OFFICIAL NOTICE OF SALE, OFFICIAL BID FORM
and
OFFICIAL STATEMENT

$7,085,000

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

(A political subdivision of the State of Texas located in Chambers County, Texas)

Unlimited Tax Qualified School Construction Bonds Taxable Series 2012 (Direct-Pay Subsidy Bonds)

Bids Due
Monday, January 23, 2012
at 10:00 a.m., Central Time

This Official Notice of Sale does not alone constitute an invitation for bids but is merely notice of sale of the Bonds described herein. The invitation for bids on such Bonds is being made by means of this Official Notice of Sale, the Official Bid Form, and the Official Statement.

OFFICIAL NOTICE OF SALE

$7,085,000
BARBERS HILL INDEPENDENT SCHOOL DISTRICT
(A political subdivision of the State of Texas located in Chambers County, Texas)

UNLIMITED TAX QUALIFIED SCHOOL CONSTRUCTION BONDS, TAXABLE SERIES 2012
(DIRECT-PAY SUBSIDY BONDS)

THE SALE

BONDS OFFERED FOR SALE AT COMPETITIVE BID: The Board of Trustees (the "Board") of the Barbers Hill Independent School District (the "District" or the "Issuer") is offering for sale at competitive bid $7,085,000 Unlimited Tax Qualified School Construction Bonds, Taxable Series 2012 (Direct-Pay Subsidy Bonds) (the "Bonds"). Bidders may submit bids for the Bonds by either of the following methods:

(1) Submit bids electronically as described below in "Bids by Internet;" or
(2) Submit bids by facsimile as described below in "Bids by Facsimile."

BIDS BY INTERNET: Interested bidders may, at their option and risk, submit their bid by electronic media, as described below, by 10:00 A.M., Central time, on Monday, January 23, 2012. Bidders submitting a bid by internet shall not be required to submit signed Official Bid Forms prior to the award. Any prospective bidder that intends to submit an electronic bid must submit its electronic bid via the facilities of the i-Deal, LLC Parity System ("PARITY") and should, as a courtesy, register with PARITY by 9:00 A.M., Central time, on Monday, January 23, 2012 indicating their intent to submit a bid by internet.

In the event of a malfunction in the electronic bidding process, bidders may submit their bids by facsimile, as described below. Any bid received after the scheduled time for their receipt will not be accepted.

The official time for the receipt of bids shall be the time maintained by PARITY. All electronic bids shall be deemed to incorporate the provisions of the Official Notice of Sale, Official Bid Form, and the Official Statement. To the extent that any instructions or directions set forth in PARITY conflict with this Official Notice of Sale, the terms of this Official Notice of Sale shall control. For further information about the PARITY System, potential bidders may contact i-Deal LLC at 1359 Broadway, 2nd Floor, New York, New York, 10018, Telephone 212-849-5021.

An electronic bid made through the facilities of the PARITY System shall be deemed an irrevocable offer to purchase the Bonds on the terms provided in the Official Notice of Sale, and shall be binding upon the bidder as if made by a signed, sealed bid delivered to the Issuer. The Issuer shall not be responsible for any malfunction or mistake made by, or as a result of the use of PARITY, the use of such facilities being the sole risk of the prospective bidder.

BIDS BY FACSIMILE: Interested bidders may, at their option and risk, submit their bid by facsimile to Doug Whitt at (214) 383-1570 by 10:00 A.M., Central time, on Monday, January 23, 2012. Bidders submitting a bid by facsimile shall not be required to submit signed Official Bid Forms prior to the award. Any prospective bidder that intends to submit a bid by facsimile should, as a courtesy, submit an email message to dwhitt@swst.com by 9:00 A.M., Central time, on Monday, January 23, 2012 indicating their intent to submit a bid by facsimile.

Neither the District nor Southwest Securities is responsible for any failure of the Financial Advisor's or the bidder's fax machine. Bids received by facsimile after the bid deadline will not be accepted. Bidders who fax bids do so at their own risk. All such bids are binding on the bidder.

PLACE AND TIME OF BID OPENING: The bids for the Bonds will be publicly opened and read at the District at 10:00 A.M. Central time, on Monday, January 23, 2012 and the winning bidder or the manager of a syndicate that produces the winning bid (the "Purchaser" or "Initial Purchaser") will be identified.

AWARD OF THE BONDS: The Board will take action to award the Bonds (or reject all bids) at a meeting to commence at 6:30 p.m., Central time, on Monday, January 23, 2012. The Issuer intends to award the Bonds on the basis of the **lowest True Interest Cost rate** (hereinafter defined) to the District. Delivery of the Bonds is conditioned on the receipt by the Issuer of the Issue Price Certificate, a copy of which is attached hereto. The Issue Price Certificate requires that the first price or yield at which at least 10% of the Bonds are sold to the public is the par amount thereof. The Bonds may not be bid or reoffered at a price greater than par. The District reserves the right to reject any and all bids. In the case of a tie bid, the District reserves the right to award the Bonds to the bidder of its choice.

THE BONDS

DESCRIPTION: The Bonds will be dated February 1, 2012 (the "Bond Date" or "Dated Date") with interest accruing from the date of delivery and payable initially on August 15, 2012 and semiannually thereafter on February 15 and August 15 until stated maturity or prior redemption. The Bonds will be issued as fully registered obligations in book-entry form only and when issued will be registered in the name of Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York. DTC will act as securities depository (the "Securities Depository"). Book-entry interests in the Bonds will be made available for purchase in the principal amount of $5,000 or any integral multiple thereof. Purchasers of the Bonds ("Beneficial Owners") will not receive physical delivery of certificates representing their interest in the Bonds purchased. So long as DTC or its nominee is the registered owner of the Bonds, the principal of and interest on the Bonds will be payable by The Bank of New York Mellon Trust Company N.A., Dallas, Texas, as Paying Agent/Registrar, to the Securities Depository, which will in turn remit such principal and interest to its Participants, which will in turn remit such principal and interest to the Beneficial Owners of the Bonds. (See "BOOK-ENTRY-ONLY SYSTEM" in the Official Statement.) The Bonds will be stated to mature on February 15, 2029.

DESIGNATION OF BONDS AS "QUALIFIED SCHOOL CONSTRUCTION BONDS" – DIRECT-PAY SUBSIDY BONDS: The Bonds are issued as "qualified school construction bonds" within the meaning of section 54F of the Internal Revenue Code of 1986, as amended (the "Code"), and as "qualified bonds" and "special tax credit bonds" within the meaning of section 6431(f) of the Code under and pursuant to the authority provided for in the federal American Recovery and Reinvestment Act of 2009, effective February 17, 2009, and the federal Hiring Incentives to Restore Employment Act, effective March 18, 2010, and in reliance on guidance released from time to time by the Internal Revenue Service. As a result of these elections and designations the District is entitled to receive directly from the United States Department of the Treasury a refundable tax credit (the "Refundable Tax Credit") in an amount equal to the lesser of (1) the amount of interest payable on the Bonds on such interest payment date and (2) the amount of interest that would have been payable on the Bonds if such interest were determined at the applicable credit rate determined under section 54A(b)(3) of the Code. **As a result of the District's designations and elections entitling it to the receipt of the Refundable Tax Credit, no owner of Bonds will be entitled to a tax credit as a result of its ownership of a Bond.**

The District's continued receipt of the Refundable Tax Credit is subject to various requirements specified by the IRS. No assurances are provided that the District will receive each of the Refundable Tax Credits. Refundable Tax Credits will only be paid by the Treasury if the Bonds remain qualified in accordance with sections 54F and 6431(f), respectively, of the Code. For the Bonds to be, and remain, designated as "qualified bonds" for which the Refundable Tax Credit will be received, the District must comply with certain covenants with respect to the Bonds regarding the use and investment of proceeds thereof, the use of property financed therewith, making timely and proper filings with the IRS, and satisfying certain other requirements of the Code. Failure on the part of the District to comply with the conditions imposed by the Code and future guidance to be provided by the Treasury and the IRS may cause the District to fail to receive the Refundable Tax Credit for the remaining term of the Bonds and it could subject the District to a claim for refund of previously received Refundable Tax Credits. Moreover, Refundable Tax Credits are subject to automatic offsets against certain amounts that may, for unrelated reasons, be owed by the District to the United States of America or an agency thereof. In addition, see "Special Mandatory Redemption" and "Extraordinary Optional Redemption" herein for information concerning redemption of the Bonds in the event of certain events that result or could result in the loss of the right or opportunity of the District to receive the Subsidy Payments with respect to the Bonds.

CUMULATIVE SINKING FUND DEPOSITS: The Code provides that an issue of "qualified school construction bonds", which includes the Bonds, shall not fail to satisfy the programmatic requirements for such obligations by reason of any fund that is expected to be used to repay such qualified school construction bonds that (i) is funded at a rate not more rapid than equal annual installments, (ii) is funded in a manner reasonably expected to result in an amount not greater than the amount necessary to repay the obligations, and (iii) is invested at a yield that is not greater than the discount rate published by the Treasury on the date of the sale of the Bonds. The District will obligate itself under the Order (defined herein) to make mandatory deposits into the Cumulative Sinking Fund Deposit Account, which is a subaccount of the Bond Fund created under the Order, with the Paying Agent/Registrar for the Bonds, on February 15 in each of the years and the respective amounts (preliminary, subject to change) set forth below:

Year	Deposit Amount	Cumulative Balance
2015	$ 470,000.00	$ 470,000.00
2016	470,000.00	940,000.00
2017	470,000.00	1,410,000.00
2018	470,000.00	1,880,000.00
2019	470,000.00	2,350,000.00
2020	470,000.00	2,820,000.00
2021	470,000.00	3,290,000.00
2022	470,000.00	3,760,000.00
2023	475,000.00	4,235,000.00
2024	475,000.00	4,710,000.00
2025	475,000.00	5,185,000.00
2026	475,000.00	5,660,000.00
2027	475,000.00	6,135,000.00
2028	475,000.00	6,610,000.00
2029	475,000.00	7,085,000.00

Any interest earnings from the investment of prior deposits will be applied as a credit against the District's next year's required Cumulative Sinking Fund Deposit Account deposit. Such deposits and any interest earned thereon (which is not used as a credit against periodic deposits) shall be used to pay the principal of the Bonds at stated maturity or prior redemption and are pledged to pay the debt service requirements on the Bonds. To the extent the aggregate cumulative sinking fund deposits and interest thereon total less than the principal amount of the Bonds due on such date, the District will contribute additional funds required to pay the debt service requirements on the Bonds upon prior redemption or on the stated maturity date for the Bonds

REDEMPTION PROVISION FOR THE BONDS: OPTIONAL REDEMPTION: The Bonds are subject to redemption prior to Stated Maturity, at the option of the District, on any date from the Closing Date through August 14, 2021, as a whole or in part, in principal amounts of $5,000 or any integral multiple thereof, at the Make-Whole Redemption Price. In addition, the Bonds are subject to redemption prior to Stated Maturity, at the option of the District, on August 15, 2021, or on any date thereafter, as a whole or in part in principal amounts of $5,000 or any integral multiple thereof (and if within a Stated Maturity at random and by lot by the Paying Agent/Registrar), at the redemption price of par plus accrued interest to the date of redemption. If a Bond (or any portion of the principal sum thereof) shall have been called for redemption and notice of such redemption shall have been given, such Bond (or the principal amount thereof to be redeemed) shall become due and payable on such redemption date and interest thereon shall cease to accrue from and after the redemption date, provided funds for the payment of the redemption price and accrued interest thereon are held by the Paying Agent/Registrar on the redemption date.

SPECIAL MANDATORY REDEMPTION: To the extent that 100% of the Available Project Proceeds are not expended for Qualified Purposes by the close of the Expenditure Period, the District shall redeem such Nonqualified Bonds in authorized denominations (rounded up to the next highest authorized denomination) within 90 days after the end of such period, at a redemption price equal to the principal amount of such Nonqualified Bonds, plus accrued (but unpaid) interest on such Nonqualified Bonds to the date of redemption, payable from such unexpended proceeds of sale of the Bonds held by the District.

DEFINITION OF TERMS: For purposes of this section, capitalized terms used herein have the following meanings:

"Available Project Proceeds" means proceeds of the sale of the Bonds other than proceeds used to pay costs of issuance (not to exceed 2 percent thereof) plus proceeds received from investing the proceeds of the sale of the Bonds.

"Expenditure Period" means the three year period beginning on the Delivery Date, plus any extension of such period granted by the Secretary of the Treasury.

"Make-Whole Redemption Price" means an amount equal to the greater of (i) the issue price of the Bonds set forth in the Order (but not less than 100%) of the principal amount of such Bonds to be redeemed or (ii) the sum of the present value of the remaining scheduled payments of principal and interest on the Bonds to be redeemed to the maturity date of such Bonds, not including any portion of those payments of interest accrued and unpaid as of the date on which the Bonds are to be redeemed, discounted to the date on which the Bonds are to be redeemed on a semi-annual basis, assuming a 360-day year containing twelve 30-day months, at the Treasury Rate plus one-hundred (100) basis points, plus accrued interest on the Bonds to be redeemed to the redemption date.

"Nonqualified Bonds" means the portion of the outstanding Bonds in an amount that, if the remaining Bonds were issued on the last day of the Expenditure Period, all of the Available Project Proceeds of the remaining Bonds would have been used for Qualified Purposes within the Expenditure Period.

"Qualified Purposes" means the construction, rehabilitation, or repair of a public school facility (including expenditures for the acquisition of equipment to be used in a portion of a public school facility being constructed, rehabilitated, or repaired with the proceeds of the Bonds) or for the acquisition of land on which such a facility is to be constructed with a portion of the proceeds of the Bonds.

"Treasury Rate" means, with respect to any redemption date for a particular Bond, the yield to maturity as of such redemption date of United States Treasury securities with a constant maturity (as compiled and published in the most recent Federal Reserve Statistical Release H.15 (519) (the "Statistical Release") that has become publicly available at least two Business Days prior to the redemption date (excluding inflation-indexed securities) (or, if the Statistical Release is no longer published, any publicly available source of similar market data) most nearly equal to the period from the redemption date to the maturity date of the Bonds to be redeemed; provided, however that if the period from the redemption date to the maturity date is less than one year, the weekly average yield on actually traded United States Treasury securities adjusted to a constant maturity of one year shall be used.

AUTHORITY FOR ISSUANCE AND SECURITY FOR PAYMENT: The Bonds are being issued pursuant to the Constitution and general laws of the State of Texas, including Sections 45.001 and 45.003(b)(1) of the Texas Education Code, as amended, an election held in the District on October 15, 2005 and May 14, 2011, and the order to be adopted by the Board of Trustees of the District on the sale date of the Bonds (the "Order"). The Bonds are direct obligations of the District and are payable as to both principal and interest from ad valorem taxes to be levied on all taxable property within the District, without legal limitation as to rate or amount. (See "THE BONDS – Security.")

PAYING AGENT/REGISTRAR: The initial Paying Agent/Registrar is The Bank of New York Mellon Trust Company N.A., Dallas, Texas. In the Order, the District covenants to provide a Paying Agent/Registrar at all times while the Bonds are outstanding, and any Paying Agent/Registrar selected by the District shall be a commercial bank or trust company organized under the laws of the United States and any state and duly qualified and legally authorized to serve and perform the duties of the Paying Agent/Registrar for the Bonds. The Paying Agent/Registrar will maintain the Security Register containing the names and addresses of the registered owners of the Bonds.

In the Order, the District retains the right to replace the Paying Agent/Registrar. If the Paying Agent/Registrar is replaced by the District, such Paying Agent/Registrar, promptly upon the appointment of a successor, is required to deliver the Security Register to the successor Paying Agent/Registrar.

In the event there is a change in the Paying Agent/Registrar, the District has agreed to notify each registered owner of the Bonds by United States mail, first-class postage prepaid, at the address in the Security Register, stating the effective date of the change and the mailing address of the successor Paying Agent/Registrar.

BOOK-ENTRY-ONLY SYSTEM: The District intends to utilize the Book-Entry-Only System of The Depository Trust Company, New York, New York ("DTC") with respect to the issuance of the Bonds. See "BOOK-ENTRY-ONLY SYSTEM" in the Official Statement.

OFFICIAL STATEMENT AND OTHER TERMS AND COVENANTS IN THE ORDER: Further details regarding the Bonds and certain covenants of the District contained in the Order are set forth in the Official Statement, to which reference is made for all purposes.

CONDITIONS OF THE SALE

TYPES OF BIDS AND INTEREST RATES: The Bonds will be sold in one block on an "All or None" basis, and at a price of not more than their par value. The Bonds shall all mature on February 15, 2029, and all Bonds shall bear interest at the same rate. **The minimum bid for the Bonds shall not be less than $7,031,862.50 (99.25% of par) nor more than $7,085,000 (100.00% of par). No bid producing a cash premium will be considered.** The Bonds may not be bid or reoffered at a price greater than par. Bidders are invited to name the rate of interest to be borne by the Bonds, provided that the rate bid must be in a multiple of 1/100 of 1% (one basis point) and the net effective interest rate for the Bonds (calculated in the manner required by Chapter 1204, as amended, Texas Government Code) must not exceed 15%. No bids involving supplemental interest rates will be considered.

BASIS OF AWARD: The sale of the Bonds will be awarded to the bidder making a bid that conforms to the specifications herein and which produces the **lowest True Interest Cost rate to the District**. The True Interest Cost rate is that rate which, when used to compute the total present value **as of the date of initial delivery of the Bonds** of all debt service payments on the Bonds on the basis of semi-annual compounding, produces an amount equal to the sum of the par value of the Bonds. **Cash premiums will not be allowed**. The Bonds may not be bid or reoffered at a price greater than par. The District reserves the right to reject any or all bids. In the case of a tie bid, the District reserves the right to award the Bonds to the bidder of its choice. In the event of a bidder's error in interest cost rate calculations, the interest rates, and premium set forth in the Official Bid Form will be considered as the intended bid.

In order to provide the District with information to enable it to comply with provisions of the Code pertaining to the designation of the Bonds as "Qualified School Construction Bonds", the Purchaser will be required to complete, execute, and deliver to the District (on or before the fifth (5^{th}) business day prior to the date of initial delivery of the Bonds) a certification as to their "issue price" in the form and to the effect attached hereto or accompanying this Official Notice of Sale. Each bidder, by submitting its bid, agrees to complete, execute, and deliver such certificate by the date of initial delivery of the Bonds, if its bid is accepted by the District. It will be the responsibility of the Purchaser to institute such syndicate reporting requirements, to make such investigation, or otherwise to ascertain the facts necessary to enable it to make such certification with reasonable certainty. Any questions concerning such certification should be directed to Bond Counsel. Receipt by the District of such certificate is a condition to the delivery of the Bonds. Upon failure to deliver the Issue Price Certificate, the District will have the right to cause the Bonds not to be delivered and to retain the Good Faith Deposit as a form of liquidated damages. In that event, the Purchaser will have no recourse against the District.

GOOD FAITH DEPOSIT: A bank cashier's check, payable to the order of "Barbers Hill Independent School District", in the amount of $141,700, which is 2% of the par value of the Bonds, is required. The Good Faith Deposit of the Purchaser will be retained uncashed by the District pending the Purchaser's compliance with the terms of its bid and this Official Notice of Sale. In the event the Purchaser should fail or refuse to take up and pay for the Bonds in accordance with its bid, then said check shall be cashed and accepted by the District as full and complete liquidated damages. The Good Faith Deposit may accompany the Official Bid Form or it may be submitted separately; however, if submitted separately, it shall be made available to the District prior to the opening of the bids, and shall be accompanied by instructions from the bank on which it is drawn which authorizes its use as a Good Faith Deposit by the Purchaser who shall be named in such instructions. **The Good Faith Deposit of the Purchaser will be returned to the Purchaser on the date of delivery.** No interest will be allowed on the Good Faith Deposit. Checks accompanying bids other than the winning bid will be returned promptly after the bids are opened, and an award of the Bonds has been made by the District. Upon failure to deliver the Issue Price Certificate in the form attached hereto, the District will have the right to retain the Good Faith Deposit.

OFFICIAL STATEMENT

To assist the Initial Purchaser in complying with Rule 15c2-12, as amended, of the United States Securities and Exchange Commission ("Rule 15c2-12"), the Issuer and the Initial Purchaser contract and agree, by the submission and acceptance of the winning bid, as follows:

COMPLIANCE WITH RULE 15c2-12: The Issuer has approved and authorized distribution of the accompanying Preliminary Official Statement for dissemination to potential purchasers of the Bonds, but does not presently intend to prepare any other document or version thereof for such purpose, except as described below. Accordingly, the Issuer deems the accompanying Preliminary Official Statement to be final as of its date, within the meaning of Rule 15c2-12, except for information relating to the offering price, interest rate, final debt service schedule, selling compensation, identity of the Purchaser and other similar information, terms and provisions to be specified in the competitive bidding process. The Initial Purchaser shall be responsible for promptly informing the Issuer of the initial offering yield of the Bonds.

Thereafter, the Issuer will complete and authorize distribution of the Official Statement identifying the Initial Purchaser and containing such omitted information. The Issuer does not intend to amend or supplement the Official Statement otherwise, except to take into account certain subsequent events, if any, as described below. By delivering the Final Official Statement or any amendment or supplement thereto in the requested quantity to the Initial Purchaser on or after the sale date, the Issuer intends the same to be final as of such date, within the meaning of Rule 15c2-12. Notwithstanding the foregoing, the Issuer makes no representation concerning the absence of material misstatements or omissions from the Official Statement, except only as and to the extent under "CERTIFICATION OF THE OFFICIAL STATEMENT" as described below.

FINAL OFFICIAL STATEMENT: The Issuer will furnish to the Purchaser, within seven (7) business days after the sale date, an aggregate maximum of one hundred (100) copies of the Official Statement, together with information regarding interest rates, the purchase of municipal bond insurance, if any, and other terms relating to the reoffering of the Bonds. The Issuer agrees to provide, or cause to be provided, to the Purchaser the Preliminary Official Statement and the Official Statement and any amendments or supplements thereto in a designated electronic format (or printed format with respect to the final Official Statement) as may be required for the Purchaser to comply with Rule 15c2-12 or the rules of the MSRB. The Issuer consents to the distribution of such documents in a designated electronic format. Upon receipt, the Purchaser shall promptly file the Official Statement with the Municipal Securities Rulemaking Board ("MSRB") in accordance with the MSRB Rule G32. The Purchaser will be responsible for providing information concerning the Issuer and the Bonds to subsequent purchasers of the Bonds, and the Issuer will undertake no responsibility for providing such information other than to make the Official Statement available to the Purchaser as provided herein. The Issuer's obligation to supplement the Official Statement to correct key representations determined to be omitted or materially misleading, after the date of the Official Statement, shall terminate 25 days after the sale date.

CHANGES TO OFFICIAL STATEMENT: If, subsequent to the date of the Official Statement, the Issuer learns, through the ordinary course of business and without undertaking any investigation or examination for such purposes, or is notified by the Initial Purchaser of any adverse event which causes the Official Statement to be materially misleading, and unless the Initial Purchaser elects to terminate its obligation to purchase the Bonds, as described below under "DELIVERY AND ACCOMPANYING DOCUMENTS - Conditions to Delivery," the Issuer will promptly prepare and supply to the Initial Purchaser, in a designated electronic format, an appropriate amendment or supplement to the Official Statement satisfactory to the Initial Purchaser.

CERTIFICATION OF THE OFFICIAL STATEMENT: At the time of payment for and delivery of the Initial Bonds (as defined below), the Initial Purchaser will be furnished a certificate, executed by proper officials of the Issuer, acting in their official capacities, in the form described in the Official Statement under the heading "Certification of the Official Statement." The Official Statement and Official Notice of Sale will be approved as to form and content and the use thereof in the offering of the Bonds will be authorized, ratified and approved by the Board of Trustees on the date of sale, and the Initial Purchaser will be furnished, upon request, at the time of payment for and the delivery of the Bonds, a certified copy of such approval, duly executed by the proper officials of the Issuer.

DELIVERY AND ACCOMPANYING DOCUMENTS

INITIAL DELIVERY OF INITIAL BOND: Initial delivery will be accomplished by the issuance of one fully registered Bond in the aggregate principal amount of $7,085,000 payable to the Purchaser (the "Initial Bond"), signed by the duly appointed officers of the Board of Trustees, by their manual or facsimile signatures, approved by the Attorney General, and registered and manually signed by the Comptroller of Public Accounts. Initial Delivery will be at the corporate trust office of the Paying Agent/Registrar. Upon delivery of the Initial Bond, it shall be immediately canceled and one definitive Bond in the aggregate principal amount of $7,085,000 payable to Cede & Co. will be delivered to DTC in connection with DTC's Book-Entry-Only System. Payment for the Bonds must be made in immediately available funds for unconditional credit to the District, or as otherwise directed by the District. The Purchaser will be given six business days' notice of the time fixed for delivery of the Bonds. It is anticipated that the delivery of the Initial Bond(s) can be made on or about February 23, 2012, but if for any reason the District is unable to make delivery by March 22, 2012, then the District shall immediately contact the Purchaser and offer to allow the Purchaser to extend its obligation to take up and pay for the Bonds an additional thirty days. If the Purchaser does not elect to extend its offer within six days thereafter, then its Good Faith Deposit will be returned, and both the District and the Purchaser shall be relieved of any further obligation. In no event shall the District be liable for any damages by reason of its failure to deliver the Bonds, provided that such failure is due to circumstances beyond the District's reasonable control.

CUSIP NUMBERS: It is anticipated that CUSIP identification numbers will be printed on the Bonds, but neither the failure to print such number on any Bond nor any error with respect thereto shall constitute cause for a failure or refusal by the Initial Purchaser to accept delivery of and pay for the Bonds in accordance with the terms of the Official Bid Form and this Official Notice of Sale. All expenses in relation to the printing of CUSIP numbers on the Bonds shall be paid by the Issuer; however, the CUSIP Service Bureau's charge for the assignment of the numbers shall be paid by the Initial Purchaser.

CONDITIONS TO DELIVERY: The obligation to take up and pay for the Bonds is subject to the following conditions: the issuance of an approving opinion of the Attorney General of Texas, the Initial Purchaser's receipt of the legal opinion of Bond Counsel and the certificate regarding the Official Statement as described therein under "CERTIFICATION OF THE OFFICIAL STATEMENT", and the non-occurrence of the events described below under the subcaption "NO MATERIAL ADVERSE CHANGE". In addition, if the Issuer fails to comply with its obligations described under "OFFICIAL STATEMENT" above, the Initial Purchaser may terminate its contract to purchase the Bonds by delivering written notice to the Issuer within five (5) days thereafter.

NO MATERIAL ADVERSE CHANGE: The obligations of the Initial Purchaser to take up and pay for the Bonds, and of the Issuer to deliver the Initial Bond, are subject to the condition that, up to the time of delivery of and receipt of payment for the Initial Bond, there shall have been no material adverse change in the affairs of the Issuer subsequent to the date of sale from that set forth in the Preliminary Official Statement, as it may have been finalized, supplemented or amended through the date of initial delivery of the Bonds.

LEGAL OPINIONS: The District will furnish the Purchaser a complete transcript of proceedings incident to the authorization and issuance of the Bonds, including the unqualified approving legal opinion of the Attorney General of the State of Texas as to the Bonds, to the effect that the Bonds are valid and legally binding obligations of the District, and based upon examination of such transcript of proceedings, the approving legal opinion of Bond Counsel, regarding the legality and validity of the Bonds issued in compliance with the provisions of the Order. (See "LEGAL OPINIONS AND NO-LITIGATION CERTIFICATE" and "Appendix C – Form of Legal Opinion of Bond Counsel" in the Official Statement.)

GENERAL CONSIDERATIONS

RATING: The Bonds are rated "AAA" by Standard & Poor's Ratings Services, a Standard & Poor's Financial Services LLC business ("S&P") and Moody's Investor Service, Inc. ("Moody's) based upon the Texas Permanent School Fund Guarantee. The District currently has an unenhanced, underlying rating of "AA" from S&P and "Aa3" by Moody's. There is no assurance that such ratings will continue for any given period of time or will not be revise downward or withdrawn entirely by such rating company, if in the judgment of said rating company, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Bonds. Neither the District nor the Purchaser has undertaken any responsibility to advise owners of the Bonds of any lowering or withdrawal of such ratings.

REGISTRATION AND QUALIFICATION OF BONDS FOR SALE: No registration statement relating to the Bonds has been filed with the United States Securities and Exchange Commission under the Securities Act of 1933, as amended, in reliance upon exemptions provided in such Act. The Bonds have not been approved or disapproved by the United States Securities and Exchange Commission, nor has the United States Securities and Exchange Commission passed upon the accuracy or adequacy of the Official Statement. Any representation to the contrary is a criminal offense. The Bonds have not been registered or qualified under the Securities Act of Texas in reliance upon exemptions contained therein, nor have the Bonds been registered or qualified under the securities acts of any other jurisdiction. The Issuer assumes no responsibility for registration or qualification of the Bonds under the securities laws of any jurisdiction in which the Bonds may be sold, assigned, pledged, hypothecated or otherwise transferred. This disclaimer of responsibility for registration or qualification for sale or other disposition of the Bonds shall not be construed as an interpretation of any kind with regard to the availability of any exemption from securities registration or qualification provisions.

It is the obligation of the Purchaser to register or qualify sale of the Bonds under the securities laws of any jurisdiction which so requires. The Issuer agrees to cooperate, at the Purchaser's written request and expense and within reasonable limits, in registering or qualifying the Bonds, or in obtaining an exemption from registration or qualification in any state where such action is necessary, but the District will in no instance execute a consent to service of process in any state in which the Bonds are offered for sale.

ADDITIONAL COPIES: Subject to the limitations described herein, additional copies of this Official Notice of Sale, the Official Bid Form, and the Official Statement may be obtained from Southwest Securities, 700 Central Expressway South, Suite 410, Allen, Texas 75013.

On the date of the sale, the Board of Trustees will, in the Order, approve the form and content of the Official Statement, and any addenda, supplement or amendment thereto, and authorize its further use in the reoffering of the Bonds by the Purchaser.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

/s/
President, Board of Trustees

ATTEST:

/s/
Secretary, Board of Trustees

Dated: January 12, 2012

OFFICIAL BID FORM

Honorable President and Board of Trustees
Barbers Hill Independent School District
9600 Eagle Drive
Mont Belvieu, Texas 77580

January 23, 2012

Ladies & Gentlemen:

Reference is made to your Official Notice of Sale and Official Statement dated January 12, 2012 of $7,085,000 BARBERS HILL INDEPENDENT SCHOOL DISTRICT Unlimited Tax Qualified School Construction Bonds, Taxable Series 2012 (Direct-Pay Subsidy Bonds), both of which constitute a part hereof.

For your legally issued Bonds, as described in said Official Notice of Sale and Official Statement, we, as the prospective purchaser of the Bonds (the "Purchaser") undertake to reoffer to the public the Bonds at a price not greater than the par value thereof. **No bid producing a cash premium will be considered. The Bonds may not be bid or reoffered at a price greater than par. The minimum bid on the Bonds shall not be less than $7,031,862.50 (99.25% of par) nor more than $7,085,000 (100% of par) for Bonds maturing and bearing interest as follows:**

Maturity (2/15)	Principal Amount	Interest Rate
2029	$7,085,000	________

The Purchaser's calculation (which is not a part of this bid) of the interest cost in accordance with the above bid is:

TRUE INTEREST COST ________________________%

By accepting this bid, the Purchaser understands the District will provide the copies of the Official Statement, as well as any amendments or supplements thereto (in a designated electronic format), all in accordance with the Official Notice of Sale.

The Initial Bond shall be registered in the name of ________________________________ (syndicate manager). The Purchaser will advise DTC of registration instructions at least five business days prior to the date set for Initial Delivery. It is the obligation of the Purchaser of the Bonds to complete the DTC Eligibility Questionnaire.

Cashier's Check of the ________________________________ (bank), _______________ (location), in the amount of $141,700 which represents our Good Faith Deposit is attached hereto or has been made available to you prior to the opening of this bid, and is submitted in accordance with the terms as set forth in the Official Notice of Sale and the Official Statement. The Good Faith Deposit of the Purchaser will be returned to the Purchaser on the date of initial delivery of the Bonds upon completion of the closing.

The Purchaser agrees to accept delivery of the Initial Bond through DTC and make payment for the Initial Bond in immediately available funds at The Bank of New York Mellon Trust Company N.A., Dallas, Texas, no later than 10:00 A.M., Central time, on February 23, 2012 or thereafter on the date the Initial Bond is tendered for delivery, pursuant to the terms set forth in the Official Notice of Sale.

The undersigned duly authorized representative of the Purchaser agrees to complete, execute and deliver to the District by the date of delivery of the Bonds, a certificate relating to the "issue price" of the Bonds in the form and to the effect attached to or accompanying the Official Notice of Sale.

Respectfully submitted,

________________________ (Syndicate Member)	________________________ (Syndicate Manager)
________________________ (Syndicate Member)	________________________ (Signature - Title)
________________________ (Syndicate Member)	________________________ (Telephone)

ACCEPTANCE CLAUSE

THE FOREGOING BID IS IN ALL THINGS HEREBY ACCEPTED this January 23, 2012 by Order of the Board of Trustees of the Barbers Hill Independent School District.

President, Board of Trustees

ATTEST:

Secretary, Board of Trustees

CERTIFICATE REGARDING ISSUE PRICE

The undersigned hereby certifies with respect to the sale of the Barbers Hill Independent School District Unlimited Tax Qualified School Construction Bonds, Taxable Series 2012 (Direct-Pay Subsidy Bonds, dated February 1, 2012 (the "Bonds"), as follows:

1. The undersigned is a duly authorized representative of the underwriter or of the manager of the syndicate of underwriters that purchased the Bonds from the Barbers Hill Independent School District (the "District") pursuant to a competitively bid sale. (Such underwriter or syndicate of underwriters is referred to herein as the "Initial Purchaser"). In this capacity, the undersigned is familiar with the facts stated herein.

2. The term "Initial Offering Price" means the initial offering prices (exclusive of accrued interest) for the Obligations (stated in term of dollars or as a percent of par) as set forth below.

MATURITY	PRINCIPAL AMOUNT	INITIAL OFFERING PRICE
2029	$ 7,085,000	______%

3. The term "Public" shall not include bond houses, brokers, and similar persons or organizations acting in the capacity of wholesalers or underwriters. The term "Sale Date" means the first day on which there was a binding contract in writing for the sale of the Bonds by the District to the Initial Purchaser on specific terms that were not later modified or adjusted in any material respect. In the case of the Bonds, the Sale Date is January __, 2012. The term "Issue Date" means the first day on which there is a physical delivery of the written evidence of the Bonds in exchange for the purchase price (but not earlier) than the day interest on the Bonds begins to accrue for federal income tax purposes). In the case of the Bonds, the Issue Date is February 23, 2012.

4. Based on the actual facts and reasonable expectations in existence, the Initial Offering Price for each Bond (a) represented the price (payable in cash, with no other consideration being included, and exclusive of accrued interest), at which the Initial Purchaser reasonably expected each such Bond would be sold to the Public, and (b) did not exceed what the Initial Purchaser believed to be the respective fair market value of each such Bond.

5. The Initial Purchaser has made a bona fide public offering to the Public of all the Bonds of each maturity at the Initial Offering Price set forth above in paragraph 2. The Initial Offering Price was determined on the Sale Date based on the Initial Purchaser's reasonable expectations regarding the Initial Offering Price, and at least 10 percent of all of the Bonds, except any Retained Bonds (as defined below) were sold to the Public at the Initial Offering Prices. For the Bonds maturing in the year _____ of which at least 10 percent of each maturity was not sold to the Public at the Initial Offering Prices (the "Retained Bonds), the Initial Purchaser reasonably expected, as of the Sale Date to sell a substantial amount of each maturity of such Bonds to the Public at the respective Initial Offering Prices.

6. The aggregate of the respective Initial Offering Price (the "Issue Price") of all of the Bonds, exclusive of accrued interest and without adjustment for any costs of issuance, is $___________. Interest on the Bonds will accrue from the date of delivery, and therefore, the Bonds will be issued with no pre-issuance accrued interest.

[Signature Page Follows]

We acknowledge that the representations herein regarding the Initial Offering Price of the Bonds will be relied on by the District with respect to its compliance with the conditions imposed by Sections 54F and 6431 of the Internal Revenue Code of 1986, as amended (the "Code") and the Treasury Regulations and IRS rulings and notices thereunder with respect to the Bonds, and by Andrews Kurth LLP, Bond Counsel to the District in connection with rendering its opinion.

EXECUTED and DELIVERED as of and on the ___ day of ___________ 2012.

INITIAL PURCHASER

____

By:_________________________________
Name:______________________________
Title:_______________________________

Rating: Moody's "Aaa"
S&P "AAA"
(See "RATINGS" and "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" herein)

PRELIMINARY OFFICIAL STATEMENT
Dated: January 12, 2012

<u>TAXABLE NEW ISSUE</u>: BOOK-ENTRY-ONLY

Interest to be paid on the Bonds will be included in gross income for federal income tax purposes. See "TAX MATTERS" herein.

$7,085,000
BARBERS HILL INDEPENDENT SCHOOL DISTRICT
(A political subdivision of the State of Texas located in Chambers County, Texas)

UNLIMITED TAX QUALIFIED SCHOOL CONSTRUCTION BONDS, TAXABLE SERIES 2012
(Direct-Pay Subsidy Bonds)

Dated: February 1, 2012 **Due: February 15, 2029**
Interest Accrues from Delivery Date

The Barbers Hill Independent School District Unlimited Tax Qualified School Construction Bonds, Taxable Series 2012 (Direct-Pay Subsidy Bonds) (the "Bonds") are issued pursuant to the Constitution and general laws of the State of Texas, particularly Sections 45.001 and 45.003(b)(1), Texas Education Code, as amended, an election held in the Barbers Hill Independent School District (the "District") on October 15, 2005 and May 14, 2011, and the order adopted by the Board of Trustees on the date of the sale of the Bonds (the "Order").

The District expects to designate the Bonds as "qualified school construction bonds ("Qualified School Construction Bonds") pursuant to Section 54F of the Code. An issuer of Qualified Tax Credit Bonds must receive an allocation of the national qualified school construction bond limitation. The State received an allocation of $538,585,000 in 2009 and $547,674,000 in 2010 from the United States Department of Treasury, and the Texas Education Agency (the "TEA") is responsible for further allocation of such funds to issuers within the State. The District submitted an application to the TEA and received an allocation sufficient for the issuance of the Bonds.

The District expects to irrevocably elect, or has irrevocably elected, to designate the Bonds as "specified tax credit bonds" within the meaning of Section 6431(f)(3)(B) of the Code. Therefore, the District will be eligible to receive a cash subsidy from the United States Treasury in connection with such election. Pursuant to Section 6431 of the Code, the District expects to receive cash subsidy payments (the "Federal Subsidy") from the United States Treasury equal to the lesser of (i) 100 percent of the interest payable on an interest payment date for the Bonds, or (ii) the amount of interest which would have been payable under such Bond on such interest payment date if such interest were determined at the applicable credit rate determined under Section 54A(b)(3) of the Code with respect to such Bond. The Federal Subsidy received by the District will not be pledge to payment of the Bonds and may be used for any lawful purpose of the District, including but not limited to, the payment of debt service on the Bonds. No holder of the Bonds will be entitled to a tax credit with respect to the Bonds.

Although the District expects to receive the Federal Subsidy contemporaneously with each applicable interest payment date of the Bonds, the District anticipates that until the subsidy program is fully implemented there may be a delay in the receipt of the payments. Accordingly, the District has covenanted and is prepared to levy ad valorem taxes for the full amount of debt service payments.

The receipt of the Federal Subsidy is subject to certain requirements, including the filing of a form with the Internal Revenue Service (the "IRS") prior to each interest payment date. The Federal Subsidy does not constitute a full faith and credit guarantee of the United States Government, but is required to be paid by the United States Treasury under the Code

Interest on the Bonds will accrue from their date of initial delivery and will be payable on February 15 and August 15 of each year, commencing August 15, 2012, until maturity or prior redemption, and will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The Bonds will be issued in fully registered form in principal denominations of $5,000 or any integral multiple thereof. Principal of the Bonds will be payable by the Paying Agent/Registrar, which initially is The Bank of New York Mellon Trust Company, N.A., Dallas, Texas (the "Paying Agent/Registrar"), upon presentation and surrender of the Bonds for payment. Interest on the Bonds is payable by check dated as of the interest payment date and mailed by the Paying Agent/Registrar to the registered owners as shown on the records of the Paying Agent/Registrar on the close of business as of the last business day of the month next preceding each interest payment date (the "Record Date").

The Bonds are payable as to principal and interest from the proceeds of an ad valorem tax levied, without legal limit as to rate or amount, against all taxable property located within the District. (See "THE BONDS - Security".) The District has applied for and received conditional approval from the Texas Education Agency for payment of the principal of and interest on the Bonds to be guaranteed under the Texas Permanent School Fund Guarantee Program, which guarantee will automatically become effective when the Attorney General of the State of Texas (the "Attorney General") approves the Bonds. (See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM"; see also "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS" and "CURRENT PUBLIC SCHOOL FINANCE SYSTEM" for a discussion of recent developments in Texas law affecting the financing of school districts in Texas.)

The District intends to utilize the Book-Entry-Only System of The Depository Trust Company ("DTC"). Such Book-Entry-Only System will affect the method and timing of payment and the method of transfer of the Bonds. (See "BOOK-ENTRY-ONLY SYSTEM").

Proceeds from the sale of the Bonds will be used for the purposes of (1) constructing, renovating, designing, acquiring, and equipping school facilities in the District and (2) paying the costs of issuing the Bonds. (See "THE BONDS - Authorization and Purpose").

The Bonds are subject to redemption in whole or in part at the times and prices and in the amounts described herein. (See "THE BONDS - Redemption").

The Bonds are offered for delivery when, as and if issued, and received by the initial purchaser (the "Purchaser") subject to the approval of legality by the Attorney General of the State of Texas and the approval of certain legal matters by Andrews Kurth LLP, Houston, Texas, Bond Counsel. The Bonds are expected to be available for initial delivery through the services of DTC on or about February 23, 2012.

$7,085,000
BARBERS HILL INDEPENDENT SCHOOL DISTRICT
UNLIMITED TAX QUALIFIED SCHOOL CONSTRUCTION BONDS, SERIES 2012

MATURITY SCHEDULE
Base CUSIP No.: 067167[1]

Maturity Date 2/15	Principal Amount	Interest Rate	Initial Yield	CUSIP No. Suffix[1]
2029	$7,085,000			

(Interest to accrue from the Delivery Date)

[1] CUSIP numbers are included solely for the convenience of owners of the Bonds. CUSIP is a registered trademark of the American Bankers Association. CUSIP data herein is provided by CUSIP Global Services, managed by Standard & Poor's Financial Services LLC on behalf of The American Bankers Association. This data is not intended to create a database and does not serve in any way as a substitute for the CUSIP Services. None of the District, the Financial Advisor, nor the Purchaser is responsible for the selection or correctness of the CUSIP numbers set forth herein.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

APPOINTED OFFICIALS

Name	**Position**	**Length of Education Service**	**Length of Service with District**
Dr. Greg Poole	Superintendent	25 Years	5 Years
John Koonce*	Assistant Superintendent / Finance	24 Years	24 Years
Stanley Frazier	Assistant Superintendent / Planning and Operations	24 Years	4 Years
Rebecca McManus	Director of Finance	7 Years	5 Years

**Mr. Koonce will be retiring summer 2012. Rebecca McManus will assume his role and duties and is currently working closely with Mr. Koonce for an effective transition.*

CONSULTANTS AND ADVISORS

Andrews Kurth LLP, Houston, Texas	Bond Counsel
Southwest Securities, Dallas, Texas	Financial Advisor
Hereford, Lynch, Sellars & Kirkham, Cleveland, Texas	Certified Public Accountants

For additional information, contact:

John Koonce
Assistant Superintendent / Finance
Barbers Hill ISD
9600 Eagle Drive
Mont Belvieu, Texas 77580
(281) 576-2221 X1206

Doug Whitt
Senior Vice President
Southwest Securities
700 Central Expressway, Suite 410
Allen, Texas 75013
(214) 859-9498

Brian Grubbs
Senior Vice President
Southwest Securities
700 Central Expressway, Suite 410
Allen, Texas 75013
(214) 859-9485

USE OF INFORMATION IN OFFICIAL STATEMENT

For purposes of compliance with Rule 15c2-12 of the United States Securities and Exchange Commission ("Rule 15c2-12"), as amended, and in effect on the date of this Preliminary Official Statement, this document constitutes an "official statement" of the District with respect to the Bonds that has been deemed "final" by the District as of its date except for the omission of no more than the information permitted by Rule 15c2-12.

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

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

The information set forth herein has been obtained from the District and other sources believed to be reliable, but such information is not guaranteed as to accuracy or completeness and is not to be construed as the promise or guarantee of the Financial Advisor. This Official Statement contains, in part, estimates and matters of opinion which are not intended as statements of fact, and no representation is made as to the correctness of such estimates and opinions, or that they will be realized.

The information and expressions of opinion contained herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the District or other matters described herein. See "CONTINUING DISCLOSURE OF INFORMATION" for a description of the District's undertaking to provide certain information on a continuing basis.

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

NONE OF THE DISTRICT, ITS FINANCIAL ADVISOR, OR THE PURCHASERS MAKE ANY REPRESENTATION OR WARRANTY WITH RESPECT TO THE INFORMATION CONTAINED IN THIS OFFICIAL STATEMENT REGARDING THE DEPOSITORY TRUST COMPANY ("DTC") OR ITS BOOK-ENTRY-ONLY SYSTEM OR THE AFFAIRS OF THE TEXAS EDUCATION AGENCY DESCRIBED UNDER "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM", AS SUCH INFORMATION WAS PROVIDED BY DTC AND THE TEXAS EDUCATION AGENCY, RESPECTIVELY.

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

TABLE OF CONTENTS

SELECTED DATA FROM THE OFFICIAL STATEMENT

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

The District	The Barbers Hill Independent School District (the "District") is a political subdivision of the State of Texas located in Chambers County, Texas. The District is governed by a seven-member Board of Trustees (the "Board"). Policy-making and supervisory functions are the responsibility of, and are vested in, the Board. The Board delegates administrative responsibilities to the Superintendent of Schools who is the chief administrative officer of the District. Support services are supplied by consultants and advisors.
The Bonds	The Bonds are being issued as Unlimited Tax Qualified School Construction Bonds, Taxable Series 2012 (Direct-Pay Subsidy Bonds) (the "Bonds"). The Bonds are being issued in the principal amount of $7,085,000 pursuant to the Constitution and general laws of the State of Texas, particularly Sections 45.001 and 45.003(b)(1), as amended, Texas Education Code, an election held in the District on October 15, 2005 and May 14, 2011 and the order adopted by the Board (the "Order") on the date of sale of the Bonds. Proceeds from the sale of the Bonds will be used for the purposes of (1) constructing, renovating, designing, acquiring, and equipping school facilities in the District and (2) paying the costs of issuing the Bonds. (See "THE BONDS - Authorization and Purpose"). **Interest on the Bonds will be included in an owner's federal income tax liability.**
Designation as Qualified School Construction Bonds	The District has designated, or will designate, the Bonds as "qualified school construction bonds" ("Qualified School Construction Bonds") under Section 54F of the Internal Revenue Code of 1986, as amended (the "Code"). Further, the District has made an irrevocable election to treat the Bonds as "specified tax credit bonds" within the meaning of Section 6431(f)(3)(B) of the Code.
Tax Matters	Interest on the Bonds will be includable in the gross income of the holders thereof for federal income tax purposes under Section 61 of the Code. See "Tax Matters" below.
Paying Agent/Registrar	The initial Paying Agent/Registrar is The Bank of New York Mellon Trust Company, N.A., Dallas, Texas. The District intends to use the Book-Entry-Only System of DTC. (See "BOOK-ENTRY-ONLY SYSTEM" herein).
Security	The Bonds will constitute direct and voted obligations of the District, payable as to principal and interest from ad valorem taxes levied annually against all taxable property located within the District, without legal limitation as to rate or amount. Payments of principal and interest on the Bonds will be further secured by the corpus of the Permanent School Fund of Texas. (See "THE BONDS – Security", "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS", and "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM").
Redemption	The Bonds are subject to redemption, prior to stated maturity at the times, prices, and in the amounts described herein. (See "THE BONDS – Redemption of Bonds").
Permanent School Fund Guarantee	The District has received conditional approval from the Texas Education Agency for the payment of the Bonds to be guaranteed under the Permanent School Fund Guarantee Program, which guarantee will automatically become effective when the Attorney General of Texas approves the Bonds. (See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM").
Rating	Moody's Investor Service, Inc. ("Moody's) and Standard & Poor's Ratings Services, a Standard & Poor's Financial Services LLC business ("S&P"), has assigned to the Bonds a rating of "Aaa" and "AAA" based upon the guaranteed repayment thereof under the Permanent School Fund Guarantee Program of the Texas Education Agency. The District's underlying rating without regard to credit enhancement is "AA3" by Moody's and "AA" by S&P. (See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" and "RATINGS" herein).
Payment Record	The District has never defaulted on the payment of its bonded indebtedness.
Legal Opinion	Delivery of the Bonds is subject to the approval by the Attorney General of the State of Texas and the rendering of an opinion as to legality by Andrews Kurth LLP, Houston, Texas, Bond Counsel.
Delivery	When issued, anticipated to be on or about February 23, 2012.

INTRODUCTORY STATEMENT

This Official Statement (the "Official Statement"), which includes the Appendices attached hereto, has been prepared by the Barbers Hill Independent School District, a political subdivision of the State of Texas located in Chambers County, Texas (the "District"), in connection with the offering by the District of its Unlimited Tax Qualified School Construction Bonds, Taxable Series 2012 (Direct-Pay Subsidy) (the "Bonds") identified on page ii hereof.

All financial and other information presented in this Official Statement has been provided by the District from its records, except for information expressly attributed to other sources. The presentation of information, including tables of receipts from taxes and other sources, is intended to show recent historic information, and is not intended to indicate future or continuing trends in the financial position or other affairs of the District. No representation is made that past experience, as is shown by that financial and other information, will necessarily continue or be repeated in the future.

There follows in this Official Statement descriptions of the Bonds and the order to be adopted by the Board of Trustees of the District authorizing the issuance of the Bonds (the "Order"), and certain other information about the District and its finances. All descriptions of documents contained herein are only summaries and are qualified in their entirety by reference to each such document. Copies of such documents may be obtained upon request by writing the Barbers Hill Independent School District, 9600 Eagle Drive, Mont Belvieu, Texas 77580 and, during the offering period, from the Financial Advisor, Southwest Securities, 700 Central Expressway South, Suite 410, Allen, Texas 75013, by electronic mail or upon payment of reasonable copying, mailing, and handling charges.

This Official Statement speaks only as to its date, and the information contained herein is subject to change. A copy of the Final Official Statement pertaining to the Bonds will be deposited with the Municipal Securities Rulemaking Board ("MSRB") through its Electronic Municipal Market Access ("EMMA") system. See "CONTINUING DISCLOSURE OF INFORMATION" herein for a description of the District's undertaking to provide certain information on a continuing basis.

For additional information regarding the District, see "Appendix A - Financial Information of the District" and "Appendix B - General Information Regarding the District and its Economy."

Concurrent Offerings

The Bonds are being offered by the District concurrently with the District's "Unlimited Tax School Building Bonds, Series 2012" (the "Tax-Exempt Bonds"). The Tax-Exempt Bonds in the approximate amount of $68,415,000 (preliminary, subject to change), are being issued pursuant to a separate order of the District and are offered under a separate disclosure document. This Official Statement only discloses the Bonds and investors who wish to purchase the Tax-Exempt Bonds should carefully review the Tax-Exempt Bonds disclosure documents.

THE BONDS

Authorization and Purpose

The Bonds are being issued in the principal amount of $7,085,000 pursuant to the Constitution and general laws of the State of Texas, particularly Sections 45.001 and 45.003(b)(1), Texas Education Code, as amended, elections held in the District on October 15, 2005 and May 14, 2011 (together the "Election"), and the Order. Proceeds from the sale of the Bonds will be used for the purposes of (1) constructing, renovating, designing, acquiring, and equipping school facilities and the purchase of the necessary sites for school facilities and (2) paying the costs of issuing the Bonds.

General Description

The Bonds will be dated February 1, 2012 but will bear interest from the date of initial delivery thereof. The Bonds will mature on the dates and in the principal amounts set forth on the inside cover page of this Official Statement. Interest on the Bonds will be computed on the basis of a 360-day year of twelve 30-day months, and is payable on August 15, 2012 and on each February 15 and August 15 thereafter until stated maturity or prior redemption.

The Bonds will be issued only as fully registered bonds. The Bonds will be issued in the denominations of $5,000 of principal or any integral multiple thereof within a maturity.

Interest on the Bonds is payable by check mailed on or before each interest payment date by the Paying Agent/Registrar, initially, The Bank of New York Mellon Trust Company, N.A., Dallas, Texas to the registered owner at the last known address as it appears on the Paying Agent/Registrar's books on the Record Date (as defined herein) or by such other customary banking arrangement acceptable to the Paying Agent/Registrar and the registered owner to whom interest is to be paid, provided, however, that such person shall bear all risk and expense of such other arrangements. The record date (the "Record Date") for the interest payable on any interest payment date is the last business day of the month next preceding such interest payment date. Principal of the Bonds will be payable only upon presentation of such Bonds at the corporate trust office of the Paying Agent/Registrar at maturity or prior redemption. So long as the Bonds are registered in the name of CEDE & CO. or other nominee for The Depository Trust Company, payments of principal and interest of the Bonds will be made as described in "BOOK-ENTRY-ONLY SYSTEM" herein.

If the date for the payment of the principal of or interest on the Bonds is a Saturday, Sunday, legal holiday or a day on which banking institutions in the city where the Paying Agent/Registrar is located are authorized by law or executive order to close, then the date for such payment shall be the next succeeding day which is not a Saturday, Sunday, legal holiday or a day on which banking institutions are authorized to close; and payment on such date shall have the same force and effect as if made on the original date payment was due.

The Bonds are being issued as "qualified school construction bonds" within the meaning of Section 54F of the Internal Revenue Code of 1986, as amended (the "Code") and are issued as "specified tax credit bonds" within the meaning of Section 6431 of the Code. See "TAX MATTERS" herein.

Qualified School Construction Bonds

The District expects to designate the Bonds as "qualified school construction bonds ("Qualified School Construction Bonds") pursuant to Section 54F of the Code. An issuer of Qualified Tax Credit Bonds must receive an allocation of the national qualified school construction bond limitation. The State received an allocation of $538,585,000 in 2009 and $547,674,000 in 2010 from the United States Department of Treasury, and the Texas Education Agency (the "TEA") is responsible for further allocation of such funds to issuers within the State. The District submitted an application to the TEA and received an allocation sufficient for the issuance of the Bonds.

The District expects to irrevocably elect, or has irrevocably elected, to designate the Bonds as "specified tax credit bonds" within the meaning of Section 6431(f)(3)(B) of the Code. Therefore, the District will be eligible to receive a cash subsidy from the United States Treasury in connection with such election. Pursuant to Section 6431 of the Code, the District expects to receive cash subsidy payments (the "Federal Subsidy") from the United States Treasury equal to the lesser of (i) 100 percent of the interest payable on an interest payment date for the Bonds, or (ii) the amount of interest which would have been payable under such Bond on such interest payment date if such interest were determined at the applicable credit rate determined under Section 54A(b)(3) of the Code with respect to such Bond. The Federal Subsidy received by the District will not be pledge to payment of the Bonds and may be used for any lawful purpose of the District, including but not limited to, the payment of debt service on the Bonds. No holder of the Bonds will be entitled to a tax credit with respect to the Bonds.

Although the District expects to receive the Federal Subsidy contemporaneously with each applicable interest payment date of the Bonds, the District anticipates that until the subsidy program is fully implemented there may be a delay in the receipt of the payments. Accordingly, the District has covenanted and is prepared to levy ad valorem taxes for the full amount of debt service payments.

The receipt of the Federal Subsidy is subject to certain requirements, including the filing of a form with the Internal Revenue Service (the "IRS") prior to each interest payment date. The Federal Subsidy does not constitute a full faith and credit guarantee of the United States Government, but is required to be paid by the United States Treasury under the Code.

Cumulative Sinking Fund Deposits

The Code provides that an issue of "qualified school construction bonds", which includes the Bonds, shall not fail to satisfy the programmatic requirements for such obligations by reason of any fund that is expected to be used to repay such qualified school construction bonds that (i) is funded at a rate not more rapid than equal annual installments, (ii) is funded in a manner reasonably expected to result in an amount not greater than the amount necessary to repay the obligations, and (iii) is invested at a yield that is not greater than the discount rate published by the Treasury on the date on which the District and the purchaser enter into a binding obligation concerning the sale and purchase of the Bonds (which discount rate for the Bonds is ___%). The District has obligated itself under the Order to make mandatory deposits into the Cumulative Sinking Fund Deposit Account, which is a subaccount of the Bond Fund created under the Order, with the Paying Agent/Registrar for the Bonds, on February 15 in each of the years and the respective amounts (preliminary, subject to change) set forth below:

Year	Deposit Amount	Cumulative Balance
2015	$ 470,000.00	$ 470,000.00
2016	470,000.00	940,000.00
2017	470,000.00	1,410,000.00
2018	470,000.00	1,880,000.00
2019	470,000.00	2,350,000.00
2020	470,000.00	2,820,000.00
2021	470,000.00	3,290,000.00
2022	470,000.00	3,760,000.00
2023	475,000.00	4,235,000.00
2024	475,000.00	4,710,000.00
2025	475,000.00	5,185,000.00
2026	475,000.00	5,660,000.00
2027	475,000.00	6,135,000.00
2028	475,000.00	6,610,000.00
2029	475,000.00	7,085,000.00

Any interest earnings from the investment of prior deposits will be applied as a credit against the District's next year's required Cumulative Sinking Fund Deposit Account deposit. Such deposits and any interest earned thereon (which is not used as a credit against periodic deposits) shall be used to pay the principal of the Bonds at stated maturity or prior redemption and are pledged to pay the debt service requirements on the Bonds. To the extent the aggregate cumulative sinking fund deposits and interest thereon total less than the principal amount of the Bonds due on such date, the District will contribute additional funds required to pay the debt service requirements on the Bonds upon prior redemption or on the stated maturity date for the Bonds.

Redemption

Optional Redemption

The Bonds are subject to redemption prior to Stated Maturity, at the option of the District, on any date from the Closing Date through August 14, 2021, as a whole or in part, in principal amounts of $5,000 or any integral multiple thereof, at the Make-Whole Redemption Price. In addition, the Bonds are subject to redemption prior to Stated Maturity, at the option of the District, on August 15, 2021, or on any date thereafter, as a whole or in part in principal amounts of $5,000 or any integral multiple thereof (and if within a Stated Maturity at random and by lot by the Paying Agent/Registrar), at the redemption price of par plus accrued interest to the date of redemption.

Special Mandatory Redemption

To the extent that 100% of the Available Project Proceeds are not expended for Qualified Purposes by the close of the Expenditure Period, the District shall redeem such Nonqualified Bonds in authorized denominations (rounded up to the next highest authorized denomination) within 90 days after the end of such period, at a redemption price equal to the principal amount of such Nonqualified Bonds, plus accrued (but unpaid) interest on such Nonqualified Bonds to the date of redemption, payable from such unexpended proceeds of sale of the Bonds held by the District.

DEFINITION OF TERMS. For purposes of this section, capitalized terms used herein have the following meanings:

"Available Project Proceeds" means proceeds of the sale of the Bonds other than proceeds used to pay costs of issuance (not to exceed 2 percent thereof) plus proceeds received from investing the proceeds of the sale of the Bonds.

"Expenditure Period" means the three year period beginning on the Delivery Date, plus any extension of such period granted by the Secretary of the Treasury.

"Make-Whole Redemption Price" means an amount equal to the greater of (i) the issue price of the Bonds set forth in the Order (but not less than 100%) of the principal amount of such Bonds to be redeemed or (ii) the sum of the present value of the remaining scheduled payments of principal and interest on the Bonds to be redeemed to the maturity date of such Bonds, not including any portion of those payments of interest accrued and unpaid as of the date on which the Bonds are to be redeemed, discounted to the date on which the Bonds are to be redeemed on a semi-annual basis, assuming a 360-day year containing twelve 30-day months, at the Treasury Rate plus one-hundred (100) basis points, plus accrued interest on the Bonds to be redeemed to the redemption date.

"Nonqualified Bonds" means the portion of the outstanding Bonds in an amount that, if the remaining Bonds were issued on the last day of the Expenditure Period, all of the Available Project Proceeds of the remaining Bonds would have been used for Qualified Purposes within the Expenditure Period.

"Qualified Purposes" means the construction, rehabilitation, or repair of a public school facility (including expenditures for the acquisition of equipment to be used in a portion of a public school facility being constructed, rehabilitated, or repaired with the proceeds of the Bonds) or for the acquisition of land on which such a facility is to be constructed with a portion of the proceeds of the Bonds.

Selection of Bonds to be Redeemed

The Bonds of a denomination larger than $5,000 may be redeemed in part (in increments of $5,000 or any integral multiple thereof). The Bonds to be partially redeemed must be surrendered in exchange for one or more new Bonds of the same series, stated maturity and interest rate for the unredeemed portion of the principal. If less than all of the Bonds of any stated maturity are to be redeemed, the District will determine the amounts of each maturity or maturities to be redeemed and will direct the Paying Agent/Registrar (or DTC while the Bonds are in Book-Entry-Only form) to select, at random and by lot, the particular Bonds, or portions thereof, within such maturity or maturities to be redeemed. If a Bond (or any portion of the principal sum thereof) will have been called for redemption and notice or such redemption will have been given, such Bond (or the principal amount thereof to be redeemed), will become due and payable on such redemption date and interest thereon will cease to accrue from and after the redemption date, provided funds for the payment of the redemption price and accrued interest thereon are held by the Paying Agent/Registrar on the redemption date.

Notice of Redemption

Not less than 30 days prior to a redemption date for the Bonds, a notice of redemption will be sent by United States mail, first class postage prepaid, in the name of the District and at the District's expense, by the Paying Agent/Registrar to each registered owner of a Bond to be redeemed in whole or in part at the address of the registered owner appearing on the registration books at the close of business on the business day next preceding the date of mailing such notice.

ANY NOTICE SO MAILED WILL BE CONCLUSIVELY PRESUMED TO HAVE BEEN DULY GIVEN, WHETHER OR NOT THE REGISTERED OWNER RECEIVES SUCH NOTICE. NOTICE HAVING BEEN SO GIVEN, THE BONDS CALLED FOR REDEMPTION WILL BECOME DUE AND PAYABLE ON THE SPECIFIED REDEMPTION DATE, AND NOTWITHSTANDING THAT ANY BOND OR PORTION THEREOF HAS NOT BEEN SURRENDERED FOR PAYMENT, INTEREST ON SUCH BOND OR PORTION THEREOF WILL CEASE TO ACCRUE.

All notices of redemption will (i) specify the date of redemption for the Bonds, (ii) identify the Bonds to be redeemed and, in the case of a portion of the principal amount to be redeemed, the principal amount thereof to be redeemed, (iii) state the redemption price, (iv) state that the Bonds, or the portion of the principal amount thereof to be redeemed, will become due and payable on the redemption date specified, and the interest thereon, or on the portion of the principal amount thereof to be redeemed, will cease to accrue from and after the redemption date, and (v) specify that payment of the redemption price for the Bonds, or the principal amount thereof to be redeemed, will be made at the designated corporate trust office of the Paying Agent/Registrar only upon presentation and surrender thereof by the registered owner. If a Bond is subject by its terms to redemption and has been called for redemption and notice of redemption thereof has been duly given or waived as provided in the Order, such Bond (or the principal amount thereof to be redeemed) so called for redemption will become due and payable, and on the redemption date designated in such notice, interest on said Bond (or the principal amount thereof to be redeemed) called for redemption will cease to accrue and such Bond will not be deemed to be outstanding.

The Paying Agent/Registrar and the District, so long as a Book-Entry-Only System is used for the Bonds, will send any notice of redemption, notice of proposed amendment to the Order or other notices with respect to the Bonds only to DTC. Any failure by DTC to advise any DTC participant, or of any DTC participant or indirect participant to notify the Beneficial Owner, will not affect the validity of the redemption of the Bonds called for redemption or any other action premised or any such notice. Redemption of portions of the Bonds by the District will reduce the outstanding principal amount of such Bonds held by DTC. In such event, DTC may implement, through its Book-Entry-Only System, a redemption of such Bonds held for the account of DTC participants in accordance with its rules or other agreements with DTC participants and then DTC participants and indirect participants may implement a redemption of such Bonds from the Beneficial Owners. Any such selection of Bonds to be redeemed will not be governed by the applicable Order and will not be conducted by the District or the Paying Agent/Registrar. Neither the District nor the Paying Agent/Registrar will have any responsibility to DTC participants, indirect participants or the persons for whom DTC participants act as nominees, with respect to the payments on the Bonds or the providing of notice to DTC participants, indirect participants, or Beneficial Owners of the selection of portions of the Bonds for redemption.

Security

The Bonds are direct obligations of the District and are payable as to both principal and interest from ad valorem taxes levied on all taxable property within the District, without legal limitation as to rate or amount. The District has received conditional approval from the Texas Education Agency for the payment of the Bonds to be guaranteed under the State of Texas Permanent School Fund Guarantee Program (hereinafter defined), which guarantee will automatically become effective when the Attorney General of Texas approves the Bonds. (See "AD VALOREM TAX PROCEDURES" and "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS" and "THE PERMANENT SCHOOL FUND GUARANTEE" herein).

Permanent School Fund Guarantee

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

In the event the District defeases any of the Bonds, the payment of such defeased Bonds will cease to be guaranteed by the Permanent School Fund Guarantee.

Legality

The Bonds are offered when, as and if issued, subject to the approval of legality by the Attorney General of the State of Texas and Andrews Kurth LLP, Houston, Texas, Bond Counsel. (See "LEGAL MATTERS" and "Appendix C - Form of Legal Opinion of Bond Counsel").

Payment Record

The District has never defaulted on the payment of its bonded indebtedness.

Amendments

The District may amend the Order without the consent of or notice to any registered owner in any manner not detrimental to the interests of the registered owners, including the curing of any ambiguity, inconsistency, or formal defect or omission therein and the provisions of the Order may be amended at any time to ensure that the Bonds continue to qualify as "qualified school construction bonds" and "qualified bonds", pursuant to the provisions of the Order and the tax credit agreement (as further defined and described in the Order). In addition, the District may, with the written consent of the owners of a majority in aggregate principal amount of the Bonds then outstanding and affected thereby, amend, add to, or rescind any of the provisions of the Order; except that, without the consent of the registered owners of all of the Bonds affected, no such amendment, addition or rescission may (1) make any change in the maturity of any of the outstanding Bonds; (2) amend the redemption price of the Bonds; (3) reduce the rate of interest borne by any of the outstanding Bonds; (4) reduce the amount of the principal or payable on any outstanding Bonds; (5) modify the terms of payment of principal, or of interest on outstanding Bonds or any of them or impose any condition with respect to such payment; or (6) change the minimum percentage of the principal amount of the Bonds necessary for consent to such amendment.

Defeasance

The Bonds may be defeased in any manner now or hereafter allowed by law.

REGISTERED OWNERS' REMEDIES

The Order establishes specific events of default with respect to the Bonds. If the District defaults in the payment, when due, of principal, interest, redemption price of the Bonds or defaults in the observation or performance of any other covenants, conditions, or obligations set forth in the Order, and the State fails to honor the Permanent School Fund Guarantee as hereinafter discussed, the failure to perform which materially, adversely affects the rights of the owners, including but not limited to, their prospective ability to be repaid in accordance with the Order, the Order provides that any registered owner is entitled to seek a writ of mandamus from a court of proper jurisdiction requiring the District to make such payment or observe and perform such covenants, obligations, or conditions. The issuance of a writ of mandamus may be sought if there is no other available remedy at law to compel performance of the Bonds or the Order and the District's obligations are not uncertain or disputed, as well as to enforce the rights of payment under the Permanent School Fund Guarantee. The issuance of a writ of mandamus is controlled by equitable principles and rests with the discretion of the court, but may not be arbitrarily refused. There is no acceleration of stated maturity of the Bonds in the event of default and, consequently, the remedy of mandamus may have to be relied upon from year to year. The Order does not provide for the appointment of a trustee to represent the interest of the owners upon any failure of the District to perform in accordance with the terms of the Order, or upon any other condition and accordingly all legal actions to enforce such remedies would have to be undertaken at the initiative of, and be financed by, the registered owners. The Texas Supreme Court has ruled in Tooke v. City of Mexia, 197 S.W.3d 325 (Tex. 2006), that a waiver of sovereign immunity in a contractual dispute must be provided for by statute in "clear and unambiguous" language. Therefore, Bondholders may not be able to bring such a suit against the District for breach of the Bonds or Order covenants in the absence of District action. Even if a judgment against the District could be obtained, it could not be enforced by direct levy and execution against the District's property. Further, the registered owners cannot themselves foreclose on property within the District or sell property within the District to enforce the tax lien on taxable property to pay the principal of and interest on the Bonds. Furthermore, the District is eligible to seek relief from its creditors under Chapter 9 of the U.S. Bankruptcy Code ("Chapter 9"). Although Chapter 9 provides for the recognition of a security interest represented by a specifically pledged source of revenues, the pledge of ad valorem taxes in support of a general obligation of a bankrupt entity is not specifically recognized as a security interest under Chapter 9. Chapter 9 also includes an automatic stay provision that would prohibit, without Bankruptcy Court approval, the prosecution of any other legal action by creditors or bondholders of an entity which has sought protection under Chapter 9. Therefore, should the District avail itself of Chapter 9 protection from creditors, the ability to enforce would be subject to the approval of the Bankruptcy Court (which could require that the action be heard in Bankruptcy Court instead of other federal or state court); and the Bankruptcy Code provides for broad discretionary powers of a Bankruptcy Court in administering any proceeding brought before it. See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" herein for a description of the procedures to be followed for payment of the Bonds by the Permanent School Fund in the event the District fails to make a payment on the Bonds when due. The opinion of Bond Counsel will note that all opinions relative to the enforceability of the Order and the Bonds are qualified with respect to the customary rights of debtors relative to their creditors and by general principles of equity which permit the exercise of judicial discretion.

BOOK-ENTRY-ONLY SYSTEM

This section describes how ownership of the Bonds is to be transferred and how the principal of and interest on the Bonds are to be paid to and credited by DTC while the Bonds are registered in its nominee name. The information in this section concerning DTC and the Book-Entry-Only System has been provided by DTC for use in disclosure documents such as this Official Statement. The District, the Financial Advisor and the Purchaser believe the source of such information to be reliable, but take no responsibility for the accuracy or completeness thereof.

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

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

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

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

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers. Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Bond documents. For example, Beneficial Owners of Bonds may wish to ascertain that the nominee holding the Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

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

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

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

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

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

The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that the District believes to be reliable, but none of the District, the Financial Advisor nor the Underwriters take any responsibility for the accuracy thereof.

Use of Certain Terms in Other Sections of this Official Statement

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

REGISTRATION, TRANSFER AND EXCHANGE

Paying Agent/Registrar

The initial Paying Agent/Registrar for the Bonds is The Bank of New York Mellon Trust Company, N.A., Dallas, Texas. In the Order, the District covenants to maintain and provide a Paying Agent/Registrar until the Bonds are duly paid.

Successor Paying Agent/Registrar

Provision is made in the Order for replacing the Paying Agent/Registrar. If the District replaces the Paying Agent/Registrar, such Paying Agent/Registrar shall, promptly upon the appointment of a successor, deliver the Paying Agent/Registrar's records to the successor Paying Agent/Registrar, and the successor Paying Agent/Registrar shall act in the same capacity as the previous Paying Agent/Registrar. Any successor Paying Agent/Registrar selected by the District shall be a commercial bank or trust company organized under the laws of the United States or any state or other entity duly qualified and legally authorized to serve and perform the duties of the Paying Agent/Registrar for the Bonds. Upon any change in the Paying Agent/Registrar for the Bonds, the District has agreed to promptly cause a written notice thereof to be sent to each registered owner of the Bonds by United States mail, first class, postage prepaid, which notice shall also give the address of the new Paying Agent/Registrar.

Initial Registration

Definitive Bonds will be initially registered and delivered only to CEDE & CO., the nominee of DTC pursuant to the Book-Entry-Only System described herein.

Future Registration

In the event the Book-Entry-Only System is discontinued, the Bonds may be transferred, registered and assigned on the registration books only upon presentation and surrender of the Bonds to the Paying Agent/Registrar, and such registration and transfer shall be without expense or service charge to the registered owner, except for any tax or other governmental charges required to be paid with respect to such registration and transfer. A Bond may be assigned by the execution of an assignment form on the Bonds or by other instrument of transfer and assignment acceptable to the Paying Agent/Registrar. A new Bond or Bonds will be delivered by the Paying Agent/Registrar in lieu of the Bond being transferred or exchanged at the corporate trust office of the Paying Agent/Registrar, or sent by United States registered mail to the new registered owner at the registered owner's request, risk and expense. To the extent possible, new Bonds issued in an exchange or transfer of Bonds will be delivered to the registered owner or assignee of the registered owner in not more than three (3) business days after the receipt of the Bonds to be canceled in the exchange or transfer and the written instrument of transfer or request for exchange duly executed by the registered owner or his duly authorized agent, in form satisfactory to the Paying Agent/Registrar. New Bonds registered and delivered in an exchange or transfer shall be in authorized denominations and for a like aggregate principal amount as the Bonds surrendered for exchange or transfer.

Record Date For Interest Payment

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

Limitation on Transfer of Bonds

Neither the District nor the Paying Agent/Registrar shall be required to issue, transfer or exchange any Bond during the period beginning at the close of business on any Record Date and ending with the next interest payment date or, with respect to any Bond or portion thereof called for redemption prior to maturity, within 45 days prior to its redemption date.

Replacement Bonds

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

AD VALOREM TAX PROCEDURES

Property Tax Code and County Wide Appraisal District

The Texas Property Tax Code (the "Tax Code") provides for county-wide appraisal and equalization of taxable property values and establishes in each county of the State an appraisal district and an appraisal district responsible for appraising property for all taxable units within the county. The Chambers County Appraisal District (the "Appraisal District") is responsible for appraising property within the District as of January 1 of each year. The appraisal values set by the Appraisal District are subject to review and change by the Appraisal Review Board (the "Appraisal Review Board") which is appointed by the Appraisal District’s Board of Directors. Such appraisal rolls, as approved by the Appraisal Review Board, are used by the District in establishing its tax roll and tax rate.

Property Subject to Taxation by the District

Except for certain exemptions provided by Texas law, all real and certain tangible personal property with a tax situs in the District is subject to taxation by the District. Principal categories of exempt property (including certain exemptions which are subject to local option by the Board) include property owned by the State of Texas or its political subdivisions if the property is used for public purposes; property exempt from ad valorem taxation by federal law; certain improvements to real property and certain tangible personal property located in designated reinvestment zones on which the District has agreed to abate ad valorem taxes, certain household goods, family supplies and personal effects; farm products owned by the producers; certain property of a nonprofit corporation used in scientific research and educational activities benefiting a college or university; and designated historic sites. Other principal categories of exempt property include tangible personal property not held or used for production of income; solar and windpowered energy devices; most individually owned automobiles; $10,000 State mandated exemption to residential homesteads of persons ages 65 or over; a State mandated exemption up to a maximum of $12,000 for real or personal property of disabled veterans or the surviving spouse or children of an individual who died while on active duty in the armed forces; a State mandated $15,000 in market value exemption for all residential homesteads (see "Residential Homestead Exemptions" below); and certain classes of intangible property. A disabled veteran who receives from the United States Department of Veterans Affairs or its successor 100% disability compensation due to a service-connected disability and a rating of 100% disabled or of individual unemployability is entitled to an exemption from taxation of the total appraised value of the veteran's residence homestead. In addition, except for increases attributable to certain improvements, the District is prohibited by state law from increasing the total ad valorem tax on the residence homestead of persons 65 years of age or older or of disabled persons above the amount of tax imposed in the year such residence qualified for an exemption based on the age or disability of the owner. The freeze on ad valorem taxes on the homesteads of persons 65 years of age or older and the disabled is also transferable to a different residence homestead. Also, a surviving spouse of a taxpayer who qualifies for the freeze on ad valorem taxes is entitled to the same exemption so long as (i) the deceased spouse died in a year in which the deceased spouse qualified for the exemption, (ii) the surviving spouse was 55 or older when the deceased spouse died and (iii) the property was the residence homestead of the surviving spouse when the deceased spouse died and remains the residence homestead of the surviving spouse. Pursuant to a constitutional amendment approved by the voters on May 12, 2007, legislation was enacted to reduce the school property tax limitation imposed by the freeze on taxes paid on residence homesteads of persons 65 years of age or over or of disabled persons to correspond to reductions in local school district tax rates from the 2005 tax year to the 2006 tax year and from the 2006 tax year to the 2007 tax year (see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - General" herein). The school property tax limitation provided by the constitutional amendment and enabling legislation apply to the 2007 and subsequent tax years. Owners of agricultural and open space land, under certain circumstances, may request valuation of such land on the basis of productive capacity rather than market value. Article VIII, Section 1-j of the Texas Constitution provides for an exemption from ad valorem taxation for "freeport property," which is defined as goods detained in the state for 175 days or less for the purpose of assembly, storage, manufacturing, processing or fabrication. Taxing units that took action prior to April 1, 1990 may continue to tax freeport property and decisions to continue to tax freeport property may be reversed in the future. However, decisions to exempt freeport property are not subject to reversal. In addition, under Section 11.253 of the Texas Tax Code, "Goods-in-transit", representing a category of tangible personal property that is distinguished from "freeport goods", are exempt from taxation unless a taxing unit opts out of the exemption. Goods-in-transit are defined as tangible personal property that: (i) is acquired in or imported into the state to be forwarded to another location in the state or outside the state; (ii) is detained at a location in the state in which the owner of the property does not have a direct or indirect ownership interest for assembling, storing, manufacturing, processing, or fabricating purposes by the person who acquired or imported the property; and (iii) is transported to another location in the state or outside the state not later than 175 days after the date the person acquired the property in or imported the property into the state. Goods-in-transit does not include oil, natural gas, petroleum products, aircraft, dealer's motor vehicle inventory, dealer's vessel and outboard motor inventory, dealer's heavy equipment inventory, or retail manufactured housing inventory. The decision to tax goods-in-transit or to exempt them from taxation can be made on an annual basis after a public hearing is conducted to be effected for the following calendar year (though an election to opt out of the exemption remains in effect until repealed). A taxpayer may receive only one of the freeport or goods-in-transit exemptions for tangible personal property. The District has adopted a resolution to tax tangible personal property in transit which would otherwise be exempt pursuant to Texas Tax Code, Section 11.253. See "THE PROPERTY TAX CODE AS APPLIED TO THE DISTRICT" and "APPENDIX A - FINANCIAL INFORMATION OF THE DISTRICT - ASSESSED VALUATION" for a schedule of the amount of exemptions granted by the District.

A city or county may create a tax increment financing zone ("TIF") within the city or county with defined boundaries and establish a base value of taxable property in the TIF at the time of its creation. Overlapping taxing units, including school districts, may agree with the city or county to contribute all or part of future ad valorem taxes levied and collected against the "incremental value" (taxable value in excess of the base value) of taxable real property in the TIF to pay or finance the costs of certain public improvements in the TIF, and such taxes levied and collected for and on behalf of the TIF are not available for general use by such contributing taxing units. Prior to September 1, 2001, school districts were allowed to enter into tax abatement agreements to encourage economic development. Under such agreements, a property owner agrees to construct certain improvements on its property. The school district in turn agrees not to levy a tax on all or part of the increased value attributable to the improvements until the expiration of the agreement. The abatement agreement could last for a period of up to 10 years. Effective September 1, 2001, school districts may not enter into tax abatement agreements under the general statute that permits cities and counties to initiate tax abatement agreements. In addition, credit will not be given by the Commissioner of Education in determining a district's property value wealth per student for (1) the appraisal value, in excess of the "frozen" value, of property that is located in a TIF created after May 31, 1999 (except in certain limited circumstances where the city creating the TIF gave notice prior to May 31, 1999 to all other taxing units that levy ad valorem taxes in the TIF of its intention to create the TIF and the TIF was created and had its final project and financing plan approved by the municipality prior to August 31, 1999) or (2) for the loss of value of abated property under any abatement agreement entered into after May 31, 1993.

Notwithstanding the foregoing, in 2001 the Legislature enacted legislation known as the Texas Economic Development Act, which provides incentives for certain school districts to grant limitations on appraised property values and provide ad valorem tax credits to certain corporations and limited liability companies to encourage economic development within the district. Generally, during the last eight years of the ten-year term of a tax limitation agreement, the school district may only levy and collect ad valorem taxes for maintenance and operation purposes on the agreed-to limited appraised property value. The taxpayer is entitled to a tax credit from the school district for the amount of taxes imposed during the first two years of the tax limitation agreement on the appraised value of the property above the agreed-to limited value. Additional State funding is provided to a school district for each year of such tax limitation in the amount of the tax credit provided to the taxpayer. During the first two years of a tax limitation agreement, the school district may not adopt a tax rate that exceeds the district's rollback tax rate (see "AD VALOREM TAX PROCEDURES – Public Hearing and Rollback Tax Rate").

Valuation of Property for Taxation

Generally, property in the District must be appraised by the Appraisal District at market value as of January 1 of each year. In determining the market value of property, different methods of appraisal may be used, including the cost method of appraisal, the income method of appraisal and the market data comparison method of appraisal, and the method considered most appropriate by the chief appraiser is to be used. Once an appraisal roll is prepared and finally approved by the Appraisal Review Board, it is used by the District in establishing its tax rolls and tax rate. Assessments under the Tax Code are based on one hundred percent (100%) of market value, except as described below, and no assessment ratio can be applied.

State law further limits the appraised value of a residence homestead for a tax year to an amount that would not exceed the lesser of (1) the property's market value in the most recent tax year in which the market value was determined by the appraisal district or (2) the sum of (a) 10% of the property's appraised value in the preceding tax year, plus (b) the property's appraised value the preceding tax year, plus (c) the market value of all new improvements to the property.

Article VII of the Texas Constitution and the Tax Code permit land designated for agricultural use, open space or timberland to be appraised at its value based on the land's capacity to produce agricultural or timber products rather than at its fair market value. Landowners wishing to avail themselves of the agricultural use designation must apply for the designation, and the appraiser is required by the Tax Code to act on each claimant's right to the designation individually. If a claimant receives the designation and later loses it by changing the use of the property or selling it to an unqualified owner, the District can collect taxes for previous years based on the new value, including three years for agricultural use and five years for agricultural open-space land and timberland prior to the loss of the designation.

The Tax Code requires the Appraisal District to implement a plan for periodic reappraisal of property to update appraisal values. The plan must provide for appraisal of all real property in the Appraisal District at least once every three years. The District, at its expense, has the right to obtain from the Appraisal District current estimates of appraised values within the District or an estimate of any new property or improvements within the District. While such current estimates of appraisal values may serve to indicate the rate and extent of growth of taxable values within the District, it cannot be used for establishing a tax rate within the District until such time as the Appraisal District chooses to formally include such values on their appraisal rolls.

Residential Homestead Exemptions

Under Section 1-b, Article VIII of the Texas Constitution and State law, the governing body of a political subdivision, at its option, may grant an exemption of not less than $3,000 of the market value of the residence homestead of persons 65 years of age or older or the disabled from all ad valorem taxes thereafter levied by the political subdivision.

Once authorized, such exemption may be repealed or decreased or increased in amount (i) by the governing body of the political subdivision or (ii) by a favorable vote of a majority of the qualified voters at an election called by the governing body of the political subdivision, which election must be called upon receipt of a petition signed by at least 20% of the number of qualified voters who voted in the preceding election of the political subdivision. In the case of a decrease, the amount of the exemption may not be reduced to less than $3,000 of the market value.

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

In addition to any other exemptions provided by the Property Tax Code, the governing body of a political subdivision, at its option, may grant an exemption of up to 20% of the market value of residence homesteads, with a minimum exemption of $5,000.

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

District and Taxpayer Remedies

Under certain circumstances, taxpayers and taxing units, including the District, may appeal orders of the Appraisal Review Board by filing a petition for review in district court within 45 days after notice is received that a final order has been entered. In such event, the property value in question may be determined by the court, or by a jury, if requested by any party, or through binding arbitration, if requested by the taxpayer. Additionally, taxing units may bring suit against an Appraisal District to compel compliance with the Tax Code.

Levy and Collection of Taxes

The District is responsible for the collection of its taxes, unless it elects to transfer such functions to another governmental entity. By the later of September 30th or 60 days after the certified appraisal roll is delivered to the District, the rate of taxation must be set by the Board based upon the valuation of property within the District as of the preceding January 1 and the amount required to be raised for debt service and maintenance and operations purposes. Taxes are due October 1, or when billed, whichever comes later, and become delinquent after January 31 of the following year. A delinquent tax incurs a penalty from six percent (6%) to twelve percent (12%) of the amount of the tax, depending on the time of payment, and accrues interest at the rate of one percent (1%) per month. If the tax is not paid by the following July 1, an additional penalty of up to twenty percent (20%) may under certain circumstances be imposed by the District. The Tax Code also makes provision for the split payment of taxes, discounts for early payment and the postponement of the delinquency date of taxes under certain circumstances.

Public Hearing and Rollback Tax Rate

In setting its annual tax rate, the governing body of a school district generally cannot adopt a tax rate exceeding the district's "rollback tax rate" without approval by a majority of the voters voting at an election approving the higher rate. The tax rate consists of two components: (1) a rate for funding of maintenance and operation expenditures and (2) a rate for debt service. For the 2007-08 fiscal year and thereafter, the rollback tax rate for a school district is the lesser of (A) the sum of (1) the product of the district's "state compression percentage" for that year multiplied by $1.50, (2) the rate of $0.04, (3) any rate increase above the rollback tax rate in prior years that were approved by voters, and (4) the district's current debt rate, or (B) the sum of (1) the district's effective maintenance and operations tax rate, (2) the product of the district's state compression percentage for that year multiplied by $0.06; and (3) the district's current debt rate (see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM" for a description of the "state compression percentage"). If for the preceding tax year a district adopted an M&O Tax rate that was less than its effective M&O Tax rate for that preceding tax year, the district's rollback tax for the current year is calculated as if the district had adopted an M&O Tax rate for the preceding tax year equal to its effective M&O Tax rate for that preceding tax year.

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

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

A district may adopt its budget after adopting a tax rate for the tax year in which the fiscal year covered by the budget begins if the district elects to adopt its tax rate before receiving the certified appraisal roll. A district that adopts a tax rate before adopting its budget must hold a public hearing on the proposed tax rate followed by another public hearing on the proposed budget rather than holding a single hearing on the two items.

District's Rights in the Event of Tax Delinquencies

Taxes levied by the District are a personal obligation of the owner of the property. The District has no lien for unpaid taxes on personal property but does have a lien for unpaid taxes upon real property, which lien is discharged upon payment. On January 1 of each year, such tax lien attaches to property to secure the payment of all taxes, penalties, and interest ultimately imposed for the year on the property. The District's tax lien is on a parity with the tax liens of other such taxing units. A tax lien on real property taxes takes priority over the claims of most creditors and other holders of liens on the property encumbered by the tax lien, whether or not the debt or lien existed before the attachment of the tax lien. The automatic stay in bankruptcy will prevent the automatic attachment of tax liens with respect to post-petition tax years unless relief is sought and granted by the bankruptcy judge. Personal property, under certain circumstances, is subject to seizure and sale for the payment of delinquent taxes, penalty, and interest.

Except with respect to taxpayers who are 65 years of age or older, at any time after taxes on property become delinquent, the District may file suit to foreclose the lien securing payment of the tax, to enforce personal liability for the tax, or both. In filing a suit to foreclose a tax lien on real property, the District must join other taxing units that have claims for delinquent taxes against all or part of the same property. Collection of delinquent taxes may be adversely affected by the amount of taxes owed to other taxing units, by the effects of market conditions on the foreclosure sale price, by taxpayer redemption rights, or by bankruptcy proceedings which restrict the collection of taxpayer debts.

THE PROPERTY TAX CODE AS APPLIED TO THE DISTRICT

The Appraisal District has the responsibility for appraising property in the District as well as other taxing units in Chambers County. The Appraisal District is governed by a board of directors appointed by members of the governing bodies of various political subdivisions within Chambers County.

Property within the District is assessed as of January 1 of each year, taxes become due October 1 of the same year and become delinquent on February 1 of the following year.

The District grants a local exemption of 20% of the market value of all residence homesteads and an additional $150,000 homestead exemption for disabled taxpayers and taxpayers 65 years of age or older.

The District does not tax personal property not used in the production of income, such as personal automobiles.

The District collects an additional 20% penalty to defray attorney costs in the collection of delinquent taxes over and above the penalty automatically assessed under the Tax Code.

The District's taxes are collected by the Barbers Hill ISD Tax Collector.

The District does not allow split payments and does not give discounts for early payment of taxes.

The District does not participate in a tax increment financing zone.

The District does not grant the "goods-in-transit" exemption.

The District has not granted the freeport exemption.

The District has entered into six tax value limitation agreements under the provisions of Chapter 313, Texas Tax Code ("Chapter 313"), known as the Texas Economic Development Act, as described below:

Company	First Year of Abatement[1]	Total Investment[2]	Capped Value for M&O Taxation	Type of Facility
Enterprise Operating LLC	2012	$300,500,000	$30,000,000	Natural Gas Fractionator Manufacturing Facility
Enterprise Operating LLC	2013	$235,000,000	$30,000,000	Natural Gas Fractionator Manufacturing Facility
Enterprise Operating LLC	2014	$310,000,000	$30,000,000	Natural Gas Fractionator Manufacturing Facility
Cedar Bayou Fractionators, L.P.	2014	$275,000,000	$30,000,000	Natural Gas Fractionator Manufacturing Facility
Lone Star NGL Asset Holdings II, LLC	2014	$375,00,000	$30,000,000	Natural Gas Fractionator Manufacturing Facility
Oneok Hydrocarbon, L.P.	2014	$275,000,000	$30,000,000	Natural Gas Fractionator Manufacturing Facility

[1] Year shown is the tax year, being the first year of the District's fiscal year ending June 30.
[2] Investment amount as set forth in the company's application to the District for tax abatement.

In accordance with Chapter 313, each agreement provides that the full value of the facility is subject to taxation during the first two years of the agreement, and thereafter the District may levy its M&O Tax against a capped value (in each case, $30 million) for 10 years. The agreements do not limit the tax value with respect to the District's debt service tax rate during any year. After year twelve, the full tax value of the facilities is subject to taxation by the District for both operating and debt service purposes. Chapter 313 and the terms of each agreement provide that each company will indemnify the District though payments in lieu of taxation to be made to the District or to an entity designated by the District, such as the District's non-profit foundation. The revenue protection payment is calculated to cover any State funding losses for operations that the District may incur as a result of the abatement agreements. Each Chapter 313 agreement also contains indemnity provisions under which the company agrees to fully indemnify the District for all maintenance and operations revenue losses incurred by it as a result of the District's approval of a tax limitation agreement. This protection is guaranteed for the duration of each agreement. In addition to the foregoing, under each agreement the District is entitled to receive additional supplemental payments from each company contracting with it, in an amount equal to the lesser of approximately 40% of the company's net tax benefit or $100 per student in average daily attendance for each agreement for each year of the agreement. See "AD VALOREM TAX PROCEDURES – Property Subject to Taxation by the District" for a description of tax limitation agreements. The District anticipates that additional agreements will be considered in the near future due to the increased use of natural gas for fuel and other purposes, which has been experienced in the State and nationally in recent years.

Charges for penalties and interest on the unpaid balance of delinquent taxes are as follows:

Date	**Penalty**	**Interest**	**Cumulative Total**
February	6%	1%	7%
March	7	2	9
April	8	3	11
May	9	4	13
June	10	5	15
July	12	6	18

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

STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS

Litigation Relating to the Texas Public School Finance System

On April 9, 2001, four property wealthy districts filed suit in the 250th District Court of Travis County, Texas (the "District Court") against the Texas Education Agency, the Texas State Board of Education, the Texas Commissioner of Education (the "Commissioner") and the Texas Comptroller of Public Accounts in a case styled West Orange-Cove Consolidated Independent School District, et al. v. Neeley, et al. The plaintiffs alleged that the $1.50 maximum maintenance and operations ("M&O") tax rate had become in effect a state property tax, in violation of Article VIII, Section 1-e of the Texas Constitution, because it precluded them and other school districts from having meaningful discretion to tax at a lower rate. Forty school districts intervened alleging that the Texas public school finance system (the "Finance System") was inefficient, inadequate, and unsuitable, in violation of Article VII, Section 1 of the Texas Constitution, because the State of Texas (the "State") did not provide adequate funding. As described below, this case has twice reached the Texas Supreme Court (the "Supreme Court"), which rendered decisions in the case on May 29, 2003 ("West Orange-Cove I") and November 22, 2005 ("West Orange-Cove II"). After the remand by the Supreme Court back to the District Court in West Orange-Cove I, 285 other school districts were added as plaintiffs or intervenors. The plaintiffs joined the intervenors in their Article VII, Section 1 claims that the Finance System was inadequate and unsuitable, but not in their claims that the Finance System was inefficient.

On November 30, 2004, the final judgment of the District Court was released in connection with its reconsideration of the issues remanded to it by the Supreme Court in West Orange-Cove I. In that case, the District Court rendered judgment for the plaintiffs on all of their claims and for the intervenors on all but one of their claims, finding that (1) the Finance System was unconstitutional in that the Finance System violated Article VIII, Section 1-e of the Texas Constitution because the statutory limit of $1.50 per $100.00 of taxable assessed valuation on property taxes levied by school districts for maintenance and operation purposes had become both a floor and a ceiling, denying school districts meaningful discretion in setting their tax rates; (2) the constitutional mandate of adequacy set forth in Article VII, Section 1, of the Texas Constitution exceeded the maximum amount of funding available under the funding formulas administered by the State; and (3) the Finance System was financially inefficient, inadequate, and unsuitable in that it failed to provide sufficient access to revenue to provide for a general diffusion of knowledge as required by Article VII, Section 1, of the Texas Constitution.

The intervening school district groups contended that funding for school operations and facilities was inefficient in violation of Article VII, Section 1 of the Texas Constitution, because children in property-poor districts did not have substantially equal access to education revenue. All of the plaintiff and intervenor school districts asserted that the Finance System could not achieve "[a] general diffusion of knowledge" as required by Article VII, Section 1 of the Texas Constitution, because the Finance System was underfunded. The State, represented by the Texas Attorney General, made a number of arguments opposing the positions of the school districts, as well as asserting that school districts did not have standing to challenge the State in these matters.

In West Orange-Cove II, the Supreme Court's holding was twofold: (1) that the local M&O tax had become a state property tax in violation of Article VIII, Section 1-e of the Texas Constitution and (2) the deficiencies in the Finance System did not amount to a violation of Article VII, Section 1 of the Texas Constitution. In reaching its first holding, the Supreme Court relied on evidence presented in the District Court to conclude that school districts did not have meaningful discretion in levying the M&O tax. In reaching its second holding, the Supreme Court, using a test of arbitrariness determined that: the public education system was "adequate," since it is capable of accomplishing a general diffusion of knowledge; the Finance System was not "inefficient," because school districts have substantially equal access to similar revenues per pupil at similar levels of tax effort, and efficiency does not preclude supplementation of revenues with local funds by school districts; and the Finance System does not violate the constitutional requirement of "suitability," since the Finance System was suitable for adequately and efficiently providing a public education.

In reversing the District Court's holding that the Finance System was unconstitutional under Article VII, Section 1 of the Texas Constitution, the Supreme Court stated:

> Although the districts have offered evidence of deficiencies in the public school finance system, we conclude that those deficiencies do not amount to a violation of Article VII, Section 1. We remain convinced, however, as we were sixteen years ago, that defects in the structure of the public school finance system expose the system to constitutional challenge. Pouring more money into the system may forestall those challenges, but only for a time. They will repeat until the system is overhauled.

In response to the intervenor districts' contention that the Finance System was constitutionally inefficient, the West Orange-Cove II decision states that the Texas Constitution does not prevent the Finance System from being structured in a manner that results in gaps between the amount of funding per student that is available to the richest districts as compared to the poorest district, but reiterated its statements in Edgewood Independent School District v. Meno, 917 S.W.2d 717 (Tex. 1995) ("Edgewood IV") that such funding variances may not be unreasonable. The Supreme Court further stated that "the standards of Article VII, Section 1 - adequacy, efficiency, and suitability - do not dictate a particular structure that a system of free public schools must have." The Supreme Court also noted that "efficiency requires only substantially equal access to revenue for facilities necessary for an adequate system," and the Supreme Court agreed with arguments put forth by the State that the plaintiffs had failed to present sufficient evidence to prove that there was an inability to provide for a "general diffusion of knowledge" without additional facilities.

Funding Changes in Response to West Orange-Cove II

In response to the decision in West Orange-Cove II, the Texas Legislature (the "Legislature") enacted House Bill 1 ("HB 1"), which made substantive changes in the way the Finance System is funded, as well as other legislation which, among other things, established a special fund in the State treasury to be used to collect new tax revenues that are dedicated under certain conditions for appropriation by the Legislature to reduce M&O tax rates, broadened the State business franchise tax, modified the procedures for assessing the State motor vehicle sales and use tax and increased the State tax on tobacco products (HB 1 and other described legislation are collectively referred to herein as the "Reform Legislation"). The Reform Legislation generally became effective at the beginning of the 2006–07 fiscal year of each district.

Current Litigation Related to the Texas Public School Finance System

Several lawsuits have been filed in District Courts of Travis County, Texas, which allege that the Finance System, as modified by legislation enacted by the Legislature since the decision in West Orange Cove II, and in particular, as modified by Senate Bill 1 in 2011 (see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - 2011 Legislation"), has resulted in a funding system that violates principles established in West Orange Cove I and West Orange Cove II, and prior decisions of the Supreme Court relating to the constitutionality of the Finance System and several provisions of the Texas Constitution. In general, each suit presents the legal perspectives and arguments of the different coalitions of school districts represented, but as a general matter, each group has challenged the adequacy of funding provided by the Legislature for the Finance System, and the plaintiffs in each suit are seeking to have an injunction issued to the State and its officials to prevent the distribution of any funds under the current Finance System until a constitutional system is created and seek a declaration that changes in funding for the Finance System since the enactment of HB 1 have effectively converted the local M&O Tax into a state property tax in violation of the Texas Constitution.. The defendants in the suits include State officials and the State Board of Education (the "State Defendants"). The first suit was filed on October 10, 2011, styled "The Texas Taxpayer & Student Fairness Coalition, et al. vs. Robert Scott, Commissioner of Education et al." A second suit was filed on December 9, 2011, styled "Calhoun County Independent School District, et al. v Robert Scott, Commissioner of Education, et al." A third suit was filed on December 13, 2011, styled "Edgewood Independent School District, et al. v. Robert Scott, Commissioner of Education, et al." and a fourth suit was filed on December 23, 2011, styled "Fort Bend Independent School District, et al. v Robert Scott, Commissioner of Education, et al.". The State Defendants have filed an answer with respect to the first suit filed, denying the plaintiff's allegations, and no further actions have occurred in that suit. The State Defendants have yet to respond to the other suits, and the statutory time limit for making such a response has not yet tolled. It is possible that the suits will be consolidated into a single suit, that additional plaintiffs will join the suits and that other, independent lawsuits may be filed challenging various aspects of the Finance System, and that any such additional legal challenges may be consolidated with the suits referenced above.

The District can make no representations or predictions concerning the effect this litigation may have on the District's financial condition, revenues or operations. See "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS – Possible Effects of Litigation and Changes in Law on District Bonds."

Possible Effects of Litigation and Changes in Law on District Bonds

The Reform Legislation and the changes made by the State Legislature to the Reform Legislation since its enactment did not alter the provisions of Chapter 45, Texas Education Code, that authorize districts to secure their bonds by pledging the receipts of an unlimited ad valorem debt service tax as security for payment of such bonds (including the Bonds). Reference is made, in particular, to the information under the heading "THE BONDS - Security" in the Official Statement.

In the future, the Legislature could enact additional changes to the Finance System which could benefit or be a detriment to a school district depending upon a variety of factors, including the financial strategies that the district has implemented in light of past State funding systems. Among other possibilities, a district's boundaries could be redrawn, taxing powers restricted, State funding reallocated, or local ad valorem taxes replaced with State funding subject to biennial appropriation. In Edgewood IV, the Supreme Court stated that any future determination of unconstitutionality "would not, however, affect the district's authority to levy the taxes necessary to retire previously issued bonds, but would instead require the Legislature to cure the system's unconstitutionality in a way that is consistent with the Contract Clauses of the U.S. and Texas Constitutions" (collectively, the "Contract Clauses"). Consistent with the Contract Clauses, in the exercise of its police powers, the State may make such modifications in the terms and conditions of contractual covenants related to the payment of the Bonds as are reasonable and necessary for the attainment of important public purposes.

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

CURRENT PUBLIC SCHOOL FINANCE SYSTEM

Overview

The following description of the Finance System is a summary of the Reform Legislation and the changes made by the State Legislature to the Reform Legislation since its enactment, including modifications made during the regular through third called sessions of the 79th Texas Legislature (collectively, the "2006 Legislative Session"), the regular session of the 81st Texas Legislature (the "2009 Legislative Session") and the regular and first called sessions of the 82nd Texas Legislature (collectively, the "2011 Legislative Session"). For a more complete description of school finance and fiscal management in the State, reference is made to Vernon's Texas Codes Annotated, Education Code, Chapters 41 through 46, as amended.

Funding for school districts in the State is provided primarily from State and local sources. State funding for all school districts is provided through a set of funding formulas comprising the "Foundation School Program," as well as two facilities financing programs. Generally, the Finance System is designed to promote wealth equalization among school districts by balancing State and local sources of funds available to school districts. In particular, because districts with relatively high levels of property wealth per student can raise more local funding, such districts receive less State aid, and in some cases, are required to disburse local funds to equalize their overall funding relative to other school districts. Conversely, because districts with relatively low levels of property wealth per student have limited access to local funding, the Finance System is designed to provide more State funding to such districts. Thus, as a school district's property wealth per student increases, State funding to the school district is reduced. As a school district's property wealth per student declines, the Finance System is designed to increase its State funding. A similar equalization system exists for facilities funding wherein districts with the same tax rate for debt service raise the same amount of combined State and local funding. Facilities funding for debt incurred in prior years is expected to continue in future years; however, State funding for new school facilities was not appropriated by the 82nd Texas Legislature for the 2012–13 fiscal biennium.

Local funding is derived from collections of ad valorem taxes levied on property located within each district's boundaries. School districts are authorized to levy two types of property taxes: a limited maintenance and operations ("M&O") tax to pay current expenses and an unlimited interest and sinking fund ("I&S") tax to pay debt service on bonds. Under current law, M&O tax rates are subject to a statutory maximum rate of $1.17 per $100 of taxable value for most school districts. Current law also requires school districts to demonstrate their ability to pay debt service on outstanding indebtedness through the levy of an ad valorem tax at a rate of not to exceed $0.50 per $100 of taxable property at the time bonds are issued. Once bonds are issued, however, districts may levy a tax to pay debt service on such bonds unlimited as to rate or amount (see "TAX RATE LIMITATIONS" herein). As noted above, because property values vary widely among school districts, the amount of local funding generated by the same tax rate is also subject to wide variation among school districts.

The Reform Legislation, which generally became effective at the beginning of the 2006–07 fiscal year of each school district in the State, made substantive changes to the Finance System, which are summarized below. While each school district's funding entitlement was calculated based on the same formulas that were used prior to the 2006–07 fiscal year, the Reform Legislation effected changes to the manner in which school districts are funded that were intended to reduce local M&O tax rates by one-third over two years through the introduction of the "State Compression Percentage," with M&O tax levies declining by approximately 11% in fiscal year 2006–07 and approximately another 22% in fiscal year 2007–08. (Prior to the Reform Legislation, the maximum M&O tax rate for most school districts was $1.50 per $100 of taxable assessed valuation.) Subject to local referenda, a district may increase its local M&O tax levy up to $0.17 above the district's compressed tax rate. Based on the current State Compression Percentage, the maximum M&O tax rate is $1.17 per $100 of taxable value for most school districts (see "TAX RATE LIMITATIONS" herein).

Local Funding for School Districts

The primary source of local funding for school districts is collections from ad valorem taxes levied against the taxable property located in each school district. As noted above, prior to the Reform Legislation, the maximum M&O tax rate for most school districts was generally limited to $1.50 per $100 of taxable value, and the majority of school districts were levying an M&O tax rate of $1.50 per $100 of taxable value at the time the Reform Legislation was enacted. The Reform Legislation required each school district to "compress" its tax rate by an amount equal to the "State Compression Percentage." For fiscal years 2007–08 through 2012–13, the State Compression Percentage has been set at 66.67%, effectively setting the maximum compressed M&O tax rate for most school districts at $1.00 per $100 of taxable value. The State Compression Percentage is set by legislative appropriation for each State fiscal biennium or, in the absence of legislative appropriation, by the Commissioner. School districts are permitted, however, to generate additional local funds by raising their M&O tax rate by $0.04 above the compressed tax rate without voter approval (for most districts, up to $1.04 per $100 of taxable value). In addition, if the voters approve the tax rate increase, districts may, in general, increase their M&O tax rate by an additional two or more cents and receive State equalization funds for such taxing effort up to a maximum M&O tax rate of $1.17 per $100 of taxable value (see "TAX INFORMATION – Public Hearing and Rollback Tax Rate" herein). Elections held in certain school districts under older laws, however, may subject M&O tax rates in such districts to other limitations (See "TAX RATE LIMITATIONS" herein).

State Funding for School Districts

State funding for school districts is provided through the Foundation School Program, which provides each school district with a minimum level of funding (a "Basic Allotment") for each student in average daily attendance ("ADA"). The Basic Allotment is calculated for each school district using various weights and adjustments. This basic level of funding is referred to as "Tier One" of the Foundation School Program. The basic level of funding is then "enriched" with additional funds known as "Tier Two" of the Foundation School Program. Tier Two provides a guaranteed level of funding for each cent of local tax effort that exceeds the compressed tax rate (for most districts, M&O tax rates above $1.00 per $100 of taxable value). The Finance System also provides an Existing Debt Allotment ("EDA") to subsidize debt service on eligible outstanding school district bonds and an Instructional Facilities Allotment ("IFA") to subsidize debt service on newly issued bonds. IFA primarily addresses the debt service needs of property-poor school districts. A New Instructional Facilities Allotment ("NIFA") also is available to help pay operational expenses associated with the opening of a new instructional facility. Future-year IFA and NIFA awards, however, were not funded by the Legislature for the 2012–13 fiscal biennium, although funding awards for IFA made in prior years will continue to be funded (but not the second year for NIFA for the 2012–13 fiscal biennium for districts that first became eligible for NIFA in the 2010–11 fiscal year).

Tier One and Tier Two allotments represent the State's share of the cost of M&O expenses of school districts, with local M&O taxes representing the district's local share. EDA and IFA allotments supplement a school district's local I&S taxes levied for debt service on eligible bonds issued to construct, acquire and improve facilities. Tier One and Tier Two allotments and existing EDA and IFA allotments are generally required to be funded each year by the Legislature. Since future-year IFA awards were not funded by the Legislature for the 2012–13 fiscal biennium, and debt service assistance on school district bonds that are not yet eligible for EDA is not available, debt service on new bonds issued by districts to construct, acquire and improve facilities must be funded solely from local I&S taxes. State funding allotments may be adjusted in certain circumstances to account for shortages in State appropriations or to allocate available funds in accordance with wealth equalization goals.

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

The cost of the basic program is based on an allotment per student known as the "Basic Allotment". The Basic Allotment is adjusted for all districts by a cost adjustment factor intended to address competitive labor markets for teachers known as the "cost of education index." In addition, district-size adjustments are made for small- and mid-size districts. The cost of education index and district-size adjustments applied to the Basic Allotment, create what is referred to as the "Adjusted Allotment". The Adjusted Allotment is used to compute a "regular program allotment," as well as various other allotments associated with educating students with other specified educational needs. For fiscal year 2007–08, the Basic Allotment was $3,135, and for fiscal year 2008–09, the Basic Allotment was increased to $3,218. For a discussion of the Basic Allotment in fiscal years 2009–10 and beyond, see "2009 Legislation" below.

Tier Two currently provides two levels of enrichment with different guaranteed yields depending on the district's local tax effort. For the 2012–13 State fiscal biennium, the first six cents of tax effort that exceeds the compressed tax rate (for most districts, M&O tax rates ranging from $1.01 to $1.06 per $100 of taxable value) will, for most districts, generate a guaranteed yield of $59.97 per cent per weighted student in average daily attendance ("WADA"). The second level of Tier Two is generated by tax effort that exceeds the compressed tax rate plus six cents (for most districts eligible for this level of funding, M&O tax rates ranging from $1.07 to $1.17 per $100 of taxable value) and has a guaranteed yield per cent per WADA of $31.95. Property-wealthy school districts are subject to recapture at the equivalent wealth per student of $319,500 (see "Wealth Transfer Provisions" below). For school districts that adopted an M&O tax rate of $1.17 per $100 in taxable value for the 2010–11 fiscal year, the $31.95 guaranteed yield is increased to $33.95, but only for the 2011–12 fiscal year.

The IFA guarantees each awarded school district a specified amount per student (the "IFA Guaranteed Yield") in State and local funds for each cent of tax effort to pay the principal of and interest on eligible bonds issued to construct, acquire, renovate or improve instructional facilities. The guaranteed yield per cent of local tax effort per student in ADA has been $35 since this program first began. To receive an IFA award, a school district must apply to the Commissioner in accordance with rules adopted by the Commissioner before issuing the bonds to be paid with IFA state assistance. The total amount of debt service assistance over a biennium for which a district may be awarded is limited to the lesser of (1) the actual debt service payments made by the district in the biennium in which the bonds are issued; or (2) the greater of (a) $100,000 or (b) $250 multiplied by the number of students in ADA. The IFA is also available for lease-purchase agreements and refunding bonds meeting certain prescribed conditions. Once a district receives an IFA award for bonds, it is entitled to continue receiving State assistance for such bonds without reapplying to the Commissioner. The guaranteed level of State and local funds per student per cent of local tax effort applicable to the bonds may not be reduced below the level provided for the year in which the bonds were issued. For the 2012–13 State biennium, however, no funds are appropriated for new IFA awards, although all current obligations are funded through the biennium.

State financial assistance is provided for certain existing eligible debt issued by school districts (referred to herein as EDA). The EDA guaranteed yield (the "EDA Yield") is the same as the IFA Guaranteed Yield ($35 per cent of local tax effort per student in ADA), subject to adjustment as described below. For bonds that became eligible for EDA funding after August 31, 2001, and prior to August 31, 2005, EDA assistance was less than $35 in revenue per student for each cent of debt service tax, as a result of certain administrative delegations granted to the Commissioner under State law. Effective September 1, 2003, the portion of the local debt service rate that has qualified for EDA assistance is limited to the first 29 cents of debt service tax or a greater amount for any year provided by appropriation by the Legislature. In general, a district's bonds are eligible for EDA assistance if (i) the district made payments on the bonds during the final fiscal year of the preceding State fiscal biennium or (ii) the district levied taxes to pay the principal of and interest on the bonds for that fiscal year. Each biennia, access to EDA funding is determined by the debt service taxes collected in the final year of the preceding biennium. A district may not receive EDA funding for the principal and interest on a series of otherwise eligible bonds for which the district receives IFA funding.

Prior to the 2012–13 biennium, a district could also qualify for a NIFA allotment, which provided assistance to districts for operational expenses associated with opening new instructional facilities. As previously mentioned, this program was not funded for the 2012–13 State fiscal biennium.

2006 Legislation

Since the enactment of the Reform Legislation in 2006, most school districts in the State have operated with a "target" funding level per student ("Target Revenue") that is based upon the "hold harmless" principles embodied in the Reform Legislation. This system of Target Revenue was superimposed on the Foundation School Program and made existing funding formulas substantially less important for most school districts. As noted above, the Reform Legislation was intended to lower M&O tax rates in order to give school districts "meaningful discretion" in setting their M&O tax rates, while holding school districts harmless by providing them with the same level of overall funding they received prior to the enactment of the Reform Legislation. Under the Target Revenue system, each school district is generally entitled to receive the same amount of revenue per student as it did in either the 2005–2006 or 2006–07 fiscal year (under existing laws prior to the enactment of the Reform Legislation), as long as the district adopted an M&O tax rate that was at least equal to its compressed rate. The reduction in local M&O taxes resulting from the mandatory compression of M&O tax rates under the Reform Legislation, by itself, would have significantly reduced the amount of local revenue available to fund the Finance System. To make up for this shortfall, the Reform Legislation authorized Additional State Aid for Tax Reduction ("ASATR") for each school district in an amount equal to the difference between the amount that each district would receive under the Foundation School Program and the amount of each district's Target Revenue funding level.

2009 Legislation

During the 2009 Legislative Session, legislation was enacted that increased the Basic Allotment for the 2009–10 fiscal year from $3,218 to $4,765. In addition, each district's Target Revenue was increased by $120 per WADA. Target Revenue amounts were also adjusted to provide for mandatory employee pay raises and to account for changes in transportation and NIFA costs since the original Target Revenues were set. Overall, the Legislature allocated approximately $1.9 billion in new State aid for school districts.

2011 Legislation

During the 2011 Legislative Session, the Legislature enacted a budget that cut $4 billion from the Foundation School Program for the 2012–13 State fiscal biennium, as compared to the funding level school districts were entitled to under the current formulas, including Target Revenue, and also cut approximately $1.3 billion in various grants (i.e., pre-kindergarten grant program, student success initiative, etc.) that were previously available. Such cuts were made in light of a projected State deficit of up to $27 billion for the 2012–13 State fiscal biennium. In order to reduce formula funding, a Regular Program Adjustment Factor ("RPAF") was applied to the formula that determines a district's regular program allotment. RPAF is multiplied by a school district's count of students in

ADA (not counting the time a student spends in special education and career & technology education) and its Adjusted Allotment, which is the $4,765 Basic Allotment adjusted for the cost of education index and the small- and mid-sized district adjustments. The RPAF is set at 0.9239 for the 2011–12 fiscal year and 0.98 for the 2012–13 fiscal year. In order to balance these reductions across the two years for formula funded districts, such districts have the option to request that an RPAF value of 0.95195 be applied for both the 2011–12 and 2012–13 fiscal years. In order to be granted the request by the Commissioner, the district must demonstrate that using the 0.9239 RPAF will cause the district a financial hardship in 2011–12. By applying the RPAF only to the Adjusted Allotment, other Tier One allotments, such as special education, career and technology, gifted and talented, bilingual and compensatory education, were not affected. The State Board of Education however, was directed to decrease funding for these programs in proportion to the reductions to the Basic Allotment. The Legislature also established an RPAF value of 0.98 for the 2013–15 State fiscal biennium, subject to increases by subsequent legislative appropriation not to exceed an RPAF value of 1.0. The RPAF factor and its related provisions are scheduled to expire on September 1, 2015.

The RPAF is the primary mechanism for formula reductions in the 2011–12 fiscal year. n the 2012–13 fiscal year, the RPAF of 0.98 is combined with a percentage reduction in each school district's Target Revenue per WADA to 92.35% of its formula amount. For the 2013–14 and subsequent fiscal years, the percentage reduction will be set by legislative appropriation. With regard to this adjustment, the ASATR relief that funds the Target Revenue system is phased out between the 2013–14 and 2017–18 fiscal years.

Wealth Transfer Provisions

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

The equalized wealth levels that subject Chapter 41 districts to wealth equalization measures for fiscal year 2011–12 are set at (i) $476,500 per student in WADA with respect to that portion of a district's M&O tax effort that does not exceed its compressed tax rate (for most districts, the first $1.00 per $100 of taxable value) and (ii) $319,500 per WADA with respect to that portion of a district's M&O tax effort that is beyond its compressed rate plus $.06 (for most districts, M&O taxes levied above $1.06 per $100 in taxable value). M&O taxes levied above $1.00 but below $1.07 per $100 of taxable value are not subject to the wealth equalization provisions of Chapter 41. Chapter 41 districts with a wealth per student above the lower equalized wealth level but below the higher equalized wealth level must equalize their wealth only with respect to the portion of their M&O tax rate, if any, in excess of $1.06 per $100 of taxable value. Chapter 41 districts may be entitled to receive ASATR from the State in excess of their recapture liability, and such districts may use their ASATR funds to offset their recapture liability.

Under Chapter 41, a district has five options to reduce its wealth per student so that it does not exceed the equalized wealth levels: (1) a district may consolidate by agreement with one or more districts to form a consolidated district; all property and debt of the consolidating districts vest in the consolidated district; (2) a district may detach property from its territory for annexation by a property-poor district; (3) a district may purchase attendance credits from the State; (4) a district may contract to educate nonresident students from a property-poor district by sending money directly to one or more property-poor districts; or (5) a district may consolidate by agreement with one or more districts to form a consolidated taxing district solely to levy and distribute either M&O taxes or both M&O taxes and I&S taxes. A Chapter 41 district may also exercise any combination of these remedies. Options (3), (4) and (5) require prior approval by the transferring district's voters; however, Chapter 41 districts may apply ASATR funds to offset recapture and to achieve the statutory wealth equalization requirements, as described above, without approval from voters.

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

The School Finance System as Applied to the District

The District's wealth per student for the 2012 fiscal year is approximately $730,000, which is above the equalized wealth level provided by the Finance System. As a result, the District is a so-called "Chapter 41 district" (referring to the provisions of the Texas Education Code that governs funding for property wealthy districts), and the District is subject to "recapture" on revenues received by it from the levy of its M&O Tax against that portion of the District's tax base that exceeds $319,500.

The District's wealth is based upon its location on the Texas Gulf Coast, just east of the City of Houston. Beneath the District is the Barbers Hill Salt Dome, one of the largest salt domes found along the Gulf Coast. It measures 2.02 miles long by 1.7 miles wide and is used to store liquefied natural gas, propane, butane and similar commodities. Approximately 69% of the District's tax base is associated with the natural gas or other chemicals stored in the salt domes or the industrial properties of the companies that operate chemical plants, pipelines and other infrastructure relating to petrochemical industry.

Since the enactment of HB 1, the District has operated with a target funding level per student that is based upon the "hold harmless" formulas set forth in HB 1. In essence, HB 1 provided tax rate relief to school district taxpayers, while holding levels of school district funding per student at levels in effect during the 2006 fiscal year. As described below, legislation enacted in the 2011 State Legislative Session will reduce funding for school districts during the State's 2012-2013 fiscal biennium, and in the second year of the biennium the target revenue provisions that pertain to Chapter 41 districts, such as the District, will begin to be phased out, resulting in greater cuts in the District's 2013 fiscal year. Since the 2006 fiscal year, the District's target revenue figure per student has been $7,189, which is above the State average of approximately $5,050 per student. Under the current Finance System, increases in assessed valuations reduce State funding to the District in proportion to the property value increases, leaving enrollment growth and increases in local tax rates, to the extent authorized by law, as the principle factors in the funding formulas that produce additional revenues to a local school district. The higher than average target revenue figure has, among other factors, contributed to the growth of the District's General Fund, its primary operating account, from approximately $4.4 million in fiscal year 2005 (representing 14% of 2005 General Fund expenditures) to over $26.9 million at the close of fiscal year 2011 (representing 59% of

2011 General Fund expenditures). The District's General Fund balance increased by $1.2 million in 2011, and during that year the District benefitted by a one-time distribution from the Chambers County Permanent Fund of approximately $3.8 million. The District has also used $6 million of its General Fund balance in 2011 for construction projects, and plans to reimburse the General Fund in 2012 from proceeds of the Bonds and the QSCBs. State funding for the District increased from $2.3 million in fiscal 2006 to $18.9 million in 2010 (the 2010 amounts included a one-time $4.9 million disaster recovery payment, described below), but declined to $10 million in 2011. The District's fiscal year 2012 General Fund budget is balanced between revenues and expenditures, with State revenue sources budgeted at $5.4 million and local revenue sources budgeted at $39 million. Based on year to date operating data, however, District management anticipates that the District will increase its fund balance by approximately $3.3 million during the year, in large part due to a settlement with an insurer of $4.8 million stemming from damage to District facilities incurred during Hurricane Ike in 2009.

In addition to the hold harmless provisions of HB 1, the District has benefitted from increased State funding in recent years, though State funding has declined in 2011 and 2012, and likely beyond. The prior year growth in funding was attributable to the growth of the District's student enrollment. The District anticipates its enrollment will grow at an average rate of 4.2% over the next ten years, which continues a similar rate of growth over the past ten years. Population growth in the District is attributed to the outflow to the District from the Houston area; central Houston is approximately 35 miles to the east of the District. The District has a recognized accountability rating from the Texas Education Agency, and it has experienced growth in the single family residential component of its tax base in each of the last six years. Starting salaries for teachers in the District are $50,000, among the highest in the State.

Other factors that have contributed to the District's strong General Fund balance at the close of fiscal year 2011 have included the receipt of funds from various local sources that are not subject to recapture to the State under the Finance System. Such "non-recapture" revenues have included funds from a $0.02 tax rate increase approved by the District's voters in 2008; revenues from the Chambers County permanent school fund, which generates funds for all school districts in the County on a per capita basis from the income of the County fund's investment and royalty income; the District's share of the County's annual equalization tax, which has generated approximately $1.5 million per year in recent years, being the District's per capita share of the $0.045 annual County equalization tax rate; funds received from a non-profit educational foundation created by the District, which receives its funding from a variety of sources, including payments that are made pursuant to property value limitation agreements entered into in accordance with the Chapter 313; and approximately $400,000 over the past 24 months received by the District for energy management purposes from a supplemental environmental project program administered by the Texas Commission on Environmental Quality ("TCEQ") that is funded by penalties assessed by TCEQ through enforcement agreements with entities in the District that violate State environmental laws. In addition, $5 million of the General Fund balance is attributable to a loan made to the District by the U.S. Federal Emergency Management Agency ("FEMA") as a result of damage suffered by the District during Hurricane Ike in 2009. The District expects to use $5 million of its fund balance in 2014 to repay that loan. The District had property damage of approximately $14 million as a result of Hurricane Ike, but recovered most of its loses through insurance settlements and a $4.9 million disaster recovery payment from the State of Texas. The District currently maintains property loss insurance coverage of $40 million to cover risks of future hurricanes and other catastrophic risks. Certain of the aforementioned revenue sources, such as the FEMA loan, were one-time funding sources or are subject to conditions that may not reoccur in the future.

During the 82nd legislative sessions in 2011, the Texas Legislature adopted SB 1, which failed to fully fund the Finance System for the 2012-13 State biennium. As a result of funding action in the 2011 Legislature, and as compared to State funding for fiscal year 2011 and assuming no growth in student enrollment, the District expects to have its State funding reduced by 4.6% ($2.4 million) in 2012 and another 8.9% in 2013 ($3.5 million). The District projects that it may need to use up to $7 million in General Fund balance in aggregate in fiscal years 2013 and 2014 to absorb cuts in State funding, the repayment of the FEMA loan and other factors. The District grants a 20% homestead exemption for all taxpayers, and an additional $150,000 homestead exemption for taxpayers 65 and older, in addition to the State mandated $15,000 homestead exemption. The District does not anticipate modifying the local homestead exemptions, at least in the near term. At present, the District does not anticipate seeking voter approval to increase its M&O Tax above the current rate of $1.06 per $100 of taxable assessed valuation.

While HB 1 generally neutralizes increases in local tax bases insofar as they affect operating budgets of school districts, local districts do benefit from growth in tax values for purposes of funding debt service obligations. The District's Interest and Sinking Fund had a balance of $4.5 million at June 30, 2011. Net debt payments are budgeted to be $8.7 million in 2012. The current tax rate for debt service is $0.2698. Because the District is a property-wealthy district, it does not receive funding from the State to supplement its debt tax. In connection with the submission of the $75 million bond referendum to the voters that was approved in May 2011 (which is being issued in the form of the Bonds and the QSCBs), the District estimated that an increase in its debt service tax rate of 1.6% per year for four years could be necessary to pay the increased debt service. However, based on the industrial properties that are being constructed in the District, several of which are subject to Chapter 313 tax limitation agreements for M&O Tax purposes, but not for debt service taxation, it is likely that no tax rate will be required to service the new debt. See "THE PROPERTY TAX CODE AS APPLIED TO THE DISTRICT."

THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM

The information below concerning the State Permanent School Fund and the Guarantee Program for school district bonds has been provided by the Texas Education Agency (the "TEA") and is not guaranteed as to accuracy or completeness by, and is not construed as a representation by the District, the Financial Advisor, or the Purchaser.

This disclosure statement provides information relating to the program administered by the TEA with respect to the Texas Permanent School Fund guarantee of Texas school district bonds, which program is referred to, and defined herein, as the Guarantee Program.

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

History and Purpose

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

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

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

The sole purpose of the PSF is to assist in the funding of public education for present and future generations. Prior to the adoption of the Total Return Constitutional Amendment, all interest and dividends produced by Fund investments flowed into the Available School Fund (the "ASF"), where they are distributed to local school districts based on average daily attendance. Any net gains from investments of the Fund accrue to the corpus of the PSF. Prior to the approval by the voters of the State of the Total Return Constitutional Amendment, costs of administering the PSF were allocated to the ASF. With the approval of the Total Return Constitutional Amendment, the administrative costs of the Fund have shifted from the ASF to the PSF. In fiscal year 2011, distributions to the ASF amounted to $246.09 per student and the total amount distributed to the ASF was $1,092.8 billion (unaudited).

Audited financial information for the PSF is provided annually through the PSF Annual Report (the "Annual Report"), which is filed with the Municipal Securities Rulemaking Board ("MSRB"). The Annual Report includes the Message of the Executive Administrator of the Fund (the "Message") and the Management's Discussion and Analysis ("MD&A"). Reference is made to the Annual Report for the complete Message and MD&A for the year ended August 31, 2010 and for a description of the financial results of the PSF for the year ended August 31, 2010, the most recent year for which audited financial information regarding the Fund is available. The 2010 Annual Report is incorporated herein and made a part hereof for all purposes, but the 2010 Annual Report speaks only as of its date and the TEA has not obligated itself to update the 2010 Annual Report or any other Annual Report. The TEA posts each Annual Report, which includes statistical data regarding the Fund as of the close of each fiscal year, the most recent disclosure for the Guarantee Program, the Statement of Investment Objectives, Policies and Guidelines of the Texas Permanent School Fund, which is codified at 19 Texas Administrative Code, Chapter 33 (the "Investment Policy"), monthly updates with respect to the capacity of the Guarantee Program (collectively, the "Web Site Materials") on the TEA web site at www.tea.state.tx.us/psf and with the MSRB at www.emma.msrb.org. Such monthly updates regarding the Guarantee Program are also incorporated herein and made a part hereof for all purposes. In addition to the Web Site Materials, the Fund is required to make quarterly filings with the Securities and Exchange Commission ("SEC") under Section 13(f) of the Securities Exchange Act of 1934. Such filings, which consist of a list of the Fund's holdings of securities specified in Section 13(f), including exchange-traded (e.g., NYSE) or NASDAQ-quoted stocks, equity options and warrants, shares of closed-end investment companies and certain convertible debt securities, is available from the SEC at www.sec.gov/edgar.shtml. A list of the Fund's equity and fixed income holdings as of August 31, 2010 has been posted to the TEA web site and filed with the MSRB. Such list excludes holdings in the Fund's securities lending program. Such list is incorporated herein and made a part hereof for all purposes.

The Total Return Constitutional Amendment

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

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

In September 2006, the SBOE established the Distribution Rate from the Fund to the ASF for fiscal years 2008 and 2009 at 3.5% of the average of the PSF market value during the Distribution Measurement Period. The decision of the SBOE regarding the

Distribution Rate for 2008 and 2009 took into account a commitment by the SLB to transfer at least $100 million per year for each year of the biennium commencing September 1, 2007. In the 2011 fiscal year, the SLB also released $100 million to the investment assets of the PSF. The SBOE set the Distribution Rate for the Fund for fiscal years 2010 and 2011 at 2.5% of the average of the PSF market value during the Distribution Measurement Period that ended in November 2008. That distribution rate produced total transfers of $1,153.5 billion to the ASF from the PSF during the 2010-11 biennium. The SBOE has set the Distribution Rate for the 2012-13 biennium at 4.2%, which rate was determined after the SLB authorized the release of a total of $500 million to the PSF in quarterly installments during the 2012-13 biennium. See "2011 Constitutional Amendment" below for a description of amendments made to the Texas Constitution on November 8, 2011 that permits the SLB to make transfers directly to the ASF up to the amount of $300 million in each fiscal year.

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

With respect to the management of the Fund's investment portfolio, the single most significant change made to date as a result of the Total Return Constitutional Amendment has been new asset allocation policies adopted by the SBOE in February 2004 (the "2004 Asset Allocation Policy"), in July 2006 (as subsequently reaffirmed in July 2008 such asset allocation is referred to herein as the "2008 Asset Allocation Policy") and in July 2010 (the "2010 Asset Allocation Policy"), which have significantly altered the asset allocations of the Fund. The Fund's investment policy provides for minimum and maximum ranges among the components of each of the three general asset classifications: equities, fixed income and alternative asset investments. The 2004 Asset Allocation Policy decreased the fixed income target from 45% to 25% of Fund investment assets and increased the allocation for equities from 55% to 75% of investment assets. In July 2006, the SBOE modified its asset allocation to reduce the equity allocation, including both domestic and foreign equity portfolios, to a target of 53% of Fund assets, further reduced the fixed income allocation target to 19% and added an alternative asset allocation, which included real estate, real return, absolute return and private equity components, totaling 28% of the Fund's asset target. Alternative asset classes diversify the SBOE-managed assets and are not as correlated to traditional asset classes, which is intended to increase investment returns over the long run while reducing risk and return volatility of the portfolio. In July 2010, the SBOE modified the 2008 Asset Allocation Policy by decreasing the equity allocation to 50%, and the fixed income allocation to 15%, while increasing the alternative asset allocation (which may include equity and fixed income investments as part of a variety of alternative investment strategies) to 35%. The new asset categories added by the 2010 Asset Allocation Policy are a new 7% allocation for risk parity investments, added in accordance with the recommendation of a new investment advisor, and a .5% allocation for charter school investments, both of which are categorized within the Fund's alternative asset category. Based on an opinion of the Texas Attorney General, which was received by the Chair of the SBOE in August 2011, and which stated that the PSF may not be invested for an objective that does not meet the prudent person investment standard, the charter school investment allocation was discontinued without being implemented in September 2011, with the .5% allocation being reallocated into other alternative investment allocations. The PSF Staff and the Fund's investment advisor are tasked with advising the SBOE with respect to the implementation of the 2010 Asset Allocation Policy, including the timing and manner of the selection of any external managers and other consultants. For a variety of reasons, each change in asset allocation for the Fund, including the 2010 Asset Allocation Policy, has been, and is being, implemented in phases. At August 31, 2011, the Fund was invested as follows: 54.60% in public market equity investments; 22.18% in fixed income investments; 10.34% in absolute return assets; 0.72% in private equity assets; 1.42% in real estate assets; 7.73% in risk parity assets; 2.88% in real return assets; and 0.13% in cash.

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

The asset allocation of the Fund is subject to change by the SBOE from time to time based upon a number of factors, including recommendations to the SBOE made by internal investment staff and external consultants, changes made by the SBOE without regard to such recommendations and directives of the Legislature. Fund performance may also be affected by factors other than asset allocation, including, without limitation, the general performance of the securities markets in the United States and abroad; political and investment considerations including those relating to socially responsible investing; application of the prudent person investment standard, which may eliminate certain investment opportunities for the Fund; and limitations on the number and compensation of internal and external investment staff, which is subject to Legislative oversight. The Guarantee Program could also be impacted by changes in State or federal law or the implementation of new accounting standards.

Management and Administration of the Fund

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

The Total Return Constitutional Amendment provides that expenses of managing the PSF are to be paid "by appropriation" from the PSF. In January 2005, at the request of the SBOE, the Attorney General issued a legal opinion, Op. Tex. Att'y Gen. No. GA-0293 (2005) ("GA-0293"), that the Total Return Constitutional Amendment requires that SBOE expenditures for managing or administering PSF investments, including payments to external investment managers, be paid from appropriations made by the Legislature, but that the Total Return Constitutional Amendment does not require the SBOE to pay from such appropriated PSF funds the indirect management costs deducted from the assets of a mutual fund or other investment company in which PSF funds have been invested.

Texas law assigns control of the Fund's land and mineral rights to the three-member SLB, which consists of the elected Commissioner of the General Land Office ("GLO"), an appointee of the Governor, and an appointee of the Attorney General. Administrative duties related to the land and mineral rights reside with the GLO, which is under the guidance of the Commissioner of the GLO. In 2007, the Legislature established the real estate special fund account of the PSF (the "Real Estate Account") consisting of the land, mineral or royalty interest, real estate investment, or other interest, including revenue received from those sources, that is set apart to the PSF under the Texas Constitution and laws, together with the mineral estate in riverbeds, channels, and the tidelands, including islands. The investment of the Real Estate Account is subject to the sole and exclusive management and control of the SLB and the Land Commissioner, who is also the head of the GLO. The 2007 legislation that established the Real Estate Account, House Bill 3699 ("HB 3699") presented constitutional questions regarding the respective roles of the SBOE and the SLB relating to the disposition of proceeds of real estate transactions to the ASF, among other questions. On April 9, 2008, the Attorney General issued a legal opinion, Op. Tex. Att'y Gen. No. GA-0617 (2008), at the request of the Chair of the SBOE advising, among other matters, that any proceeds from the sale of real estate that are not reinvested by the SLB in other real estate assets must be invested under the direction of the SBOE, and that the provisions of H.B. 3699 that permit the SLB to directly transfer real estate investment proceeds to the ASF (in lieu of transfer to the investment portfolio of the PSF under the management of the SBOE), would likely be determined by a court to be in violation of the State constitution. Amounts in the investment portfolio of the PSF are taken into account by the SBOE for purposes of determining the Distribution Rate. An amendment to the Texas Constitution was approved by State voters on November 8, 2011, which permits the SLB to make transfers directly to the ASF, see "2011 Constitutional Amendment" below.

The SBOE contracts with its securities custodial agent to measure the performance of the total return of the Fund. A consultant is typically retained for the purpose of providing consultation with respect to strategic asset allocation decisions and to assist the SBOE in selecting external fund management advisors. The SBOE also contracts with financial institutions for custodial and securities lending services. The SBOE has established the Committee of Investment Advisors, which consists of independent investment experts each appointed by a member of the SBOE to closely advise the respective SBOE member on investment issues.

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

The Guarantee

The Guarantee Program for School District Bonds (the "Guarantee Program") was authorized by an amendment to the Texas Constitution in 1983 and by Subchapter C of Chapter 45 of the Texas Education Code (the "Act"). If the conditions for the Guarantee Program are satisfied, the guarantee becomes effective upon approval of the Bonds by the Attorney General and remains in effect until the guaranteed bonds are paid or defeased, by a refunding or otherwise.

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

If a district fails to pay principal or interest on a bond as it is stated to mature, other amounts not due and payable are not accelerated and do not become due and payable by virtue of the district's default. The Guarantee Program does not apply to the payment of principal and interest upon redemption of bonds, except upon mandatory sinking fund redemption, and does not apply to the obligation, if any, of a school district to pay a redemption premium on bonds.

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

For a discussion of legislative developments that have authorized the use of the Fund to guarantee revenue bonds issued by certain open-enrollment charter schools, see "Other 2011 Legislative Actions – Charter School Guarantee Program" below.

Capacity Limits for the Guarantee Program

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

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

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

Since July 1991, when the SBOE amended the Guarantee Program Rules to broaden the range of bonds that are eligible for guarantee under the Guarantee Program to encompass most Texas school district bonds, the principal amount of bonds guaranteed under the Guarantee Program has increased sharply. In addition, in recent years a number of factors have caused an increase in the amount of bonds issued by school districts in the State. See the table "Permanent School Fund Guaranteed Bonds" below. The SBOE has approved and modified the Guarantee Program Rules in recent years, most recently in May 2010. Generally, the Guarantee Program Rules limit guarantees to certain types of notes and bonds, including, with respect to refunding bonds, a requirement that the bonds produce debt service savings, and that bonds issued for capital facilities must have been voted as unlimited tax debt of the issuing district. The Guarantee Program regulations include certain accreditation criteria for districts applying for a guarantee of their bonds, and limit guarantees to districts that have less than the amount of annual debt service per average daily attendance that represents the 90th percentile of annual debt service per average daily attendance for all districts, but such limitation will not apply to school districts that have enrollment growth of at least 25% over the previous five school years. Effective September 1, 2009, the Act provides that the SBOE may annually establish a percentage of the cost value of the Fund to be reserved from use in guaranteeing bonds. The capacity of the Guarantee Program in excess of any reserved portion is referred to herein as the "Capacity Reserve." The Guarantee Program Rules provide for a minimum Capacity Reserve of no less than 5%, and provide that the amount of the Capacity Reserve may be increased by a majority vote of the SBOE. The Commissioner is authorized to change the Capacity Reserve, which decision must be ratified or rejected by the SBOE at its next meeting following any change made by the Commissioner. The Guarantee Program Rules are codified in the Texas Administrative Code at 19 TAC sections 33.65 et seq., and are available on the TEA website at www.tea.state.tx.us/rules/tac/chapter033/index.html. The current Capacity Reserve is noted in the monthly updates with respect to the capacity of the Guarantee Program on the TEA web site at www.tea.state.tx.us/psf, which are also filed with the MSRB.

Based upon historical performance of the Fund, the legal restrictions relating to the amount of bonds that may be guaranteed has generally resulted in a lower ratio of guaranteed bonds to available assets as compared to many other types of credit enhancements that may be available for Texas school district bonds. However, changes in the value of the Fund due to changes in securities markets, investment objectives of the Fund, an increase in bond issues by school districts in the State or legal restrictions on the Fund, the implementation of a guarantee program for revenue bonds issued by certain open-enrollment charter schools, or an increase in the calculation base of the Fund for purposes of making transfers to the ASF (see "Other 2011 Legislative Actions – Charter School Guarantee Program" below), among other factors, could adversely affect the ratio of Fund assets to guaranteed bonds and the growth of the Fund in general. It is anticipated that the issuance of the IRS Notice will substantially increase the amount of bonds guaranteed under the Guarantee Program.

The Act requires that the Commissioner prepare, and the SBOE approve, an annual report on the status of the Guarantee Program (the Annual Report). The State Auditor audits the financial statements of the PSF, which are separate from other State financial statements. The TEA has filed the audited annual report of the PSF for the year ended August 31, 2010 with the MSRB. The 2010 Annual Report has also been filed with the Municipal Advisory Council of Texas and posted to the PSF web site. Such report speaks only as of the date thereof.

Ratings of Bonds Guaranteed Under the Guarantee Program

Moody's Investors Service, Standard & Poor's Rating Service, a Standard & Poor's Financial Service LLC business, and Fitch Ratings rate bonds guaranteed by the PSF "Aaa," "AAA" and "AAA," respectively. Not all districts apply for multiple ratings on their bonds, however. See "RATINGS" herein.

Valuation of the PSF and Guaranteed Bonds

Permanent School Fund Valuations

Fiscal Year Ended 8/31	Book Value[(1)]	Market Value[(1)]
2007	$21,234,323,093	$29,251,882,931
2008	22,926,299,922	29,336,248,611
2009	23,117,052,793	25,443,104,623
2010	23,653,185,489	27,066,200,259
2011	24,789,514,108[(2)]	29,900,679,571[(2)]

[(1)] SLB managed assets are included in the market value and book value of the Fund. In determining the market value of the PSF from time to time during a fiscal year, the TEA uses current, unaudited values for TEA managed investment portfolios and cash held by the SLB. Market values of land and mineral interests, and investments in externally managed real estate funds managed by the SLB are based upon information reported to the PSF by the SLB. Beginning in fiscal year 2009, the SLB reported that information to the PSF on a quarterly basis. The valuation of such assets at any point in time is dependent upon a variety of factors, including economic conditions in the State and nation in general, and the values of these assets, and, in particular, the valuation of mineral holdings administered by the SLB, can be volatile and subject to material changes from period to period. At August 31, 2011, land, external real estate investments, mineral assets and cash managed by the SLB had

unaudited book values of approximately $352.24 million, $1.41 billion, $13.39 million and $1.30 billion, respectively, and unaudited market values of approximately $691.50 million, $1.19 billion, $2.37 billion and $1.30 billion, respectively.

(2) Unaudited. At October 31, 2011, the PSF had a book value of $24,689,411,383 and a market value of $29,734,790,178 (in each case, based on unaudited data).

Permanent School Fund Guaranteed Bonds

At 8/31	Principal Amount(1)
2007	$44,856,621,419
2008	49,860,572,025
2009	50,032,724,439
2010(1)	49,301,683,338
2011	52,653,930,546(2)

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

(2) Unaudited. As of August 31, 2011, the TEA expected that the principal and interest to be paid by school districts over the remaining life of the bonds guaranteed by the Guarantee Program is $90,023,091,264 billion, of which $37,369,160,718 billion represents interest to be paid. At October 31, 2011, there were $53,192,621,484 of bonds guaranteed under the Guarantee Program and the capacity of the Guarantee Program was $74,068,234,149 based on the three times cost value multiplier approved by the SBOE on May 21, 2010. Such capacity figures include the Reserve Capacity.

Discussion and Analysis Pertaining to Fiscal Year Ended August 31, 2010

The following discussion is derived from the Annual Report for the year ended August 31, 2010, including the Message of the Executive Administrator of the Fund and the Management's Discussion and Analysis contained therein. Reference is made to the Annual Report for the complete Message and MD&A. Investment assets managed by the fifteen member SBOE are referred to throughout this MD&A as the PSF(SBOE) assets. As of August 31, 2010, the Fund's land, mineral rights and certain real assets are managed by the three-member SLB and these assets are referred to throughout as the PSF(SLB) assets. The 2008 Asset Allocation Policy includes an allocation for real estate investments, and as such investments are made, and become a part of the PSF investment portfolio, those investments will be managed by the SBOE and not the SLB. The discussion below will be revised to reflect PSF results for the year ended August 31, 2011 when audited financial statements become available.

At the end of fiscal 2010, the total Fund balance was $24.4 billion. Fund balance increased $1.80 billion from the prior year primarily attributable to the increase in the fair value of the PSF(SBOE) investments and the recovering markets. During the year, the SBOE continued implementing its revised long term strategic asset allocation to diversify and strengthen the PSF(SBOE) investment assets of the Fund. The revised allocation is projected to increase returns over the long run while reducing risk and return volatility of the portfolio. The one year, three year, five year and ten year annualized total returns for the PSF(SBOE) assets were 7.51%, -2.64%, 3.11% and 2.87% respectively (total return takes into consideration the change in the market value of the Fund during the year as well as the interest and dividend income generated by the Fund's investments). In addition, the SLB continued its shift into externally managed real asset investment funds and the one year, three year, and five year annualized total returns for the PSF(SLB) real assets, including cash, are -2.85%, -4.68%, and 2.19% respectively.

The market value of the Fund's assets is directly impacted by the performance of the various financial markets in which the assets are invested. The most important factors affecting investment performance are the asset allocation decisions made by the SBOE and SLB. The current SBOE long term asset allocation policy allows for diversification of the PSF(SBOE) portfolio into alternative asset classes whose returns are not as correlated to traditional asset classes. The implementation of the long term asset allocation will occur over several fiscal years and is expected to provide incremental total return at reduced risk. As of August 31, 2010, the PSF(SBOE) portion of the Fund had diversified into emerging market international equities, absolute return funds, real estate and private equity. Other asset classes such as risk parity and real return will be strategically added commensurate with the economic environment and the goals and objectives of the SBOE.

The PSF(SLB) portfolio is generally characterized by three broad categories: (1) discretionary real assets investments, (2) sovereign and other lands, and (3) mineral interests. Discretionary real assets investments consist of externally managed real estate, infrastructure, and energy/minerals investment funds; internally managed direct real estate investments, and cash. Sovereign and other lands consist primarily of the lands set aside to the PSF when it was created. Mineral interests consist of all of the minerals that are associated with PSF lands. The investment focus of PSF(SLB) discretionary real assets investments has shifted from internally managed direct real estate investments to externally managed real assets investment funds. Approximately $230 million of capital commitments to externally managed real assets investment funds were funded during fiscal year 2010. At August 31, 2010, the SLB had approved total capital commitments, net of the original capital commitments associated with any investments that were subsequently sold or dissolved, of $2.122 billion to thirty-four funds, and one co-investment vehicle, of which approximately $971 million remains unfunded.

The PSF(SBOE)'s investment in equity securities experienced a return of 5.50% during the fiscal year ended August 31, 2010. The PSF(SBOE)'s investment in fixed income securities produced a return of 11.29% during the fiscal year and absolute return investments yielded a return of 7.85%. Combined, all PSF(SBOE) asset classes produced an investment return of 7.51% for the fiscal year ended August 31, 2010, outperforming the target index by approximately 84 basis points. All PSF(SLB) real assets (including cash) returned -2.85% for the fiscal year ending August 31, 2010.

For fiscal year 2010, total revenues, inclusive of unrealized gains and losses and net of security lending rebates and fees, totaled $1.93 billion, an increase of $3.92 billion from fiscal year 2009 negative earnings of $1.98 billion. This increase is primarily attributable to the recovery of domestic and international securities markets in fiscal year 2010. In fiscal year 2010, revenues earned by the Fund included lease payments, bonuses and royalty income received from oil, gas and mineral leases; lease payments from commercial real estate; surface lease and easement revenues; revenues from the resale of natural and liquid gas supplies; dividends, interest, and securities lending revenues; the net change in the fair value of the investment portfolio; and, other miscellaneous fees and income.

Expenditures are paid from the Fund before distributions are made under the total return formula. Such expenditures include the costs incurred by the SLB to manage the land endowment, as well as operational costs of the Fund, including external management fees paid from appropriated funds. Total operating expenditures, net of security lending rebates and fees, decreased 41.7% for the fiscal year ending August 31, 2010. This decrease is primarily attributable to the decrease in the expenditures for gas supplies purchased for resale within the State Energy Management Program.

The Fund supports the public school system in the State by distributing a predetermined percentage of its asset value to the ASF. For fiscal years 2009 and 2010, this distribution to the ASF totaled $716.53 million and $60.7 million, respectively.

At the end of the 2010 fiscal year, PSF assets guaranteed $49.3 billion in bonds issued by 776 local school districts. Since its inception in 1983, the Fund has guaranteed 4,243 school district bond issues totaling $88.9 billion in principal amount. During the 2010 fiscal year, the number of outstanding issues guaranteed under the Guarantee Program decreased by 76, or -3.1%. The dollar amount of guaranteed school bond issues outstanding decreased by $731.0 million or 1.5%. The guarantee capacity of the Fund increased by $13.167 billion, or 22.8%, during fiscal year 2010 due to the change in the multiplier.

2011 Constitutional Amendment

During the Regular Session of the 82nd Legislature, which concluded May 30, 2011, a joint resolution ("HJR 109") was enacted proposing amendments to various sections of the Texas Constitution that pertain to the PSF. In accordance with HJR 109, a referendum was held in the State on November 8, 2011. At that referendum, voters of State approved non-substantive changes to the Texas Constitution to clarify references to the Fund, and, in addition, approved an amendment that effects an increase to the base amount used in calculating the Distribution Rate from the Fund to the ASF. The amendments approved at the referendum include an increase to the base used to calculate the Distribution Rate by adding to the calculation base certain discretionary real assets and cash in the Fund that is managed by entities other than the SBOE (at present, by the SLB). The value of those assets were already included in the value of the Fund for purposes of the Guarantee Program, but prior to the amendment had not been included in the calculation base for purposes of making transfers from the Fund to the ASF. While the amendment provides for an increase in the base for the calculation of approximately $2 billion, no new resources were provided for deposit to the Fund. As described under "The Total Return Constitutional Amendment" the SBOE is prevented from approving a Distribution Rate or making a pay out from the Fund if the amount distributed would exceed 6% of the average of the market value of the Fund, excluding real property in the Fund, but including discretionary real asset investments on the last day of each of the sixteen State fiscal quarters preceding the Regular Session of the Legislature that begins before that State fiscal biennium or if such pay out would exceed the Ten Year Total Return. The new calculation base is required to be used to determine all payments to the ASF from the Fund beginning with the 2012-13 biennium. As described under "The Total Return Constitutional Amendment" the SBOE approved a distribution rate of 4.2% in January 2011 based on a commitment of the SLB to transfer $500 million to the PSF during the biennium.

The constitutional amendments approved on November 8, 2011 also provides authority to the GLO or other entity other than the SBOE that has responsibility for the management of land or other properties of the Fund to determine in its sole discretion whether to transfer each year from Fund assets to the ASF revenue derived from such land or properties, an amount not to exceed $300 million. Any amount transferred to the ASF by an entity other than the SBOE is excluded from the 6% Distribution Rate limitation applicable to SBOE transfers.

The impact of the increase in the base against which the Distribution Rate is applied will be an increase in the distributions from the PSF to the ASF, provided that there are no reductions in the percentage established biennially by the SBOE to be the Distribution Rate. For the 2012-13 biennium, the Distribution Rate has been set by the SBOE at 4.2%. Given the increase in the calculation base effected by the November 8, 2011 constitutional amendment, the effect on transfers made by the SBOE in 2012-12 will be an increase in the total return distribution by an estimated $73.7 million in each year of the biennium. Going forward, it may be necessary for the SBOE to reduce the Distribution Rate in order to preserve the corpus of the Fund in accordance with its management objective of preserving intergenerational equity. Assuming a static Distribution Rate in the 2014-15 biennium and beyond, as the value of the real assets investments increase annually, distributions to the ASF would increase in the out years. The increased amounts distributed from the Fund will be a loss to either the investment corpus of the PSF managed by SBOE or, should the SLB increase its transfers to the SBOE to cover this share of the distribution, to the assets managed by the SLB. In addition, the changes made by the amendment will reduce the compounding interest in the Fund that would be derived from these assets remaining in the corpus of the Fund. Other factors that may affect the corpus of the Fund that are associated with this change include the decisions that are made by the SLB or others that are or may in the future be authorized to make transfers of funds from the PSF to the ASF. While the SBOE has oversight of the Guarantee Program, it will not have the decision making power with respect to all transfers to the ASF, as it has had in the past, which could adversely affect the ability of the SBOE to optimally manage its portion of the PSF assets.

Other 2011 Legislative Actions – Charter School Guarantee Program

During the First Called Session of the 82nd Texas Legislature, which ended June 29, 2011, Senate Bill 1 ("SB 1") was enacted. Among other provisions, SB 1 authorizes the use of the PSF to guarantee revenue bonds issued by certain open-enrollment charter schools that are designated as "charter districts" by the Commissioner. The program authorized by SB 1 is referred to herein as the "Charter School Guarantee Program." It is anticipated that the Charter School Guarantee Program will not become effective until certain contingent requirements are satisfied, including the establishment of regulations by the Commissioner for the administration of the program. It is also expected that the new program will not be implemented until the SBOE has received a response from the IRS with respect to certain federal tax law matters concerning the Charter School Guarantee Program that have been submitted to the IRS for review. As a result, the date of implementation and the ultimate structure of the Charter School Guarantee Program are presently unknown, although the program could be implemented in calendar year 2012.

In general, the Charter School Guarantee Program has been authorized through the enactment of amendments to the Act. As amended, the Act provides that a qualified charter district may make application to the Commissioner under the Act for a guarantee of its bonds, including refunding bonds, by the PSF. The capacity of the Charter School Guarantee Program is limited to the total amount that equals the result of the percentage that is equal to the ratio of the number of students enrolled in open-enrollment charter schools in the State compared to the total number of students enrolled in all public schools in the State multiplied by the of the combined capacities of the Guarantee Program and Charter School Guarantee Program. As of March 1, 2011 (the most recent date for which data is available), the percentage of students enrolled in open-enrollment charter schools to the total State scholastic census was approximately 2.72%. For the capacity of the Guarantee Program, see "Capacity Limits for the Guarantee Program."

The amendments to the Act further provide that the Commissioner may not approve charter district bonds for guarantee if such guarantees will result in lower bond ratings for public school district bonds that are guaranteed under the Guarantee Program. To be eligible for a guarantee, the Act provides that a charter district's bonds must be approved by the Attorney General, rated without the guarantee as investment grade by a nationally recognized investment rating firm, and satisfy an investigation conducted by the TEA as to the charter district's accreditation.

The amendments to the Act further provide for the establishment of a reserve fund in the State treasury. Each charter district that has a bond guaranteed must annually remit to the Commissioner, for deposit in the charter district bond guarantee reserve fund, an amount equal to 10% (or such higher amount as may be determined by the Commissioner) of the savings to the charter district that result from the lower interest rate on the bond due to the guarantee by the PSF.

The Act provides that immediately following receipt of notice that a charter district will be or is unable to pay maturing or matured principal or interest on a guaranteed bond, the Commissioner is required to instruct the transfer from the charter district bond guarantee reserve fund to the district's paying agent an amount necessary to pay the maturing or matured principal or interest. If money in the charter district bond guarantee reserve fund is insufficient to pay the amount due on a bond for which a notice of default has been received, the Commissioner shall instruct the transfer from the PSF to the district's paying agent the amount necessary to pay the balance of the unpaid maturing or matured principal or interest. If a total of two or more payments are made under the Charter School Guarantee Program on charter district bonds and the Commissioner determines that the charter district is acting in bad faith under the program, the Commissioner may request the Attorney General to institute appropriate legal action to compel the charter district and its officers, agents, and employees to comply with the duties required of them by law in regard to the guaranteed bonds.

Other Events and Disclosures

The State Investment Ethics Code governs the ethics and disclosure requirements for financial advisors and other service providers who advise certain State governmental entities, including the PSF. In accordance with the provisions of the State Investment Ethics Code, the SBOE periodically modifies its code of ethics, which occurred most recently in May 2010. The SBOE code of ethics includes prohibitions on sharing confidential information, avoiding conflict of interests and requiring disclosure filings with respect to contributions made or received in connection with the operation or management of the Fund. The code of ethics applies to members of the SBOE as well as to persons who are responsible by contract or by virtue of being a TEA PSF staff member for managing, investing, executing brokerage transactions, providing consultant services, or acting as a custodian of the PSF, and persons who provide investment and management advice to a member of the SBOE, with or without compensation under certain circumstances. The code of ethics is codified in the Texas Administrative Code at 19 TAC sections 33.5 et seq., and is available on the TEA web site at www.tea.state.tx.us/rules/tac/chapter033/index.html.

Since 2007, TEA has made supplemental appropriation requests to the Legislature for the purpose of funding the implementation of the 2008 Asset Allocation Policy, but those requests have been denied or partly funded. In the 2011 legislative session, the Legislature approved an increase of 31 positions in the full-time equivalent employees for the administration of the Fund, which was funded as part of an $18 million appropriation for each year of the 2012-13 biennium, in addition to the operational appropriation of $11 million for each year of the biennium. The TEA plans to retain a consultant to make recommendations on how to structure any increase in staffing.

As of August 31, 2010, certain lawsuits were pending against the State and/or the GLO, which challenge the Fund's title to certain real property and/or past or future mineral income from that property. Reference is made to the Annual Report for a description of such lawsuits that are pending, which may represent contingent liabilities of the Fund.

The SBOE is a named defendant in litigation described in the Official Statement pertaining to the Bonds that has been filed in State District Court that has challenged the constitutionality of the Texas public school finance system, and which, among other relief requested, seeks an injunction to prohibit the State and its officials from distributing any funds under the current finance system until a constitutional system is created. The TEA does not anticipate that the security for payment of the Bonds, including the PSF guarantee of school district bonds, would be adversely affected by such litigation.

PSF Continuing Disclosure Undertaking

The SBOE has adopted an investment policy rule (the "TEA Rule") pertaining to the PSF and the Guarantee Program. The TEA Rule is codified in Section I of the TEA Investment Procedure Manual, which relates to the Guarantee Program. The most recent amendment to the TEA Rule was adopted by the SBOE on November 19, 2010, and is summarized below. Through the adoption of the TEA Rule and its commitment to guarantee the Bonds, the SBOE has made the following agreement for the benefit of the District and holders and beneficial owners of the Bonds. The TEA (or its successor with respect to the management of the Guarantee Program) is required to observe the agreement for so long as it remains an "obligated person," within the meaning of SEC Rule 15c2-12 ("Rule 15c2-12"), with respect to the Bonds. Nothing in the TEA Rule obligates the Agency to make any filings or disclosures with respect to guaranteed bonds, as the obligations of the Agency under the TEA Rule pertain solely to the Guarantee Program. The district issuing the guaranteed bonds has assumed the applicable obligation under Rule 15c-12 to make all disclosures and filings relating directly to guaranteed bonds, and the TEA takes no responsibility with respect to such district undertakings. Under the TEA agreement, the TEA will be obligated to provide annually certain updated financial information and operating data, and timely notice of specified material events, to the MSRB.

The MSRB has established the Electronic Municipal Market Access ("EMMA") system, and the TEA is required to file its continuing disclosure information using the EMMA system. Investors may access continuing disclosure information filed with the MSRB at www.emma.msrb.org.

Annual Reports

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

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

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

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

Material Event Notices

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

Availability of Information

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

Limitations and Amendments

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

The continuing disclosure agreement of the TEA is made only with respect to the PSF and the Guarantee Program. The District may make a continuing disclosure undertaking in accordance with Rule 15c2-12 with respect to its obligations arising under Rule 15c2-12 pertaining to financial and operating data concerning the District and notices of material events relating to the Bonds. A description of the District's undertaking, if any, is included elsewhere in the Official Statement relating to the Bonds.

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

Compliance with Prior Undertakings

The TEA has not previously failed to substantially comply with its previous continuing disclosure agreements in accordance with Rule 15c2-12.

SEC Exemptive Relief

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

TAX RATE LIMITATIONS

A school district is authorized to levy maintenance and operation taxes subject to approval of a proposition submitted to district voters under Section 45.003 of the Texas Education Code. The maximum tax rate that may be approved by voters for maintenance and operations is $1.50 per $100 of assessed valuation. The District voted its maintenance and operations tax at a rate of not to exceed $1.50 pursuant to Texas Revised Civil Statutes Annotated, Article 2784e-1, as amended ("Article 2784e-1"), at an election held on March 16, 1963.

Article 2784e-1 limits the District's annual, local maintenance and operations tax levy based upon a comparison between the District's outstanding bonded indebtedness and the District's taxable assessed value per $100 of assessed valuation. Article 2784e-1 provides for a reduction of $0.10 for each one percent (1%) or major fraction thereof increase in bonded indebtedness beyond seven percent (7%) of assessed value of property in the District. This limitation is capped when the District's bonded indebtedness is ten percent (10%) (or greater) of the District's assessed valuation which would result in an annual maintenance and operations tax levy not to exceed $1.20. Lastly, the Texas Attorney General in reviewing the District's transcript of proceedings will allow the District to reduce the amount of its outstanding bonded indebtedness by the amount of funds (on a percentage basis) that the District receives in State assistance for the repayment of this bonded indebtedness (for example, if the District anticipates that it will pay 75% of its bonded indebtedness from State assistance, for the purposes of Article 2784e-1, the Texas Attorney General will assume that only 25% of the District's bonded indebtedness is outstanding and payable from local ad valorem taxes). The bonded indebtedness of the District after the issuance of the Bonds will be approximately 5.50% of the District's current taxable assessed valuation of property. See "APPENDIX A – Voted General Obligation Debt" herein.

Prior to the adoption of the Reform Legislation in 2006 (see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - General"), the maximum tax rate that could have been adopted by the District in any fiscal year for maintenance and operations was $1.50 per $100 of assessed valuation, subject to the limitations described in the preceding paragraph. With the adoption of the Reform Legislation, for any fiscal year beginning with the 2006-07 fiscal year, the maximum tax rate per $100 of assessed valuation that may be adopted by the District may not exceed the lesser of (A) $1.50, or such lower rate as described in the preceding paragraph, and (B) the sum of (1) the rate of $0.17, and (2) the product of the "state compression percentage" multiplied by $1.50. The state compression percentage was 88.67% for fiscal year 2006-07 and 66.67% for fiscal year 2007-08, 2008-09 and 2009-10. For fiscal year 2010-11 and thereafter, the Commissioner is required to determine the state compression percentage for each fiscal year which is based on the amount of State funds appropriated for distribution to the District for the current fiscal year. For fiscal year 2010-11, the Commissioner has determined to maintain the State compression percentage at 66.67%.For a more detailed description of the state compression percentage, see "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - General". Furthermore, a school district cannot annually increase its tax rate in excess of the district's "rollback tax rate" without submitting such tax rate to a referendum election and a majority of the voters voting at such election approving the adopted rate. See "AD VALOREM TAX PROCEDURES - Public Hearing and Rollback Tax Rate."

A school district is also authorized to issue bonds and levy taxes for payment of bonds subject to voter approval of a proposition submitted to the voters under Section 45.003(b)(1), Texas Education Code, as amended, which provides for a tax unlimited as to rate or amount for the support of school district bonded indebtedness (see "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS").

Chapter 45 of the Texas Education Code, as amended, requires a district to demonstrate to the Texas Attorney General that it has the prospective ability to pay debt service on a proposed issue of bonds, together with debt service on other outstanding "new debt" of the district, from a tax levied at a rate of $0.50 per $100 of assessed valuation before bonds may be issued. In demonstrating the ability to pay debt service at a rate of $0.50, a district may take into account State allotments to the district which effectively reduce the district's local share of debt service. Once the prospective ability to pay such tax has been shown and the bonds are issued, a district may levy an unlimited tax to pay debt service. Taxes levied to pay debt service on bonds approved by district voters at an election held on or before April 1, 1991 and issued before September 1, 1992 (or debt issued to refund such bonds) are not subject to the foregoing threshold tax rate test. The Bonds are "new debt" and are subject to the $0.50 threshold tax rate test. A district may demonstrate its ability to comply with the $0.50 threshold tax rate test by applying the $0.50 tax rate to an amount equal to 90% of projected future taxable value of property in the district, as certified by a registered professional appraiser, anticipated for the earlier of the tax year five years after the current tax year or the tax year in which the final payment for the bonds is due. However, if a district uses projected future taxable values to meet the $0.50 threshold tax rate test and subsequently imposes a tax a tax rate greater than $0.50 per $100 of valuation to pay for bonds subject to the test, then for subsequent bond issues, the Attorney General must find that the district has the projected ability to pay principal and interest on the proposed bonds and all previously issued bonds subject to the $0.50 threshold tax rate test from a tax rate of $0.45 per $100 of valuation. See "CURRENT PUBLIC SCHOOL FINANCE SYSTEM". The District has not utilized projected values to satisfy the $0.50 test.

DEBT LIMITATIONS

Under State law, there is no explicit bonded indebtedness limitation, although the tax rate limits described above under "TAX RATE LIMITATIONS" effectively impose a limit on the incurrence of debt. Such tax rate limits require school districts to demonstrate the ability to pay new debt secured by the district's debt service tax from a tax rate of $0.50, and to pay all debt and operating expenses which must be paid from receipts of the district's maintenance tax from a tax not to exceed the maintenance tax limit described under the caption "TAX RATE LIMITATIONS." In demonstrating compliance with the requirement, a district may take into account State equalization payments, and, effective September 1, 1997, if compliance with such requirement is contingent on receiving State assistance, a district may not adopt a tax rate for a year for purposes of paying the principal of and interest on the bonds unless the district credits to the interest and sinking fund of the bond the amount of state assistance received or to be received in that year. The State Attorney General reviews a district's calculations showing the compliance with such test as a condition to the legal approval of the debt. The Bonds are "new debt" and are therefore subject to the $0.50 threshold tax rate test. See also "TAX RATE LIMITATIONS".

EMPLOYEE BENEFIT PLANS AND OTHER POST-EMPLOYMENT BENEFITS

The District's employees participate in a retirement plan (the "Plan") with the State of Texas. The Plan is administered by the Teacher Retirement System of Texas ("TRS"). State contributions are made to cover costs of the TRS retirement plan up to certain statutory limits. The District is obligated for a portion of TRS costs relating to employee salaries that exceed the statutory limit. Aside from the District's contribution to TRS, the District has no pension fund expenditures or liabilities. For fiscal year ended June 30, 2011, the District made a contribution of $479,670 to TRS on a portion of its employees' salaries that exceeded the statutory minimum. The District generally does not offer any post-employment retirement benefits and has no liabilities for "Other Post Employment Retirement Benefits" as defined in GASB Statement No. 45. For a discussion of the TRS retirement plan, see "Note IV. C. Defined Benefit Pension Plan" to the audited financial statements of the District that are attached hereto as Appendix D (the "Financial Statements").

During the year ended June 30, 2011, active employees of the District were covered by a fully-insured health insurance plan administered by TRS (the "Health Care Plan"). The District contributed $330 per month per employee to the Health Care Plan.

Employees, at their option, authorize payroll withholdings to pay premiums for dependents. See “Note IV. Other Information A. Health Care Coverage” of the Financial Statements.

The District also contributes to the Texas Public School Retired Employees Group Insurance Program (the "Retiree Health Plan"), a cost sharing multiple-employer defined benefit postemployment health care plan administered by TRS, which is known as TRS-Care. TRS-Care provides health coverage for certain persons (and their dependents) who retired under TRS. For fiscal year ended June 30, 2011, the District was required to a contribute $288,658 to TRS-Care as required by State law. For more information concerning the Retiree Health Plan, see “Note IV. Other Information D. School District Retiree Health Plan” of the Financial Statements.

Formal collective bargaining agreements relating directly to wages and other conditions of employment are prohibited by State law, as are strikes by teachers. There are various local, state and national organized employee groups who engage in efforts to better terms and conditions of employment of school employees. Some districts have adopted a policy to consult with employer groups with respect to certain terms and conditions of employment. Some examples of these groups are the Texas State Teachers Association, the Texas Classroom Teachers Association, the Association of Texas Professional Educators and the National Education Association.

RATINGS

Moody’s Investors Service, Inc. (“Moody’s) and Standard & Poor’s Ratings Services, a Standard & Poor’s Financial Services LLC business (“S&P”), has assigned to the Bonds ratings of “Aaa” and “AAA”, respectively, based upon the guaranteed repayment thereof under the Permanent School Fund Guarantee Program of the Texas Education Agency. The District’s underlying rating without regard to credit enhancement is “Aa3” by Moody’s and “AA“ by S&P. (See “THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM” herein.)

An explanation of the significance of such ratings may be obtained from Moody’s and S&P. The ratings of the Bonds by Moody’s and S&P reflects only the views of each company at the time the ratings are given, and the District makes no representations as to the appropriateness of the ratings. There is no assurance that the ratings will continue for any given period of time, or that the ratings will not be revised downward or withdrawn entirely by Moody’s and S&P, if, in the judgment of Moody’s and S&P, circumstances so warrant. Any such downward revision or withdrawal of the rating may have an adverse effect on the market price of the Bonds.

The above ratings are not a recommendation to buy, sell or hold the Bonds, and such ratings may be subject to revision or withdrawal at any time by Moody’s and S&P. Any downward revision or withdrawal of the rating may have an adverse effect on the market price of the Bonds.

LEGAL MATTERS

The delivery of the Bonds is subject to the approval of the Attorney General of Texas to the effect that the Bonds are valid and legally binding obligations of the District payable from the proceeds of an annual ad valorem tax levied, without legal limit as to rate or amount, upon all taxable property in the District, and the approving legal opinion of Andrews Kurth LLP, Bond Counsel to the District ("Bond Counsel") in substantially the form attached hereto as Appendix C. The legal fee to be paid to Bond Counsel for services rendered in connection with the issuance of the Bonds is contingent upon the sale and delivery of the Bonds.

Though it represents the Financial Advisor and purchasers and underwriters of Texas school district bonds from time to time in matters unrelated to the issuance of the Bonds, Bond Counsel has been engaged by and only represents the District in connection with the issuance of the Bonds. Except as noted below, Bond Counsel was not requested to participate, and did not take part in the preparation of the Official Statement, and such firm has not assumed any responsibility with respect thereto or undertaken independently to verify any of the information contained herein except that in its capacity as Bond Counsel, such firm has reviewed the information appearing under the captions or subcaptions “THE BONDS” (except under the subcaptions “Payment Record” and “PERMANENT SCHOOL FUND GUARANTEE” as to which no opinion is expressed), “REGISTRATION, TRANSFER AND EXCHANGE”, “STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS”, “CURRENT PUBLIC SCHOOL FINANCE SYSTEM” (except under the subcaptions “Possible Effects of Wealth Transfer Provisions on the District’s Financial Condition” and “82nd Texas Legislature – Impact of Texas Budget on the District” as to which no opinion is expressed), “TAX RATE LIMITATIONS (the first paragraph only)”, “LEGAL MATTERS”, “TAX MATTERS”, “LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS”, “REGISTRATION AND QUALIFICATION OF THE BONDS FOR SALE” and “CONTINUING DISCLOSURE OF INFORMATION” (except under the subcaption “Compliance with Prior Undertakings,” as to which no opinion is expressed) and such firm is of the opinion that the information relating to the Bonds and the Order contained under such captions is a fair and accurate summary of the information purported to be shown and that the information and descriptions contained under such captions relating to the provisions of applicable state and federal laws are correct as to matters of law.

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

TAX MATTERS

The following is a general summary of the United States federal income tax consequences of the purchase and ownership of the Bonds. The discussion is based upon laws, Treasury Regulations, rulings and decisions now in effect, all of which are subject to change or possibly differing interpretations. No assurances can be given that future changes in the law will not alter the conclusions reached herein. The discussion below does not purport to deal with United States federal income tax consequences applicable to all categories of investors. Further, this summary does not discuss all aspects of United States federal income taxation that may be relevant to a particular investor in the Bonds in light of the investor’s particular personal investment circumstances or to certain types of investors subject to special treatment under United States federal income tax laws (including insurance companies, tax exempt organizations, financial institutions, brokers-dealers, and persons who have hedged the risk of owning the Bonds). The summary is therefore limited to certain issues relating to initial investors who will hold the Bonds as “capital assets” within the meaning of section 1221 of the Code and acquire such Bonds for investment and not as a dealer or for resale. Prospective investors should note that no rulings have been or will be sought from the IRS with respect to any of the U.S. federal income tax consequences discussed below, and no assurance can be given that the IRS will not take contrary positions.

INVESTORS SHOULD CONSULT THEIR OWN TAX ADVISORS IN DETERMINING THE FEDERAL, STATE, LOCAL, FOREIGN AND ANY OTHER TAX CONSEQUENCES TO THEM FROM THE PURCHASE, OWNERSHIP AND DISPOSITION OF THE BONDS.

Internal Revenue Service Circular 230 Notice

You should be aware that: (i) the discussion with respect to United States federal tax matters in this Official Statement was not intended or written to be used, and cannot be used, by any taxpayer for the purpose of avoiding penalties that may be imposed on the taxpayer; (ii) such discussion was written to support the promotion or marketing (within the meaning of IRS Circular 230) of the transactions or matters addressed by such discussion; and (iii) each taxpayer should seek advice based on his or her particular circumstances from an independent tax advisor.

This notice is given solely for purposes of ensuring compliance with IRS Circular 230.

Interest on the Bonds

Any interest paid on the Bonds will be includable in the gross income of the holders thereof for federal income tax purposes under Section 61 of the Code.

Reporting of Interest Payments

Subject to certain exceptions, interest payments made to beneficial owners with respect to the Bonds will be reported to the IRS. Such information will be filed each year with the IRS on Form 1099, which will reflect the name, address, and TIN of the beneficial owner. A copy of Form 1099 will be sent to each beneficial owner of a Bond for U.S. federal income tax purposes.

Original Issue Discount

If a substantial amount of the Bonds are purchased at original issuance for a purchase price (the "Issue Price") that is less than their face amount by more than one quarter of one percent times the number of complete years to maturity, the Bonds will be treated as being issued with "original issue discount." The amount of the original issue discount will equal the excess of the principal amount payable on such Bonds at maturity over its Issue Price, and the amount of the original issue discount on the Bonds will be amortized over the life of the Bonds using the "constant yield method" provided in the Treasury Regulations. As the original issue discount accrues under the constant yield method, the beneficial owners of the Bonds, regardless of their regular method of accounting, will be required to include such accrued amount in their gross income as interest. This can result in taxable income to the beneficial owners of the Bonds that exceeds actual cash distributions to the beneficial owners in a taxable year.

The amount of the original issue discount that accrues on the Bonds each taxable year will be reported annually to the IRS and to the beneficial owners. The portion of the original issue discount included in each beneficial owner's gross income while the beneficial owner holds the Bonds will increase the adjusted tax basis of the Bonds in the hands of such beneficial owner.

Disposition of Bonds and Market Discount

A beneficial owner of Bonds will generally recognize gain or loss on the redemption, sale or exchange of a Bond equal to the difference between the redemption or sales price (exclusive of the amount paid for accrued interest) and the beneficial owner's adjusted tax basis in the Bonds. Generally, the beneficial owner's adjusted tax basis in the Bonds will be the beneficial owner's initial cost, increased by the original issue discount previously included in the beneficial owner's income to the date of disposition. Any gain or loss generally will be capital gain or loss and will be long-term or short-term, depending on the beneficial owner's holding period for the Bonds.

Under current law, a purchaser of a Bonds who did not purchase the Bonds in the initial public offering (a "subsequent purchaser") generally will be required, on the disposition of the Bonds, to recognize as ordinary income a portion of the gain, if any, to the extent of the accrued "market discount." Market discount is the amount by which the price paid for the Bonds by a subsequent purchaser is less than the sum of Issue Price and the amount of original issue discount previously accrued on the Bonds. The Code also limits the deductibility of interest incurred by a subsequent purchaser on funds borrowed to acquire a Bond with market discount. As an alternative to the inclusion of market discount in income upon disposition, a subsequent purchaser may elect to include market discount in income currently as it accrues on all market discount instruments acquired by the subsequent purchaser in that taxable year or thereafter, in which case the interest deferral rule will not apply. The re-characterization of gain as ordinary income on a subsequent disposition of a bond could have a material effect on the market value of the Bonds.

Backup Withholding

Under section 3406 of the Code, a beneficial owner of the Bonds who is a United States person, as defined in section 7701(a)(30 of the Code, may, under certain circumstances, be subject to "backup withholding" on payments of current or accrued interest on the Bonds. This withholding applies if such beneficial owner of Bonds: (i) fails to furnish to the payor such beneficial owner's social security number or other taxpayer identification number ("TIN"); (ii) furnishes the payor an incorrect TIN; (iii) fails to report properly interest, dividends, or other "reportable payments" as defined in the Code; or (iv) under certain circumstances, fails to provide the payor with a certified statement, signed under penalty of perjury, that the TIN provided to the payor is correct and that such beneficial owner is not subject to backup withholding.

Backup withholding will not apply, however, with respect to payments made to certain beneficial owners of the Bonds. Beneficial owners of the Bonds should consult their own tax advisors regarding their qualification for exemption from backup withholding and the procedures for obtaining such exemption.

Withholding on Payments to Nonresident Alien Individuals and Foreign Corporations

Under sections 1441 and 1442 of the Code, nonresident alien individuals and foreign corporations are generally subject to withholding at the rate of 30% on periodic income items arising from sources within the United States, provided such income is not effectively connected with the conduct of a United States trade or business. Assuming the interest received by the beneficial owners of the Bonds is not treated as effectively connected income within the meaning of section 864 of the Code, such interest will be subject to 30% withholding, or any lower rate specified in an income tax treaty, unless such income is treated as portfolio interest. Interest will be treated as portfolio interest if: (i) the beneficial owner provides a statement to the payor certifying, under penalties of perjury, that such beneficial owner is not a United States person and providing the name and address of such beneficial owner; (ii) such interest is treated as not effectively connected with the beneficial owner's United States trade or business; (iii) interest payments are not made to a person within a foreign country which the IRS has included on a list of countries having provisions inadequate to prevent United States tax evasion; (iv) interest payable with respect to the Bonds is not deemed contingent interest within the meaning of the portfolio debt provision; (v) such beneficial owner is not a controlled foreign corporation, within the meaning of section 957 of the Code; and (vi) such beneficial owner is not a bank receiving interest on the Bonds pursuant to a loan agreement entered into in the ordinary course of the bank's trade or business.

Assuming payments on the Bonds are treated as portfolio interest within the meaning of sections 871 and 881 of the Code, then no backup withholding under section 1441 and 1442 of the Code and no backup withholding under section 3406 of the Code is required with respect to beneficial owners or intermediaries who have furnished Form W-8 BEN, Form W-8 EXP or Form W-8 IMY, as applicable, provided the payor does not have actual knowledge that such person is a United States person.

INVESTMENT POLICIES

Investments

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

Legal Investments

Under Texas law, the District is authorized to invest in (1) obligations, including letters of credit, of the United States or its agencies and instrumentalities, (2) direct obligations of the State of Texas or its agencies and instrumentalities, (3) collateralized mortgage obligations directly issued by a federal agency or instrumentality of the United States, the underlying security for which is guaranteed by an agency or instrumentality of the United States, (4) other obligations, the principal and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of the State of Texas or the United States or their respective agencies and instrumentalities, (5) obligations of states, agencies, counties, cities, and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm not less than A or its equivalent, (6) (a) certificates of deposit and share certificates issued by a depository institution that has its main office or branch office in the State of Texas, that are guaranteed or insured by the Federal Deposit Insurance Corporation or the National Credit Union Share Insurance Fund or their respective successors, or are secured as to principal by obligations described in clauses (1) through (5) and clause (13) or in any other manner and amount provided by law for District deposits, and in addition (b) the District is authorized, subject to certain conditions, to invest in certificates of deposit with a depository institution that has its main office or branch office in the State of Texas and that participates in the Certificate of Deposit Account Registry Service® network (CDARS®) and as further provided by Texas law, (7) fully collateralized repurchase agreements that have a defined termination date, are fully secured by obligations described in clause (1) and require the security being purchased by the District to be pledged to the District, held in the District's name and deposited at the time the investment is made with the District or with a third party selected and approved by the District, and are placed through a primary government securities dealer or a financial institution doing business in the State of Texas, (8) bankers' acceptances with the remaining term of 270 days or less from the date of issuance, if the short-term obligations of the accepting bank or its parent are rated at least A-1 or P-1 or the equivalent by at least one nationally recognized credit rating agency, (9) commercial paper with the remaining term of 270 days or less from the date of issuance that is rated at least A-1 or P-1 or the equivalent by at least (a) two nationally recognized credit rating agencies or (b) one nationally recognized credit rating agency if the paper is fully secured by an irrevocable letter of credit issued by a U.S. or state bank, (10) no-load money market mutual funds registered with and regulated by the United States Securities and Exchange Commission that have a dollar weighted average portfolio maturity of 90 days or less and include in their investment objectives the maintenance of a stable net asset value of $1 for each share, (11) no-load mutual fund registered with the United States Securities and Exchange Commission that: have an average weighted maturity of less than two years, invest exclusively in obligations described in the preceding clauses and clause (13), and are continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than AAA or its equivalent, (12) public funds investment pools that have an advisory board which includes participants in the pool and are continuously rated as to investment quality by at least one nationally recognized investment rating firm of not less than AAA or its equivalent or no lower than investment grade with a weighted average maturity no greater than 90 days, and (13) bonds issued, assumed or guaranteed by the State of Israel. Texas law also permits the District to invest bond proceeds in a guaranteed investment contract subject to the limitations set forth in Chapter 2256, as amended, Texas Government Code.

Entities such as the District may enter into securities lending programs if (i) the securities loaned under the program are 100% collateralized including accrued income, a loan made under the program allows for termination at any time and a loan made under the program is either secured by (a) obligations that are described in clauses (1) through (5) and clause (13) above, (b) pledged irrevocable letters of credit issued by a state or national bank that is continuously rated by a nationally recognized investment rating firm at not less than A or its equivalent or (c) cash invested in obligations described in clauses (1) through (5) and clause (13) above, clause (9) above and clauses (10) and (11) above, or an authorized investment pool; (ii) securities held as collateral under a loan are pledged to such investing entity or a third party designated by such investing entity; (iii) a loan made under the program is placed through either a primary government securities dealer or a financial institution doing business in the State of Texas; and (iv) the agreement to lend securities has a term of one year or less.

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

Under Texas law, the District may contract with an investment management firm registered under the Investment Advisers Act of 1940 (15 U.S.C. Section 80b-1 et seq.) or with the State Securities Board to provide for the investment and management of its public funds or other funds under its control for a term up to two years, but the District retains ultimate responsibility as fiduciary of its assets. In order to renew or extend such a contract, the District must do so by order, ordinance or resolution. The District has not contracted with, and has no present intention of contracting with, any such investment management firm or the State Securities Board to provide such services.

Investment Policies

Under Texas law, the District is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity; that address investment diversification, yield, maturity, and the quality and capability of investment management; and that includes a list of authorized investments for District funds, maximum allowable stated maturity of any individual investment owned by the District and the maximum average dollar-weighted maturity allowed for pooled fund groups.

All District funds must be invested consistent with a formally adopted "Investment Strategy Statement" that specifically addresses each fund's investment. Each Investment Strategy Statement will describe its objectives concerning: (1) suitability of investment type, (2) preservation and safety of principal, (3) liquidity, (4) marketability of each investment, (5) diversification of the portfolio, and (6) yield.

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

Additional Provisions

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

Current Investments

As of November 30, 2011, the District had approximately $7,432,852 (unaudited) invested in government investment pools that generally have the characteristics of a money-market mutual fund; $2,000,720 in U.S. Treasury securities; $2,000,000 in U.S. Agency Securities; $1,065,890 in tax-exempt bonds; $484,091 in bank certificates of deposit; and $13,097,053 in a demand deposit account at Wells Fargo Bank, the District's depository bank and an Underwriter of the Bonds. The market value of such investments (as determined by the District by reference to published quotations, dealer bids, and comparable information) is approximately 100% of the book value. No funds of the District are invested in derivative securities, i.e., securities whose rate of return is determined by reference to some other instrument, index, or commodity.

REGISTRATION AND QUALIFICATION OF BONDS FOR SALE

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

FINANCIAL ADVISOR

Southwest Securities is employed as Financial Advisor to the District to assist in the issuance of the Bonds. In this capacity, the Financial Advisor has compiled certain data relating to the Bonds that is contained in this Official Statement. The Financial Advisor has not independently verified any of the data contained herein or conducted a detailed investigation of the affairs of the District to determine the accuracy or completeness of this Official Statement. Because of their limited participation, the Financial Advisor assumes no responsibility for the accuracy or completeness of any of the information contained herein. The fee of the Financial Advisor for services with respect to the Bonds is contingent upon the issuance and sale of the Bonds. In the normal course of business, the Financial Advisor may from time to time sell investment securities to the District for the investment of bond proceeds or other funds of the District upon the request of the District.

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

LEGAL INVESTMENTS AND ELIGIBILITY TO SECURE PUBLIC FUNDS IN TEXAS

Section 1201.041 of the Public Securities Procedures Act (Chapter 1201, Texas Government Code) provides that the Bonds are negotiable instruments governed by Chapter 8, Texas Business and Commerce Code, and are legal and authorized investments for insurance companies, fiduciaries, and trustees, and for the sinking funds of municipalities or other political subdivisions or public agencies of the State of Texas. With respect to investment in the Bonds by municipalities or other political subdivisions or public agencies of the State of Texas, the Public Funds Investment Act, Chapter 2256, Texas Government Code, requires that the Bonds be assigned a rating of not less than "A" or its equivalent as to investment quality by a national rating agency. See

"RATING" herein. In addition, various provisions of the Texas Finance Code provide that, subject to a prudent investor standard, the Bonds are legal investments for state banks, savings banks, trust companies with at least $1 million of capital, and savings and loan associations. The Bonds are eligible to secure deposits of any public funds of the State, its agencies, and its political subdivisions, and are legal security for those deposits to the extent of their market value.

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

CONTINUING DISCLOSURE OF INFORMATION

In the Order, the District has made the following agreement for the benefit of the holders and beneficial owners of the Bonds. The District is required to observe the agreement for so long as it remains obligated to advance funds to pay the Bonds. Under the agreement, the District will be obligated to provide certain updated financial information and operating data annually and timely notice of specified events to the Municipal Securities Rulemaking Board (the "MSRB"). See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" for a description of the continuing disclosure undertaking to provide certain updated financial information and operating data annually with respect to the Permanent School Fund and the State, as the case may be, and to provide timely notice of specified events related to the guarantee, to the MSRB. The information provided to the MSRB will be available to the public free of charge via the Electronic Municipal Market Access ("EMMA") system at www.emma.msrb.org.

Annual Reports

The District will provide certain updated financial information and operating data to EMMA annually. The information to be updated includes all quantitative financial information and operating data with respect to the District of the general type included in Appendices A and D to this Official Statement. The District will update and provide this information within six months after the end of each Fiscal Year ending in or after 2011. The District will provide the updated information to the MSRB in an electronic format, which will be available through EMMA to the general public without charge.

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

The District's current fiscal year end is June 30. Accordingly, it must provide updated information by the last day of December in each year following the end of its fiscal year, unless the District changes its fiscal year. If the District changes its fiscal year, it will notify the MSRB of the change.

Event Notices

The District will also provide notices of certain events to the MSRB. The District will provide notice of any of the following events with respect to the Bonds to the MSRB in a timely manner and not more than 10 business days after occurrence of the event: (1) principal and interest payment delinquencies; (2) non-payment related defaults, if material; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB), or other material notices or determinations with respect to the tax-exempt status of the Bonds, or other material events affecting the tax status of the Bonds; (7) modifications to rights of holders of the Bonds, if material; (8) bond calls, if material, and tender offers; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the Bonds, if material; (11) rating changes; (12) bankruptcy, insolvency, receivership, or similar event of the District, which shall occur as described below; (13) the consummation of a merger, consolidation, or acquisition involving the District or the sale of all or substantially all of its assets, other than in the ordinary course of business, the entry into of a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; and (14) appointment of a successor or additional trustee or the change of name of a trustee, if material. For these purposes, any event described in the immediately preceding paragraph (12) is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent, or similar officer for the District in a proceeding under the United States Bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the District, or if such jurisdiction has been assumed by leaving the existing governing body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement, or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the District. Neither the Bonds nor the Order make any provision for debt service reserves, credit enhancement (except for the Permanent School Fund guarantee), or liquidity enhancement. In addition, the District will provide timely notice of any failure by the District to provide information, data, or financial statements in accordance with its agreement described above under "Annual Reports". The District will provide each notice described in this paragraph to the MSRB.

Availability of Information

Effective July 1, 2009, the SEC implemented amendments to the Rule which approved the establishment by the MSRB of EMMA, which is now the sole successor to the national municipal securities information repositories with respect to filings made in connection with undertakings made under the Rule. All information and documentation filing required to be made by the District in accordance with its undertaking made for the Bonds will be made with the MSRB in electronic format in accordance with MSRB guidelines. Access to such filings will be provided, without charge to the general public, by the MSRB.

With respect to debt of the District issued prior to the EMMA Effective Date, the District remains obligated to make annual required filings, as well as notices of material events, under its continuing disclosure obligations relating to those debt obligations (which includes a continuing obligation to make such filings with the Texas state information depository (the "SID")). Prior to EMMA Effective Date, the Municipal Advisory Council of Texas (the "MAC") had been designated by the State and approved by the SEC staff as a qualified SID. Subsequent to the EMMA Effective Date, the MAC entered into a Subscription Agreement with the MSRB pursuant to which the MSRB makes available to the MAC, in electronic format, all Texas-issuer continuing disclosure documents and related information posted to EMMA's website simultaneously with such posting. Until the District receives notice of a change in this contractual agreement between the MAC and EMMA or of a failure of either party to perform as specified thereunder, the District has determined, in reliance on guidance from the MAC, that making its continuing disclosure filings solely with the MSRB will satisfy its obligations to make filings with the SID pursuant to its continuing disclosure agreements entered into prior to the EMMA Effective Date.

Limitations and Amendments

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

The District may amend its continuing disclosure agreement from time to time to adapt to changed circumstances that arise from a change in legal requirements, a change in law, or a change in the identity, nature, status, or type of operations of the District, if (i) the agreement, as amended, would have permitted an underwriter to purchase or sell Bonds in the offering described herein in compliance with the Rule, taking into account any amendments or interpretations of the Rule to the date of such amendment, as well as such changed circumstances, and (ii) either (a) the holders of a majority in aggregate principal amount of the outstanding Bonds consent to the amendment or (b) any person unaffiliated with the District (such as nationally recognized bond counsel) determines that the amendment will not materially impair the interests of the registered owners of the Bonds. The District may also amend or repeal the provisions of this continuing disclosure agreement if the SEC amends or repeals the applicable provisions of the SEC Rule 15c2-12 or a court of final jurisdiction enters judgment that such provisions of the SEC Rule 15c2-12 are invalid, but only if and to the extent that the provisions of this sentence would not prevent an underwriter from lawfully purchasing or selling Bonds in the primary offering of the Bonds. If the District so amends the agreement, it has agreed to include with the next financial information and operating data provided in accordance with its agreement described above under "Annual Reports" an explanation, in narrative form, of the reasons for the amendment and of the impact of any change in the type of financial information and operating data so provided.

Compliance with Prior Undertakings

During the last five years, the District has substantially complied in all material respects with all continuing disclosure agreements made by it in accordance with the Rule.

LITIGATION

In the opinion of District officials, except as described in this Official Statement, the District is not a party to any litigation or other proceeding pending or to their knowledge threatened, in any court, agency or other administrative body (either state or federal) which, if decided adversely to the District, would have a material adverse effect on the financial condition of the District.

FORWARD LOOKING STATEMENTS

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

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

WINNING BIDDER

On January 23, 2012 the Bonds were awarded to an investment bank or group of investment banks managed by ________. The initial reoffering yields were supplied to the District by the Purchaser. The initial reoffering yield shown on the inside cover page will produce compensation to the Purchaser of approximately $_____________. The District can give no assurance that any trading market will be developed for the Bonds after their sale by the District to the Purchaser. The District has no control over the price at which the Bonds are subsequently sold and the initial yield at which the Bonds will be priced and reoffered will be established by and will be the responsibility of the Purchaser.

CERTIFICATION OF THE OFFICIAL STATEMENT

At the time of payment for and delivery of the Initial Bonds, the initial Purchaser will be furnished a certificate, executed by proper officials of the District, acting in their official capacities, to the effect that to the best of their knowledge and belief: (a) the descriptions and statements of or pertaining to the District contained in its Official Statement, and any addenda, supplement or amendment thereto, for the Bonds, on the date of such Official Statement, on the date of sale of said Bonds and the acceptance of the best bid therefor, and on the date of the delivery, were and are true and correct in all material respects; (b) insofar as the District and its affairs, including its financial affairs, are concerned, such Official Statement did not and does not contain an untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading; (c) insofar as the descriptions and statements including financial data, of or pertaining to entities, other than the District, and their activities contained in such Official Statement are concerned, such statements and data have been obtained from sources which the District believes to be reliable and the District has no reason to believe that they are untrue in any material respect; and (d) there has been no material adverse change in the financial condition of the District, since June 30, 2011, the date of the last financial statements of the District appearing in the Official Statement.

CONCLUDING STATEMENT

No person has been authorized to give any information or to make any representations other than those contained in this Official Statement, and if given or made, such other information or representations must not be relied upon as having been authorized by the District. This Official Statement does not constitute an offer to sell or solicitation of an offer to buy in any state in which such offer or solicitation is not authorized or in which the person making such offer or solicitation is not qualified to do so or to any person to whom it is unlawful to make such offer of solicitation.

The information set forth herein has been obtained from the District's records, audited financial statements and other sources which the District considers to be reliable. There is no guarantee that any of the assumptions or estimates contained herein will ever be realized. All of the summaries of the statutes, documents and the Order contained in this Official Statement are made subject to all of the provisions of such statutes, documents, and the Order. These summaries do not purport to be complete statements of such provisions and reference is made to such summarized documents for further information. Reference is made to official documents in all respects.

The Order authorizing the issuance of the Bonds will also approve the form and content of this Official Statement and any addenda, supplement or amendment thereto and authorize its further use in the re-offering of the Bonds by the Purchaser.

This Official Statement will be approved by the Board of Trustees of the District for distribution in accordance with the provisions of the United States Securities and Exchange Commission's rule codified at 17 C.F.R. Section 240.15c2-12, as amended.

President, Board of Trustees

ATTEST:

Secretary, Board of Trustees

APPENDIX A

FINANCIAL INFORMATION OF THE DISTRICT

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

Financial Information

ASSESSED VALUATION [(1)]

2011/12 Total Valuation……………………………………………………………………………………		$ 3,741,602,196
Less Exemptions & Deductions [(2)]:		
State Homestead Exemption	$ 65,608,040	
State Over-65 Exemption	8,946,090	
Disabled Homestead Exemption	997,200	
Local Over-65 Exemption	87,116,710	
Local 20% Homestead Exemption	153,981,210	
Veterans Exemption	316,720	
Pollution Control Exemption	89,770,213	
Productivity Loss	65,457,320	
Homestead Cap Loss	2,751,120	
	$ 474,944,623	
2011/12 Net Taxable Valuation …………………………………………………………………………		$ 3,266,657,573

(1) Source: Comptroller of Public Accounts - Property Tax Division.
(2) Excludes the values on which property taxes are frozen for persons 65 years of age or older and disabled taxpayers.

VOTED GENERAL OBLIGATION DEBT

Unlimited Tax Bonds Outstanding [(1)]		$ 108,558,771
Plus: The Unlimited Tax Qualified School Construction Bonds, Series 2012 [(2)] [(3)]		7,085,000
Plus: The Unlimited Tax School Building Bonds, Series 2012 [(1)] [(2)]		68,415,000
Total Unlimited Tax Bonds [(1)] [(2)]		184,058,771
Less: Interest & Sinking Fund Balance (As of June 30, 2011)		(4,491,194)
Net General Obligation Debt		$ 179,567,577
Ratio of Net G.O. Debt to Net Taxable Valuation [(4)]	5.50%	
2011 Population Estimate	13,888	
Per Capita Net Taxable Valuation	$235,214	
Per Capita Net G.O. Debt	$12,930	

(1) Excludes interest accreted on outstanding capital appreciation bonds.
(2) Preliminary, subject to change.
(3) Simultaneously with the issuance of its Unlimited Tax Qualified School Construction Bonds, Series 2012 (Direct-Pay Subsidy Bonds) (the "Bonds"), the District will issue its Unlimited Tax School Building Bonds, Series 2012 (the "Tax-Exempt Bonds") in the amount of $68,415,000 (preliminary, subject to change). This Official Statement, however, describes only the Bonds and not the Tax-Exempt Bonds. Investors interested in purchasing the Tax-Exempt Bonds should review the separate disclosure documents of the District relating thereto.
(4) See "CURRENT PUBLIC SCHOOL FINANCE SYSTEM" in the Official Statement and "DEBT SERVICE REQUIREMENTS" in this appendix and see the "Audited Financial Report Fiscal Year Ended June 30, 2011" in Appendix D for more information relative to the District's outstanding obligations.

PROPERTY TAX RATES AND COLLECTIONS

Fiscal Year	Net Taxable Valuation [(1)]	Tax Rate	% Collections [(2)] Current [(3)]	Total [(3)]
2006/07	$ 2,787,057,320	$ 1.6199 [(4)]	97.95%	99.47%
2007/08	2,900,935,170	1.3299 [(4)]	96.60%	98.72%
2008/09	3,249,747,280	1.3299	96.80%	97.71%
2009/10	2,874,386,720	1.3299	98.58%	101.32%
2010/11	2,793,938,060	1.3299	99.01%	100.38%
2011/12	3,266,657,573	1.3298	(In Process of Collection)	

(1) Source: Comptroller of Public Accounts - Property Tax Division.
(2) Source: Barbers Hill ISD Audited Financial Statements.
(3) Excludes penalties and interest.
(4) The declines in the District's Maintenance & Operation Tax for the 2006/07 and 2007/08 fiscal years are a function of House Bill 1 adopted by the Texas Legislature in May 2006. See "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS" and "CURRENT PUBLIC SCHOOL FINANCE SYSTEM" in the Official Statement.

TAX RATE DISTRIBUTION

	2007/08	2008/09	2009/10	2010/11	2011/12
Maintenance & Operations	$1.0400	$1.0601	$1.0601	$1.0601	$1.0600
Debt Service	$0.2899	$0.2698	$0.2698	$0.2698	$0.2698
Total Tax Rate	$1.3299	$1.3299	$1.3299	$1.3299	$1.3298

VALUATION AND FUNDED DEBT HISTORY

Fiscal Year	Net Taxable Valuation	Bond Debt Outstanding (1)	Ratio Debt to A.V. (2)
2006/07	$ 2,787,057,320	$ 110,508,771	3.97%
2007/08	2,900,935,170	108,093,771	3.73%
2008/09	3,249,747,280	105,838,771	3.26%
2009/10	2,874,386,720	102,593,771	3.57%
2010/11	2,793,938,060	108,558,771	3.89%
2011/12	3,266,657,573	180,358,771 (3)	5.52%

(1) At fiscal year end. Excludes interest accreted on outstanding capital appreciation bonds.
(2) See "CURRENT PUBLIC SCHOOL FINANCE SYSTEM" in the Official Statement, "DEBT SERVICE REQUIREMENTS" in this Appendix and see the "Audited Financial Report Fiscal Year Ended June 30, 2011" in Appendix D for more information.
(3) Includes the Bonds and the Tax-Exempt Bonds. Preliminary, subject to change.

ESTIMATED OVERLAPPING DEBT STATEMENT

Taxing Body	Amount	Percent Overlapping	Amount Overlapping
Chambers Co.	$ 6,005,000	49.75%	$ 2,987,488
Chambers Co ID #1	31,020,000	1.43%	443,586
City of Mont Belvieu	35,110,450	100.00%	35,110,450
Total Overlapping Debt (1)			$ 38,541,524
Barbers Hill Independent School District (2)			184,058,771
Total Direct & Overlapping Debt			$ 222,600,295
Ratio of Direct & Overlapping Debt to Net Taxable Valuation		6.81%	
Per Capita Direct & Overlapping Debt		$16,028	

(1) Equals gross debt less self-supporting debt.
(2) Includes the Bonds and the Tax-Exempt Bonds. Excludes interest accreted on outstanding capital appreciation bonds. Preliminary, subject to change.

Source: Municipal Advisory Council of Texas. The District has not independently verified the accuracy or completeness of such information (except for the amounts relating to the District), and no person should rely upon such information as being accurate or complete.

PRINCIPAL TAXPAYERS [1]

2011/12 Top Ten Taxpayers

Name of Taxpayer	Type of Business	Taxable Value	% of Net Valuation
Enterprise Prod. Operating LP	Natural Gas Plant/Storage	$ 605,348,532	18.53%
Exxon Mobil Corp.	Plastics Plant	313,487,342	9.60%
Equistar Chemicals LP	Petroleum	169,453,223	5.19%
ConocoPhillips Co.	Oil & Gas	103,166,725	3.16%
Marathon Petroleum LLC	Oil & Gas	88,303,867	2.70%
Chevron Phillips Chemical Co.	Chemicals	64,091,397	1.96%
Lyondell Chemical Co.	Chemicals	61,467,658	1.88%
Cedar Bayou Fractionators LP	Commercial	57,879,898	1.77%
Koch Supply & Trading LP	Petroleum Products	51,085,355	1.56%
LDH Energy Pipeline	Natural Gas Pipeline	49,363,729	1.51%
		$ 1,563,647,726	47.87%

2010/11 Top Ten Taxpayers

Name of Taxpayer	Type of Business	Taxable Value	% of Net Valuation
Enterprise Prod. Operating LP	Natural Gas Plant/Storage	$ 340,880,500	12.20%
Exxon Mobil Corp.	Plastics Plant	304,262,400	10.89%
Equistar Chemicals LP	Petroleum	203,820,480	7.30%
Chevron Phillips Chemical Co.	Chemicals	68,422,620	2.45%
ConocoPhillips Co.	Oil & Gas	68,359,550	2.45%
Dow Hydrocarbon & Resources	Natural Gas Plant/Storage	58,648,040	2.10%
LDH Energy Pipeline	Natural Gas Pipeline	48,780,220	1.75%
MTBV Caverns LLC	Natural Gas Plant/Storage	46,298,270	1.66%
Marathon Petroleum LLC	Oil & Gas	46,133,120	1.65%
Koch Supply & Trading LP	Petroleum Products	44,773,960	1.60%
		$ 1,230,379,160	44.04%

2009/10 Top Ten Taxpayers

Name of Taxpayer	Type of Business	Taxable Value	% of Net Valuation
Enterprise Prod. Operating LP	Natural Gas Plant/Storage	$ 392,201,540	13.64%
Exxon Mobil Corp.	Plastics Plant	290,465,130	10.11%
Chevron Phillips Chemical Co.	Chemicals	158,251,410	5.51%
Dow Hydrocarbon & Resources	Natural Gas Plant/Storage	103,204,920	3.59%
Equistar Chemicals LP	Petroleum	95,221,310	3.31%
ConocoPhillips Co.	Oil & Gas	65,293,110	2.27%
Mont Belvieu Storage Partners	Natural Gas Plant/Storage	55,358,620	1.93%
Valero Marketing & Supply	Petrochemical	47,953,640	1.67%
Total Petrochemicals USA Inc.	Petrochemical	47,933,720	1.67%
MTBV Caverns LLC	Natural Gas Plant/Storage	47,410,350	1.65%
		$ 1,303,293,750	45.34%

(1) Source: Comptroller of Public Accounts - Property Tax Division.

Note: As shown in the tables above, the top ten taxpayers in the District currently account for almost half of the District's tax base, with such property associated with the natural gas or other chemicals stored in the Barbers Hill Salt Dome formation that lies beneath the District or the industrial properties of the companies that operate chemical plants, pipelines and other infrastructure relating to petrochemical industry. Adverse developments in economic conditions, especially in the natural gas refining industry, could adversely impact the businesses that own properties in the District or that store chemicals in the salt domes, and the tax values in the District, resulting in less local tax revenue. If any major taxpayer were to default in the payment of taxes, the ability of the District to make timely payment of debt service on the Bonds will be dependent on its ability to enforce and liquidate its tax lien, which is a time-consuming process, or, perhaps, to sell tax anticipation notes until such amounts could be collected, if ever. See "REGISTERED OWNERS' REMEDIES" and AD VALOREM TAX PROCEDURES - District's Rights in the Event of Tax Delinquencies" in the Official Statement.

CLASSIFICATION OF ASSESSED VALUATION BY USE CATEGORY

Category		2011/12 (1)	% of Total		2010/11 (1)	% of Total		2009/10 (1)	% of Total
Real, Residential, Single-Family	$	886,544,120	23.69%	$	868,883,170	26.55%	$	812,789,930	24.66%
Real, Residential, Multi-Family		8,299,190	0.22%		2,173,040	0.07%		2,010,490	0.06%
Real, Vacant Lots/Tracts		28,137,140	0.75%		30,585,880	0.93%		33,608,210	1.02%
Real, Acreage		111,993,520	2.99%		132,274,400	4.04%		132,886,360	4.03%
Real, Farm & Ranch Improvements		11,535,110	0.31%		11,547,650	0.35%		13,127,210	0.40%
Real, Commercial & Industrial		1,343,067,097	35.90%		1,012,086,750	30.92%		1,095,238,100	33.24%
Oil & Gas		33,750,196	0.90%		50,823,960	1.55%		45,207,360	1.37%
Utilities		74,035,987	1.98%		68,254,790	2.09%		63,836,710	1.94%
Tangible Personal, Commercial		13,638,240	0.36%		13,252,340	0.40%		14,589,310	0.44%
Tangible Personal, Industrial		1,223,986,796	32.71%		1,072,304,930	32.76%		1,072,181,220	32.54%
Tangible Personal, Mobile Homes & Other		3,593,890	0.10%		3,690,550	0.11%		3,633,060	0.11%
Tangible Personal, Residential Inventory		2,104,860	0.06%		6,022,480	0.18%		5,126,740	0.16%
Tangible Personal, Special Inventory		916,050	0.02%		960,110	0.03%		1,131,440	0.03%
Other		-	0.00%		-	0.00%		-	0.00%
Total Appraised Value	$	3,741,602,196	100.00%	$	3,272,860,050	100.00%	$	3,295,366,140	100.00%
Less:									
Homestead Cap Adjustment	$	2,751,120		$	4,631,590		$	3,992,410	
Productivity Loss		65,457,320			80,833,210			78,682,140	
Exemptions		406,736,183			393,457,190			338,304,870	
Total Exemptions/Deductions (2)	$	474,944,623		$	478,921,990		$	420,979,420	
Net Taxable Assessed Valuation	$	3,266,657,573		$	2,793,938,060		$	2,874,386,720	

Category		2008/09 (1)	% of Total		2007/08 (1)	% of Total		2006/07 (1)	% of Total
Real, Residential, Single-Family	$	775,726,580	21.15%	$	653,666,240	19.92%	$	570,912,270	18.39%
Real, Residential, Multi-Family		2,679,560	0.07%		3,276,070	0.10%		3,927,560	0.13%
Real, Vacant Lots/Tracts		32,263,110	0.88%		32,264,270	0.98%		26,981,840	0.87%
Real, Acreage		140,460,620	3.83%		138,924,870	4.23%		81,159,100	2.61%
Real, Farm & Ranch Improvements		13,775,550	0.38%		12,806,820	0.39%		11,165,180	0.36%
Real, Commercial & Industrial		1,101,238,130	30.02%		1,011,098,750	30.81%		939,619,360	30.26%
Oil & Gas		72,202,300	1.97%		73,037,190	2.23%		71,719,200	2.31%
Utilities		63,309,870	1.73%		61,844,770	1.88%		56,544,330	1.82%
Tangible Personal, Commercial		14,550,290	0.40%		11,915,250	0.36%		11,701,440	0.38%
Tangible Personal, Industrial		1,437,002,180	39.18%		1,270,643,830	38.72%		1,321,558,000	42.57%
Tangible Personal, Mobile Homes & Other		4,018,470	0.11%		4,209,260	0.13%		4,254,880	0.14%
Tangible Personal, Residential Inventory		9,667,560	0.26%		6,788,990	0.21%		3,813,530	0.12%
Tangible Personal, Special Inventory		1,131,440	0.03%		1,191,440	0.04%		1,340,380	0.04%
Other		-	0.00%		-	0.00%		-	0.00%
Total Appraised Value	$	3,668,025,660	100.00%	$	3,281,667,750	100.00%	$	3,104,697,070	100.00%
Less:									
Homestead Cap Adjustment	$	13,297,720		$	9,147,910		$	4,821,150	
Productivity Loss		84,036,280			88,469,070			51,627,870	
Exemptions		320,944,380			283,115,600			261,190,730	
Total Exemptions/Deductions (2)	$	418,278,380		$	380,732,580		$	317,639,750	
Net Taxable Assessed Valuation	$	3,249,747,280		$	2,900,935,170		$	2,787,057,320	

(1) Source: Comptroller of Public Accounts - Property Tax Division.
(2) Excludes values on which property taxes are frozen for persons 65 years of age or older and disabled taxpayers.

PRINCIPAL REPAYMENT SCHEDULE [1]

	Principal Repayment Schedule					
		Plus:	Plus:			
			The		Bonds	Percent of
Fiscal Year	Outstanding		Tax-Exempt		Unpaid	Principal
Ending 8/31	Bonds [2]	The Bonds [3] [4]	Bonds [2] [3]	Total [2] [3]	At Year End	Retired
2012	$ 3,700,000.00	$ -	$ -	$ 3,700,000.00	$ 180,358,771.20	2.01%
2013	4,060,000.00	-	-	4,060,000.00	176,298,771.20	4.22%
2014	4,230,000.00	-	540,000.00	4,770,000.00	171,528,771.20	6.81%
2015	3,133,771.20	-	1,660,000.00	4,793,771.20	166,735,000.00	9.41%
2016	4,500,000.00	-	1,525,000.00	6,025,000.00	160,710,000.00	12.69%
2017	4,695,000.00	-	1,385,000.00	6,080,000.00	154,630,000.00	15.99%
2018	4,925,000.00	-	1,230,000.00	6,155,000.00	148,475,000.00	19.33%
2019	5,130,000.00	-	1,120,000.00	6,250,000.00	142,225,000.00	22.73%
2020	5,365,000.00	-	2,400,000.00	7,765,000.00	134,460,000.00	26.95%
2021	5,615,000.00	-	2,485,000.00	8,100,000.00	126,360,000.00	31.35%
2022	5,890,000.00	-	2,565,000.00	8,455,000.00	117,905,000.00	35.94%
2023	6,165,000.00	-	2,665,000.00	8,830,000.00	109,075,000.00	40.74%
2024	6,465,000.00	-	2,780,000.00	9,245,000.00	99,830,000.00	45.76%
2025	6,785,000.00	-	2,890,000.00	9,675,000.00	90,155,000.00	51.02%
2026	7,100,000.00	-	3,035,000.00	10,135,000.00	80,020,000.00	56.52%
2027	7,450,000.00	-	3,155,000.00	10,605,000.00	69,415,000.00	62.29%
2028	4,065,000.00	-	3,165,000.00	7,230,000.00	62,185,000.00	66.21%
2029	4,260,000.00	7,085,000.00	3,300,000.00	14,645,000.00	47,540,000.00	74.17%
2030	2,885,000.00		3,455,000.00	6,340,000.00	41,200,000.00	77.62%
2031	2,125,000.00		3,610,000.00	5,735,000.00	35,465,000.00	80.73%
2032	1,830,000.00		3,780,000.00	5,610,000.00	29,855,000.00	83.78%
2033	1,915,000.00		3,955,000.00	5,870,000.00	23,985,000.00	86.97%
2034	2,000,000.00		4,135,000.00	6,135,000.00	17,850,000.00	90.30%
2035	2,090,000.00		4,325,000.00	6,415,000.00	11,435,000.00	93.79%
2036	2,180,000.00		4,525,000.00	6,705,000.00	4,730,000.00	97.43%
2037			4,730,000.00	4,730,000.00	-	100.00%
Total	$ 108,558,771.20	$ 7,085,000.00	$ 68,415,000.00	$ 184,058,771.20		

(1) The Bonds are illustrated on the basis of the State's fiscal year end of August 31st, although the District's ends on June 30th.
(2) Excludes the accreted value of outstanding capital appreciation bonds.
(3) Preliminary, subject to change.
(4) The Order authorizing the Bonds obligates the District to make mandatory deposits into a Cumulative Sinking Fund Deposit Account on February 15 in the years and the amounts of each required mandatory deposit (which are to be off-set by interest earnings on amounts held in such fund so that no more than the amount required in the authorizing order shall ever be held in such account). All amounts held in the Cumulative Sinking Fund Deposit Account will be used to pay the Bonds on the maturity date of February15, 2029 or the date of prior redemption thereof.

DEBT SERVICE REQUIREMENTS [1]

Fiscal Year Ending 8/31	Outstanding Debt Service [2]	The Bonds [3] Cumulative Sinking Fund Deposits [4]	The Bonds [3] Interest	The Bonds [3] Total	The Tax-Exempt Bonds [2] [3] Principal	The Tax-Exempt Bonds [2] [3] Interest	The Tax-Exempt Bonds [2] [3] Total	Combined Total [2] [3] [5]
2012	$ 8,860,519.41	$ -	$ 169,252.78	$ 169,252.78	$ -	$ 1,367,201.53	$ 1,367,201.53	$ 10,396,973.72
2013	8,857,060.03	-	354,250.00	354,250.00	-	2,537,075.00	2,537,075.00	11,748,385.03
2014	8,857,416.28	-	354,250.00	354,250.00	540,000.00	2,531,675.00	3,071,675.00	12,283,341.28
2015	8,828,016.28	470,000.00	354,250.00	824,250.00	1,660,000.00	3,156,275.00	4,816,275.00	14,468,541.28
2016	8,779,328.78	470,000.00	354,250.00	824,250.00	1,525,000.00	3,336,275.00	4,861,275.00	14,464,853.78
2017	8,761,110.03	470,000.00	354,250.00	824,250.00	1,385,000.00	3,496,275.00	4,881,275.00	14,466,635.03
2018	8,779,157.53	470,000.00	354,250.00	824,250.00	1,230,000.00	3,636,275.00	4,866,275.00	14,469,682.53
2019	8,762,467.52	470,000.00	354,250.00	824,250.00	1,120,000.00	3,761,275.00	4,881,275.00	14,467,992.52
2020	8,752,436.26	470,000.00	354,250.00	824,250.00	2,400,000.00	2,490,275.00	4,890,275.00	14,466,961.26
2021	8,740,186.26	470,000.00	354,250.00	824,250.00	2,485,000.00	2,417,000.00	4,902,000.00	14,466,436.26
2022	8,738,242.51	470,000.00	354,250.00	824,250.00	2,565,000.00	2,341,250.00	4,906,250.00	14,468,742.51
2023	8,723,623.76	475,000.00	354,250.00	829,250.00	2,665,000.00	2,249,475.00	4,914,475.00	14,467,348.76
2024	8,719,492.51	475,000.00	354,250.00	829,250.00	2,780,000.00	2,140,575.00	4,920,575.00	14,469,317.51
2025	8,719,592.51	475,000.00	354,250.00	829,250.00	2,890,000.00	2,027,175.00	4,917,175.00	14,466,017.51
2026	8,696,195.01	475,000.00	354,250.00	829,250.00	3,035,000.00	1,908,675.00	4,943,675.00	14,469,120.01
2027	8,700,120.01	475,000.00	354,250.00	829,250.00	3,155,000.00	1,784,875.00	4,939,875.00	14,469,245.01
2028	5,044,222.51	475,000.00	354,250.00	829,250.00	3,165,000.00	1,658,475.00	4,823,475.00	10,696,947.51
2029	5,037,836.88	475,000.00	117,125.00	592,125.00	3,300,000.00	1,529,175.00	4,829,175.00	10,459,136.88
2030	3,491,235.00				3,455,000.00	1,385,437.50	4,840,437.50	8,331,672.50
2031	2,613,450.00				3,610,000.00	1,226,475.00	4,836,475.00	7,449,925.00
2032	2,228,597.50				3,780,000.00	1,060,200.00	4,840,200.00	7,068,797.50
2033	2,229,900.00				3,955,000.00	886,162.50	4,841,162.50	7,071,062.50
2034	2,229,312.50				4,135,000.00	704,137.50	4,839,137.50	7,068,450.00
2035	2,231,093.75				4,325,000.00	513,787.50	4,838,787.50	7,069,881.25
2036	2,227,687.50				4,525,000.00	314,662.50	4,839,662.50	7,067,350.00
2037					4,730,000.00	106,425.00	4,836,425.00	4,836,425.00
	$ 167,608,300.33	$ 7,085,000.00	$ 5,954,377.78	$ 13,039,377.78	$ 68,415,000.00	$ 50,566,564.03	$ 118,981,564.03	$ 299,629,242.14

(1) Debt service for the Bonds are illustrated on the basis of the State's fiscal year end of August 31st, although the District's ends on June 30th.
(2) Includes the accreted value of outstanding capital appreciation bonds.
(3) Preliminary, subject to change.
(4) The Order authorizing the Bonds obligates the District to make mandatory deposits into a Cumulative Sinking Fund Deposit Account on February 15 in the years and the amounts of each required mandatory deposit (which are to be off-set by interest earnings on amounts held in such fund so that no more than the amount required in the authorizing order shall ever be held in such account). All amounts held in the Cumulative Sinking Fund Deposit Account will be used to pay the Bonds on the maturity date of February 15, 2029 or the date of prior redemption thereof.
(5) Based on its wealth per student, the District does not expect to receive state financial assistance for the payment of debt service for the fiscal years 2011/12. The amount of state financial assistance for debt service, if any, may differ substantially each year depending on a variety of factors, including the amount, if any, appropriated for that purpose by the state legislature and a school district's wealth per student. See "CURRENT PUBLIC SCHOOL FINANCE SYSTEM" in the Official Statement.

TAX ADEQUACY WITH RESPECT TO THE DISTRICT'S BONDS

Projected Maximum Debt Service Requirement [1]	$ 14,469,682.53
Projected Maximum State Financial Assistance for Debt Service [2]	-
Projected Net Debt Service Requirement	$ 14,469,682.53
$0.44743 Tax Rate @ 99% Collections Produces	$ 14,469,845.92
2011/12 Certified Net Taxable Assessed Valuation	$ 3,266,657,573

(1) Includes the Bonds and the Tax-Exempt Bonds. Preliminary, subject to change.
(2) The amount of state financial assistance for debt service, if any, may differ substantially each year depending on a variety of factors, including the amount, if any, appropriated for that purpose by the state legislature and a school district's wealth per student. See "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - The School Finance System as Applied to the District."

AUTHORIZED BUT UNISSUED BONDS

Following the issuance of the Bonds and the Tax-Exempt Bonds, the District will not have authorized but unissued unlimited ad valorem tax bonds from any bond election, however, the District may incur other financial obligations payable from its collection of taxes and other sources of revenue, including maintenance tax notes payable from its collection of maintenance taxes, public property finance contractual obligations, delinquent tax notes, and leases for various purposes payable from State appropriations an surplus maintenance taxes. The District does not anticipate issuing additional tax-supported debt in the next twelve months.

COMPARATIVE STATEMENT OF GENERAL FUND REVENUES AND EXPENDITURES [1]

	Fiscal Year Ended June 30				
	2007	2008	2009 [2]	2010	2011
Beginning Fund Balance	**$ 7,252,247**	**$ 12,215,109**	**$ 18,234,068**	**$ 21,415,280**	**$ 25,642,034**
Revenues:					
Local and Intermediate Sources	$ 40,942,136	$ 34,166,634	$ 44,099,098	$ 33,592,437	$ 35,842,619
State Sources	5,705,017	14,567,986	12,433,749	18,944,135	10,050,542
Federal Sources & Other	34,883	(3,139)	4,408	-	197,864
Total Revenues	**$ 46,682,036**	**$ 48,731,481**	**$ 56,537,255**	**$ 52,536,572**	**$ 46,091,025**
Expenditures:					
Instruction	$ 15,540,479	$ 16,799,674	$ 19,579,756	$ 20,757,378	$ 22,848,075
Instructional Resources & Media Services	581,455	619,786	681,190	681,943	694,980
Curriculum & Instructional Staff Development	492,833	543,521	623,168	719,400	951,711
Instructional Leadership	147,273	152,030	180,919	207,879	221,996
School Leadership	1,596,790	1,832,323	1,990,138	2,113,012	2,351,491
Guidance, Counseling & Evaluation Services	838,853	960,430	949,572	1,027,608	1,042,994
Health Services	370,329	406,396	406,174	452,142	465,416
Student (Pupil) Transportation	1,223,163	1,433,670	1,351,444	1,421,307	1,660,743
Food Services	-	-	1,631,751	6,975	-
Cocurricular/Extracurricular Activities	1,076,829	1,160,556	1,375,247	1,730,050	1,631,450
General Administration	1,570,121	1,821,031	2,066,672	1,817,932	1,900,178
Plant Maintenance and Operations	4,281,829	5,268,049	12,883,545	6,691,512	6,267,992
Security and Monitoring Services	32,815	137,816	220,516	229,552	306,547
Data Processing Services	92,444	112,957	102,986	110,543	116,765
Community Services	7,847	14,558	30,426	62,835	70,406
Capital Outlay	-	-	-	3,172,337	-
Contracted Instructional Serivces Between Schools	13,885,315	11,518,380	14,361,125	7,066,446	4,391,255
Payments to Juvenile Justice Alt. Education Program	73,866	34,453	16,587	16,920	22,634
Other Intergovernmental Charges	-	-	-	317,801	366,221
Total Expenditures	**$ 41,812,241**	**$ 42,815,630**	**$ 58,451,216**	**$ 48,603,572**	**$ 45,310,854**
Excess (Deficiency) of Revenues					
over Expenditures	$ 4,869,795	$ 5,915,851	$ (1,913,961)	$ 3,933,000	$ 780,171
Other Resources and (Uses):					
Operating Transfers In	$ 93,067	$ 103,108	$ 108,923	$ 293,754	$ 494,158
Non-Current Loan Proceeds	-	-	5,000,000		
Opearting Transfers Out	-	-	(13,750)	-	-
Total Other Resources (Uses)	**$ 93,067**	**$ 103,108**	**$ 5,095,173**	**$ 293,754**	**$ 494,158**
Excess (Deficiency) of					
Revenues and Other Sources					
over Expenditures and Other Uses	$ 4,962,862	$ 6,018,959	$ 3,181,212	$ 4,226,754	$ 1,274,329
Ending Fund Balance	**$ 12,215,109**	**$ 18,234,068**	**$ 21,415,280**	**$ 25,642,034**	**$ 26,916,363**

(1) See "MANAGEMENT'S DISCUSSION AND ANALYSIS - Economic and Other Factors and Fiscal Year 2011-12 Budget" in Appendix D and "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - Effects of Wealth Transfer Provisions on the District's Financial Condition" in the Official Statement.
(2) The non-current loan proceeds of $5,000,000 in the 2008/09 fiscal year was a loan from the Federal Emergency Management Agency (FEMA) given on March 23, 2009 to assist the District in rebuilding after the Hurricane Ike natural disaster. The interest rate on the loan is 2.00%. Principal and interest on the loan is due on April 27, 2014.

CHANGE IN NET ASSETS [1]

	Fiscal Year Ended June 30				
	2007	2008	2009	2010	2011
Revenues:					
Program Revenues:					
Charges for Services	$ 1,352,136	$ 1,794,420	$ 9,965,465	$ 1,866,622	$ 1,799,951
Operating Grants and Contributions	2,766,876	2,706,811	5,871,735	4,405,055	5,092,074
General Revenues:					
Property Taxes Levied for General Purposes	38,810,692	32,633,458	33,558,846	30,906,658	29,995,894
Property Taxes Levied for Debt Service	7,088,250	8,992,938	8,531,266	7,867,339	7,509,562
State Aid - Formula Grants	5,886,615	-	-	-	-
Grants and Contributions Not Restricted	1,750	13,300,700	10,894,835	17,314,045	8,253,943
Investment Earnings	2,065,590	1,555,166	434,671	100,173	101,988
Miscellaneous	16,240	1,502,538	1,824,024	1,548,422	5,444,328
Total Revenue	$ 57,988,149	$ 62,486,031	$ 71,080,842	$ 64,008,314	$ 58,197,740
Expenses:					
Instruction	$ 18,290,568	$ 19,399,622	$ 21,744,656	$ 23,421,742	$ 27,203,086
Instruction Resources & Media Services	748,208	739,925	788,044	1,055,552	1,020,550
Curriculum & Staff Development	600,873	658,855	714,379	827,254	1,135,835
Instructional Leadership	161,180	165,389	192,460	207,474	222,050
School Leadership	1,746,952	1,997,673	2,116,762	2,108,937	2,352,255
Guidance, Counseling & Evaluation Services	956,620	1,173,497	1,194,001	1,033,216	1,043,594
Health Services	418,026	456,058	443,055	461,270	469,164
Student Transportation	1,384,351	1,620,257	1,500,742	1,666,242	1,744,351
Food Service	1,806,108	1,893,311	3,649,561	2,004,717	2,347,933
Cocurricular/Extracurricular Activities	1,280,407	1,275,254	1,480,475	2,118,303	2,067,988
General Administration	1,763,552	2,016,607	2,244,506	1,818,015	1,967,164
Plant Maintenance & Operations	4,952,816	5,561,474	16,246,376	7,809,251	6,437,865
Security and Monitoring Services	35,873	165,350	245,193	360,309	443,592
Data Processing Services	101,058	122,788	109,761	186,808	116,779
Community Services	7,847	14,558	30,426	62,835	70,406
Debt Service - Investment on Long-term Debt	4,517,154	4,798,627	4,903,235	4,832,615	4,901,870
Bond Issuance Costs and Fees	-	70,683	65,069	-	-
Capital Outlay	2,546,001	304,868	-	-	-
Current Debt Fees	-	-	-	65,430	73,833
Facilities Acquisition and Construction	-	-	-	1,339,629	3,358,019
Contracted Instructional Serivces Between Schools	13,885,315	11,518,380	14,361,125	7,066,446	4,391,255
Payments related to Shared Services	33,135	51,938	-	-	-
Payments to Juvenile Justice Alt. Education Program	73,866	34,453	16,587	16,920	22,634
Other Intergovernmental Charges	-	-	-	317,801	366,221
Total Expenditures	$ 55,309,910	$ 54,039,567	$ 72,046,413	$ 58,780,766	$ 61,756,444
Change in Net Assets	$ 2,678,239	$ 8,446,464	$ (965,571)	$ 5,227,548	$ (3,558,704)
Beginning Net Assets	$ 10,474,552	$ 13,152,791	$ 21,599,255	$ 20,633,684	$ 27,060,766
Prior Period Adjustment	$ -	$ -	$ -	$ 1,199,534	$ -
Ending Net Assets	$ 13,152,791	$ 21,599,255	$ 20,633,684	$ 27,060,766	$ 23,502,062

(1) The foregoing information represents government-wide financial information provided in accordance with GASB 34, which the District adopted for the 2002 fiscal year.

APPENDIX B

GENERAL INFORMATION REGARDING THE DISTRICT AND ITS ECONOMY

BARBERS HILL INDEPENDENT SCHOOL DISTRICT
General and Economic Information

Barbers Hill Independent School District (the "District") is a petroleum producing area that includes the City of Mont Belvieu, a retail center located 28 miles east of the downtown Houston business district on I-10. Salt domes within the District are used by oil companies as chemical storage facilities.

Chambers County was created in 1858 and is located in southeast Texas on Galveston Bay. The County's current estimated population is 28,356.

Source: Texas Municipal Report for Barbers Hill ISD and Chambers County.

Enrollment Statistics

Year Ending 8/31	Enrollment
2000	2,526
2001	2,681
2002	2,790
2003	2,943
2004	3,018
2005	3,255
2006	3,517
2007	3,549
2008	3,708
2009	3,901
2010	4,111
2011	4,205
Current	4,399

District Staff

Teachers	310
Auxiliary Personnel	154
Teachers' Aides & Secretaries	109
Administrators	29
Other	43
Total	645

Facilities

Campus	Grades	Present Enrollment	Capacity	Year Built	Year of Addition/ Renovation
Kindergarten Center	PK-K	430	660	1974	Multi, 2005
Primary School	1-2	662	735	1980	Multi, 2005
Elementary School	3-4	622	720	2006	2009
Intermediate School	5-6	728	705	1981	Multi, 2004
Middle School	7-8	675	765	1968	Multi, 2011
High School	9-12	1,282	1,980	2001	Multi, 2004

Principal Employers within the District

Name of Company	Type of Business	Number of Employees
Enterprise Products	Industrial	650
Barbers Hill ISD	Public Education	645
Chevron Cedar Bayou	Industrial	592
Exxon Mobil Chemicals	Industrial	200
City of Mont Belvieu/Eagle Pointe	Government	159
ConocoPhillips/Gulf Coast Fractionators	Industrial	28
Oneok	Industrial	25

Unemployment Rates

	October 2009	October 2010	October 2011
Chambers County	10.7%	8.9%	9.2%
State of Texas	8.1%	7.9%	8.0%

Source: Texas Workforce Commission

APPENDIX C

FORM OF LEGAL OPINION OF BOND COUNSEL

ANDREWS KURTH LLP
ATTORNEYS

600 Travis, Suite 4200
Houston, Texas 77002
713.220.4200 Phone
713.220.4285 Fax
andrewskurth.com

February 23, 2012

WE HAVE ACTED as Bond Counsel for the Barbers Hill Independent School District (the "District") in connection with an issue of bonds (the "Bonds") described as follows:

> BARBERS HILL INDEPENDENT SCHOOL DISTRICT UNLIMITED TAX QUALIFIED SCHOOL CONSTRUCTION BONDS, TAXABLE SERIES 2012Q (DIRECT-PAY SUBSIDY BONDS), dated February 1, 2012, in the aggregate principal amount of $7,085,000.
>
> The Bonds bear interest, are subject to redemption prior to maturity and may be transferred and exchanged as set out in the Bonds and in the order (the "Order") adopted by the Board of Trustees of the District (the "Board") authorizing their issuance.

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

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

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

WE CALL TO YOUR ATTENTION that interest on the Bonds is not excludable from gross income for federal income tax purposes under existing law, that the District has designated the Bonds as "qualified school construction bonds" under Section 54F of the Internal Revenue Code of 1986, as amended (the "Code"), and that the District has made an irrevocable election to treat the Bonds as "specified tax credit bonds" within the meaning of Section 6431(f)(3)(B) of the Code. The District has represented that it has complied with all requirements of the Code with respect to the qualification of the Bonds as qualified school construction bonds and election to treat such Bonds as specified tax credit bonds.

PURSUANT TO PROCEDURES prescribed by the Secretary of the Treasury, the ownership of the Bonds and the federal income tax credit attributable to such Bond may be separated, and in the event of a subsequent separation of the tax credit from the Bond in compliance with such procedures, the federal income tax credit shall be allowed to the person who on the credit allowance date holds the instrument evidencing the entitlement to the credit and not to the owner of the Bond. We express no opinion with respect to any separation of the federal tax credit attributable to the Bonds.

WE EXPRESS NO OPINION AS TO ANY FEDERAL, STATE OR LOCAL TAX CONSEQUENCES UNDER PRESENT LAW, OR FUTURE LEGISLATION, RESULTING FROM THE OWNERSHIP OF, RECEIPT OR ACCRUAL OF INTEREST ON, OR THE ACQUISITION OR DISPOSITION OF, THE BOND. OWNERSHIP OF THE BOND MAY RESULT IN COLLATERAL FEDERAL INCOME TAX CONSEQUENCES. INVESTORS SHOULD CONSULT THEIR OWN TAX ADVISORS REGARDING SUCH CONSEQUENCES BASED ON THEIR PARTICULAR CIRCUMSTANCE.

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

IRS CIRCULAR 230 DISCLOSURE:

TO ENSURE COMPLIANCE WITH REQUIREMENTS IMPOSED BY THE IRS, WE INFORM YOU THAT ANY U.S. FEDERAL TAX ADVICE CONTAINED IN THIS COMMUNICATION (INCLUDING ANY ATTACHMENTS) IS NOT INTENDED OR WRITTEN TO BE USED, AND CANNOT BE USED, FOR THE PURPOSE OF (I) AVOIDING PENALTIES UNDER THE INTERNAL REVENUE CODE OR (II) PROMOTING, MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY TRANSACTION OR TAX-RELATED MATTERS.

APPENDIX D

AUDITED FINANCIAL REPORT
FISCAL YEAR ENDED JUNE 30, 2011

BARBERS HILL
INDEPENDENT SCHOOL DISTRICT

ANNUAL FINANCIAL
&
COMPLIANCE REPORT

JUNE 30, 2011

Mont Belvieu, Texas

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

ANNUAL FINANCIAL REPORT
TABLE OF CONTENTS
FOR THE YEAR ENDED JUNE 30, 2011

CERTIFICATE OF BOARD

BARBERS HILL INDEPENDENT SCHOOL DISTRICT	CHAMBERS	036-902
Name of School	County	Co.-Dist Number

We, the undersigned, certify that the attached annual financial reports of the above named school district were reviewed and

[✓] APPROVED --- [ ] DISAPPROVED
(Check One)

for the year ended June 30, 2011 at a meeting of the Board of Trustees of such school district on the 24th day of October, 2011.

SIGNATURE OF BOARD SECRETARY

Carmena Goss
SIGNATURE OF BOARD PRESIDENT

If the Board of Trustees disapproved the auditor's report, the reason(s) for disapproving it is/are (attach list as necessary):

FINANCIAL SECTION

HLS&K

Hereford, Lynch, Sellars & Kirkham

Certified Public Accountants • A Professional Corporation

Members of the
American Institute of Certified Public Accountants
Texas Society of Certified Public Accounts
Private Companies Practice Section
of the AICPA Division for Firms

1406 Wilson Road
Conroe, Texas 77304
(936) 756-8127
Fax (936) 756-8132

111 E. Boothe
Cleveland, Texas 77327
(281) 592-6443
Fax (281) 592-7706

INDEPENDENT AUDITORS' REPORT

Board of Trustees
Barbers Hill Independent School District
P.O. Box 1108
Mont Belvieu, Texas 77580

Members of the Board of Trustees:

We have audited the accompanying financial statements of the governmental activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the Barbers Hill Independent School District (District), as of and for the year ended June 30, 2011, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the District, as of June 30, 2011, and the respective changes in financial position, thereof and the respective budgetary comparison for the General Fund for the year then ended and six months ended for the component unit in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 17, 2011, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, as listed in the table of contents, 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's financial statements as a whole. The other supplementary information is presented for purposes of additional analysis and is not a required part of the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the financial statements. The other supplementary information and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information, excluding the Fund Balance and Cash Flow Calculation Worksheet (Exhibit J-2), has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information, excluding the Fund Balance and Cash Flow Calculation Worksheet (Exhibit J-2), is fairly stated in all material respects in relation to the financial statements as a whole. The Fund Balance and Cash Flow Calculation Worksheet (Exhibit J-2), as listed in the table of contents, has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Respectfully submitted,

Hereford, Lynch, Sellars & Kirkham, P.C.

HEREFORD, LYNCH, SELLARS & KIRKHAM, P.C.
Certified Public Accountants

Conroe, Texas
October 17, 2011

Management's Discussion and Analysis

As management of the Barbers Hill Independent School District ("the District"), we offer readers of the accompanying report this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2011. In reviewing this report, readers should be mindful that it is often necessary for management to make and use estimates in the preparation of financial statements. Examples of the use of such estimates may be found in amounts reported for depreciation, net taxes receivable and claims payable of the District's self-insured workers' compensation program.

Financial Highlights

- Assets exceeded liabilities at year-end by $23,502,062 (net assets). Of this amount, $19,022,820 (unrestricted net assets) is available to meet the District's ongoing obligations in subsequent years.
- The District's total net assets decreased by $3,558,704 primarily because Disaster Aid Assistance was received in 2009-10 for Hurricane Ike relief and not in the current year.
- At the end of the year, unassigned fund balance in the general fund was $12,019,545 while total fund balance in the general fund was $26,916,363, an increase of $1.2 million.

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 comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the basic financial statements. This report also contains other supplementary information in addition to the basic financial statements.

Government-wide financial statements. The *government-wide financial statements* are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector enterprise.

The *Statement of Net Assets* (Exhibit A-1) presents information on all of the District's assets and liabilities, with the difference between the two reported as *net assets.* Over time, increases or decreases in net assets may serve as an indicator of how the financial position of the District is changing.

The *Statement of Activities* (Exhibit B-1) presents information showing how the District's net assets changed during the year. Changes in net assets are reported upon occurrence of the underlying event giving rise to the change, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some transactions that will not result in cash flows until future fiscal periods (e.g., uncollected taxes and incurred but unpaid workers' compensation benefits).

The government-wide financial operations (*governmental activities*) of the District are principally supported by taxes and intergovernmental revenues. The governmental activities of the District include *Instruction, Instructional Resources and Media Services, Curriculum and Staff Development, Instructional Leadership, School Leadership, Guidance, Counseling, and Evaluation Services, Health Services, Student Transportation, Food Service, Cocurricular/Extracurricular Activities, General Administration, Plant Maintenance and Operations, Security and Monitoring Services, Data Processing Services, Community Services, Interest on Long-term Debt, Current Debt Fees, Facilities Repair and Maintenance, Contracted Instructional Services between Public Schools, Payments to Juvenile Justice Alternative Education Programs, and Other Intergovernmental Charges.*

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 District, as do other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the District can be divided into two categories: governmental funds and fiduciary funds.

Governmental funds. *Governmental funds* are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of cash resources, as well as on *balances of cash resources* available at the end of the fiscal year. Such information may be useful in evaluating near-term financing requirements.

Because the focus of governmental funds financial statements 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 effect of the District'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 District maintained eighteen individual governmental funds during the year. 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, debt service fund, and capital projects fund, which are considered to be major funds. Data from the other fifteen governmental funds are combined into a single, aggregated presentation titled *other governmental funds.*

The District adopts an annual revenue and appropriations budget for its general fund. Subsequent to adoption, amendments approved by the governing body are reflected in a revised budget. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

The basic governmental fund financial statements are noted in the table of contents of this report.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of students and student organizations. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the District's own programs and activities. A statement of fiduciary assets and liabilities is the only financial statement presented for fiduciary funds, as noted in the table of contents of this report.

Notes to the basic 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 basic financial statements are noted in the table of contents of this report.

Other information. In addition to the basic financial statements and accompanying notes, this report presents other supplementary information, including schedules required by the Texas Education Agency. Other supplementary information is noted in the table of contents of this report.

Government-wide Financial Analysis

As mentioned earlier, net assets may, over time, serve as an indicator of a District's changing financial position. At the close of the District's most recent fiscal year, assets exceeded liabilities by $23,502,062.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT'S NET ASSETS

	Governmental Activities					
	2011		2010		Increase (Decrease)	
	Amount	%	Amount	%	Amount	%
Current and Other Assets	$ 44,365,103	30	$ 42,316,987	29	$ 2,048,116	1
Capital Assets, net of Depreciation	103,439,066	70	101,154,067	71	2,284,999	1
Total Assets	**147,804,169**	**100**	**143,471,054**	**100**	**4,333,115**	
Noncurrent Liabilities Outstanding	115,650,701	93	109,311,841	94	6,338,860	1
Other Liabilities	8,651,406	7	7,098,447	6	1,552,959	1
Total Liabilities	**124,302,107**	**100**	**116,410,288**	**100**	**7,891,819**	
Net Assets:						
Invested in Capital Assets, net of Related Debt	2,613,218	11	2,151,810	8	461,408	1
Restricted	1,866,024	8	2,653,715	10	(787,691)	1
Unrestricted	19,022,820	81	22,255,241	82	(3,232,421)	1
Total Net Assets	**$ 23,502,062**	**100**	**$ 27,060,766**	**100**	**$ (3,558,704)**	

The largest portion of the District's net assets is unrestricted. Investment in capital assets (e.g., capitalized bond and debt issuance cost, land, buildings and improvements, furniture and equipment and construction in progress), less any related debt used to acquire those assets that are still outstanding represent 11 percent of the District's net assets. The District uses these capital assets to provide services to students; consequently, these assets are *not* available for future spending. 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. Net assets ($1,866,024 or 8 percent of net assets) are restricted for debt service. The remaining balance of net assets, *unrestricted net assets* ($19,022,820), may be used to meet future obligations to students and creditors.

Governmental activities. Governmental activities decreased the District's net assets by $3,558,704. The elements giving rise to this change may be determined from the table below.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT'S CHANGES IN NET ASSETS

	Governmental Activities					
	2011		2010		Increase (Decrease)	
	Amount	%	Amount	%	Amount	%
Revenue:						
Program Revenues:						
Charges for Services	$ 1,799,951	3	$ 1,866,622	3	$ (66,671)	(28)
Operating Grants and Contributions	5,092,074	9	4,405,055	7	687,019	6.412
General Revenues:						
Property Taxes, Levied for General Purpose	29,995,894	52	30,906,658	48	(910,764)	(33.9)
Property Taxes, Levied for Debt Service	7,509,562	13	7,867,339	12	(357,777)	(22)
Grants and Contributions Not Restricted to Specific Programs	8,253,943	14	17,314,045	27	(9,060,102)	(1.91)
Investment Earnings	101,988	-	100,173	-	1,815	55.19
Miscellaneous	5,444,328	9	1,548,422	3	3,895,906	0.397
Total Revenues	**58,197,740**	**100**	**64,008,314**	**100**	**(5,810,574)**	
Expenses:						
Instruction	27,203,086	44	23,421,742	40	3,781,344	6.194
Instructional Resources and Media Services	1,020,550	2	1,055,552	2	(35,002)	(30.2)
Curriculum and Staff Development	1,135,835	2	827,254	1	308,581	2.681
Instructional Leadership	222,050	-	207,474	-	14,576	14.23
School Leadership	2,352,255	4	2,108,937	4	243,318	8.667
Guidance, Counseling, & Evaluation Services	1,043,594	2	1,033,216	2	10,378	99.56
Health Services	469,164	1	461,270	1	7,894	58.43
Student Transportation	1,744,351	3	1,666,242	3	78,109	21.33
Food Service	2,347,933	4	2,004,717	3	343,216	5.841
Cocurricular/Extracurricular Activities	2,067,988	3	2,118,303	4	(50,315)	(42.1)
General Administration	1,967,164	3	1,818,015	3	149,149	12.19
Plant Maintenance and Operations	6,437,865	10	7,809,251	13	(1,371,386)	(5.69)
Security and Monitoring Services	443,592	1	360,309	1	83,283	4.326
Data Processing Services	116,779	-	186,808	-	(70,029)	(2.67)
Community Services	70,406	-	62,835	-	7,571	8.299
Interest on Long-term Debt	4,901,870	8	4,832,615	8	69,255	69.78
Current Debt Fees	73,833	-	65,430	-	8,403	7.787
Facilities Repair and Maintenance	3,358,019	5	1,339,629	2	2,018,390	0.664
Contracted Instructional Services		-		-		
betw een Public Schools	4,391,255	7	7,066,446	12	(2,675,191)	(2.64)
Payments to Juvenile Justice Alternative		-		-		
Ed. Programs	22,634	-	16,920	-	5,714	2.961
Other Intergovernmental Charges	366,221	1	317,801	1	48,420	6.563
Total Expenses	**61,756,444**	**100**	**58,780,766**	**100**	**2,975,678**	
Change in Net Assets	(3,558,704)		5,227,548		(8,786,252)	
Prior Period Adjustment	-		1,199,534		(1,199,534)	
Net Assets - Beginning	27,060,766		20,633,684		6,427,082	
Net Assets - Ending	**$ 23,502,062**		**$ 27,060,766**		**$ (3,558,704)**	

The decrease in net assets was primarily the result of a decrease in grants and contributions not restricted to specific programs resulting from Disaster Aid Assistance having been received in 2009-10 and not in 2010-11.

Revenues, aggregating $58,197,740, were generated primarily from two sources. Property taxes totaling $37,505,456 represent 65 percent of total revenues while grants and contributions (including those not restricted for program-specific use as well as for general operations, totaling $13,346,017), represent 23 percent of total revenues. The remaining 12 percent is generated from investment earnings, charges for services, and miscellaneous revenues.

The primary functional expense of the District is *Instruction* $27,203,086, which represents 44 percent of total expenses. *Plant Maintenance and Operations* $6,437,865 represents 10 percent of total expenses, while all remaining expense categories are individually less than 8 percent of total expenses.

Financial Analysis of the Government's Funds

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

Governmental funds. At the end of the fiscal year, the District's governmental funds had combined ending fund balances of $34,426,162, an increase of $613,250 from the preceding year. Comments as to each major individual fund's change in fund balance follow.

The general fund is the primary operating fund of the District. At year-end, unassigned fund balance of the general fund was $12,019,545, while total fund balance was $26,916,363. To evaluate the general fund's liquidity, it may be helpful to compare both unassigned fund balance and total fund balance to total fund expenditures. Unassigned fund balance represents 27 percent of total general fund expenditures, while total fund balance represents 59 percent of that same total.

The fund balance of the general fund increased $1,274,329 during the year, primarily because an increase in local and intermediate revenues, a decrease in plant maintenance and operations, capital outlay, and contracted instructional services between public schools expenditures was offset by a reduction in state program revenues.

The debt service fund ended the year with a total fund balance of $4,491,194, all of which is reserved for the payment of principal and interest on debt. The debt service fund balance decreased by $646,313 during the year due to the increased debt requirements exceeded the increase in property tax revenue.

The capital projects fund ended the year with a total fund balance of $2,829,953, all of which is reserved for capital acquisition program and contractual obligations. The capital projects fund balance increased by $172,629 during the year representing new bond funds exceeded current year expenditures.

Governmental funds financial statements may be found by referring to the table of contents.

General Fund Budgetary Highlights

The significant differences between the originally-adopted budget and the final amended budget of the general fund were primarily from an increase in federal and local revenues of $1.3 million, an increase in expenditures for plant maintenance and operations and contracted instructional services between public schools of $1.9 million. Net change in budgeted fund balance was projected to decrease fund balance approximately $1.9 million. There were no significant variations between the final budget appropriations and actual expenditures. Amendments were approved by the governing body.

Capital Asset and Debt Administration

Capital assets. The District's investment in capital assets for its governmental activities as of June 30, 2011 was $103,439,066 (net of accumulated depreciation). This investment in capital assets includes land, buildings and improvements, furniture and equipment, and construction in progress. The increase in net investment in capital assets for the current fiscal year was $2,284,999.

Major capital asset activity during the year included the following:

- $1,678,042 Multiple Campus Renovations
- $2,093,360 Middle School Science Wing
- $691,556 District Wide Energy Project
- $265,270 two buses and three vehicles

BARBERS HILL INDEPENDENT SCHOOL DISTRICT'S CAPITAL ASSETS

	Governmental Activities								
	2011			2010			Increase (Decrease)		
		Amount	%		Amount	%		Amount	%
Revenue:									
Land	$	4,756,459	5	$	4,549,638	4	$	206,821	22
Buildings and Improvements		88,653,069	85		90,538,361	90		(1,885,292)	(48)
Furniture and Equipment		5,874,156	6		6,066,068	6		(191,912)	(32)
Construction in Progress		4,155,382	4		-	-		4,155,382	-
Totals	$	**103,439,066**	**100**	$	**101,154,067**	**100**	$	**2,284,999**	

Additional information on the District's capital assets can be found in Note C in the notes to the financial statements as noted in the table of contents of this report.

Noncurrent Liabilities. At the end of the current fiscal year, the District had total liabilities outstanding of $115,650,701. Of this amount, $110,061,585 comprises debt backed by the full faith and credit of the District, $280,840 is an outstanding liability for workers' compensation claims, $308,276 is an outstanding liability for compensated absences, and a $5,000,000 note payable to Federal Emergency Management Agency.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT'S NONCURRENT LIABILITIES

	Governmental Activities					
	2011		2010		Increase (Decrease)	
	Amount	%	Amount	%	Amount	%
Revenue:						
General Obligation Bonds (Net)	$ 110,061,585	96	$ 103,762,216	95	$ 6,299,369	100
Note Payable	5,000,000	4	5,000,000	5	-	-
Workers' Compensation	280,840	-	249,934	-	30,906	-
Compensated Absences	308,276	-	299,691	-	8,585	-
Totals	**$ 115,650,701**	**100**	**$ 109,311,841**	**100**	**$ 6,338,860**	

The District's total bonded debt increased by $6,299,369. The key factor was scheduled debt payments.

The District is rated "AAA" by Standard and Poor's and "Aaa" by Moody's for the general obligation debt, both ratings reflecting the guarantee of the State of Texas Permanent School Fund.

State statutes do not limit the tax rate or amount of local tax support of school districts' bonded indebtedness. However, approval of the Attorney General of the State of Texas is required prior to the sale of bonds.

Additional information on the District's long-term debt can be found in Note E in the notes to the financial statements as noted in the table of contents of this report.

Economic and Other Factors and Fiscal Year 2011-12 Budgets

- School year (2011-12) student enrollment is, 4,389, a 4% increase from the preceding year.
- District staff totals 641 employees in 2011-12, excluding substitutes and other part-time employees, which is ten fewer than 2010-11.
- Property values of the District increased by 17% for the 2011-12 year.
- A maintenance and operations tax rate of $1.06 and a debt service tax rate of $.2698, a total rate of $1.3298 was adopted for 2011-12.
- The total cost of pay raises for all employees is $1.1 million and health insurance increased by 9.5% over the previous year.

All of these factors and others were considered in preparing the District's budget for the 2011-12 fiscal year.

During the current fiscal year, unassigned (previously unreserved) fund balance in the general fund increased to $12,019,545. The District plans to utilize unassigned fund balance to fund current period expenditures prior to collecting the current year tax levy.

Requests for Information

This financial report is intended to provide a general overview of the District's finances for those with an interest in this information. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Assistant Superintendent of Finance, Barbers Hill Independent School District, P.O. Box 1108, Mont Belvieu, Texas 77580.

BASIC FINANCIAL STATEMENTS

BARBERS HILL INDEPENDENT SCHOOL DISTRICT **EXHIBIT A-1**

STATEMENT OF NET ASSETS

JUNE 30, 2011

Data Control Codes		1 Governmental Activities	Component Unit Barbers Hill ISD Educ. Foundation
	ASSETS:		
1110	*Cash and Cash Equivalents*	$ 15,112,152	$ 10,543
1120	*Current Investments*	14,350,716	285,823
1225	*Property Taxes Receivable, Net*	2,028,860	-
1240	*Due from Other Governments*	10,763,169	-
1267	*Due From Fiduciary*	13,186	-
1290	*Other Receivables*	15,123	-
1300	*Inventories*	212,114	-
1410	*Prepaid Items*	684,704	-
1420	*Capitalized Bond and Other Debt Issuance Costs*	1,185,079	-
	Capital Assets:		
1510	*Land*	4,756,459	-
1520	*Buildings and Improvements, Net*	88,653,069	-
1530	*Furniture and Equipment, Net*	5,874,156	-
1580	*Construction in Progress*	4,155,382	-
1000	Total Assets	147,804,169	296,366
	LIABILITIES:		
2110	*Accounts Payable*	2,770,150	-
2140	*Interest Payable*	1,973,034	-
2165	*Accrued Liabilities*	3,072,409	-
2180	*Due to Other Governments*	835,548	-
2300	*Unearned Revenue*	265	-
	Noncurrent Liabilities:		
2501	*Due Within One Year*	4,289,116	-
2502	*Due in More Than One Year*	111,361,585	-
2000	Total Liabilities	124,302,107	-
	NET ASSETS		
3200	*Invested in Capital Assets, Net of Related Debt*	2,613,218	-
3850	*Restricted For Debt Service*	1,866,024	-
3900	*Unrestricted Net Assets*	19,022,820	296,366
3000	Total Net Assets	$ 23,502,062	$ 296,366

The accompanying notes are an integral part of this statement.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT **EXHIBIT B-1**

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2011

Data Control Codes	Functions/Programs	1 Expenses	3 Program Revenues Charges for Services	4 Program Revenues Operating Grants and Contributions	Net (Expense) Revenue and Changes in Net Assets Governmental Activities	Component Unit Barbers Hill ISD Education Foundation
	Governmental Activities:					
11	*Instruction*	$ 27,203,086	$ 14,050	$ 3,495,687	$ (23,693,349)	-
12	*Instructional Resources and Media Services*	1,020,550	-	37,291	(983,259)	-
13	*Curriculum and Staff Development*	1,135,835	-	278,537	(857,298)	-
21	*Instructional Leadership*	222,050	-	11,637	(210,413)	-
23	*School Leadership*	2,352,255	-	121,331	(2,230,924)	-
31	*Guidance, Counseling, & Evaluation Services*	1,043,594	-	50,689	(992,905)	-
33	*Health Services*	469,164	-	20,741	(448,423)	-
34	*Student Transportation*	1,744,351	-	62,981	(1,681,370)	-
35	*Food Service*	2,347,933	1,597,684	525,445	(224,804)	-
36	*Cocurricular/Extracurricular Activities*	2,067,988	83,487	75,385	(1,909,116)	-
41	*General Administration*	1,967,164	-	66,459	(1,900,705)	-
51	*Plant Maintenance and Operations*	6,437,865	104,730	319,825	(6,013,310)	-
52	*Security and Monitoring Services*	443,592	-	18,192	(425,400)	-
53	*Data Processing Services*	116,779	-	3,531	(113,248)	-
61	*Community Services*	70,406	-	-	(70,406)	-
72	*Interest on Long-term Debt*	4,901,870	-	-	(4,901,870)	-
73	*Current Debt Fees*	73,833	-	-	(73,833)	-
81	*Facilities Repair and Maintenance*	3,358,019	-	-	(3,358,019)	-
91	*Contracted Instructional Services between Public Schools*	4,391,255			(4,391,255)	-
95	*Payments to Juvenile Justice Alternative Ed. Programs*	22,634	-	4,343	(18,291)	-
99	*Other Intergovernmental Charges*	366,221	-	-	(366,221)	-
TG	Total Governmental Activities	61,756,444	1,799,951	5,092,074	(54,864,419)	
TP	Total Primary Government	$ 61,756,444	$ 1,799,951	$ 5,092,074	(54,864,419)	
1C	Barbers Hill ISD Education Foundation	$ 120	$ -	$ -		$ (120)
	General Revenues:					
MT	*Property Taxes, Levied for General Purposes*				29,995,894	-
DT	*Property Taxes, Levied for Debt Service*				7,509,562	-
IE	*Investment Earnings*				101,988	-
GC	*Grants and Contributions Not Restricted to Specific Programs*				8,253,943	158,584
MI	*Miscellaneous*				5,444,328	-
TR	Total General Revenues				51,305,715	158,584
CN	Change in Net Assets				(3,558,704)	158,464
NB	Net Assets - Beginning				27,060,766	137,902
NE	Net Assets - Ending				$ 23,502,062	$ 296,366

The accompanying notes are an integral part of this statement.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT
BALANCE SHEET - GOVERNMENTAL FUNDS
JUNE 30, 2011

Data Control Codes		199 General Fund	599 Debt Service Fund
	ASSETS:		
1110	*Cash and Cash Equivalents*	$ 9,688,145	$ 619,411
1120	*Current Investments*	9,653,081	3,928,951
1225	*Property Taxes Receivable, Net*	1,679,164	349,696
1240	*Due from Other Governments*	10,154,271	-
1260	*Due from Other Funds*	364,757	-
1290	*Other Receivables*	15,123	-
1310	*Inventories*	212,114	-
1410	*Prepaid Items*	684,704	-
1000	Total Assets	$ 32,451,359	$ 4,898,058
	LIABILITIES:		
	Current Liabilities:		
2110	*Accounts Payable*	$ 208,492	$ -
2140	*Interest Payable*	-	46,630
2160	*Accrued Wages Payable*	2,567,891	-
2170	*Due to Other Funds*	506	-
2180	*Due to Other Governments*	835,548	-
2200	*Accrued Expenditures*	243,130	10,538
2300	*Unearned Revenue*	1,679,429	349,696
2000	Total Liabilities	5,534,996	406,864
	FUND BALANCES:		
3410	*Nonspendable Inventories*	212,114	-
3430	*Nonspendable Prepaid Items*	684,704	-
3450	*Restricted for Federal/State funds grant restrictions*	-	-
3470	*Restricted for Capital Acquisition Program and Contractual Obligations*	-	-
3480	*Restricted for Retirement of Long-term Debt*	-	4,491,194
3510	*Committed Fund Balance - Construction*	4,000,000	-
3520	*Committed Fund Balance - Claims and Judgements*	2,000,000	-
3530	*Committed Fund Balance - Capital Expenditures for Equipment*	3,820,350	-
3545	*Other Committed Fund Balance*	4,179,650	-
3600	*Unassigned Fund Balance*	12,019,545	-
3000	Total Fund Balances	26,916,363	4,491,194
4000	Total Liabilities and Fund Balances	$ 32,451,359	$ 4,898,058

The accompanying notes are an integral part of this statement.

699 Capital Projects Fund	Other Governmental Funds	98 Total Governmental Funds
$ 4,459,950	$ 344,646	$ 15,112,152
768,684	-	14,350,716
-	-	2,028,860
-	608,898	10,763,169
-	506	365,263
-	-	15,123
-	-	212,114
-	-	684,704
$ 5,228,634	$ 954,050	$ 43,532,101
$ 2,398,681	$ 162,977	$ 2,770,150
-	-	46,630
-	230,750	2,798,641
-	351,571	352,077
-	-	835,548
-	20,100	273,768
-	-	2,029,125
2,398,681	765,398	9,105,939
-	-	212,114
-	-	684,704
-	81	81
2,829,953	-	2,829,953
-	-	4,491,194
-	-	4,000,000
-	-	2,000,000
-	-	3,820,350
-	188,571	4,368,221
-	-	12,019,545
2,829,953	188,652	34,426,162
$ 5,228,634	$ 954,050	$ 43,532,101

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BARBERS HILL INDEPENDENT SCHOOL DISTRICT

EXHIBIT C-1R

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS
JUNE 30, 2011

Total Fund Balances - Governmental Funds (Exhibit C-1)		$ 34,426,162
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets used in governmental activities are not financial resources and, therefore, are not reported as assets in governmental funds. The governmental capital assets at year-end consist of:		
Governmental Capital Assets Costs	$ 146,897,091	
Accumulated Depreciation of Governmental Capital Assets	(43,458,025)	103,439,066
Property taxes receivable, which will be collected subsequent to year-end, but are not available soon enough to pay expenditures and, therefore, are deferred in the funds.		2,028,860
Issuance cost related to debt is not a financial resource and, therefore, is not reported in the funds. Issuance cost is amortized over the life of the debt.		1,185,079
Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported as liabilities in the funds. Liabilities at year-end related to bonds payable, consist of:		
Bonds Payable, at Original Par	$ (108,558,771)	
Premium on Bonds Payable	(2,420,463)	
Discount on Bonds Payable	168,072	
Accreted Interest	(1,261,065)	
Defeasance Costs	2,010,642	
Accrued Interest on the Bonds	(1,713,801)	
Notes Payable	(5,000,000)	
Accrued Interest on Notes Payable	(212,603)	
Compensated Absences	(308,276)	
Workers' Compensation	(280,840)	
		(117,577,105)
Total Net Assets - Governmental Activities (Exhibit A-1)		$ 23,502,062

The accompanying notes are an integral part of this statement.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
IN FUND BALANCES - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2011

Data Control Codes		199 General Fund	599 Debt Service Fund
	REVENUES:		
5700	*Local and Intermediate Revenue*	$ 35,842,619	$ 7,542,548
5800	*State Program Revenues*	10,050,542	-
5900	*Federal Program Revenues*	197,864	-
5020	Total Revenues	46,091,025	7,542,548
	EXPENDITURES:		
	Current:		
0011	*Instruction*	22,848,075	-
0012	*Instructional Resources and Media Services*	694,980	-
0013	*Curriculum and Staff Development*	951,711	-
0021	*Instructional Leadership*	221,996	-
0023	*School Leadership*	2,351,491	-
0031	*Guidance, Counseling, and Evaluation Services*	1,042,994	-
0033	*Health Services*	465,416	-
0034	*Student Transportation*	1,660,743	-
0035	*Food Service*	-	-
0036	*Cocurricular/Extracurricular Activities*	1,631,450	-
0041	*General Administration*	1,900,178	-
0051	*Plant Maintenance and Operations*	6,267,992	-
0052	*Security and Monitoring Services*	306,547	-
0053	*Data Processing Services*	116,765	-
0061	*Community Services*	70,406	-
0071	*Principal on Long-term Debt*	-	3,535,000
0072	*Interest on Long-term Debt*	-	4,639,260
0073	*Bond Issuance Costs and Fees*	-	14,601
0081	*Capital Outlay*	-	-
0091	*Contracted Instructional Services between Public Schools*	4,391,255	-
0095	*Payments to Juvenile Justice Alternative Education Programs*	22,634	-
0099	*Other Intergovernmental Charges*	366,221	-
6030	Total Expenditures	45,310,854	8,188,861
1100	Excess (Deficiency) of Revenues Over (Under)		
1100	Expenditures	780,171	(646,313)
	Other Financing Sources and (Uses):		
7911	*Issuance of Bonds*	-	-
7915	*Transfers In*	494,158	-
7916	*Premium or Discount on Issuance of Bonds*	-	-
8911	*Transfers Out*	-	-
7080	Total Other Financing Sources and (Uses)	494,158	-
1200	Net Change in Fund Balances	1,274,329	(646,313)
0100	Fund Balances - Beginning	25,642,034	5,137,507
3000	Fund Balances - Ending	$ 26,916,363	$ 4,491,194

The accompanying notes are an integral part of this statement.

699 Capital Projects Fund	Other Governmental Funds	98 Total Governmental Funds
$ 5,768	$ 1,597,684	$ 44,988,619
-	210,367	10,260,909
-	2,887,244	3,085,108
5,768	4,695,295	58,334,636
468,737	2,205,806	25,522,618
74,232	-	769,212
-	247,589	1,199,300
-	-	221,996
-	-	2,351,491
-	58	1,043,052
8,000	-	473,416
90,880	-	1,751,623
379,229	1,935,079	2,314,308
25,000	-	1,656,450
36,867	-	1,937,045
123,727	-	6,391,719
40,000	-	346,547
-	-	116,765
-	-	70,406
-	-	3,535,000
-	-	4,639,260
161,508	-	176,109
8,086,467	-	8,086,467
-	-	4,391,255
-	-	22,634
-	-	366,221
9,494,647	4,388,532	67,382,894
(9,488,879)	306,763	(9,048,258)
9,500,000	-	9,500,000
-	-	494,158
161,508	-	161,508
-	(494,158)	(494,158)
9,661,508	(494,158)	9,661,508
172,629	(187,395)	613,250
2,657,324	376,047	33,812,912
$ 2,829,953	$ 188,652	$ 34,426,162

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

EXHIBIT C-3

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2011

Total Net Changes in Fund Balances - Governmental Funds (Exhibit C-2)		$ 613,250
Amounts reported for governmental activities in the statement of activities are different because:		
Capital outlays are reported in governmental funds as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense.		
Capital Assests *increased*	$ 6,134,051	
Depreciation Expense	(3,842,776)	2,291,275
The net effect of miscellaneous transactions involving capital assets (transfers, adjustments and dispositions) is a increase (decrease) to net assets.		(6,276)
Because some property taxes will not be collected for several months after the District's fiscal year end, they are not considered "available" revenues and are deferred in the governmental funds. Deferred tax revenues increased (decreased) by this amount this year.		(130,620)
Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, is not reported as expenditures in the governmental funds:		
Bond Issuance Costs *increased*	$ 161,508	
Amortization of Issuance Costs	(59,232)	102,276
Issuance of bonds provides current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets.		
Par Value	$ (9,500,000)	
(Premium) Discount	(161,508)	(9,661,508)
Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.		3,535,000
Interest on long-term debt in the statement of activities differs from the amount reported in the governmental funds because interest is recognized as an expenditure in the funds when it is due, and thus requires the use of current financial resources. In the statement of activities, however, interest expense is recognized as the interest accrues, regardless of when it is due. The increase (decrease) in interest reported in the statement of activities consist of the following:		
Accrued Interest on Current Interest Bonds Payable *increased*	$ 10,251	
Accrued Interest on Notes Payable *increased*	(100,000)	
Interest Accreted on the Capital Appreciation Bonds	(241,233)	
Amortization of Bond Premium and Discount	194,508	
Amortization of Defeasance Costs	(126,136)	(262,610)
The (increase) decrease in compensated absences is reported in the statement of activities but does not require the use of current financial resources and, therefore, is not reported as expenditures in the governmental funds.		(8,585)
The (increase) decrease in workers' compensation is reported in the statement of activities but does not require the use of current financial resources and, therefore, is not reported as expenditures in the governmental funds.		(30,906)
Change in Net Assets for Governmental Activities (Exhibit B-1)		$ (3,558,704)

The accompanying notes are an integral part of this statement.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

EXHIBIT C-4

GENERAL FUND
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCE - BUDGET (GAAP BASIS) AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2011

Data Control Codes		Budgeted Amounts Original	Budgeted Amounts Final	Actual	Variance with Final Budget Positive (Negative)
	REVENUES:				
5700	*Local and Intermediate Revenue*	$ 30,858,741	$ 31,753,823	$ 35,842,619	$ 4,088,796
5800	*State Program Revenues*	13,657,384	13,662,384	10,050,542	(3,611,842)
5900	*Federal Program Revenues*	-	420,000	197,864	(222,136)
5020	Total Revenues	44,516,125	45,836,207	46,091,025	254,818
	EXPENDITURES:				
	Current:				
	Instruction & Instructional Related Services:				
0011	*Instruction*	23,738,369	23,753,987	22,848,075	905,912
0012	*Instructional Resources and Media Services*	717,765	717,765	694,980	22,785
0013	*Curriculum and Staff Development*	900,983	955,983	951,711	4,272
	Total Instruction & Instr. Related Services	25,357,117	25,427,735	24,494,766	932,969
	Instructional and School Leadership:				
0021	*Instructional Leadership*	223,993	223,993	221,996	1,997
0023	*School Leadership*	2,270,237	2,353,237	2,351,491	1,746
	Total Instructional & School Leadership	2,494,230	2,577,230	2,573,487	3,743
	Support Services - Student (Pupil):				
0031	*Guidance, Counseling, and Evaluation Services*	1,103,342	1,110,342	1,042,994	67,348
0033	*Health Services*	468,291	473,291	465,416	7,875
0034	*Student Transportation*	1,504,932	1,704,932	1,660,743	44,189
0036	*Cocurricular/Extracurricular Activities*	1,518,479	1,638,479	1,631,450	7,029
	Total Support Services - Student (Pupil)	4,595,044	4,927,044	4,800,603	126,441
	Administrative Support Services:				
0041	*General Administration*	2,259,090	2,259,090	1,900,178	358,912
	Total Administrative Support Services	2,259,090	2,259,090	1,900,178	358,912
	Support Services - Nonstudent Based:				
0051	*Plant Maintenance and Operations*	5,779,948	6,529,948	6,267,992	261,956
0052	*Security and Monitoring Services*	302,097	317,097	306,547	10,550
0053	*Data Processing Services*	115,516	118,516	116,765	1,751
	Total Support Services - Nonstudent Based	6,197,561	6,965,561	6,691,304	274,257
	Ancillary Services:				
0061	*Community Services*	38,000	73,000	70,406	2,594
	Total Ancillary Services	38,000	73,000	70,406	2,594
	Debt Service:				
0072	*Interest on Long-term Debt*	345,000	345,000	-	345,000
	Total Debt Service	345,000	345,000	-	345,000
	Intergovernmental Charges:				
0091	*Contracted Instructional Services between Public Schools*	3,300,000	4,496,000	4,391,255	104,745
0095	*Payments to Juvenile Justice Alternative Education Programs*	18,000	33,000	22,634	10,366
0099	*Other Intergovernmental Charges*	-	367,000	366,221	779
	Total Intergovernmental Charges	3,318,000	4,896,000	4,780,110	115,890
6030	Total Expenditures	44,604,042	47,470,660	45,310,854	2,159,806
1100	Excess (Deficiency) of Revenues Over (Under)				
1100	Expenditures	(87,917)	(1,634,453)	780,171	2,414,624
	Other Financing Sources (Uses):				
7915	*Transfers In*	(124,439)	(494,439)	494,158	988,597
8911	*Transfers Out*	(25,000)	(25,000)	-	25,000
7080	Total Other Financing Sources and (Uses)	(149,439)	(519,439)	494,158	1,013,597
1200	Net Change in Fund Balance	(237,356)	(2,153,892)	1,274,329	3,428,221
0100	Fund Balance - Beginning	25,642,034	25,642,034	25,642,034	-
3000	Fund Balance - Ending	$ 25,404,678	$ 23,488,142	$ 26,916,363	$ 3,428,221

The accompanying notes are an integral part of this statement.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

EXHIBIT E-1

STATEMENT OF FIDUCIARY ASSETS AND LIABILITIES
FIDUCIARY FUNDS
JUNE 30, 2011

Data Control Codes			865 Agency Fund Student Activity
	ASSETS:		
1110	*Cash and Cash Equivalents*	$	122,366
1120	*Current Investments*		286,368
1000	Total Assets	$	408,734
	LIABILITIES:		
	Current Liabilities:		
2170	*Due to Other Funds*	$	13,186
2190	*Due to Student Groups*		395,548
2000	Total Liabilities	$	408,734

The accompanying notes are an integral part of this statement.

I. Summary of Significant Accounting Policies

A. Reporting Entity

The Barbers Hill Independent School District (District) is governed by a seven-member board of trustees (Board), which has governance responsibilities over all activities related to public, elementary and secondary, education within the District. Because members of the Board are elected by the public; have authority to make decisions; appoint management and significantly influence operations; and have primary accountability for fiscal matters; the District is not included in any other governmental reporting entity. The accompanying financial statements present the District.

The District is considered an independent entity for financial reporting purposes and is considered a primary government. As required by generally accepted accounting principles, these basic financial statements have been prepared, based on considerations regarding the potential for inclusion of other entities, organizations, or functions, as part of the District's financial reporting entity. Based on these considerations, the District's basic financial statements include the Barbers Hill ISD Education Foundation as a component unit. Additionally, as the District is considered a primary government for financial reporting purposes, its activities are not considered a part of any other governmental or other type of reporting entity.

The District receives funding from local, state, and federal government sources and must comply with the requirements of these funding sources' entities.

The Barbers Hill Independent School District Education Foundation ("the Foundation") meets the criteria set out by governmental accounting standards and has been included as a discretely presented component unit of the District. The Foundation, a non-profit entity, was organized to provide scholarships to Barbers Hill ISD students. None of the other PTO, Booster clubs or other organizations meet the criteria specified by governmental accounting standards to be included as a component unit within the reporting entity.

B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the District. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities* normally are supported by taxes and intergovernmental revenues.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. Depreciation expense and workers' compensation have been allocated to all applicable functions in order to present the expenditures of the District more accurately in the Statement of Activities. *Program revenues* include 1) charges to students or users who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

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

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

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

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

Grant revenues and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the District.

The District reports the following major governmental funds:

The *general fund* is the District's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The *debt service fund* accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

The *capital projects fund* is used to account for the expenditures of resources accumulated from sales of bonds and related interest earnings for the acquisition and construction of school facilities.

Additionally, the District reports the following fund type:

The *agency fund* is used to account for assets held by the District as an agent for student organizations. The fund is custodial in nature (assets equal liabilities) and does not involve measurement or results of operation.

Interfund activities between governmental funds appear as due to/from other funds on the governmental fund balance sheet and as other resources and other uses on the governmental fund statement of revenues, expenditures and changes in fund balance. Interfund activities between governmental funds and fiduciary funds remain as due to/from other funds on the government-wide statement of activities.

Amounts reported as *program revenues* include 1) charges to students or users for goods, services, or privileges provided and 2) operating grants and contributions. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise, general revenues include all taxes and investment income.

When both restricted and unrestricted (committed, assigned, or unassigned) resources are available for use, it is the District’s policy to use restricted resources first, then unrestricted resources as they are needed. The District considers that committed amounts would be reduced first, followed by assigned amounts, and then unassigned amounts when expenditures are incurred for purposes for which amounts in any unrestricted fund balance classification could be used.

D. Assets, Liabilities, and Equity

1. Deposits and Investments
The District's cash and cash equivalents are considered to be cash on hand and demand or time deposits.

The District's funds are required to be deposited and invested under the terms of a depository contract pursuant to the Texas School Depository Act. The depository bank pledges collateral, which complies with state law. The collateral is approved by the Texas Education Agency and shall be in an amount sufficient to protect District funds on a day-to-day basis during the period of the contract. The pledge of collateral is waived only to the extent of the depository bank's dollar amount of Federal Deposit Insurance Corporation ("FDIC") insurance.

State statutes authorize the District to invest in obligations of the U.S. Treasury or the State of Texas, certain U.S. Agencies, certificates of deposit, money market savings accounts, certain municipal securities, repurchase agreements, or investment pools. Investments are held by the District’s agent in the District’s name.

Investments for the District are reported at fair value. The investment pools operate in accordance with appropriate state laws and regulations. The reported value of the pools is the same as the fair value of the pool shares.

2. Receivables and Payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

All property tax receivables are shown net of estimated allowance for uncollectible amounts. The property tax receivable allowance approximates 6 percent of outstanding property taxes at June 30, 2011. Revenues from property taxes are recognized when levied to the extent they are available. The District considers property taxes as available when collected. However, not all outstanding property taxes are expected to be collected within one year of the date of financial statements.

Property values are determined by the County Central Appraisal District as of January 1 of each year. Prior to July 1 of each year, the District adopts its annual budget and as soon thereafter as practicable, shall adopt a tax rate thus creating the tax levy. Property taxes for the current calendar year are levied on approximately October 1 of each year and are payable by January 31 of the following year. Property tax receivables are recorded as of the date levied. Unpaid taxes become delinquent on February 1 and a tax lien on real property is created as of January 1 of each year.

A concentration of risk exists for local revenue sources since approximately 23% of the District's taxable property value is attributed to two taxpayers. Similarly, the District's ten largest taxpayers approximate 44% of the total taxable value of the District.

3. Inventories and Prepaid Items (Deferred Expenditures)

All inventories are valued at cost using the first-in first-out (FIFO) method. Inventories of governmental funds are recorded as expenditures when consumed rather than when purchased.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items (deferred expenditures) in both government-wide and fund financial statements.

4. Capital Assets

Capital assets, which include land, buildings and improvements, furniture and equipment, and construction in progress, are reported in the governmental activities column in the government-wide financial statements. The District's infrastructure includes parking lots and sidewalks associated with various buildings. The cost of the infrastructure was initially capitalized with the building cost and is being depreciated over the same useful life as the building. Capital assets are defined by the District as assets with an initial, individual cost which equals or exceeds $5,000 and an estimated useful life in excess of five years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed.

Land and construction in progress are not depreciated. Buildings and improvements and furniture and equipment of the District are depreciated using the straight line method over the following estimated useful lives:

Assets	Years
Buildings and Improvements	5-50
Furniture and Equipment	5-40

5. Compensated Absences
School employees are allowed one day of sick leave per contract month each year and may accumulate and carry forward to subsequent years all unused sick leave days. Effective July 1, 1995, sick leave days accumulate, but do not vest. Prior to July 1, 1995, all accrued sick leave days are vested and will be paid upon retirement from the District.

An employee may be paid in a single cash payment for unused sick leave accumulated prior to July 1, 1995 (with limitations of 60 days for retirement and 30 days for other reasons) at his/her current pay rate provided the employee completes his/her contract before terminations. Otherwise, all rights to the accrued sick leave pay are forfeited. A liability for accrued, vested amounts is included in long-term liabilities in the Statement of Net Assets.

6. Long-term Obligations
In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities. Effective September 1, 2001, bond premiums and discounts are deferred and amortized over the life of the bonds using the bonds outstanding method, which approximates the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

7. Fund Equity
Beginning with fiscal year 2011, the District implemented GASB Statement No. 54, "Fund Balance Reporting and Governmental Fund Type Definitions." This Statement provides more clearly defined fund balance categories to make the nature and extent of the constraints placed on a government's fund balances more transparent. The following classifications describe the relative strength of the spending constraints:

- Nonspendable fund balance - amounts that are not in spendable form (such as inventory) or are required to be maintained intact.

- Restricted fund balance - amounts constrained to specific purposes by their providers (such as grantors, bondholders, and higher levels of government), through constitutional provisions, or by enabling legislation.

- Committed fund balance - amounts constrained to specific purposes by the District itself, using its highest level of decision-making authority (i.e., Board of Trustees). To be reported as committed, amounts cannot be used for any other purpose unless the District takes the same highest level action to remove or change the constraint.

- Assigned fund balance - amounts the District intends to use for a specific purpose. Intent can be expressed by the Board or by an official or body to which the Board delegates the authority.

- Unassigned fund balance - amounts that are available for any purpose. Positive amounts are reported only in the general fund.

Beginning fund balances for the Districts governmental funds have been restated to reflect the above classifications.

The Board establishes (and modifies or rescinds) fund balance commitments by passage of a resolution. This is typically done through adoption and amendment of the budget. A fund balance commitment is further indicated in the budget document as a designation or commitment of the fund (such as for special incentives). Assigned fund balance is established by the Superintendent or his designee through adoption or amendment of the budget as intended for specific purpose (such as the purchase of fixed assets, construction, debt service, or for other purposes).

8. Use of Estimates

The presentation of financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, 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.

9. Data Control Codes

The Data Control Codes refer to the account code structure prescribed by TEA in the *Financial Accountability System Resource Guide*. Texas Education Agency requires school districts to display these codes in the financial statements filed with the Agency in order to insure accuracy in building a statewide data base for policy development and funding plans.

II. Stewardship, Compliance, and Accountability

A. Budgetary Information

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for the general fund, *national school breakfast/lunch program* special revenue fund, and debt service fund. All annual appropriations lapse at fiscal year-end. The following procedures are followed in establishing the budgetary data reflected in the financial statements.

1. Prior to June 20 of the preceding fiscal year, the District prepares a budget for the next succeeding fiscal year beginning July 1. The operating budget includes proposed expenditures and the means of financing them.
2. A meeting of the Board is then called for the purpose of adopting the proposed budget after ten days' public notice of the meeting has been given.
3. Prior to July 1, the budget is legally enacted through passage of a resolution by the Board.

The appropriated budget is prepared by fund, function, and campus/department. The District's campus/department heads may make transfers of appropriations within a department. Transfers of appropriations between campus/departments require the approval of the District's management. Transfers of appropriations between functions require the approval of the Board. The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriations) is the function level within a fund. The District made several supplemental budgetary appropriations throughout the year. The supplemental budgetary amendments made in the general fund were primarily to increase appropriations primarily for contracted instructional services between schools and plant maintenance and operations.

The supplemental budgetary appropriations made in the *national school breakfast and lunch program* special revenue fund were to appropriate funds for the purchase of additional food supplies.

B. Excess of Expenditures Over Appropriations

For the year ended June 30, 2011, expenditures exceeded appropriations in the functions (the legal level of budgetary control) of the following funds:

None

III. Detailed Notes on All Funds

A. Deposits and Investments

As of June 30, 2011, the District had the following governmental activities investments:

Investment Type	Fair Value	Percentage of Total Investments	Weighted Average Maturity (Years)
Texpool	$ 4,567,595	32%	0.23
Lonestar - Government Overnight	1,975,947	14%	0.34
Lonestar - Corporate Overnight	294,216	2%	0.16
TexStar	1,018,342	7%	0.20
Commercial Paper	6,494,616	45%	0.21
Total Fair Value	**$ 14,350,716**	**100%**	
Portfolio Weighted Average Maturity			**0.23**

Credit risk. State law and District policy limits credit risk by allowing investing in 1) Obligations of the United States or its agencies which are backed by the full faith and credit of the United States, obligations of the State of Texas or its agencies, counties, cities and other political subdivisions of any state rated as to investment quality by a nationally recognized investment rating firm (NRIRF) not less than A or its equivalent; 2) Certificates of deposit issued by a depository located in Texas which is insured by the FDIC; 3) Repurchase agreements secured by obligations of the United States or its agencies not to exceed 90 days to maturity from the date of purchase; 4) Bankers acceptances with a stated maturity of 270 days or fewer which are eligible for collateral for borrowing from a Federal Reserve Bank; 5) No-load money market mutual funds which shall be registered with the Securities and Exchange Commission which have an average weighted maturity of less than two years, investments comply with the Public Funds Investment Act and are continuously rated not less than AAA by at least one NRIRF. 6) A guaranteed investment contract (for bond proceeds only) which meets the criteria and eligibility requirements established by the Public Funds Investment Act; 7) Public funds investment pools which meets the requirements of the Public Funds Investment Act. State law limits investments in commercial paper to the top two ratings issued by nationally recognized statistical rating organizations.

At year-end, the balances in commercial paper were rated A1 by Standard & Poor's. At year-end, the balances in Texpool, a privately managed public funds investment pool, were rated AAAm by Standard & Poor's. At year-end, the balances in Lone Star, a privately managed public funds investment pool, were rated AAAm by Standard & Poor's. At year-end, the balances in TexStar were rated AAAm by Standard & Poor's. All credit ratings met acceptable levels required by legal guidelines prescribed in both the PFIA and the District's investment policy

Interest rate risk. Interest rate risk is the risk that changes in interest rates may adversely affect the value of the investments. The District monitors interest rate risk utilizing weighted average maturity analysis. In accordance with its investment policy, the District reduces its exposure to declines in fair values by limiting the weighted average maturity of its investment portfolio as a whole to no more than 180 days, diversification, and by holding securities to maturity.

Concentration of credit risk. The District's investment policy does not limit an investment in any one issuer. The investment portfolio shall be diversified in terms of investment instruments, maturity scheduling, and financial institutions to reduce risk of loss resulting from over-concentration of assets in a specific class of investments, specific maturity, or specific issuer.

Custodial credit risk – deposits. In the case of deposits, this is the risk that in the event of a bank failure, the District's deposits may not be returned to it. As of June 30, 2011, District's banks' balances of $15,796,845 was not exposed to custodial credit risk because it was insured and collateralized with securities held by the District's agent in the District's name.

Custodial credit risk – investments. For an investment, this is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The District's investments are held by the District's agent in the District's name for the benefit of the District.

B. Receivables

Receivables as of year-end for the District's individual major funds and nonmajor funds in the aggregate, including the applicable allowances for uncollectible accounts, are as follows:

	General	Debt Service	Nonmajor and Other Funds	Total
Receivables:				
Property Taxes	$ 1,786,345	$ 372,017	$ -	$ 2,158,362
Due From Other Governments:				
County	3,880,437	-	-	3,880,437
State	6,273,834	-	4,625	6,278,459
Federal	-	-	604,273	604,273
Other	15,123	-	-	15,123
Gross Receivables	11,955,739	372,017	608,898	12,936,654
Less: Allowance for Uncollectibles	(107,181)	(22,321)	-	(129,502)
Net Total Receivables	**$ 11,848,558**	**$ 349,696**	**$ 608,898**	**$ 12,807,152**

Tax revenues of the general and debt service funds are reported net of estimated uncollectible amounts. Total uncollectible amounts related to revenues of the current period increased (decreased) revenues as follows:

Uncollectibles Related to General Fund Property Taxes	$ 6,758
Uncollectibles Related to Debt Service Property Taxes	1,434
Total Uncollectibles of the Current Fiscal Year	**$ 8,192**

Governmental funds report deferred revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period or in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of deferred revenue reported in the governmental funds were as follows:

	Unavailable	Unearned
Delinquent Property Taxes Receivable (General Fund)	$ 1,679,164	$ -
Delinquent Property Taxes Receivable (Debt Service Fund)	349,696	-
Escrow Local Taxes (General Fund)	-	265
Total Deferred/Unearned Revenue For Governmental Funds	**$ 2,028,860**	**$ 265**

C. Capital Assets

Capital asset activity for the year ended June 30, 2011 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Governmental Activities:				
Capital Assets, not being Depreciated:				
Land and Improvements	$ 4,549,638	$ 206,821	$ -	$ 4,756,459
Construction in Progress	-	4,155,382	-	4,155,382
Total Capital Assets, not being Depreciated	**4,549,638**	**4,362,203**	**-**	**8,911,841**
Capital Assets, being Depreciated:				
Building and Improvements	120,534,979	899,158	-	121,434,137
Furniture and Equipment	15,698,244	872,690	(19,821)	16,551,113
Total Capital Assets, being Depreciated	**136,233,223**	**1,771,848**	**(19,821)**	**137,985,250**
Less Accumulated Depreciation for:				
Building and Improvements	(29,996,618)	(2,784,450)	-	(32,781,068)
Furniture and Equipment	(9,632,176)	(1,058,326)	13,545	(10,676,957)
Total Accumulated Depreciation	**(39,628,794)**	**(3,842,776)**	**13,545**	**(43,458,025)**
Total Capital Assets, being Depreciated, net	**96,604,429**	**(2,070,928)**	**(6,276)**	**94,527,225**
Governmental Activities Capital Assets, net	**$ 101,154,067**	**$ 2,291,275**	**$ (6,276)**	**$ 103,439,066**

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

	Governmental Activities:		
11	Instruction	$	1,800,091
12	Instructional Resources and Media Services		294,614
13	Curriculum and Staff Development		2,271
23	School Leadership		176
31	Guidance, Counseling, & Evaluation Services		288
33	Health Services		1,090
34	Student Transportation		211,806
35	Food Service		58,144
36	Cocurricular/Extracurricular Activities		411,268
41	General Administration		39,799
51	Plant Maintenance and Operations		891,619
52	Security and Monitoring Services		131,610
	Total Depreciation Expense-Governmental Activities	**$**	**3,842,776**

Construction Commitments

The District has active construction projects as of June 30, 2011. The projects include the construction and equipment of school facilities. At year-end, the District's commitments with contractors are as follows:

Project		**Remaining Commitment**
Fire Sprinkler System at Primary School	$	246,623
Chilled Water Lines at Barbers Hill Middle School		589,585
Science Labs at Barbers Hill Middle School		150,593
District Retrofit Light Replacement		187,424
Totals	**$**	**1,174,225**

D. Interfund Receivables, Payables, and Transfers

The composition of interfund balances as of June 30, 2011, is as follows:

Due From/To Other Funds		**Interfund Receivables**		**Interfund Payables**
General fund	$	364,757	$	506
Other Governmental Funds - Nonmajor				
Special Revenue Funds:				
ARRA of 2009 Title XIV State		-		91,615
Student Success Initiative		506		-
FEMA Public Assistance		-		259,956
Total Special Revenue Funds		506		351,571
Fiduciary Funds:				
Agency		-		13,186
Totals	**$**	**365,263**	**$**	**365,263**

Interfund balances consist of short-term lending/borrowing arrangements that result primarily from payroll and other regularly occurring charges that are paid by the general fund and then charged back to the appropriate other fund. Additionally, some lending/borrowing may occur between two or more nonmajor governmental funds.

Interfund Transfers

Interfund transfers are defined as "flows of assets without equivalent flow of assets in return and without a requirement for repayment." The following is a summary of the District's transfers for the year ended June 30, 2011.

Transfer Out	Transfers In	Amount
Other Governmental Funds	General Fund	$ 494,158
Total		**$ 494,158**

Transfers are used to: (1) move revenues from the fund that is required to collect them to the fund that is required or allowed to expend them; and (2) use unrestricted revenues collected in the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

E. Long-term Liabilities

The District's long-term liabilities consist of bond indebtedness, notes payable, compensated absences, and workers' compensation claims. The current requirements for general obligation bonds principal and interest expenditures are accounted for in the debt service fund. The current requirements for the notes payable, compensated absences, and workers' compensation claims are accounted for in the general fund. In prior years, the general fund has been used to liquidate any other long-term liability not accounted for in the debt service fund.

Changes in Long-term Liabilities

Long-term liability activity for the year ended June 30, 2011, was as follows:

	Beginning Balance	Provision or Additions	Reductions	Ending Balance	Due Within One Year
Governmental Activities:					
Bonds Payable:					
General Obligation Bonds	$ 102,593,771	$ 9,500,000	$ (3,535,000)	$ 108,558,771	$ 3,700,000
Less Deferred Amounts:					
For Issuance Premiums (CIB's)	2,462,009	161,508	(203,054)	2,420,463	-
For Issuance Discounts (CIB's)	(176,618)	-	8,546	(168,072)	-
For Accreted Interest (CAB's)	1,019,832	241,233	-	1,261,065	-
Deferred Interest Expense Adjustment	(2,136,778)	-	126,136	(2,010,642)	-
Total Bonds Payable, net	103,762,216	9,902,741	(3,603,372)	110,061,585	3,700,000
Note Payable	5,000,000	-	-	5,000,000	-
Workers' Compensation	249,934	106,078	(75,172)	280,840	280,840
Compensated Absences	299,691	14,219	(5,634)	308,276	308,276
Governmental Activity Long-term Liabilities	**$ 109,311,841**	**$ 10,023,038**	**$ (3,684,178)**	**$ 115,650,701**	**$ 4,289,116**

General Obligation Bonds

The District issues general obligation bonds to provide funds for the construction and equipment of school facilities and to refund general obligation bonds.

General obligation bonds are direct obligations and pledge the full faith and credit of the District. These bonds are issued as 3-26 year current interest or capital appreciation bonds (CAB) with various amounts of principal maturing each year. Rates may be fixed or variable.

The following is a summary of changes in the general obligation bonds for the fiscal year:

Series	Interest Rate	Original Issue	Maturity Date	Beginning Balance	Additions	Reductions	Ending Balance
2003	3-5.25%	$ 20,545,000	2029	$ 19,165,000	$ -	$ (425,000)	$ 18,740,000
2005	2.5-5.25%	11,920,000	2030	10,435,000	-	(330,000)	10,105,000
2005 REF	3-5%	42,150,000	2027	39,530,000	-	(1,730,000)	37,800,000
2005 CAB REF	4.18%	753,771	2015	753,771	-	-	753,771
2006	4-5%	24,000,000	2031	22,140,000	-	(675,000)	21,465,000
2007	4-5.5%	9,660,000	2032	8,090,000	-	(245,000)	7,845,000
2007 CAB	3.87%	140,000	2012	140,000	-	-	140,000
2010 REF	3-4%	2,340,000	2027	2,340,000	-	(130,000)	2,210,000
2011	4.25-4.5%	9,450,000	2036	-	9,450,000	-	9,450,000
2011 CAB	0.7-1.25%	50,000	2014	-	50,000	-	50,000
Totals				**$ 102,593,771**	**$ 9,500,000**	**$ (3,535,000)**	**$ 108,558,771**
Deferred Amounts:							
Issuance Premium				$ 2,462,009	$ 161,508	$ (203,054)	$ 2,420,463
Insurance Discount				(176,618)	-	8,546	(168,072)
Accreted Interest (CAB)				1,019,832	241,233	-	1,261,065
Deferred Interest Expense Adjustment				(2,136,778)	-	126,136	(2,010,642)
Totals				**$ 103,762,216**	**$ 9,902,741**	**$ (3,603,372)**	**$ 110,061,585**

Annual debt service requirements to maturity for general obligation bonds are as follows:

General Obligation Bonds

Year Ending June 30	Principal Value	Interest	Total Requirements
2012	$ 3,700,000	$ 4,847,588	$ 8,547,588
2013	4,060,000	4,822,266	8,882,266
2014	4,230,000	4,651,854	8,881,854
2015	3,133,771	4,482,979	7,616,750
2016	4,500,000	4,383,054	8,883,054
2017	4,695,000	4,175,604	8,870,604
2018	4,925,000	3,956,616	8,881,616
2019	5,130,000	3,751,699	8,881,699
2020	5,365,000	3,513,236	8,878,236
2021	5,615,000	3,261,636	8,876,636
2022	5,890,000	2,988,736	8,878,736
2023	6,165,000	2,707,749	8,872,749
2024	6,465,000	2,409,499	8,874,499
2025	6,785,000	2,099,486	8,884,486
2026	7,100,000	1,769,699	8,869,699
2027	7,450,000	1,422,691	8,872,691
2028	4,065,000	1,077,549	5,142,549
2029	4,260,000	880,896	5,140,896
2030	2,885,000	674,778	3,559,778
2031	2,125,000	537,693	2,662,693
2032	1,830,000	439,208	2,269,208
2033	1,915,000	357,987	2,272,987
2034	2,000,000	271,812	2,271,812
2035	2,090,000	186,812	2,276,812
2036	2,180,000	95,375	2,275,375
Totals	**$ 108,558,771**	**$ 59,766,502**	**$ 168,325,273**

As of June 30, 2011, the District has $75,500,000 in authorized but unissued bonds.

In prior years, the District defeased certain previously issued and outstanding bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the District's financial statements. At June 30, 2011, there were no outstanding defeased bonds.

Note Payable
On March 23, 2009, the District received a community disaster loan from the Federal Emergency Management Agency (FEMA) in the amount of $5,000,000. The interest rate on the loan is 2.00%. Principal and interest on the loan is due on April 27, 2014.

Operating Lease
Total rental expense under all operating leases for fiscal year 2011 was approximately $179,915.

The District also leases various properties to local organizations and governmental agencies for nominal amounts.

F. Fund Balance
Other committed fund balance includes the following commitments of funds:

General Fund:		
Potential Property Value Losses	$	4,179,650
Other Governmental Fund:		
Food Service		188,571
Total Other Committed Fund Balance	**$**	**4,368,221**

G. Revenues from Local and Intermediate Sources
During the current year, revenues from local and intermediate sources consisted of the following:

	General	Debt Service	Capital Projects Fund	Other Funds	Totals
Property Taxes	$ 29,609,215	$ 7,532,561	$ -	$ -	$ 37,141,776
Investment Income	86,233	9,987	5,768	-	101,988
Food Sales	-	-	-	1,597,684	1,597,684
County Equalization	1,277,077	-	-	-	1,277,077
County Available	3,883,439	-	-	-	3,883,439
Other	986,655	-	-	-	986,655
Total	**$ 35,842,619**	**$ 7,542,548**	**$ 5,768**	**$ 1,597,684**	**$ 44,988,619**

IV. Other Information
A. Risk Management
General
Like all public school districts, the District is exposed to various risks of loss related to torts, theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the fiscal year 2011, the District purchased commercial insurance for claims related to all risks. There were no significant reductions in coverage in the past fiscal year, and there were no settlements exceeding insurance coverage for any of the past three fiscal years.

Health Care Coverage
During the year ended June 30, 2011, employees of the District were covered by TRS-Active Care (the Plan) a statewide health coverage program for Texas public education employees, implemented by the Teacher Retirement System of Texas (TRS). The District paid premiums of $330 per month, per employee to the Plan. Employees, at their option, authorized payroll withholdings to pay premiums for dependents. All premiums were paid to the TRS. The legislature created the Plan for public school employee group health coverage in 2002-03, requiring all Districts with fewer than 500 employees to participate in the Plan.

Workers' Compensation
During the year ended June 30, 2011, the District met its statutory workers' compensation obligations through participation in the TASB Risk Management Fund (the Fund). The Fund was created and is operated under the provisions of the Interlocal Cooperation Act, Chapter 791 of the Texas Government Code. The Fund's Workers' Compensation Program is authorized by Chapter 504, Texas Labor Code. All members participating in the Fund execute Interlocal Agreements that define the responsibilities of the parties. The Fund provides statutory workers' compensation benefits to its members and their injured employees.

Barbers Hill ISD participates in the Fund's reimbursable aggregate deductible program. As such, the member is responsible for a certain amount of claims liability as outlined on the member's Contribution and Coverage Summary document. After the member's deductible has been met, the Fund is responsible for additional claims.

The Fund and its members are protected against higher than expected claims costs through the purchase of stop loss coverage for any claim in excess of the Fund's self-insured retention of $1.5 million. The Fund uses the services of an independent actuary to determine reserve adequacy and fully funds those reserves. There were no significant reductions in insurance coverage from the prior year or settlements exceeding insurance coverage for each of the past three fiscal years. As of August 31, 2010, the Fund carried reserves of $73,463,401 for future development on reported claims and claims that have been incurred but not yet reported. For the year ended August 31, 2010, member districts will have no additional liability beyond their contractual obligations for payment of contributions and reimbursable aggregate deductibles.

The liability estimation requires the estimate of loss development over an extended period of time. During the time, numerous internal and external factors will affect the ultimate settlement value of claims. Due to the inherent uncertainty with regard to the impact of these factors, there can be no guarantee that actual losses will not vary, perhaps significantly, from the estimates. The following is a summary of the changes in the balances of claims liabilities for workers' compensation for the year ended June 30:

	Year Ended 6/30/2011	Year Ended 6/30/2010
Unpaid Claims, Beginning of Fiscal Year	$ 249,934	$ 122,394
Incurred Claims (including IBNRs and changes in provisions)	106,078	177,504
Claim Payments	(75,172)	(49,964)
Unpaid Claims, End of Fiscal Year	**$ 280,840**	**$ 249,934**

The Fund engages the services of independent auditors to conduct a financial audit after the close of each plan year on August 31. The audit is approved by the Fund's Board of Trustees in February of the following year. The Fund's audited financial statements as of August 31, 2010, are available at the TASB offices and have been filed with the Texas Department of Insurance in Austin.

Unemployment Compensation Pool
During the year ended June 30, 2011, the District provided unemployment compensation coverage to its employees through participation in the TASB Risk Management Fund (the Fund). The Fund was created and is operated under the provisions of the Interlocal Cooperation Act, chapter 791 of the Texas Government Code. The Fund's Unemployment Compensation Program is authorized by section 22.055 of the Texas Education Code and Chapter 172 of the Texas Local Government Code. All members participating in the Fund execute Interlocal Agreements that define the responsibilities of the parties.

The Fund meets its quarterly obligation to the Texas Workforce Commission. Expenses are accrued each month until the quarterly payment has been made. Expenses can be reasonably estimated; therefore, there is no need for specific or aggregate stop loss coverage for Unemployment Compensation pool members.

The Fund engages the services of an independent auditor to conduct a financial audit after the close of each plan year on August 31. The audit is accepted by the Fund's Board of Trustees in February of the following year. The Fund's audited financial statements as of August 31, 2010 are available at the TASB offices and have been filed with the Texas Department of Insurance in Austin.

B. Contingent Liabilities
Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures that may be disallowed by the grantor cannot be determined at this time, although the District expects such amounts, if any, to be immaterial.

The District is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, in the opinion of the District's counsel, the resolution of these matters will not have a material adverse effect on the financial condition of the District.

C. Defined Benefit Pension Plan
Pension Plan for Employees Participating in Teacher Retirement System
Plan Description. The Barbers Hill Independent School District contributes to the Teacher Retirement System of Texas (TRS), a cost-sharing multiple employer defined benefit pension plan. TRS administers retirement and disability annuities, and death and survivor benefits to employees and beneficiaries of the employees of the public school systems of Texas. It operates primarily under the provisions of the Texas Constitution, Article XVI, Sec. 67, and Texas Government Code, Title 8, Subtitle C. TRS also administers proportional retirement benefits and service credit transfer under Texas Government Code, Title 8, Chapter 803 and 805, respectively. The Texas state legislature has the authority to establish and amend benefit provisions of the pension plan and may, under certain circumstances, grant special authority to the TRS Board of Trustees. TRS issues a publicly-available financial report that includes financial statements and required supplementary information for the defined benefit pension plan. That report may be obtained by downloading the report from the TRS Internet website, www.trs.state.tx.us, under the TRS Publications headings, or by calling the TRS Communications Department at 1-800-223-8778, or by writing to the TRS Communications Department, 1000 Red River Street, Austin, Texas 78701.

Funding Policy. Contribution requirements are not actuarially determined but are established and amended by the Texas state legislature. The state funding policy is as follows: (1) the state constitution requires the legislature to establish a member contribution rate of not less than 6.0% of the member's annual compensation and a state contribution rate of not less than 6.0% and not more than 10% of the aggregate annual compensation of all members of the system; (2) a state statute prohibits benefit improvements or contribution reductions if, as a result of the particular action(s), the time required to amortize TRS's unfunded actuarial liabilities would be increased to a period that exceeds 31 years, or, (3) if the amortization period already exceeds 31 years, the period would be increased by such action. State law provides for a member contribution rate of 6.4% for fiscal year 2011, 2010, and 2009 and a state contribution rate of 6.644% for the fiscal years 2011 and 2010, 6.58% for the fiscal year 2009. State contributions to TRS made on behalf of the Barbers Hill Independent School District's employees for the years ended June 30, 2011, 2010, and 2009 were $1,486,722, $1,327,159, and $1,302,431, respectively. The District paid additional state contributions for the years ended June 30, 2011, 2010, and 2009 in the amount of $479,670, $435,121, and $364,449, respectively, on the portion of the employees' salaries that exceeded the statutory minimum.

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

Funding Policy. Contribution requirements are not actuarially determined but are legally established each biennium by the Texas Legislature. Texas Insurance Code, Sections 1575.202, 203, and 204 establish state, active employee and public school contributions, respectively. The State of Texas and active public school employee contribution rates were 1.0% and 0.65% of public school payroll, respectively, with school districts contributing a percentage of payroll set at 0.55% for fiscal years 2011, 2010 and 2009. Per Texas Insurance Code, Chapter 1575, the public school contribution may not be less than 0.25% or greater than 0.75% of the salary of each active employee of the public school. For the years ended June 30, 2011, 2010, and 2009, the States contributions to TRS-Care were $288,658, $259,288, and $244,254, respectively, the active member contributions were $192,377, $173,226, and $158,765, respectively, and the school district's contributions were $162,781, $146,576, and $134,340, respectively, which equaled the required contributions each year. In addition, the State of Texas contributed $83,286, $72,131, and $59,689 in 2011, 2010 and 2009, respectively, for on-behalf payments for Medicare Part D.

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OTHER SUPPLEMENTARY INFORMATION

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

SCHEDULE OF DELINQUENT TAXES RECEIVABLE

FOR THE YEAR ENDED JUNE 30, 2011

	1	2	3
	Tax Rates		Assessed/Appraised
Year Ended June 30	Maintenance	Debt Service	Value For School Tax Purposes
2002 and Prior Years	$ Various	$ Various	$ Various
2003	1.50	.199	1,710,698,882
2004	1.50	.2899	1,883,701,827
2005	1.50	.2899	1,899,129,002
2006	1.50	.2899	2,268,743,840
2007	1.37	.2499	2,810,963,084
2008	1.04	.2899	2,897,453,267
2009	1.0601	.2698	3,245,583,126
2010	1.0601	.2698	2,886,732,837
2011 (School Year Under Audit)	1.0601	.2698	2,788,955,260
1000 Totals			

9000 - Portion of Row 1000 for Taxes Paid into Tax Increment Zone Under Chapter 311, Tax Code

10 Beginning Balance 7/1/10	20 Current Year's Total Levy	31 Maintenance Collections	32 Debt Service Collections	40 Entire Year's Adjustments	50 Ending Balance 6/30/11
$ 269,545	$ -	$ 3,244	$ 470	$ (22,008)	$ 243,823
55,333	-	351	46	(45)	54,891
635,204	-	820	158	(47)	634,179
347,916	-	1,857	359	(46)	345,654
45,702	-	7,676	1,483	(852)	35,691
86,234	-	11,539	2,105	52	72,642
97,273	-	24,432	6,811	4,775	70,805
214,173	-	49,171	12,514	7,934	160,422
545,794	-	118,208	30,085	(225,490)	172,011
-	37,090,316	29,230,060	7,439,176	(52,836)	368,244
$ 2,297,174	$ 37,090,316	$ 29,447,358	$ 7,493,207	$ (288,563)	$ 2,158,362
$ -	$ -	$ -	$ -	$ -	$ -

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

EXHIBIT J-2

FUND BALANCE AND CASH FLOW CALCULATION WORKSHEET (UNAUDITED)
GENERAL FUND
AS OF JUNE 30, 2011

Data Control Codes	Explanation	Amount
1	Total General Fund Balance as of June 30, 2011 (Exhibit C-1 object 3000 for the General Fund only)	$ 26,916,363
2	Total Non-Spendable Fund Balance (from Exhibit C-1 - total of object 341X-344X for the General Fund only)	896,818
3	Total Restricted Fund Balance (from Exhibit C-1 - total of object 345X-349X for the General Fund only)	-
4	Total Committed Fund Balance (from Exhibit C-1 - total of object 351X-354X for the General Fund only)	14,000,000
5	Total Assigned Fund Balance (from Exhibit C-1 - total of object 355X-359X for the General Fund only)	-
6	Estimated amount needed to cover fall cash flow deficits in the General Fund (net of borrowed funds and funds representing deferred revenues)	5,262,033
7	Estimate of two month's average cash disbursements during the fiscal year	3,610,000
8	Estimate of delayed payments from state sources (58XX)	-
9	Estimate of underpayment from state sources equal to variance between Legislative Payment Estimate (LPE) and District Planning Estimate (DPE) or District's calculated earned state aid amount	-
10	Estimate of delayed payments from federal sources (59XX)	-
11	Estimate of expenditures to be reimbursed to General Fund from Capital Projects Fund (uses of General Fund cash after bond referendum and prior to issuance of bonds)	2,355,000
12	Optimum Fund Balance and Cash Flow (Lines 2+3+4+5+6+7+8+9+10+11)	26,123,851
13	Excess (Deficit) Unassigned General Fund Balance (Line 1 minus Line 12)	$ 792,512

<u>If Item 13 is a Positive Number</u>
Explanation of need for and/or projected use of net positive Unassigned General Fund Balance:

Excess Fund Balance needed to fund construction projects prior to issuance of bonds.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

EXHIBIT J-3

NATIONAL SCHOOL BREAKFAST AND LUNCH PROGRAM
BUDGETARY COMPARISON SCHEDULE
FOR THE YEAR ENDED JUNE 30, 2011

Data Control Codes		Budgeted Amounts Original	Budgeted Amounts Final	Actual	Variance with Final Budget Positive (Negative)
	REVENUES:				
5700	*Local and Intermediate Revenue*	$ 1,613,000	$ 1,613,000	$ 1,597,684	$ (15,316)
5800	*State Program Revenues*	7,000	47,000	48,188	1,188
5900	*Federal Program Revenues*	390,000	478,000	477,257	(743)
5020	Total Revenues	2,010,000	2,138,000	2,123,129	(14,871)
	EXPENDITURES:				
	Current:				
	Support Services - Student (Pupil):				
0035	*Food Service*	1,962,930	2,452,930	1,935,079	517,851
	Total Support Services - Student (Pupil)	1,962,930	2,452,930	1,935,079	517,851
6030	Total Expenditures	1,962,930	2,452,930	1,935,079	517,851
1100	Excess (Deficiency) of Revenues Over (Under)				
1100	Expenditures	47,070	(314,930)	188,050	502,980
	Other Financing Sources (Uses):				
7915	*Transfers In*	-	375,000	-	(375,000)
8911	*Transfers Out*	-	(375,000)	(375,000)	-
7080	Total Other Financing Sources and (Uses)	-	-	(375,000)	(375,000)
1200	Net Change in Fund Balance	47,070	(314,930)	(186,950)	127,980
0100	Fund Balance - Beginning	375,521	375,521	375,521	-
3000	Fund Balance - Ending	$ 422,591	$ 60,591	$ 188,571	$ 127,980

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

EXHIBIT J-4

DEBT SERVICE FUND
BUDGETARY COMPARISON SCHEDULE
FOR THE YEAR ENDED JUNE 30, 2011

Data Control Codes		Budgeted Amounts Original	Final	Actual	Variance with Final Budget Positive (Negative)
	REVENUES:				
5700	*Local and Intermediate Revenue*	$ 7,441,775	$ 7,532,775	$ 7,542,548	$ 9,773
5020	Total Revenues	7,441,775	7,532,775	7,542,548	9,773
	EXPENDITURES:				
	Debt Service:				
0071	*Principal on Long-term Debt*	3,535,000	3,535,000	3,535,000	-
0072	*Interest on Long-term Debt*	4,640,000	4,640,000	4,639,260	740
0073	*Bond Issuance Costs and Fees*	17,000	17,000	14,601	2,399
	Total Debt Service	8,192,000	8,192,000	8,188,861	3,139
6030	Total Expenditures	8,192,000	8,192,000	8,188,861	3,139
1200	Net Change in Fund Balance	(750,225)	(659,225)	(646,313)	12,912
0100	Fund Balance - Beginning	5,137,507	5,137,507	5,137,507	-
3000	Fund Balance - Ending	$ 4,387,282	$ 4,478,282	$ 4,491,194	$ 12,912

OVERALL COMPLIANCE, INTERNAL CONTROL SECTION AND FEDERAL AWARDS

HLS&K

Hereford, Lynch, Sellars & Kirkham

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

Board of Trustees
Barbers Hill Independent School District
P.O. Box 1108
Mont Belvieu, Texas 77580

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Barbers Hill Independent School District (District), as of and for the year ended June 30, 2011, which collectively comprise the District's basic financial statements and have issued our report thereon dated October 17, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

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

This report is intended solely for the information and use of management, the Board of Trustees, others within the entity, federal awarding agencies, and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

Hereford, Lynch, Sellars & Kirkham, P.C.

HEREFORD, LYNCH, SELLARS & KIRKHAM, P.C.
Certified Public Accountants

Conroe, Texas
October 17, 2011

HLS&K

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REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Board of Trustees
Barbers Hill Independent School District
P.O. Box 1108
Mont Belvieu, Texas 77580

Compliance

We have audited Barbers Hill Independent School District's (District) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the District's major federal programs for the year ended June 30, 2011. The District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the District's management. Our responsibility is to express an opinion on the District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the District's compliance with those requirements.

In our opinion, the District complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2011.

Internal Control Over Compliance

Management of the District, is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the District's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of management, the Board of Trustees, others within the entity, federal awarding agencies, and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

Hereford, Lynch, Sellars & Kirkham, P.C.

HEREFORD, LYNCH, SELLARS & KIRKHAM, P.C.
Certified Public Accountants

Conroe, Texas
October 17, 2011

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BARBERS HILL INDEPENDENT SCHOOL DISTRICT
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2011

SECTION I – SUMMARY OF AUDITORS' RESULTS	
FINANCIAL STATEMENTS	
1. Type of auditors' report issued	Unqualified
2. Internal Control over Financial Reporting:	
a. Material Weakness(es) identified?	No
b. Significant Deficiency(ies) identified that are not considered to be material weaknesses?	None reported
3. Noncompliance material to Financial Statements noted?	No
FEDERAL AWARDS	
4. Internal control over major programs:	
a. Material Weakness(es) identified?	No
b. Significant Deficiency(ies) identified that are not considered to be material weaknesses?	None reported
5. Type of auditors' report issued on compliance with major programs	Unqualified
6. Any Audit Findings Disclosed that are Required to be Reported in Accordance with Section 510(a) of OMB Circular A-133	No
7. Identification of Major Programs	Special Education Cluster (IDEA) 84.394A ARRA of 2009 Title XIV SFSF
8. Dollar Threshold Used to Distinguish Between Type A and Type B Federal Programs	$300,000
9. Auditee Qualified as a Low-Risk Auditee?	Yes
SECTION II –FINANCIAL STATEMENT FINDINGS	
None reported	
SECTION III-FEDERAL AWARD FINDINGS AND QUESTIONED COSTS	
None reported	

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2011

PRIOR YEAR FINDINGS
None reported .

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

CORRECTIVE ACTION PLAN
FOR THE YEAR ENDED JUNE 30, 2011

CURRENT YEAR FINDINGS
None reported

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

EXHIBIT K-1

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE YEAR ENDED JUNE 30, 2011

(1) Federal Grantor/ Pass-Through Grantor/ Program Title	(2) Federal CFDA Number	(2A) Project Number	(3) Federal Expenditures
U.S. DEPARTMENT OF HOMELAND SECURITY:			
Passed Through State Department of Public Safety's Division of Emergency Management:			
Disaster Grants - FEMA Hurricane Reimbursement	97.036	DR1791 TX	$ 163,884
U.S. GENERAL SERVICES ADMINISTRATION:			
Passed Through Texas Facilities Commission/Federal Surplus Program:			
Donation of Federal Surplus Personal Property	39.003	40140	33,980
U.S. DEPARTMENT OF EDUCATION:			
Passed Through State Department of Education:			
ESEA Title I Part A - Improving Basic Programs	84.010A	11610101036902	146,321
ESEA Title IV Part A-Safe & Drug-Free Schools & Communities Act	84.186A	10691001036902	1,018
ESEA Title II Part A - Teacher & Principal Training & Recruiting	84.367A	11694501036902	55,669
ESEA Title II Part A - Teacher & Principal Training & Recruiting	84.367A	10694501036902	11,915
Total Program 84.367A			**67,584**
Title III Part A English Language Acquisition and Language Enhancement	84.365A	11671001036902	11,228
Title VI, Part A, Summer School LEP	84.369A	6955100	2,149
Special Education Cluster (IDEA):			
IDEA - Part B Formula	84.027A	116600010369026600	486,348
IDEA - Part B Formula	84.027A	106600010369026600	98,177
IDEA - Part B Preschool	84.173A	116610010369026610	10,166
IDEA - Part B Preschool	84.173A	106610010369026610	837
ARRA IDEA - Part , Formula	84.391A	10554001036902	401,956
ARRA IDEA - Part B Preschool	84.392A	10555001036902	9,680
Total Special Education Cluster (IDEA):			**1,007,164**
ARRA Title XIV State Fiscal Stabilization Fund	84.394A	11557001036902	1,095,167
ARRA Title XIV State Fiscal Stabilization Fund	84.394A	10557001036902	79,356
Total Program 84.394A			**1,174,523**
Total Passed Through State Department of Education			**2,409,987**
TOTAL U.S. DEPARTMENT OF EDUCATION			**2,409,987**
U.S. DEPARTMENT OF AGRICULTURE			
Pass-Through - State Department of Education:			
Child Nutrition Cluster:			
Non-Cash Assistance (Commodities):			
National School Lunch Program	10.555	036001A	63,319
Cash Assistance:			
School Breakfast Program	10.553	71401101	106,044
National School Lunch Program	10.555	71301101	307,894
TOTAL U.S. DEPARTMENT OF AGRICULTURE - CHILD NUTRITION CLUSTER			**477,257**
TOTAL EXPENDITURES OF FEDERAL AWARDS			**$ 3,085,108**

The accompanying notes are an integral part of this schedule.

BARBERS HILL INDEPENDENT SCHOOL DISTRICT

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
JUNE 30, 2011

Basis of Presentation:

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Barbers Hill Independent School District and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133 and *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the basic financial statements. Presented below is a reconciliation of federal revenues:

Total Expenditures of Federal Awards per Exhibit K-1	**$ 3,085,108**
Total Federal Revenues per Exhibit C-2	**$ 3,085,108**