>192,536</u>
Contracted Services:	
Bookkeeping	38,922
Operator	80,532
	<u>119,454</u>
Utilities	<u>12,006</u>
Repairs and Maintenance	<u>482,163</u>
Administrative Expenditures:	
Directors Fees	22,800
Office Supplies	20,326
Insurance	14,714
	<u>57,840</u>
Garbage	210,392
Other Expenditures	437,770
Capital Outlay	<u>524,648</u>
TOTAL EXPENDITURES	<u>\$ 2,342,411</u>

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**SCHEDULE OF TEMPORARY INVESTMENTS
DECEMBER 31, 2012**

<u>Funds</u>	<u>Interest Rate</u>	<u>Maturity Date</u>	<u>Balance December 31, 2012</u>	<u>Accrued Interest Receivable December 31, 2012</u>
<u>General Fund</u>				
Certificate of Deposit:				
No. XXXX4348	0.50%	5/12/13	150,000	479
No. XXXX2564	0.35%	8/27/13	95,000	56
No. XXXX1004	0.60%	6/19/13	95,000	304
No. XXXX1807	0.65%	2/20/13	190,000	1164
No. XXXX4141	0.30%	3/12/13	240,000	580
No. XXXX1667	0.35%	7/9/13	95,000	83
No. XXXX7895	0.75%	7/27/13	95,000	306
No. XXXX0133	0.60%	5/1/13	95,000	381
No. XXXX0092	0.35%	4/12/13	150,000	378
No. XXXX6537	0.75%	4/20/13	95,000	498
No. XXXX4478	0.50%	7/25/13	240,000	523
TexPool	Var.	Var.	54,747	
Total			1,594,747	4,752
<u>Debt Service Fund</u>				
TexPool	Var.	Var.	195,054	-
Total			195,054	-
Total - All Funds			\$ 1,789,801	\$ 4,752

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**TAXES LEVIED AND RECEIVABLE
DECEMBER 31, 2012**

	Maintenance Taxes	Debt Service Taxes
	<u> </u>	<u> </u>
Taxes Receivable, January 1, 2012	\$ 420,225	\$ 371,057
Adjustments	13,731	13,322
	<u>433,956</u>	<u>384,379</u>
Year 2012 Original Tax Rolls	878,876	638,337
	<u>1,312,832</u>	<u>1,022,716</u>
Tax Collections:		
Current Year	(455,676)	(330,962)
Prior Years	(395,142)	(350,111)
Total Collections	<u>(850,818)</u>	<u>(681,073)</u>
 Taxes Receivable, December 31, 2012	 <u>\$ 462,014</u>	 <u>\$ 341,643</u>
 Taxes Receivable By Years:		
2012	\$ 423,200	\$ 307,375
2011	11,085	9,826
2010	5,871	4,837
2009	4,223	3,681
2008	2,885	3,022
2007	3,324	1,475
2006	2,468	1,519
2005	1,890	983
2004	1,541	501
2003	1,512	786
2002	1,383	720
2001	1,181	615
2000	41	1,310
1999	418	1,399
1998	493	1,652
1997	102	340
1996	94	334
1995	81	324
1994	153	610
1993	69	274
1992	60	60
	<u>\$ 462,014</u>	<u>\$ 341,643</u>

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**TAXES LEVIED AND RECEIVABLE
DECEMBER 31, 2012**

Property Valuations:	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Land	\$ 69,918,346	\$ 69,918,346	\$ 69,936,515	\$ 67,221,660
Improvements	290,713,123	290,713,123	290,788,669	279,500,589
Personal Property	<u>7,359,826</u>	<u>7,359,826</u>	<u>7,361,739</u>	<u>7,075,964</u>
 Total Property Valuations	 <u>\$ 367,991,295</u>	 <u>\$ 367,991,295</u>	 <u>\$ 368,086,923</u>	 <u>\$ 353,798,213</u>
 Tax Rate Per \$100 Valuation:				
Debt service tax rates	\$ 0.2375	\$ 0.2300	\$ 0.2211	\$ 0.2306
Maintenance tax rates	<u>0.1725</u>	<u>0.2595</u>	<u>0.2684</u>	<u>0.2646</u>
 Total Tax Rates per \$100 Valuation	 <u>\$ 0.4100</u>	 <u>\$ 0.4895</u>	 <u>\$ 0.4895</u>	 <u>\$ 0.4952</u>
 Original Tax Levy:	 <u>\$ 1,517,213</u>	 <u>\$ 1,801,317</u>	 <u>\$ 1,801,785</u>	 <u>\$ 1,752,010</u>
 Percentage of Taxes Collected to Taxes Levied	 <u>51.8%</u>	 <u>98.8%</u>	 <u>99.4%</u>	 <u>99.6%</u>

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

GENERAL LONG-TERM DEBT SERVICE REQUIREMENTS - BY YEARS
DECEMBER 31, 2012

For The Years Ending December 31,	Series 2011		
	Principal Due March 1	Interest Due September 1, March 1	Total
2013	\$ 200,000	\$ 240,135	\$ 440,135
2014	210,000	228,860	438,860
2015	220,000	217,035	437,035
2016	230,000	204,660	434,660
2017	245,000	191,597	436,597
2018	255,000	177,848	432,848
2019	270,000	163,410	433,410
2020	285,000	151,710	436,710
2021	300,000	142,748	442,748
2022	315,000	132,941	447,941
2023	335,000	121,960	456,960
2024	350,000	109,754	459,754
2025	370,000	96,241	466,241
2026	390,000	81,516	471,516
2027	410,000	65,658	475,658
2028	435,000	48,546	483,546
2029	455,000	30,069	485,069
2030	480,000	10,200	490,200
	<u>\$ 5,755,000</u>	<u>\$ 2,414,888</u>	<u>\$ 8,169,888</u>

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**GENERAL LONG-TERM DEBT SERVICE REQUIREMENTS - BY YEARS
DECEMBER 31, 2012**

For The Years Ending December 31,	Annual Requirements For All Series		
	Total Principal Due	Total Interest Due	Total Principal and Interest Due
2013	\$ 200,000	\$ 240,135	\$ 440,135
2014	210,000	228,860	438,860
2015	220,000	217,035	437,035
2016	230,000	204,660	434,660
2017	245,000	191,597	436,597
2018	255,000	177,848	432,848
2019	270,000	163,410	433,410
2020	285,000	151,710	436,710
2021	300,000	142,748	442,748
2022	315,000	132,941	447,941
2023	335,000	121,960	456,960
2024	350,000	109,754	459,754
2025	370,000	96,241	466,241
2026	390,000	81,516	471,516
2027	410,000	65,658	475,658
2028	435,000	48,546	483,546
2029	455,000	30,069	485,069
2030	480,000	10,200	490,200
	<u>\$ 5,755,000</u>	<u>\$ 2,414,888</u>	<u>\$ 8,169,888</u>

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**ANALYSIS OF CHANGES IN GENERAL LONG-TERM DEBT
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Bond Issues</u>		<u>Totals</u>
	<u>Series 2004</u>	<u>Series 2011</u>	
Interest Rate	2.00%-3.50%	3.00%-5.50%	
Dates Interest Payable	March 1, September 1	March 1, September 1	
Maturity Dates	March 1, 2005/2012	March 1, 2013/2030	
Bonds Outstanding January 1, 2012	\$ 795,000	\$ 5,755,000	\$ 6,550,000
Bonds Sold During the Current Year	-	-	-
Retirements: Principal	<u>795,000</u>	<u>-</u>	<u>795,000</u>
Bonds Outstanding December 31, 2012	\$ <u>-</u>	\$ <u>5,755,000</u>	\$ <u>5,755,000</u>
Retirements: Interest	\$ -	\$ -	\$ -

Paying Agent Name & Address:

Series 2004 - Bank of New York, Houston, Tx

Series 2011 - The Bank of New York Mellon Trust Co., N.A., Dallas, Texas

Bond Authority:	<u>Tax Bonds*</u>	<u>Other Bonds</u>	<u>Refunding Bonds</u>
Amount Authorized By Voters	\$ 56,160,000	\$ N/A	\$ 14,160,000
Amount Issued	14,160,000	N/A	8,931,317
Remaining To Be Issued	42,000,000	N/A	5,228,683

*Includes all bonds secured with tax revenues.

Debt Service Fund Cash & Temporary Investments
balances at December 31, 2012

\$ 853,126

Average annual Debt Service payment (Principal &
Interest) for remaining term of all debt:

\$ 453,883

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**COMPARATIVE STATEMENT OF REVENUES AND EXPENDITURES -
GENERAL AND DEBT SERVICE FUNDS**

FOR THE THREE YEARS ENDED JUNE 30, 2010,

THE EIGHTEEN MONTHS ENDED DECEMBER 31, 2011 AND THE YEAR ENDED DECEMBER 31, 2012

	<u>Amount</u>		
	<u>2012</u>	<u>2011</u>	<u>2010</u>
GENERAL FUND			
REVENUES:			
Service Revenue	\$ 1,216,322	\$ 1,889,876	\$ 1,030,605
Penalty and Interest	11,893	17,365	9,162
Water Tap Revenue	44,070	43,990	43,646
Covenant Revenue	5,210	12,518	14,365
Interest	8,157	19,632	19,183
Maintenance Tax Revenue	850,818	1,577,608	933,309
Other	14,753	20,074	20,518
Total Revenues	<u>2,151,223</u>	<u>3,581,063</u>	<u>2,070,788</u>
EXPENDITURES:			
Professional Fees	305,602	136,534	65,012
Purchased Services for Resale	192,536	369,666	308,097
Contracted Services	119,454	162,559	103,926
Utilities	12,006	19,190	11,900
Repairs and Maintenance	482,163	1,014,823	284,058
Other	706,002	585,016	326,118
Capital Outlay Expenditures	524,648	1,199,463	346,092
Total Expenditures	<u>2,342,411</u>	<u>3,487,251</u>	<u>1,445,203</u>
EXCESS REVENUES (EXPENDITURES)	<u>\$ (191,188)</u>	<u>\$ 93,812</u>	<u>\$ 625,585</u>
DEBT SERVICE FUND			
REVENUES:			
Tax Revenue	\$ 681,073	\$ 1,336,045	\$ 814,829
Penalty and Interest	4,074	9,246	21,007
Interest	394	499	727
Other			708
Total Revenues	<u>685,541</u>	<u>1,345,790</u>	<u>837,271</u>
EXPENDITURES:			
Contracted Services	12,527	20,203	13,349
Other	1,335	(18,595)	724
Debt Service and Related Expenditures	1,115,956	837,148	822,448
Total Expenditures	<u>1,129,818</u>	<u>838,756</u>	<u>836,521</u>
EXCESS REVENUES (EXPENDITURES)	<u>\$ (444,277)</u>	<u>\$ 507,034</u>	<u>\$ 750</u>
Total Active Retail Water And/Or Wastewater Connections	<u>1,459</u>	<u>1,458</u>	<u>1,409</u>

		Percent				
2009	2008	2012	2011	2010	2009	2008
\$ 1,037,134	\$ 871,051	56.5%	52.8%	49.8%	50.7%	41.7%
14,867	9,936	0.6%	0.5%	0.4%	0.7%	0.5%
62,390	149,965	2.0%	1.2%	2.1%	3.0%	7.2%
10,598	20,754	0.2%	0.3%	0.7%	0.5%	1.0%
13,313	38,946	0.4%	0.5%	0.9%	0.7%	1.9%
894,884	982,370	39.6%	44.1%	45.1%	43.7%	47.0%
14,349	18,278	0.7%	0.6%	1.0%	0.7%	0.9%
<u>2,047,535</u>	<u>2,091,300</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>
67,267	57,483	14.2%	3.8%	3.1%	3.3%	2.7%
332,433	451,414	9.0%	10.3%	14.9%	16.2%	21.6%
91,539	80,268	5.6%	4.5%	5.0%	4.5%	3.8%
15,013	12,354	0.6%	0.5%	0.6%	0.7%	0.6%
351,003	181,564	22.4%	28.3%	13.7%	17.1%	8.7%
286,948	209,325	32.8%	16.3%	15.7%	14.0%	10.0%
398,473	659,375	24.4%	33.5%	16.7%	19.5%	31.5%
<u>1,542,676</u>	<u>1,651,783</u>	<u>108.9%</u>	<u>97.4%</u>	<u>69.8%</u>	<u>75.3%</u>	<u>79.0%</u>
<u>\$ 504,859</u>	<u>\$ 439,517</u>	<u>-8.9%</u>	<u>2.6%</u>	<u>30.2%</u>	<u>24.7%</u>	<u>21.0%</u>
\$ 881,885	\$ 438,665	99.3%	99.3%	97.3%	96.8%	96.6%
27,958	13,199	0.6%	0.7%	2.5%	3.1%	2.9%
997	2,427	0.1%	0.0%	0.1%	0.1%	0.5%
62		0.0%	0.0%	0.1%	0.0%	0.0%
<u>910,902</u>	<u>454,291</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>
13,728	12,030	1.8%	1.5%	1.6%	1.5%	2.6%
723	871	0.2%	-1.4%	0.1%	0.1%	0.2%
820,848	821,848	162.8%	62.2%	98.2%	90.1%	180.9%
<u>835,299</u>	<u>834,749</u>	<u>164.8%</u>	<u>62.3%</u>	<u>99.9%</u>	<u>91.7%</u>	<u>183.7%</u>
<u>\$ 75,603</u>	<u>\$ (380,458)</u>	<u>-64.8%</u>	<u>37.7%</u>	<u>0.1%</u>	<u>8.3%</u>	<u>-83.7%</u>
<u>1,425</u>	<u>1,341</u>					

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**BOARD MEMBERS, KEY ADMINISTRATIVE PERSONNEL AND CONSULTANTS
FOR THE YEAR ENDED DECEMBER 31, 2012**

Complete District Mailing Address: 3 E. Greenway Plaza, Suite 2000, Houston, Tx 77046

District Business Telephone Number: (713) 651-0111

Submission Date of the most recent District Registration Form: 7/3/12
(TWC Sections 36.054 and 49.054)

Limit on Fees of Office that a Director may receive during a fiscal year: \$7,200
(Set by Board Resolution-TWC Section 49.060)

<u>Name</u>	<u>Term of Office (Elected or Appointed) or Date Hired</u>	<u>Fees of Office Paid 12/31/12</u>	<u>Expense Reimburse- ments 12/31/12</u>	<u>Title at Year End</u>
BOARD MEMBERS				
Frederick Stow	Elected 5/12 - 5/16	\$ -	\$ -	President
J. Frank Haasbeek	Elected 5/10 - 5/14	1,950	-	Vice-President/ Investment Officer
Gary S. North	Elected 5/10 - 5/14	7,200	-	Secretary/ Treasurer
Carl D. Clay	Elected 5/12 - 5/16	7,200	-	Director
Marvin Carter	Elected 5/12 - 5/16	6,450	-	Director

KEY ADMINISTRATIVE PERSONNEL

N/A

Note: No director has any business or family relationships (as defined by the Texas Water Code) with major landowners in the District, with the District's developers or with any of the District's consultants.

See accompanying auditor's report.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 4

**BOARD MEMBERS, KEY ADMINISTRATIVE PERSONNEL AND CONSULTANTS
FOR THE YEAR ENDED DECEMBER 31, 2012**

<u>Name</u>	<u>Term of Office (Elected or Appointed) or Date Hired</u>	<u>Fees Paid 12/31/12</u>	<u>Expense Reimburse- ments 12/31/12</u>	<u>Title at Year End</u>
CONSULTANTS				
Hays Utility North Corp.	04/01/95	\$ 80,532	\$ -	Operator
Municipal Accounts & Consulting, LP	01/01/95	38,922	-	Bookkeeper
J.R. Moore, Jr.	03/01/95	317	-	Tax Collector
David L. Merritt, P.C.	09/18/96	14,300	-	Auditor
Bleyl & Associates	06/18/02	55,297	-	Engineer
RBC Capital Markets, LLC	09/15/96	-	-	Financial Advisor
Coats, Rose, Yale, Ryman & Lee, P.C.	2/25/10	236,005	-	Attorney

See accompanying auditor's report.