

PRELIMINARY OFFICIAL STATEMENT DATED APRIL 29, 2010

Standard and Poor's Ratings Group: " "
See ("PERMANENT SCHOOL FUND GUARANTEE PROGRAM", AND
"OTHER INFORMATION – RATING") HEREIN

NEW ISSUE - Book-Entry-Only

In the opinion of Bond Counsel, interest on the Bonds is excludable from gross income for federal income tax purposes under existing law, subject to the matters described under "TAX MATTERS" herein, and is not includable in the alternative minimum taxable income of individuals or corporations. See "TAX MATTERS" for a discussion of the opinion of Bond Counsel.

The District has designated the Bonds as qualified tax exempt obligations. See QUALIFIED TAX-EXEMPT OBLIGATIONS."

\$11,039,595.20*
DIBOLL INDEPENDENT SCHOOL DISTRICT
(Angelina County, Texas)
UNLIMITED TAX SCHOOL BUILDING BONDS
SERIES 2010

Dated Date: June 1, 2010

Due: February 15, as shown on the inside cover page hereof

The Diboll Independent School District Unlimited Tax School Building Bonds, Series 2010 (the "Bonds") are issued in part as current interest bonds ("CIBs") and in part as premium capital appreciation bonds ("CABs"). The Bonds are issued pursuant to the Constitution and general laws of the State of Texas (the "State"), including particularly Chapter 45, Texas Education Code, as amended, an order adopted by the Board of Trustees of the Diboll Independent School District (the "District") authorizing the issuance of the Bonds (the "Order"), and an election held within the District on November 3, 2009, and are direct obligations of the Diboll Independent School District (the "District"), payable from a continuing direct annual ad valorem tax levied, without legal limitation as to rate or amount, on all taxable property located within the District, as provided by the "Order". (See "THE BONDS – Authority for Issuance").

Interest on the CIBs will accrue from June 1, 2010 (the "Dated Date"), and will be payable on August 15 and February 15 of each year until maturity or prior redemption, commencing August 15, 2010. See "THE BONDS – Optional Redemption". Interest on the CABs will accrete from the date they are initially delivered to the Underwriters (as defined herein), compounded semiannually on February 15 and August 15, commencing August 15, 2010, and will be payable only upon maturity. The CIBs will be issued in principal denominations of \$5,000 or any integral multiple thereof within a maturity. The CABs will be issued in denominations of \$5,000 of the total amount of principal, plus the initial premium, if any, and accrued interest payable upon maturity (the "Maturity Amount"), or any integral multiple thereof within a maturity. Principal of the CIBs and the Maturity Amount of the CABs will be payable by the Paying Agent/Registrar, initially Wells Fargo Bank, N.A., Austin, Texas (the "Paying Agent/Registrar"), upon presentation and surrender of the Bonds for payment. Interest accruing on the CIBs and the accreted/compounded interest on the CABs will be calculated on the basis of a 360-day year of twelve 30-day months. (See "THE BONDS—Description").

The definitive Bonds will be initially registered and delivered to Cede & Co., the nominee of the Depository Trust Company ("DTC") pursuant to the Book-Entry-Only System described herein. Beneficial ownership of the Bonds may be acquired in denominations of \$5,000 of principal or Maturity Amount, as applicable, or integral multiples thereof. **No physical delivery of the Bonds will be made to the beneficial owners thereof.** Principal, premium, if any, interest on the CIBs and the Maturity Amount of the CABs will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amount so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Bonds. (See "THE BONDS – Book-Entry-Only System").

The District has applied for and received conditional approval for the payment of the principal and interest of the Bonds to be guaranteed by the corpus of the Permanent School Fund of the State of Texas. (See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM").

Proceeds from the sale of the Bonds will be used for (1) the construction, acquisition and equipping of school buildings (2) the acquisition of necessary sites for school buildings in the District and (3) the payment of the costs of issuing the Bonds. (See "THE BONDS—Sources and Uses of Funds").

The CIBs maturing on and after February 15, 2020, are subject to optional redemption in whole or in part on February 15, 2019, or any date thereafter, at a price equal to the principal amount thereof, plus accrued interest to the date of redemption. The CABs are not subject to redemption prior to maturity. (See "THE BONDS—Optional Redemption").

SEE MATURITY SCHEDULE ON THE INSIDE COVER PAGE

The Bonds are offered for delivery when, as and if issued and received by the underwriters listed below (the "Underwriters") and will be subject to the approving opinion of the Attorney General of Texas and the approval of certain legal matters by Andrews Kurth LLP, Houston, Texas, Bond Counsel (see "APPENDIX C – FORM OF BOND COUNSEL'S OPINION"). Certain legal matters will be passed upon for the Underwriters by their Counsel, Petruska & Associates, A Professional Limited Liability Company, Dallas, Texas.

It is expected that the Bonds will be available for delivery through the facilities of The Depository Trust Company on or about June 8, 2010.

* Preliminary, subject to change.

Southwest Securities, Inc.

Raymond James

The Preliminary Official Statement and the information contained herein are subject to completion or amendment. These securities may not be sold, nor any offers to buy be accepted prior to the time the Official Statement is delivered in final form. Under no circumstances shall this Preliminary Official Statement constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of these securities in any jurisdiction in which such offer, solicitation, or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction.

MATURITY SCHEDULE

**DIBOLL INDEPENDENT SCHOOL DISTRICT
(Angelina County, Texas)**

\$11,039,595.20* UNLIMITED TAX SCHOOL BUILDING BONDS, SERIES 2010

\$10,985,000.00* Current Interest Bonds

<u>Maturity</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Initial</u>		<u>CUSIP No. (c)</u>	<u>Maturity</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Initial</u>		<u>CUSIP No. (c)</u>
			<u>Reoffering Yield (b)</u>						<u>Reoffering Yield (b)</u>		
2/15/2011	\$ 25,000	%	%	%	****	2/15/2033 (a)	\$ 795,000	%	%		
****	****	****	****	****	****	2/15/2034 (a)	830,000				
2/15/2027 (a)	645,000					2/15/2035 (a)	865,000				
****	****	****	****	****	****	2/15/2036 (a)	905,000				
2/15/2029 (a)	675,000					2/15/2037 (a)	945,000				
2/15/2030 (a)	700,000					2/15/2038 (a)	990,000				
2/15/2031 (a)	730,000					2/15/2039 (a)	1,035,000				
2/15/2032 (a)	760,000					2/15/2040 (a)	1,085,000				

(Interest to accrue from the Dated Date)

\$54,595.20* Capital Appreciation Bonds (d)

<u>Maturity</u>	<u>Principal</u>	<u>Yield to Maturity</u>	<u>Maturity Amount</u>	<u>Initial Offering</u>		<u>CUSIP No. (c)</u>
				<u>Price per \$5,000</u>	<u>in Maturity Amount</u>	
2/15/2028	\$ 54,595.20	%	\$	\$		

(Interest to accrete from the Date of Delivery)

* Preliminary, subject to change.

(a) The District reserves the right, at its option, to redeem CIBs having stated maturities on and after February 15, 2020, in whole or in part, in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2019, or any date thereafter, at the par value thereof plus accrued interest to the date of redemption. (See "THE BONDS – Optional Redemption")

(b) The initial yields at which Bonds are priced are established by and are the sole responsibility of the Underwriters and may be changed at any time at the discretion of the Underwriters.

(c) CUSIP numbers have been assigned to this issue by CUSIP Global Services managed by Standard & Poor's Financial Services LLC on behalf of the American Bankers Association and are included solely for the convenience of the purchasers of the Bonds. None of the District, the Financial Advisor, or the Underwriters shall be responsible for the selection or correctness of the CUSIP numbers set forth herein.

(d) The CABs are not subject to redemption prior to maturity.

DISTRICT OFFICIALS, STAFF AND CONSULTANTS

Board of Trustees

<u>Name</u>	<u>Title</u>	<u>Years of Service</u>	<u>Term Expires May</u>	<u>Occupation</u>
Trey L. Wilkerson	President	9	2011	Financial Advisor
Chuck Mann	Vice President	4	2011	Prison Guard
Andrea Swor	Secretary	4	2012	Business Owner
Ruben Esteves	Member	3	2010	Salesman
C. Lynn Pavlic	Member	12	2011	Comptroller
Kent Havard	Member	2	2010	Police Chief
Irvin McWilliams	Member	1	2012	Business Owner

Administrators

<u>Name</u>	<u>Title</u>	<u>Years in Position</u>	<u>Total Years in Similar Position</u>
Gary Martel	Superintendent	2	2
Kevin Mathis	Assistant Superintendent / CFO	2	7

Consultants and Advisors

Certified Public Accountant John R. Pechacek, C.P.A.
 Bellville, Texas

Bond Counsel Andrews Kurth LLP
 Houston, Texas

Financial Advisor Coastal Securities, Inc.
 Houston, Texas

USE OF INFORMATION IN OFFICIAL STATEMENT

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.

For purposes of compliance with Rule 15c2-12 of the Securities and Exchange Commission (the "Rule"), as amended, and in effect on the date hereof, 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 the Rule.

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 or the Underwriters. 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 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.

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

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.

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

TABLE OF CONTENTS

MATURITY SCHEDULE.....	ii		
DISTRICT OFFICIALS, STAFF AND CONSULTANTS.....	iii		
USE OF INFORMATION IN OFFICIAL STATEMENT.....	iv		
TABLE OF CONTENTS.....	v		
OFFICIAL STATEMENT SUMMARY.....	vi		
SELECTED FINANCIAL INFORMATION.....	vii		
INTRODUCTION.....	1		
THE BONDS.....	1		
YIELD ON CABS.....	2		
AUTHORITY FOR ISSUANCE.....	2		
SECURITY AND SOURCE OF PAYMENT.....	2		
ADDITIONAL INDEBTEDNESS.....	2		
OPTIONAL REDEMPTION.....	2		
NOTICE OF REDEMPTION.....	2		
DEFEASANCE.....	3		
BOOK-ENTRY-ONLY SYSTEM.....	3		
PAYING AGENT/REGISTRAR.....	5		
TRANSFER, EXCHANGE AND REGISTRATION.....	5		
RECORD DATE FOR INTEREST PAYMENT.....	5		
BONDHOLDERS' REMEDIES.....	6		
SOURCES AND USES OF FUNDS.....	6		
THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM.....	6		
HISTORY AND PURPOSE.....	7		
THE TOTAL RETURN CONSTITUTIONAL AMENDMENT.....	7		
MANAGEMENT AND ADMINISTRATION OF THE FUND.....	9		
THE GUARANTEE PROGRAM.....	10		
CAPACITY LIMITS FOR THE GUARANTEE PROGRAM.....	10		
RATINGS OF BONDS GUARANTEED UNDER THE GUARANTEE PROGRAM.....	11		
VALUATION OF THE PSF AND GUARANTEED BONDS.....	12		
DISCUSSION AND ANALYSIS PERTAINING TO FISCAL YEAR ENDED AUGUST 31, 2009.....	12		
OTHER EVENTS AND DISCLOSURES.....	13		
PSF CONTINUING DISCLOSURE UNDERTAKING.....	14		
ANNUAL REPORTS.....	14		
MATERIAL EVENT NOTICES.....	15		
AVAILABILITY OF INFORMATION.....	15		
LIMITATIONS AND AMENDMENTS.....	15		
COMPLIANCE WITH PRIOR UNDERTAKINGS.....	15		
SEC EXEMPTIVE RELIEF.....	15		
STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS.....	16		
LITIGATION RELATING TO THE TEXAS PUBLIC SCHOOL FINANCE SYSTEM.....	16		
FUNDING CHANGES IN RESPONSE WEST ORANGE-COVE II....	17		
POSSIBLE EFFECTS OF LITIGATION AND CHANGES IN LAW ON DISTRICT BONDS.....	17		
CURRENT PUBLIC SCHOOL FINANCE SYSTEM.....	17		
GENERAL.....	17		
STATE FUNDING FOR LOCAL SCHOOL DISTRICTS.....	18		
LOCAL REVENUE SERVICES - PROPERTY TAX AUTHORITY.....	19		
WEALTH TRANSFER PROVISIONS.....	20		
		POSSIBLE EFFECTS OF WEALTH TRANSFER PROVISIONS AND HBI ON THE DISTRICT'S FINANCIAL CONDITION.....	20
		AD VALOREM TAX PROCEDURES.....	21
		TAX CODE AND COUNTY-WIDE APPRAISAL DISTRICT.....	21
		PROPERTY SUBJECT TO TAXATION BY THE DISTRICT.....	21
		VALUATION OF PROPERTY FOR TAXATION.....	22
		RESIDENTIAL HOMESTEAD EXEMPTION.....	22
		DISTRICT AND TAXPAYER REMEDIES.....	22
		PUBLIC HEARING AND ROLLOVER TAX RATE.....	23
		LEVY AND COLLECTION OF TAXES.....	23
		DISTRICT'S RIGHTS IN THE EVENT OF TAX DELINQUENCIES.....	23
		PENALTIES AND INTEREST.....	24
		DISTRICT APPLICATION OF TAX CODE.....	24
		TAX RATE LIMITATIONS.....	25
		EMPLOYEES' BENEFIT PLANS.....	25
		THE DISTRICT.....	25
		ADMINISTRATION.....	25
		DISTRICT SCHOOL OPERATIONS.....	25
		FINANCIAL POLICIES.....	25
		INVESTMENTS.....	26
		LEGAL INVESTMENTS.....	26
		INVESTMENT POLICIES.....	26
		ADDITIONAL PROVISIONS.....	27
		CURRENT INVESTMENTS.....	27
		TAX MATTERS.....	27
		TAX TREATMENT OF ORIGINAL ISSUE DISCOUNT AND PREMIUM BONDS.....	28
		DISCOUNT BONDS.....	28
		PREMIUM BONDS.....	29
		QUALIFIED TAX EXEMPT OBLIGATIONS.....	29
		CONTINUING DISCLOSURE OF INFORMATION.....	29
		ANNUAL REPORTS.....	29
		MATERIAL EVENT NOTICES.....	30
		LIMITATIONS AND AMENDMENTS.....	30
		COMPLIANCE WITH PRIOR UNDERTAKINGS.....	30
		OTHER INFORMATION.....	30
		RATING.....	30
		NO LITIGATION CERTIFICATE.....	30
		REGISTRATION AND QUALIFICATION OF BONDS FOR SALE.....	30
		THE BONDS AS LEGAL INVESTMENTS IN TEXAS.....	31
		LEGAL MATTERS.....	31
		FINANCIAL ADVISOR.....	32
		UNDERWRITING.....	32
		MISCELLANEOUS.....	32
		FORWARD LOOKING STATEMENTS.....	32
		CONCLUDING STATEMENT.....	32
		SCHEDULE I	
		APPENDICES	
		INFORMATION REGARDING THE DISTRICT.....	A
		EXCEPTS FROM THE DISTRICT'S AUDITED FINANCIAL REPORT.....	B
		FORM OF BOND COUNSEL'S OPINION.....	C

OFFICIAL STATEMENT SUMMARY

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

- The District** Diboll Independent School District (the “District”) operates as an independent school district under the laws of the State of Texas. It is located in Angelina County, Texas. (See “THE DISTRICT”).
- The CIBs** The current interest bonds (the “CIBs”) are being issued in the principal amounts and mature on the dates set forth on the inside cover page hereof. The CIBs bear interest from June 1, 2010, at the rates per annum set forth on the inside cover hereof, which interest is payable each August 15 and February 15, commencing August 15, 2010, until maturity or prior redemption. (See “THE BONDS—Description”).
- The CABs** The premium capital appreciation bonds (the “CABs”) are being issued in Maturity Amounts (hereafter defined) and mature on the dates set forth on the inside cover page hereof. Interest on the CABs accretes from the date of delivery to the Underwriters and will be compounded February 15 and August 15 of each year, commencing August 15, 2010, and will be payable only at maturity (see “THE BONDS – Description”).
- Authority for Issuance** ... The Bonds are being issued pursuant to an order passed by the Board of Trustees of the District (the “Order”), the Constitution and general laws of the State of Texas, including particularly Chapter 45, Texas Education Code, as amended, and an election held in the District on November 3, 2009. (See “THE BONDS - Authority for Issuance”).
- Security for Bonds** Principal of and interest on the Bonds will be payable from the receipts of a continuing direct annual ad valorem tax levied, without limit as to rate or amount, on all taxable property within the District. (See “THE BONDS - Security and Source of Payment” and “TAX RATE LIMITATIONS”).
- Permanent School Fund Guarantee** The District has applied to the Texas Education Agency and has received conditional approval for the payment of the principal and interest of the Bonds to be guaranteed by the corpus of the Permanent School Fund of the State of Texas. (See “THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM”).
- Optional Redemption** The District reserves the right, at its option, to redeem the CIBs having stated maturities on and after February 15, 2020, in whole or in part, in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2019, or any date thereafter, at the par value thereof plus accrued interest from the most recent interest payment date to the date of redemption. The CABs are not subject to redemption prior to maturity. (See “THE BONDS – Optional Redemption”).
- Use of Proceeds** Proceeds from the sale of the Bonds will be used for (1) the construction, acquisition and equipping of school buildings (2) the acquisition of necessary sites for school buildings in the District, and (3) the payment of the costs of issuing the Bonds. (See “THE BONDS—Sources and Uses of Funds”).
- Tax Exemption** In the opinion of Bond Counsel, interest on the Bonds is excludable from gross income for federal income tax purposes under existing law, subject to the matters described under “TAX MATTERS” herein, and is not includable in the alternative minimum taxable income of individuals or corporations. See “TAX MATTERS” for a discussion of the opinion of Bond Counsel.
- Qualified Tax-Exempt Obligations** The District designated the Bonds as qualified tax-exempt obligations. See “QUALIFIED TAX-EXEMPT OBLIGATIONS”
- Rating** Standard & Poor’s Ratings Group (“S&P”) has assigned its municipal bond rating of “_____” to the Bonds by virtue of the guarantee of the Permanent School Fund of the State of Texas on the Bonds. (See “OTHER INFORMATION - Rating”, and “PERMANENT SCHOOL FUND GUARANTEE PROGRAM”).
- Book-Entry-Only System** The definitive Bonds will be initially registered and delivered only to Cede & Co., the nominee of DTC pursuant to the Book-Entry-Only System described herein. Beneficial ownership of the Bonds may be acquired in denominations of \$5,000 of principal or Maturity Amount, as applicable, or integral multiples thereof. No physical delivery of the Bonds will be made to the beneficial owners thereof. Principal of, premium, if any, and interest on the CIBs and Maturity Amount of the CABs will be payable by the Paying Agent/Registrar to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Bonds. (See “THE BONDS - Book-Entry-Only System”).
- Payment Record** The District has never defaulted in the payment of its tax-supported debt.

SELECTED FINANCIAL INFORMATION

Fiscal Year Ended 31-Aug	Estimated District Population ^(a)	Taxable Assessed Valuation ^(b)	Per Capita Taxable Assessed Valuation	Ad Valorem Tax-Supported Debt	Per Capita Tax-Supported Tax Debt	Ratio Tax Debt to Assessed Valuation	Tax Year
2004	9,252	\$ 232,981,640	\$ 25,181.76	\$ 2,630,360	\$ 284.30	1.13%	2003
2005	9,308	254,298,174	27,320.39	4,406,973	473.46	1.73%	2004
2006	9,348	256,690,811	27,459.44	4,047,193	432.95	1.58%	2005
2007	9,025	251,800,866	27,900.37	3,684,204	408.22	1.46%	2006
2008	8,769	269,541,472	30,737.99	3,381,932	385.67	1.25%	2007
2009	8,964	269,180,359	30,029.04	3,037,039	338.80	1.13%	2008
2010	8,964	263,921,662	29,442.40	13,728,030 ^(c)	1,531.46 ^(c)	5.20% ^(c)	2009

^(a) Population estimates obtained from Texas Municipal Reports.

^(b) Net of exemptions. Assessed valuations do not include adjustments in supplemental rolls made after the end of each fiscal year.

^(c) Includes the Bonds. Preliminary, subject to change.

General Fund Consolidated Statement Summary

	2008	2007	2006	2005	2004
Beginning Balance	\$ 2,819,904	\$ 3,634,631	\$ 4,361,893	\$ 6,705,317	\$ 6,138,109
Total Revenue	12,700,797	12,697,319	12,542,625	12,900,542	12,654,959
Total Expenditures	12,798,694	13,358,196	13,269,887	15,197,437	12,087,751
Net Other Resources (Uses)	-	(501,548)	-	(46,529)	-
Ending Balance	\$ 2,722,007	\$ 2,472,206	\$ 3,634,631	\$ 4,361,893	\$ 6,705,317

For additional information regarding the District, please contact:

Gary Martel
 Superintendent
 Diboll ISD
 215 N. Temple Drive
 Diboll, Texas 75941
 Telephone (936) 829-6108

Kevin Mathis
 Assistant Superintendent / CFO
 Diboll ISD
 215 N. Temple Drive
 Diboll, Texas 75941
 Telephone (936) 829-6106

Lewis A. Wilks
 Financial Advisor
 Coastal Securities, Inc.
 5555 San Felipe, Suite 2200
 Houston, Texas 77056
 Telephone (713) 435-4336
 Facsimile (713) 435-4448

DIBOLL INDEPENDENT SCHOOL DISTRICT
(Angelina County, Texas)

\$11,039,595.20*
UNLIMITED TAX SCHOOL BUILDING BONDS
SERIES 2010

INTRODUCTION

This Official Statement, including the Appendices hereto, provides certain information regarding the issuance of the Diboll Independent School District (the "District") the Unlimited Tax School Building Bonds, Series 2010 (the "Bonds"). Except as otherwise indicated herein, capitalized terms used in this Official Statement have the same meanings assigned to such terms in the order (the "Order") adopted by the Board of Trustees of the District authorizing the issuance of the Bonds.

There follows in this Official Statement descriptions of the Bonds and certain information regarding 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 from the Financial Advisor, Coastal Securities, Inc., Houston, Texas by electronic mail or upon payment of reasonable handling, mailing, and delivery charges.

This Official Statement speaks only as to its date, and the information contained herein is subject to change. Copies of the Final Official Statement pertaining to the Bonds will be deposited with the Municipal Securities Rulemaking Board, 1900 Duke Street, Suite 600, Alexandria, Virginia 22314. See "CONTINUING DISCLOSURE OF INFORMATION" for a description of the District's undertaking to provide certain information on a continuing basis.

THE BONDS

The Bonds shall be dated June 1, 2010, and will be issued in part as current interest bonds ("CIBs") and in part as premium capital appreciation bonds ("CABs"). Interest accruing on the CIBs and the accreted/compounded interest on the CABs will be calculated on the basis of a 360-day year of twelve 30-day months. The paying agent and transfer agent (the "Paying Agent/Registrar") for the Bonds is initially Wells Fargo Bank, N.A., Austin, Texas.

Initially, the Bonds will be registered and delivered only to Cede & Co., the nominee of The Depository Trust Company ("DTC") pursuant to the Book-Entry-Only System described below. No physical delivery of the bonds will be made to the beneficial owners. Principal and Maturity Amount of the Bonds at maturity or upon a prior redemption date (with respect to the CIBs), and interest on the CIBs will be payable by the Paying Agent/Registrar to Cede & Co., which will distribute the amounts paid to the participating members of DTC for subsequent payment to the beneficial owners of the Bonds. See "BOOK-ENTRY-ONLY SYSTEM" for a more complete description of such system.

The definitive Bonds will be issued only in fully registered form in any integral multiple of \$5,000 of principal amount or Maturity Amount (hereinafter defined) for any one maturity and will be initially registered and delivered only to Cede & Co., the nominee of The Depository Trust Company ("DTC") pursuant to the Book-Entry-Only System described herein. **No physical delivery of the Bonds will be made to the beneficial owners thereof.** Principal of, premium, if any, and accrued interest on the CIBs and the Maturity Amount of the CABs will be payable by the Paying Agent/Registrar, initially Wells Fargo Bank, N.A., Austin, Texas (the "Paying Agent/Registrar"), to Cede & Co., which will make distribution of the amounts so paid to the participating members of DTC for subsequent payment to the beneficial owners of the Bonds. See "THE BONDS - Book-Entry-Only System" herein.

CIBs. The CIBs are to mature on the dates and in the principal amounts shown on page ii hereof. The CIBs will each be issued as fully registered obligations in principal denominations of \$5,000 or any integral multiple thereof within a maturity. Interest on the CIBs will accrue from June 1, 2010, at the interest rates shown on page ii hereof and such interest shall be payable to the registered owners thereof on August 15, 2010, and semiannually thereafter on February 15 and August 15 in each year, until maturity or prior redemption.

* Preliminary, subject to change.

Interest on the CIBs will be payable to the registered owner whose name appears on the bond registration books of the Paying Agent/Registrar at the close of business on the Record Date (hereinafter defined) and such accrued interest will be paid by (i) check sent United States mail, first class, postage prepaid, to the address of the registered owner appearing on such registration books of the Paying Agent/Registrar or (ii) such other method, acceptable to the Paying Agent/Registrar, requested by, and at the risk and expense of, the registered owner. See "Transfer, Exchange and Registration" and "Record Date for Interest Payment." The principal of the CIBs at maturity or on a prior redemption date will be payable only upon presentation of such Bonds at the designated office of the Paying Agent/Registrar.

CABs. The CABs will mature on the dates and in the Maturity Amounts set forth on page ii hereof. The CABs will be issued as fully registered obligations in Maturity Amounts of \$5,000 or any integral multiple thereof within a maturity. The "Maturity Amount" for the CABs represents the total amount of principal, plus the initial premium, if any, paid therefore, and the accreted/compounded interest thereon at maturity. The CABs will be initially priced by discounting the Maturity Amount to the issue price paid therefore by the initial purchaser (being the original principal amount shown on page ii and any premium paid therefore) and using the applicable approximately yield shown on page ii of this Official Statement as the discount rate and providing for such Maturity Amount to be discounted semiannually on February 15 and August 15 in each year, commencing August 15, 2010. The Maturity Amount of the CABs will be payable only at maturity. A table of Accreted Values of the CABs per \$5,000 Maturity Amount based on (i) the initial offering prices and (ii) the approximate initial yields set forth on page ii of this Official Statement is presented in Schedule I attached hereto, and such table of Accreted Values is provided for informational purposes only and may not reflect the prices or yields for the CABs in the secondary market. The Maturity Amount of the CABs will be payable only upon presentation of such Bonds at the designated office of the Paying Agent/Registrar.

Yield on CABs

The approximate yields of the CABs as set forth on the inside cover page of this Official Statement are the approximate yields based upon the initial offering prices therefor set forth on the inside cover page of this Official Statement. Such offering price includes the principal amount of such CABs plus premium, if any, equal to the amount by which such offering price exceeds the principal amount of such CABs. Because of such premium, the approximate offering yield on the CABs is lower than the bond interest rates thereon. The yield on the CABs to a particular purchaser may differ depending upon the price paid by that purchaser. For various reasons, securities that do not pay interest periodically, such as the CABs, have traditionally experienced greater price fluctuations in the secondary market than securities that pay interest on a periodic basis.

Authority for Issuance

The Bonds are issued pursuant to the Constitution and laws of the State of Texas, including particularly Chapter 45, Texas Education Code, as amended, the Order and an election held in the District on November 3, 2009 (the "Election"). The Bonds constitute the second installment of the total \$22,500,000 of unlimited tax school building bonds approved at the Election. After the issuance of the Bonds, the District will have \$5,730,000 authorized but unissued bonds.

Security and Source of Payment

The Bonds constitute direct obligations of the District, payable as to principal and interest from a continuing direct annual ad valorem tax levied, without limit as to rate or amount, against all taxable property within the District. Additionally, the payment of principal and interest on the Bonds is expected to be guaranteed by the Permanent School Fund Guarantee Program of Texas. See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" herein.

Additional Indebtedness

The District plans to issue \$5,730,000 Unlimited Tax Qualified School Construction Bonds, Taxable Series 2010A (Direct Pay to Issuer) before December 31, 2010.

Optional Redemption

The District reserves the right, at its option, to redeem CIBs having stated maturities on and after February 15, 2020, in whole or in part in principal amounts of \$5,000 or any integral multiple thereof, on February 15, 2019, or any date thereafter, at the par value thereof plus accrued interest from the most recent interest payment date 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. The CABs are not subject to redemption prior to maturity.

Notice of Redemption

Not less than 30 days prior to a redemption date for the CIBs, the Paying Agent/Registrar shall cause a notice of redemption to be sent by United States mail, first class, postage prepaid, to the registered owners of the CIBs to be redeemed, in whole or in part at the address of the registered owner appearing on the registration books of the Paying Agent/Registrar.

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

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, shall not affect the validity of the redemption of the CIBs called for redemption or any other action premised on any such notice. Redemption of portions of the CIBs by the District will reduce the outstanding principal amount of such CIBs held by DTC.

In such an event, DTC may implement, through its Book-Entry-Only System, a redemption of such CIBs 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 CIBs from the beneficial owners.

Any such selection of CIBs to be redeemed will not be governed by the 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 CIBs or the providing of notice to DTC participants, indirect participants, or beneficial owners of the selection of portions of the CIBs selected for redemption (see "THE BONDS – Book-Entry Only System").

Defeasance

The Order provides for the defeasance of the Bonds in any manner now or hereafter permitted by law, including when payment of the principal amount plus accrued interest on the Bonds, to their due date (whether such due date be by reason of maturity or otherwise), is provided by irrevocably depositing with a paying agent or other authorized entity, in trust (1) money sufficient to make such payment or (2) Defeasance Securities scheduled to mature as to principal and interest in such amounts and at such times to insure the availability, without reinvestment, of an amount sufficient to make such payment, and all necessary and proper fees, compensation and expenses of the paying agent/registrar for the Bonds. The Order provides that "Defeasance Securities" means (a) direct, noncallable obligations of the United States of America, including obligations that are unconditionally guaranteed by the United States of America, (b) noncallable obligations of an agency or instrumentality of the United States of America, including obligations that are unconditionally guaranteed or insured by the agency or instrumentality and that are rated as to investment quality by a nationally recognized investment rating firm not less than AAA or its equivalent, and (c) noncallable obligations of a state or an agency or a county, municipality, or other political subdivision of a state that have been refunded and that are rated as to investment quality by a nationally recognized investment rating firm not less than AAA or its equivalent. The District has additionally reserved the right, subject to satisfying the requirements of (1) and (2) above, to substitute other Defeasance Securities for the Defeasance Securities originally deposited, to reinvest the uninvested money on deposit for such defeasance and to withdraw for the benefit of the District moneys in excess of the amount required for such defeasance. Upon such deposit as described above, such Bonds shall no longer be regarded to be outstanding obligations for purposes of applying any limitation on indebtedness or for purposes of taxation. Provided, however, the District has reserved the option, to be exercised at the time of the defeasance of the Bonds, to call for redemption, at an earlier date, those Bonds which have been defeased to their maturity date, if the District: (i) in the proceedings providing for the firm banking and financial arrangements, expressly reserves the right to call such Bonds for redemption; (ii) gives notice of the reservation of that right to the owners of such Bonds immediately following the making of the firm banking and financial arrangements; and (iii) directs that notice of the reservation be included in any redemption notices that it authorizes.

Book-Entry-Only System

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

The District cannot and does not give any assurance that (1) DTC will distribute payment 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

Securities and Exchange Commission, and the current procedures of DTC to be followed in dealing with DTC Participants are on file with DTC.

DTC will act as securities depository for the Bonds. The Bonds will be issued as fully-registered securities 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 certificate will be issued for the Bonds, in the aggregate principal amount of such issue, 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 a 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 companies that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: "AAA." The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com and www.dtc.org.

Purchases of 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 confirmation 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 physical 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 Paying Agent/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 CABs within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Bonds unless authorized by a Direct Participant in accordance with DTC's 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).

Redemption proceeds, principal, and interest payments on the CIBs and the Maturity Amount of the CABs 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 nor its nominee, the Paying Agent/Registrar, or the District, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, principal, and interest payments on the CIBs and the Maturity Amount of the CABs 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 reimbursement 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 CIBs 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. Discontinuance by the District of use of the system of book-entry transfers through DTC may require compliance with DTC operational arrangements.

The District may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). Discontinuance of the system of book-entry transfers by the District may require the consent of Participants under DTC's Operational Arrangements. In that event, Bond certificates will be printed and delivered.

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 or the Underwriters take 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 Participant acquires an interest in the Bonds, but (i) all rights of ownership must be exercised through DTC and the Book-Entry-Only System, and (ii) except as described above, notices that are to be given to registered owners under the Order will be given only to DTC.

Paying Agent/Registrar

The initial Paying Agent/Registrar is Wells Fargo Bank, N.A., Austin, Texas. In the Order, the District retains the right to replace the Paying Agent/Registrar. The District covenants to maintain and provide a Paying Agent/Registrar at all times while any Bonds are outstanding and any successor Paying Agent/Registrar shall be a commercial bank or trust company organized under the laws of the United States or any state and duly qualified and legally authorized to serve as and perform the duties and services of Paying Agent/Registrar for the Bonds. Upon any change in the Paying Agent/Registrar for the Bonds, the District agrees to promptly cause a written notice thereof to be sent to each registered owner of the Bonds by United States mail, first class, postage prepaid, which notice shall also give the address of the new Paying Agent/Registrar.

Transfer, Exchange and Registration

In the event the Book-Entry-Only System should be discontinued, the Bonds may be transferred and exchanged on the registration books of the Paying Agent/Registrar only upon presentation and surrender thereof to the Paying Agent/Registrar or its principal payment office and such transfer or exchange shall be without expenses or service charge to the registered owner, except for any tax or other governmental charges required to be paid with respect to such registration, exchange and transfer. Bonds may be assigned by the execution of an assignment form on the 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 or Bonds being transferred or exchanged, at the principal payment office of the Paying Agent/Registrar, or sent by the United States mail, first class, postage prepaid, to the new registered owner or his designee. To the extent possible, new Bonds issued in an exchange or transfer of Bonds will be delivered to the registered owner or assignee of the registered owner in not more than three business days after the receipt of the Bonds to be canceled, and the written instrument of transfer or request for exchange duly executed by the registered owner or his duly authorized agent, in form satisfactory to the Paying Agent/Registrar. New Bonds registered and delivered in an exchange or transfer shall be in any integral multiple of \$5,000 of principal or Maturity Amount, as applicable, for any one maturity and for a like aggregate principal amount or Maturity Amount as the Bond or Bonds surrendered for exchange or transfer. See "THE BONDS - Book-Entry-Only System" herein defined for a description of the system to be utilized initially in regard to ownership and transferability of the Bonds.

Record Date for Interest Payment

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

Bondholders' Remedies

The Order does not establish specific events of default with respect to the Bonds or provide for the appointment of a trustee to represent the interests of the bondholders upon any failure of the District to perform in accordance with the terms of the Order, or upon any other condition. If the District defaults in any payment due on the Bonds, and if the State of Texas fails to honor the Permanent School Fund Guarantee as hereinafter discussed, or if the District defaults in the observance or performance of any of the covenants, conditions, or obligations set forth in the Order, any registered owner is entitled to seek a writ of mandamus or mandatory injunction from a court of proper jurisdiction to compel the District to levy, assess and collect an annual ad valorem tax sufficient to pay principal or Maturity Amount of and interest on the Bonds as they become due or to perform other material covenants, conditions or obligations contained in the Order, as well as, for the Bonds, enforce rights of payment under the Permanent School Fund Guarantee. In general, Texas courts have held that a writ of mandamus may be issued to require a public official to perform legally imposed ministerial duties necessary for the performance of a valid contract; and, Texas law provides that, following their approval by the Attorney General and issuance, the Bonds are valid and binding obligations for all purposes according to their terms. However, the enforcement of any such remedy may be difficult and time consuming and a registered owner could be required to enforce such remedy on a periodic basis. Such rights are in addition to any other rights the registered owners of the Bonds may be provided by the laws of the State of Texas with respect to the Bonds. Under Texas law there is no right to the acceleration of maturity of the Bonds upon the failure of the District to observe any covenant under the Order. A registered owner of Bonds could file suit against the District if a default occurred in the payment of principal or Maturity Amount of or interest on any such Bonds; however, a suit for monetary damages could be vulnerable to the defense of sovereign immunity and any judgment could not be satisfied by execution against any property of the District.

The District is also 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 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. 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.

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. Also see "THE BONDS - Book-Entry-Only System" herein for a description of the duties of DTC with regard to ownership of Bonds.

Initially, the only registered owner of the Bonds will be The Depository Trust Company. See "THE BONDS - Book-Entry-Only System" herein.

Sources and Uses of Funds

Proceeds from the sale of the Bonds will be applied in the amounts shown below.

Sources of Funds

Par Amount of the CIBs	\$
Par Amount of the CABs	
Accrued Interest on the CIBs	
Net Premium	
Total	\$

Uses of Funds

Deposit to Construction Fund	\$
Costs of Issuance	
Underwriters' Discount	
Deposit to Debt Service Fund (Accrued Interest & Additional Proceeds)	
Total	\$

THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM

This disclosure statement provides information relating to the program administered by the Texas Education Agency (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 2009, distributions to the ASF amounted to \$163.07 per student and the total amount distributed to the ASF was \$716.54 million.

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, 2009, and for a description of the financial results of the PSF for the year ended August 31, 2009, the most recent year for which audited financial information regarding the Fund is available. The 2009 Annual Report is incorporated herein and made a part hereof for all purposes, but the 2009 Annual Report speaks only as of its date and the TEA has not obligated itself to update the 2009 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, AMEX) 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, 2009, 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 (see "Other Events and Disclosures").

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. The SLB has advised the SBOE that it anticipates that it will make similar \$100 million releases to the PSF in the 2010 and 2011 fiscal years. In November, 2008, 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, and in January 2009, the SBOE reconfirmed the 2.5% Distribution Rate, which was expected to produce transfers of approximately \$1.15 billion during the 2010-11 biennium, but also adopted a contingency plan in case the Distribution Rate should temporarily exceed the Ten Year Total Return during the 2010-2011 biennium. In November 2009, in accordance with GA-0707, and due to one of the constitutional measurements that limit transfers from the PSF, the SBOE determined that the authorized transfer amount for fiscal year 2010 would be limited to \$60.7 million. Depending on the value of the PSF and market conditions, the 2011 transfer could be sufficient to reach the full \$1.15 billion for the biennium, provided that the increase is in accordance with the Total Return Constitutional Amendment and a calculation to be made in 2011 of historic Fund returns. 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, the investment of the Fund has 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 and in July 2006, which have significantly altered the asset allocations of the Fund. In February 2004, the SBOE adopted a new asset allocation for the Fund, which 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 the first quarter of fiscal year 2006, a new investment advisor for the Fund was engaged by the SBOE and tasked with recommending a new asset allocation mix for the Fund. In July 2006, the SBOE adopted a revised asset allocation (the "2006 Asset Allocation Policy"), and the Investment Policy was modified in accordance with the 2006 Asset Allocation Policy. The 2006 Asset Allocation Policy included an equity allocation, including both domestic and foreign equity portfolios, of 53%; a fixed income allocation of 19%; and an alternative asset allocation, which includes real estate, real return, absolute return and private equity components, totaling 28% of the Fund's asset target. The Fund's investment policy provides for minimum and maximum ranges among the components of each of the three general asset classifications. In July 2008, the SBOE reapproved the 2006 Asset Allocation Policy (hereinafter, the "2008 Asset Allocation Policy"). In August 2009, the SBOE engaged a new investment advisor.

The Fund's investment advisor is tasked with advising the SBOE with respect to the implementation of the 2008 Asset Allocation Policy, including the timing and manner of the selection of any external managers and other consultants. For a variety of reasons, including the requirement that the SBOE obtain additional appropriations from the Legislature to pay administrative costs associated with certain types of investments included in the 2008 Asset Allocation Policy, the 2008 Asset Allocation Policy is being implemented in phases. At August 31, 2009, based on unaudited records, the Fund was invested as follows: 67.40% in equity investments; 21.87% in fixed income investments; 10.70% in alternative assets; and 0.03% in cash.

In accordance with the Texas Constitution, the SBOE views the PSF as a perpetual institution. Consistent with its perpetual nature, the PSF 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. Moreover, while the SBOE may continue to change allocations within the various asset categories of the investment portfolios, and the 2008 Asset Allocation Policy includes an allotment for a portion of Fund assets to investment classes other than fixed income and equities, including hedge funds and real estate and other alternative asset classes, it is assumed that the new distribution formula will result in fewer large-scale reallocations of Fund assets than have occurred in prior years as the SBOE modified Fund asset allocations on a regular basis to produce income for distribution in light of changes in the financial markets.

Notwithstanding the assumption that asset allocations for the Fund will be more consistent after the changes made to implement the Total Return Constitutional Amendment have occurred, 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.

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 the fiduciary standards, and to provide transactional advice in connection with the investment of Fund assets in non-traditional investments.

Prior to June 1995, the PSF was invested exclusively by the internal staff of the TEA's Investments Office, under the direction of the Executive Administrator of the Fund. The portion of the Fund that is managed by external managers declined from 39% at August 31, 2002 to 26.46% at August 31, 2008, in large part due to legislative appropriations riders that reduced the appropriation for the administrative costs of managing the Fund during that period, including, in particular, the payment of fees of external managers. As the TEA has implemented the 2008 Asset Allocation in a manner outlined in GA-0293, the portion of the Fund that is administered by external managers has begun to increase, in large part due to changes in the fair market value of the various asset classes, and at August 31, 2009 29.87% of the Fund was managed by external managers.

The Guarantee Program

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, as amended (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. At present, no new guarantees are being authorized by TEA under the Guarantee Program. See "Capacity Limits for the Guarantee Program."

In the event of default, holders of guarantee 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. Effective September 1, 2009, 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 may 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.

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 \$23,463,749,653 (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. In 2010, the SBOE is expected to consider a variety of issues pertaining to the administration of the Guarantee Program, which issues arise as a result of the higher IRS Limit established by the IRS Notice. Among those issues will be the amount of the State Law Capacity to be established in accordance with SB 389. For a variety of reasons, including the need for the SBOE to consider new Guarantee Program regulations and State law public notice provisions that affect the timing of the implementation of SBOE actions, the decision of the SBOE with respect to the new State Law Capacity may not occur until mid-2010. However, as a result of the increase in cost value of the Fund's assets and the issuance of refunding bonds by school districts since the closure of the Guarantee Program in March 2009, the State Law Capacity has increased to a sufficient level under the current capacity multiplier to provide bond guarantees for at least part of 2010. See "Valuation of the PSF and Guaranteed Bonds," below.

Since July 1991, when the SBOE amended the regulations that govern the Guarantee Program 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, which reflects the trend of growth of guaranteed bonds for the last five fiscal years. The SBOE has modified its regulations that govern access to the Guarantee Program in recent years, most recently in January 2009. Generally, the regulations limit Guarantee Program guarantees to certain types of 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 with less than \$1,650 of annual debt service per student in average daily attendance. 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". Regulations adopted by the SBOE in January 2009 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. Since January 2009, the Capacity Reserve has been set at 8%. Program regulations provide that subject to the 5% minimum Capacity Reserve, 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 regulations are codified in the Texas Administrative Code at 19 TAC sections 33.65 et seq., and are available on the TEA web site 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, 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). For the years ending on and after August 31, 1998, the State Auditor has separately audited the financial statements of the PSF. The TEA has filed the audited annual report of the PSF for the year ended August 31, 2009, with the MSRB. The 2009 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, a division of The McGraw-Hill Companies, Inc., and Fitch Ratings rate bonds guaranteed by the PSF "Aaa," "AAA" and "AAA," respectively. Not all issuers 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⁾
2005	\$18,497,507,739	\$25,994,480,027
2006	19,359,570,146	26,537,687,968
2007	21,234,323,093	29,251,882,931
2008	22,926,299,922	29,336,248,611
2009	23,117,052,793 ⁽²⁾	25,443,104,623 ⁽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, 2009, land, external real estate investments and mineral assets managed by the SLB had book values of approximately \$471.4 million, \$979.9 million, and \$13.4 million, respectively, and market values of approximately \$817.3 million, \$622.8 million, and \$2.628 billion, respectively.

⁽²⁾ At December 31, 2009, the PSF had a book value of \$23,493,121,292 and a market value of \$27,844,707,983 (in each case, based on unaudited data).

Permanent School Fund Guaranteed Bonds	
At 8/31	Principal Amount ⁽¹⁾
2005	\$35,230,425,201
2006	37,793,429,328
2007	44,856,621,419
2008	49,860,572,025
2009 ⁽²⁾	50,032,724,439

⁽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⁾ At December 31, 2009, there were \$49,727,788,715 of bonds guaranteed under the Guarantee Program and the capacity of the Guarantee Program was \$58,732,803,231 (in each case based on unaudited data). Such capacity figure includes the Reserve Capacity.

Discussion and Analysis Pertaining to Fiscal Year Ended August 31, 2009

The following discussion is derived from the Annual Report for the year ended August 31, 2009, 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, 2009, 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.

At the end of fiscal 2009, the total Fund balance was \$22.6 billion and includes a restatement of beginning Fund balance by \$197 million, resulting from the implementation of GASB Statement 52, *Land and Other Real Estate Held as Investments by Endowments*. Including the result of the restatement, Fund balance decreased \$2.6 billion from the prior year. 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 -8.47%, -0.63%, 4.35% and 3.67% 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 -17.63%, -0.24%, and 4.00% 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, 2009, the PSF(SBOE) portion of the Fund had diversified into emerging market international equities and absolute return funds. Searches for real estate and private equity advisors are underway and other asset classes such as 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 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. During fiscal year 2009, the SLB made capital commitments to four externally managed real assets investment funds in a total amount of \$200 million. At August 31, 2009, the SLB had approved total capital commitments of \$1.9 billion to thirty-three funds, of which \$920 million remains unfunded.

The PSF(SBOE)'s investment in equity securities experienced a return of -16.68% during the fiscal year ended August 31, 2009. The PSF(SBOE)'s investment in fixed income securities produced a return of 10.20% during the fiscal year and absolute return investments yielded a return of -4.86%. Combined, all PSF(SBOE) asset classes produced an investment return of -8.47% for the fiscal year ended August 31, 2009, outperforming the target index by approximately 17 basis points. All PSF(SLB) real assets (including cash) returned -17.63% for the fiscal year ending August 31, 2009.

For fiscal year 2009, total revenues, inclusive of unrealized gains and losses and net of security lending rebates and fees, continued to decline, totaling negative \$1.98 billion by the end of the year. This decline is primarily attributable to the fact that domestic and international securities markets were lower in all sectors in fiscal year 2009 and the fair market valuations of the Fund's assets experienced declines commensurate with market conditions. In fiscal year 2009, 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. Total operating expenditures, net of security lending rebates and fees, decreased 29.3% for the fiscal year ending August 31, 2009. 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 2008 and 2009, this distribution to the ASF totaled \$716.54 million and \$716.5 million, respectively.

At the end of the 2009 fiscal year, PSF assets guaranteed \$50.03 billion in bonds issued by 781 local school districts. Since its inception in 1983, the Fund has guaranteed 4,050 school district bond issues totaling \$85.9 billion in principal amount. During the 2009 fiscal year, the number of outstanding issues guaranteed under the Guarantee Program decreased by 65, or -2.5%. The dollar amount of guaranteed school bond issues outstanding increased by \$172.1 million or 0.3%. The guarantee capacity of the Fund increased by \$445.7 million, or 0.8%, during fiscal year 2009.

Other Events and Disclosures

In November 2008 and January 2009, the Chairman of the SBOE submitted requests to the Attorney General for a legal opinion relating to certain questions pertaining to the Ten Year Total Return and the Distribution Rate. In April 2009, the Attorney General issued GA-0707 in response to the Chairman's questions. The Attorney General advised as follows: (1) certain key terms used in the Total Return Constitutional Amendment, including "investment assets" and "total return" are undefined in State law and therefore the SBOE, relying upon its fiduciary obligations and industry standards, "must, in the first instance" determine the methodology to calculate the Fund's total return; (2) the methodology currently used by the SBOE to calculate total return – net appreciation or decline in value of the investment assets, plus income – appears to be consistent with common financial industry usage and would likely be held reasonable by a court; (3) the Ten Year Total Return should be calculated on an annual basis; (4) State law is completely silent as to any remedy concerning an excess transfer from the PSF to the ASF and absent further legislative guidance, no advice could be rendered with regard to the possibility that if after final or audited numbers become available it is determined that any part of a transfer made to the ASF from the PSF exceeded the Ten Year Total Return; and (5) a contingency plan adopted by the SBOE, such as the one adopted in January 2009, 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 that in no event may the amount distributed from the Fund in a fiscal year exceed 6% of the average of the market value of the Fund.

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 August 2008. 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.

For the 2008-2009 biennium, the SBOE requested an additional appropriation of approximately \$18 million to be used for the implementation of the 2008 Asset Allocation Policy. Such amount was requested in addition to a general operating appropriation for 2008-2009 of \$14 million. The 2007 Legislature appropriated \$9 million of the requested 2008-2009 additional appropriation for external management services, and a \$14 million operating appropriation. For the 2010-2011 biennium, the SBOE made an exceptional item request of approximately \$12.5 million to fund costs of implementing the 2008 Asset Allocation Policy, but the exceptional item was not funded. The Legislature provided a total appropriation of \$23.2 million for the general administration of the Fund for the 2010-2011 biennium. While funds were not appropriated in the 2009 Legislature to implement the 2008 Asset Allocation Policy, Fund management is of the view that there are sufficient resources available to continue the phased implementation of new alternative asset allocations during the 2010-2011 biennium. In accordance with HB 3699, the SLB approved a resolution on August 7, 2007, to begin depositing revenues previously deposited with the PSF into the Real Estate Account, commencing September 1, 2007. Also on August 7, 2007, July 23, 2008, and August 6, 2009, the SLB adopted resolutions to make four quarterly payments of \$25,000,000 during fiscal years 2008, 2009 and 2010, respectively, from the Real Estate Account to the SBOE for investment, which action was taken to honor a SLB commitment to the Fund that was made prior to the enactment of HB 3699.

As of August 31, 2009, 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.

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 H of the TEA Investment Procedure Manual, which relates to the Guarantee Program. 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. Under the 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. The TEA will provide notice of any of the following events with respect to the Guarantee Program, if such event is material within the meaning of the federal securities laws: (1) principal and interest payment delinquencies; (2) non-payment related defaults; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions or events affecting the tax-exempt status of the Guarantee Program; (7) modifications to rights of holders of Bonds guaranteed by the Guarantee Program; (8) Bond calls; (9) defeasances; (10) release, substitution, or sale of property securing repayment of Bonds guaranteed by the Guarantee Program; and (11) rating changes. (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, or early redemption.) 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.

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 tax rate (the “M&O Tax”) 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 “[t]he 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

"[e]fficiency 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.

Possible Effects of Litigation and Changes in Law on District Bonds

The Reform Legislation did not alter the provisions of Chapter 45, Texas Education Code, as amended, that authorizes districts to secure their bonds by pledging the receipts of an unlimited ad valorem debt service tax as security for payment of such bonds. Reference is made, in particular, to the information under the heading "THE BONDS – Security and Source of Payment" 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 would be adversely affected by any such litigation or legislation. See "CURRENT PUBLIC SCHOOL FINANCE SYSTEM."

CURRENT PUBLIC SCHOOL FINANCE SYSTEM

General

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 session of the 81st Texas Legislature (the "2009 Regular 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.

The Reform Legislation, which generally became effective at the beginning of the 2006-07 fiscal year of each district, made substantive changes to the manner in which the Finance System is funded, but did not modify the basic structure of the Finance System. The changes to the manner in which the Finance System is funded were intended to reduce local M&O Tax rates by one third over two years, with M&O Tax levies declining by approximately 11% in fiscal year 2006-07 and approximately another 22% in fiscal year 2007-08, subject to local referenda that may increase local M&O Tax levies, thus offsetting a part of the compression in local M&O Tax levies (see "AD VALOREM TAX PROCEDURES – Tax Rate Limitations"). Additional State funding needed to offset local tax rate reductions must be generated by the modified State franchise, motor vehicle and tobacco taxes or any other revenue source appropriated by the Legislature. The Legislative Budget Board projected that the Reform Legislation would be underfunded from the Reform Legislation revenue sources by a cumulative amount of \$25 billion over fiscal years 2006-07 through 2010-11, however State surpluses have been appropriated to offset the revenue shortfall in fiscal year 2006-07 and for the 2008-09 and 2010-11 State biennia.

Under the Finance System, as modified during the 2009 Regular Legislative Session, a school district that imposes an M&O Tax at least equal to the product of the "state compression percentage" (as defined below) multiplied by the district's 2005-06 M&O Tax rate is entitled to at least the amount of State funding necessary to provide the district with the sum of (A) the amount of State and local revenue per weighted average daily attendance ("WADA") to which the school district would be entitled for the 2009-10 school year as calculated under the law as it existed on January 1, 2009, (B) an additional \$120 per WADA, (C) an amount to which the district is entitled based on

supplemental payments owed to any tax increment fund for a reinvestment zone and (D) any amount due to the district to the extent the district contracts for students residing in the district to be educated in another district (i.e., tuition allotment). If a district adopts an M&O Tax rate in any fiscal year below a rate equal to the state compression percentage for the district in that year multiplied by the M&O Tax rate adopted by the district for the 2005-06 fiscal year, the district's guaranteed amount is reduced in a proportionate amount. If a district would receive more State and local revenue from the Tier One and Tier Two allotments (each as hereinafter defined) and wealth equalization than the guaranteed amount described above, the amount of State funding will be reduced by the amount of such surplus over the guaranteed amount described above.

In general terms, funds are allocated to districts in a manner that requires districts to "compress" their tax rates in order to receive increased State funding at a level that equalizes local tax wealth at the 88th percentile yield for the 2006-07 fiscal year. The state compression percentage is a basic component of the funding formulas. The state compression percentage was 66.67% for fiscal years 2007-08 and 2008-09. For fiscal year 2009-10 and thereafter, the Commissioner is required to determine the state compression percentage for each fiscal year based on the percentage by which a district is able to reduce its M&O Tax rate for that year, as compared to such district's adopted M&O Tax rate for the 2005-06 fiscal year, as a result of State funds appropriated for distribution for the current fiscal year from the property tax relief fund established under the Reform Legislation, or from any other funding source made available by the Legislature for school district property tax relief. For fiscal year 2009-10, the Commissioner determined the State compression percentage to be 66.67%.

State Funding for Local School Districts

To limit disparities in school district funding abilities, the Finance System (1) compels districts with taxable property wealth per weighted student higher than the "equalized wealth level" (described under "Wealth Transfer Provisions") to reduce their wealth to the equalized wealth level or to divert a portion of their tax revenues to other districts as described below and (2) provides various State funding allotments, including a basic funding allotment and other allotments for "enrichment" of the basic program, for debt service tax assistance and for new facilities construction.

The Finance System provides for (1) State guaranteed basic funding allotments per student ("Tier One") and (2) State guaranteed revenues per student for each cent of local tax effort that exceeds the compressed tax rate to provide operational funding for an "enriched" educational program ("Tier Two"). In addition, to the extent funded by the Legislature, the Finance System includes, among other funding allotments, an allotment to subsidize existing debt service up to certain limits ("EDA"), the Instructional Facilities Allotment ("IFA"), and an allotment to pay operational expenses associated with the opening of a new instructional facility. Tier One, Tier Two, EDA and IFA are generally referred to as the Foundation School Program. Tier One and Tier Two allotments represent the State funding share of the cost of maintenance and operations of school districts and supplement local ad valorem M&O Taxes levied for that purpose. Tier One and Tier Two allotments and prior year IFA allotments are generally required to be funded each year by the Legislature. EDA and future year IFA allotments supplement local ad valorem taxes levied for debt service on bonds issued by districts to construct, acquire and improve facilities and are generally subject to appropriation by the Legislature. State funding allotments may be altered and adjusted to penalize school districts with high administrative costs and, 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 program of education rated academically acceptable and meeting other applicable legal standards. If needed, the State will subsidize local tax receipts at a tax rate of the state compression percentage multiplied by the lesser of (a) \$1.50 or (b) the district's 2005 M&O Tax to ensure that the cost to a district of the basic program is met. 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 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 "Tier One Basic Allotment." The Tier One Basic Allotment is adjusted for all districts by a cost-of-living factor known as the "cost of education index." In addition, a district-size adjustment further adjusts the Tier One Basic Allotment for districts that (i) have not more than 1,600 students in average daily attendance (with alternative formulas established for such districts that contain at least 300 square miles and those districts that contain less than 300 square miles) or (ii) offer a kindergarten through grade 12 program and have less than 5,000 students in average daily attendance. For fiscal year 2007-08, the Tier One Basic Allotment was \$3,135 based upon a guaranteed yield of \$36.45 for each cent of tax effort, and for fiscal year 2008-09, the Tier One Basic Allotment was \$3,218 based upon a guaranteed yield of \$37.42 for each cent of tax effort. For the 2009-10 through 2012-13 school years, the basic allotment is set at the greater of \$4,765 or 1.65% of the statewide average property value per student in WADA and, thereafter, at the lesser of \$4,765 or that amount multiplied by the quotient of the district's compressed tax rate divided by the State maximum compressed tax rate of 1.00. This increase was due to changes in law effected by the Legislature during the 2009 Regular Legislative Session, which combined certain funding allotments that previously were separate components of Tier Two funding into the Tier One Basic Allotment. An additional change made during the 2009 Regular Legislative Session limits, beginning with 2010-11 school year, the annual increases in a district's M&O Tax revenue per WADA for purposes of State funding to not more than \$350, excluding Tier Two funds. For the 2009-10 school year, the revenue increases are limited to the funds that a district would have received under the school finance formulas as they existed on January 1, 2009, plus an additional \$350 per WADA, excluding Tier Two funds.

Tier Two currently provides two levels of enrichment with different guaranteed yields depending on the district's local tax effort. For fiscal year 2009-10, the first six cents of tax effort that exceeds the compressed tax rate will generate a guaranteed yield equivalent to (a) that of the Austin Independent School District or (b) the amount of tax revenue per WADA received on that tax effort in the previous year, whichever is greater. The second level of Tier Two is generated by tax effort that exceeds the compressed tax rate plus six cents and has a guaranteed yield per penny of local tax effort of \$31.95. Before 2009-10, Tier Two consisted of a district's M&O Tax levy above \$0.86. For fiscal year 2008-09, State funding to equalize local M&O Tax levies above \$0.86, up to a district's compressed rate, was funded at a guaranteed yield of \$37.42 per student in WADA for each cent of tax effort; any amount above a district's compressed rate up to \$0.04 was funded at a guaranteed yield of \$50.98 per WADA for each cent of tax effort; and any tax effort associated with a tax approved by voters at a rollback election was funded at a guaranteed yield of \$31.95 per WADA for each cent of tax effort above a district's compressed rate plus \$0.04. See "CURRENT PUBLIC SCHOOL FINANCE SYSTEM - General" for a discussion of the state compression percentage.

The IFA guarantees each school district a specified amount per student (the "IFA Guaranteed Yield") in State and local funds for each cent of tax effort to pay principal of and interest on eligible bonds issued to construct, acquire, renovate or improve instructional facilities. To receive an IFA, a school district must apply to the Commissioner in accordance with rules adopted by the Commissioner before issuing the bonds to be paid with 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 average daily attendance. The IFA is also available for lease-purchase agreements and refunding bonds meeting certain prescribed conditions. If the total amount appropriated by the State for IFA in a year is less than the amount of money school districts applying for IFA are entitled to for that year, districts applying will be ranked by the Commissioner by wealth per student, and State assistance will be awarded to applying districts in ascending order of adjusted wealth per student beginning with the district with the lowest adjusted wealth per student. In determining wealth per student for purposes of IFA, adjustments are made to reduce wealth for certain fast growing districts. Once a district receives an IFA award for bonds, it is entitled to continue receiving State assistance without reapplying to the Commissioner and the guaranteed level of State and local funds per student per cent of tax effort applicable to the bonds may not be reduced below the level provided for the year in which the bonds were issued. In 2007, the Legislature appropriated funds for outstanding school district bonds that qualified in prior budget cycles for IFA allotments and added funding for qualified debt to be issued for instructional facilities in the State's 2008-09 fiscal biennium; however, the Texas Education Agency has indicated that it intends to reserve all such new appropriation for the second year of the biennium.

State financial assistance is provided for certain existing debt issued by school districts (referred to herein as EDA) to produce a guaranteed yield (the "EDA Yield"), which for the 2009-11 State Biennium is \$35.00 (subject to adjustment as described below) in State and local revenue per student for each cent of debt service tax levy; however, for bonds that became eligible for EDA funding after August 31, 2001, and prior to August 31, 2005, EDA assistance for such eligible bonds may be less than \$35.00 in revenue per student for each cent of debt service tax, as a result of certain administrative delegations to the Commissioner under State law. Effective September 1, 2003, the portion of the local debt service rate that has qualified for equalization funding by the State has been 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 school year of the preceding State fiscal biennium or (ii) levied taxes to pay the principal of and interest on the bonds for that school year. Access to EDA funding will be determined by the debt service taxes collected in the final year of the preceding biennium. A district may not receive EDA funding for the principal and interest on a series of otherwise eligible bonds for which the district receives IFA funding.

A district may also qualify for an allotment for operational expenses associated with opening new instructional facilities. This funding source may not exceed \$25,000,000 in one school year on a State-wide basis. For the first school year in which students attend a new instructional facility, a district is entitled to an allotment of \$250 for each student in average daily attendance at the facility. For the second school year in which students attend that facility, a district is entitled to an allotment of \$250 for each additional student in average daily attendance at the facility. The new facility operational expense allotment will be deducted from wealth per student for purposes of calculating a district's Tier Two State funding.

Local Revenue Sources - Property Tax Authority

The primary source of local funding for school districts is ad valorem taxes levied against the local tax base. The former provision of the Education Code, Section 45.003, as amended, that in general limited the M&O Tax rate to \$1.50 per \$100 of taxable assessed value, was replaced by the Reform Legislation with a formula using the state compression percentage so that the maximum tax rate that may be adopted by a district in any fiscal year is limited based on the amount of State funds to be received by the District in that year. For the 2006-07 and 2007-08 fiscal years, districts were permitted to generate additional local funds by raising their M&O Tax rate by \$0.04 above the compressed tax rates (without taking into account changes in taxable valuation) without voter approval, and such amounts generated equalized funding dollars from the State under the Tier Two program. In fiscal year 2008-09 and thereafter, districts may, in general, increase their tax rate by an additional two or more cents and receive State equalization funds for such taxing effort so long as the voters approve such tax rate increase. Many school districts, however, voted their M&O Tax under prior law and may be subject to other limitations on the M&O Tax rate. School districts are also authorized to levy a bond debt service tax that may be unlimited in rate. See "AD VALOREM TAX PROCEDURES – Tax Rate Limitations" herein. The governing body of a school district cannot adopt an annual tax rate which exceeds the district's "rollback tax rate" without submitting such proposed tax rate to the voters at a referendum election. See "AD VALOREM TAX PROCEDURES" – Public Hearing and Rollback Tax Rate" herein.

Wealth Transfer Provisions

Under the Finance System, districts are required, with certain limited exceptions, to effectively adjust taxable property wealth per weighted student ("wealth per student") for each school year to no greater than the "equalized wealth level", determined in accordance with a formula set forth in the Reform Legislation. A district may effectively reduce its wealth per student either by reducing the amount of taxable property within the district relative to the number of weighted students, by transferring revenue out of the district or by exercising any combination of these remedies.

The wealth level that required wealth reduction measures for fiscal year 2006-07 was \$319,500 per student in average daily attendance. For 2007-08 that wealth level was increased to \$364,500 per student in average daily attendance with respect to that portion of a district's M&O tax effort that did not exceed its compressed tax rate, and remained at \$319,500 with respect to that portion of a district's local tax effort that was beyond its compressed rate plus \$.04. For 2008-09 that wealth level was further increased to \$374,200 per student in average daily attendance with respect to that portion of a district's M&O Tax effort that did not exceed its compressed tax rate, and remained at \$319,500 with respect to that portion of a district's local tax effort that was beyond its compressed rate plus \$0.06. For 2009-10 that wealth level has been increased to \$476,500 per student in average daily attendance with respect to that portion of a district's M&O Tax effort that does not exceed its compressed tax rate, and remains at \$319,500 with respect to that portion of a district's local tax effort that is beyond its compressed rate plus \$.06.

Property wealthy districts may also be able to levy up to an additional six cents per \$100 of assessed valuation of M&O Taxes above their compressed rate to provide revenue that is not subject to recapture.

A district has four options to reduce its wealth per student so that it does not exceed the equalized wealth level: (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) Subject to approval by the voters of all affected districts, 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 debt service taxes. (3) A district may detach property from its territory for annexation by a property-poor district. (4) A district may educate students from other districts who transfer to the district without charging tuition to such students.

A district has three options to transfer tax revenues from its excess property wealth. First, a district with excess wealth per student may purchase "attendance credits" by paying the tax revenues to the State for redistribution under the Foundation School Program. Second, it can contract to disburse the tax revenues to educate students in another district, if the payment does not result in effective wealth per student in the other district to be greater than the equalized wealth level. Both options to transfer property wealth are subject to approving elections by the transferring district's qualified voters. Third, a wealthy district may reduce its wealth by paying tuition to a non-wealthy district for the education of students that reside in the wealthy district.

A district may not adopt a tax rate until its effective wealth per student is the equalized wealth level or less. If a final court decision holds any of the preceding permitted remedial options unlawful, districts may exercise any remaining option under a revised schedule approved by the Commissioner.

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.

Possible Effects of Wealth Transfer Provisions and HB 1 on the District's Financial Condition

The District's wealth per student for the 2009-10 school year is \$166,750 which is less than the equalized wealth value. Accordingly, the District has not been required to exercise one of the permitted wealth equalization options.

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

AD VALOREM TAX PROCEDURES

Tax Code and County-Wide Appraisal District

The Texas 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 review board responsible for appraising property for all taxable units within the county. The Harris County Appraisal District (the "Appraisal District") is responsible for appraising property within the District, generally, 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"), the members of which are appointed by the Appraisal District. 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 of Trustees) 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; so-called "freeport property" including property detained in the District for up to 175 days for purpose of assembly or other processing; certain household goods, family supplies and personal effects; farm products owned by the producers; certain real property and tangible personal property owned by a non-profit community business organization or a charitable organization. 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 exemption to residential homesteads of disabled persons or persons ages 65 or over; an exemption from \$5,000 to a maximum of \$12,000 for real or personal property of disabled veterans or the surviving spouse or children of a deceased veteran who died while on active duty in the armed forces; \$15,000 in market value for all residential homesteads, (see "Residential Homestead Exemption" below); and certain classes of intangible property. Effective January 1, 2010, State law mandates a complete exemption for the residential homestead of disabled veterans determined to be 100% disabled by the U.S. Department of Veterans Affairs. A constitutional amendment was approved by the voters on November 6, 2007, that authorizes the Legislature to enact legislation to reduce the frozen amount of taxes for taxpayers 65 years of age or older and the disabled, so that the frozen tax amount will be proportionate to the reduction in local ad valorem taxes under the Reform Legislation. Legislation to implement the constitutional amendment has been passed by the 80th Legislature and signed by the Governor. 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.

A city or a county may create a tax increment financing district ("TIF") within the city or county, as applicable, 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. 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. Under current law, the Comptroller of Public Accounts is to determine taxable value of property within each school district in the State (which taxable value figure is used in calculating a district's wealth per student) and in making such determination the taxable value is to exclude (i) the total dollar amount of any captured appraised value of property located in a reinvestment zone on August 31, 1999, that generates taxes paid into a tax increment fund and is eligible for tax increment financing under a reinvestment zone financing plan approved before September 1, 1999, and (ii) the total dollar value of taxable property covered by a tax abatement agreement entered into prior to June 1, 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 tax abatements on certain eligible property to encourage economic development in their tax base and provides additional State funding for each year of such tax abatement in the amount of the tax credit provided to the taxpayer by the district.

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.

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

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 market data comparison method of appraisal. The Appraisal District's chief appraiser determines the method 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 not to exceed the lesser of (1) the market value of the property or (2) 110% of the appraised value of the resident homestead for the preceding tax year plus the market value of all new improvements to the property.

The Tax Code permits 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 a current estimate of appraised values within the District or an estimate of any new property or improvements within the District. While such current estimate 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 its appraisal rolls.

Residential Homestead Exemption

The Texas Constitution permits the exemption of certain percentages of the market value of residential homesteads from ad valorem taxation. The Constitution authorizes the governing body of each political subdivision in the State to exempt up to twenty percent (20%) of the market value of all residential homesteads from ad valorem taxation, and permits an additional optional homestead exemption for taxpayers 65 years of age or older and disabled persons.

District and Taxpayer Remedies

Under certain circumstances, taxpayers and taxing units, including the District, may appeal an order 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 the Appraisal District to compel compliance with the Tax Code.

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 - General" 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, as amended, 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, as amended, 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, as amended. Section 44.004(e) of the Texas Education Code, as amended, 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. Beginning September 1, 2009, 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.

Levy and Collection of Taxes

The District is responsible for the collection of its taxes, unless it elects to transfer such function to another governmental entity. By September 30 or the 60th day after the District receives the appraisal roll, whichever is later, the rate of taxation must be set by the Board of Trustees of the District based upon the valuation of property within the District as of the preceding January 1. 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 accrued 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.

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. 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.

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

Penalties and Interest

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

<u>Month</u>	<u>Cumulative Penalty</u>	<u>Cumulative Interest</u>	<u>Total</u>
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, the cumulative penalty remains at 12%, and interest increases at the rate of 1% each month. In addition, if an account is delinquent in July, a 20% attorney’s collection fee may be added to the total tax, penalty and interest charge.

District Application of Tax Code

The District has granted an additional \$35,000 exemption to the market value of the residence homestead of persons 65 years of age or older over the state-mandated exemption.

The District has granted an additional local exemption of 20% of the market value of residence homesteads; but the District does grant the minimum exemption of \$5,000.

Ad valorem taxes are not levied by the District against the exempt value of residence homesteads for the payment of debt. The District does not tax non-business personal property. The District does not permit split payments, and discounts are not allowed. The District does not tax freeport property. The District does not tax goods in transit.

TAX RATE LIMITATIONS

A school district is authorized to levy maintenance and operations taxes ("M&O Tax") subject to approval of a proposition submitted to district voters. The maximum M&O Tax rate that may be levied by a district cannot exceed the voted maximum rate or the maximum rate described in the next succeeding paragraph. The maximum voted M&O Tax rate for the District is \$1.50 per \$100 of assessed valuation as approved by the voters at an election held on March 28, 1964, pursuant to Article 2784e-1, Texas Revised Civil Statutes Annotated, as amended ("Article 2784e-1"). Article 2784e-1 limits the District's annual M&O Tax rate 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 valuation 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 M&O Tax rate 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 8.53% of the District's current taxable assessed valuation of property. See "APPENDIX A - Table 1 Valuation, Exemptions and Tax Supported Debt" herein.

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 66.67% for fiscal years 2007-08 and 2008-09. For fiscal year 2009-10 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 2009-10, 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 a tax unlimited as to rate or amount for the support school district bonded indebtedness (see "THE BONDS – Security and Source of Payment")

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 reduces 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. In addition, taxes levied to pay refunding bonds issued pursuant to Chapter 1207, Texas Government Code, are not subject to the \$0.50 tax rate test; however, taxes levied to pay debt service on such bonds are included in the calculation of the \$0.50 tax rate test as applied to subsequent issues of "new debt." The Bonds are "new debt" and are subject to the \$0.50 threshold tax rate test. Under current law, a district may demonstrate its ability to comply with the \$0.50 threshold tax rate test by applying the \$0.50 tax rate to an amount equal to 90% of projected future taxable value of property in the district, as certified by a registered professional appraiser, anticipated for the earlier of the tax year five years after the current tax year or the tax year in which the final payment for the bonds is due. However, if a district uses projected future taxable values to meet the \$0.50 threshold tax rate test and subsequently imposes a tax at a rate greater than \$0.50 per \$100 of valuation to pay for bonds subject to the test, then for subsequent bond issues, the Attorney General must find that the district has the projected ability to pay principal and interest on the proposed bonds and all previously issued bonds subject to the \$0.50

threshold tax rate test from a tax rate of \$0.45 per \$100 of valuation. The District has not used projected property values to satisfy this threshold test.

EMPLOYEES' BENEFIT PLANS

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. For the year ended August 31, 2009 (unaudited), the State contributed \$469,039.89 to TRS on behalf of the District, District employees paid \$652,406 and other contributions into the plan made from private grants and from the District for salaries above the statutory minimum were \$178,020.53.

In addition to the TRS retirement plan, the District provides health care coverage for its employees. For a discussion of the TRS retirement plan and the District's medical benefit plan, see the audited financial statements of the District that are attached hereto as Appendix B.

Formal collective bargaining agreements relating directly to wages and other conditions of employment are prohibited by Texas law, as are strikes by teachers. There are various local, state and national organized employee groups who engage in efforts to better the 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.

THE DISTRICT

The District is an independent school district and political subdivision of the State of Texas located within Angelina County, Texas. The City of Diboll, Angelina County and the Angelina County Junior College District, each have authority to levy ad valorem taxes on territory located in the District. See APPENDIX A – Table 6 – "Estimated Overlapping Debt."

For additional information regarding the District, see also "APPENDIX A – INFORMATION REGARDING THE DISTRICT."

Administration

The Board of Trustees is the governing body of the District and consists of seven members, who serve three-year terms without salary. The District is under the administrative supervision of the Superintendent of Schools, who is employed by the Board.

District School Operations

On April 1, 2010, the District owned and operated a high school, middle school, and an elementary school. The following table provides information regarding student enrollment in the District.

	Fiscal Year Ended August 31					
	<u>2010</u> ^(a)	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>
Student Enrollment	1,942	1,833	1,832	1,866	1,865	1,915
Average Daily Attendance	1,715	1,687	1,678	1,727	1,724	1,781
Cost Per Student ^(a)	\$7,808	\$7,536	\$6,591	\$7,253	\$7,594	\$6,550

^(a) Projected

Financial Policies

General Fund – This is the District's primary operating fund. It accounts for all financial resources of the District except those required to be accounted for in another fund.

Debt Service Fund – This fund is used to account for resources accumulated from the proceeds of debt service taxes levied for the purpose of the repayment of debt, the issuance of which has been approved by the voters of the District. Other resources include State Foundation program funds received for the purpose of bonded debt repayment. This fund is required to be budgeted on an annual basis.

Capital Projects Fund – This fund is used to account for revenues and expenses related to projects financed by the proceeds of bond issues or for capital projects otherwise mandated to be accounted for in this fund. This fund is not required to be budgeted on an annual basis.

Internal Service Funds –These funds are used to account for revenues and expenses related to services provided to parties inside the District. These funds facilitate distribution of support costs to the issues of support services on a cost-reimbursement basis. Because the principal users of the internal services are the District’s governmental activities, this fund type is included in the “Governmental Activities” column of the government-wide financial statements.

Private-Purpose Trust Funds – These funds are used to report trust arrangements under which the principal and income benefit individuals, private organizations, or other governments not reported in other fiduciary fund types.

Agency Funds – These funds are used to report student activity funds and other resources held in a purely custodial capacity (assets equal liabilities). Agency funds typically involve only the receipt, temporary investment, and remittance of fiduciary resources to individuals, private organizations, or other governments.

Fiduciary Funds are reported in the fiduciary fund financial statements. However, because their assets are held in a trustee or agent capacity and are therefore not available to support District programs, these funds are not included in the government-wide statements.

INVESTMENTS

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

Legal Investments

Current Texas law provides the District with authority to invest in: (1) obligations 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 of and interest on 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) certificates of deposit that are issued by a state or national bank domiciled in the State of Texas, a savings bank domiciled in the State of Texas, or a state or federal credit union domiciled in the State of Texas and are guaranteed or insured by the Federal Deposit Insurance Corporation or the National Credit Union Share Insurance Fund or are secured as to principal by obligations described in the preceding clauses or in any other manner and amount provided by law for District deposits, (7) fully collateralized repurchase agreements that have a defined termination date, are fully secured by obligations described in clause (1), and are placed through a primary government securities dealer or a financial institution doing business in the State of Texas, (8) certain bankers’ acceptances with the remaining term of 270 days or less, if the short-term obligations of the accepting bank or its parent are rated at least A-1 or P-1 or the equivalent by at least one nationally recognized credit rating agency, (9) commercial paper with a stated maturity of 270 days or less that is rated at least A-1 or P-1 or the equivalent by either (a) two nationally recognized credit rating agencies or (b) one nationally recognized credit rating agency if the paper is fully secured by an irrevocable letter of credit issued by a U.S. or state bank, (10) no-load money market mutual funds registered with the Securities and Exchange Commission that have a dollar-weighted average stated maturity of 90 days or less and include in their investment objectives the maintenance of a stable net asset value of \$1 for each share, (11) no-load mutual funds registered with the Securities and Exchange Commission that have an average weighted maturity of less than two years, invest exclusively in the foregoing obligations and are continuously rated as to investment quality by at least one nationally recognized investment rating firm of no less than AAA or its equivalent, (12) bonds issued, assumed, or guaranteed by the State of Israel, and (13) guaranteed investment contracts that have a defined termination date and are secured by obligations described in clause (1) above in an amount at least equal to the amount of bond proceeds invested under such contract.

The District may invest in such obligations directly or through government investment pools that invest solely in such obligations provided that the pools are rated no lower than Aaa or AAA-m, or its 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.

Investment Policies

Under Texas law, the District is required to invest its funds under written investment policies that primarily emphasize safety of principal and liquidity; that address investment diversification, yield, maturity, and the quality and capability of investment management; and that include a list of authorized investments for District funds, maximum allowable stated maturity of any individual investment, 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 will 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) require any investment officers with personal business relationships or relatives with firms seeking to sell securities to the District to disclose the relationship and file a statement with the Texas Ethics Commission and the Board of Trustees; (3) require the registered principal of firms seeking to sell securities to the District to: (a) receive and review the District’s investment policy, (b) acknowledge that reasonable controls and procedures have been implemented to preclude imprudent investment activities, and (c) deliver a written statement attesting to these requirements; (4) perform an annual audit of the management controls on investments and adherence to the District’s investment policy; (5) provide specific investment training for the Treasurer, Chief Financial Officer, or other investment officers; (6) restrict reverse repurchase agreements to not more than 90 days and restrict the investment of reverse repurchase agreement funds to no greater than the term of the reverse repurchase agreement; (7) restrict the investment in mutual funds in the aggregate to no more than 80% of the District’s monthly average fund balance, excluding bond proceeds and reserves and other funds held for debt service, and further restrict the investment in non-money market mutual funds of any portion of bond proceeds, reserves and funds held for debt service, and 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; and (8) require local government investment pools to conform to the new disclosure, rating, net asset value, yield calculation and advisory board requirements.

Current Investments

As of February 28, 2010, the District had approximately \$3,640,882 invested in LoneStar Investment Pool, \$8,462,630 invested in First Bank & Trust, \$468,889 invested in JP Morgan Chase Bank, and \$1,340,515.96 invested in UMB Bank. The market value of such investments is approximately 100% of their 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.

TAX MATTERS

In the opinion of Andrews Kurth LLP, Houston, Texas, Bond Counsel, interest on the Bonds is (1) excludable under Section 103 of the Internal Revenue Code of 1986, as amended (the “Code”), from gross income of the owners thereof for federal income tax purposes and (2) is not includable in the alternative minimum taxable income of individuals or corporations.

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

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

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

Bond Counsel’s opinion is not a guarantee of a result, but represents its legal judgment based upon its review of existing statutes, regulations, published rulings and court decisions and the representations and covenants of the District described above. No ruling has been sought from the Service with respect to the matters addressed in the opinion of Bond Counsel, and Bond Counsel’s opinion is not binding on the Service. The Service has an ongoing program of auditing the tax-exempt status of the interest on municipal obligations. If an audit of the Bonds is commenced, under current procedures the Service is likely to treat the District as the “taxpayer,” and the owners of

the Bonds may have no right to participate in the audit process. In responding to or defending an audit of the tax-exempt status of the interest on the Bonds, the District may have different or conflicting interests from the owners of the Bonds. Public awareness of any future audit of the Bonds could adversely affect the value and liquidity of the Bonds during the pendency of the audit, regardless of its ultimate outcome.

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

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

TAX TREATMENT OF ORIGINAL ISSUE DISCOUNT AND PREMIUM BONDS

Discount Bonds

Some of the Bonds may be offered at initial offering prices which are less than the stated redemption prices at maturity of such Bonds. If a substantial amount of any maturity of the Bonds is sold to members of the public (which for this purpose excludes bond houses, brokers and similar persons or entities acting in the capacity of wholesalers or underwriters) at such initial offering price, an initial owner who purchases the Bonds of that maturity (the "Discount Bonds") will be considered to have "original issue discount" for federal income tax purposes equal to the difference between (a) the stated redemption price payable at the maturity of such Discount Bond and (b) the initial offering price to the public of such Discount Bond. Under existing law, such original issue discount will be treated for federal income tax purposes as additional interest on a Bond and such initial owner will be entitled to exclude from gross income for federal income tax purposes that portion of such original issue discount deemed to be earned (as discussed below) during the period while such Discount Bond continues to be owned by such initial owner. Except as otherwise provided herein, the discussion regarding interest on the Bonds under the caption "TAX EXEMPTION" generally applies to original issue discount deemed to be earned on a Discount Bond while held by an owner who has purchased such Bond at the initial offering price in the initial public offering of the Bond and that discussion should be considered in connection with this portion of the Official Statement.

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

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

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

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

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

Premium Bonds

Some of the Bonds may be offered at initial offering prices which exceed the stated redemption prices payable at the maturity of such Bonds. If a substantial amount of any maturity of the Bonds is sold to members of the public (which for this purpose excludes bond houses, brokers and similar persons or entities acting in the capacity of wholesalers or underwriters) at such initial offering price, each of the Bonds of such maturity ("Premium Bonds") will be considered for federal income tax purposes to have "bond premium" equal to the amount of such excess. The basis for federal income tax purposes of a Premium Bond in the hands of an initial purchaser who purchases such Bond in the initial offering must be reduced each year and upon the sale or other taxable disposition of the Bond by the amount of amortizable bond premium. This reduction in basis will increase the amount of any gain (or decrease the amount of any loss) recognized for federal income tax purposes upon the sale or other taxable disposition of a Premium Bond by the initial purchaser. Generally, no corresponding deduction is allowed for federal income tax purposes, for the reduction in basis resulting from amortizable bond premium. The amount of bond premium on a Premium Bond which is amortizable each year (or shorter period in the event of a sale or disposition of a Premium Bond) is determined under special tax accounting rules which use a constant yield throughout the term of the Premium Bond based on the initial purchaser's original basis in such Bond.

The federal income tax consequences of the purchase, ownership, redemption, sale or other disposition by an owner of Bonds that are not purchased in the initial offering or which are purchased at an amount representing a price other than the initial offering prices for the Bonds of the same maturity may be determined according to rules which differ from those described above. Moreover, all prospective purchasers of Bonds should consult their tax advisors with respect to the federal, state, local and foreign tax consequences of the purchase, ownership, redemption, sale or other disposition of Premium Bonds.

QUALIFIED TAX-EXEMPT OBLIGATIONS

Section 265(a) of the Code provides, in general, that interest expenses incurred to acquire or carry tax-exempt obligations are not deductible from the gross income of the holder. For certain holders that are "financial institutions" within the meaning of such section, complete disallowance of such expense would apply to taxable years beginning after December 31, 1986, with respect to tax-exempt obligations acquired after August 7, 1986. Section 265(b) of the Code provides an exception to this rule for interest expense incurred by financial institutions to carry tax-exempt obligations (other than certain private activity bonds) which are designated by an issuer as "qualified tax-exempt obligations." An issuer may only designate an issue as an issue of "qualified tax-exempt obligations" where less than \$30 million of tax-exempt obligations are issued by the issuer during the calendar years 2009 and 2010.

The District will designate the Bonds as "qualified tax-exempt obligations." Further, the District will represent that it has or will take such action necessary for the Bonds to constitute "qualified tax-exempt obligations."

Notwithstanding the designation of the Bonds as "qualified tax-exempt obligations," financial institutions acquiring the Bonds will be subject to a twenty percent (20%) disallowance of interest expenses allocable to the Bonds.

Section 265(b) of the Code provides an exception to the disallowance provision described above for an amount of tax-exempt obligations issued after December 31, 2008 and before January 1, 2011, in a total amount not exceeding two percent (2%) of the adjusted basis of all of the assets of the financial institution.

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 material events, to the Municipal Securities Rulemaking Board (the "MSRB"). Information will be available free of charge via the Electronic Municipal Market Access ("EMMA") system at www.emma.msrb.org.

Annual Reports

The District will provide updated financial information and operating data to the MSRB annually via EMMA. The information to be updated includes all quantitative financial information and operating data of the general type included in this Official Statement in APPENDIX A, Tables 1 through 5 and Tables 7 through 10, and APPENDIX B. The District will update and provide this information within six months after the end of each fiscal year.

The District may provide updated information in full text or may incorporate by reference 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 the audit is completed by the required time. If audited financial statements are not available by the required time, the District will provide such financial statements on an unaudited basis within the required time and audited financial statements when they become available. Any such financial statements will be prepared in accordance with the accounting principles described in APPENDIX B or such other accounting principles as the District may be required to employ from time to time pursuant to State law or regulation.

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

Material Event Notices

The District also will provide timely notices of certain events to the MSRB. Specifically, the District will provide notice of any of the following events with respect to the Bonds, if such event is material to a decision to purchase or sell Bonds: (1) principal and interest payment delinquencies; (2) non-payment related defaults; (3) unscheduled draws on debt service reserves reflecting financial difficulties; (4) unscheduled draws on credit enhancements reflecting financial difficulties; (5) substitution of credit or liquidity providers, or their failure to perform; (6) adverse tax opinions or events affecting the tax-exempt status of the Bonds; (7) modifications to rights of holders of the Bonds; (8) Bond calls; (9) defeasances; (10) release, substitution, or sale of property securing repayment of the Bonds; and (11) rating changes. Neither the Bonds nor the Order makes any provision for liquidity enhancement or require the funding of debt service reserves. In addition, the District will provide timely notice of any failure by the District to provide annual financial 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 only to the MSRB.

Limitations and Amendments

The District has agreed to update information and to provide notices of material 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 has been 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. Nothing in this paragraph is intended or shall act to disclaim, waive or limit the District's duties under federal or state securities laws.

The District may amend its continuing disclosure agreement to adapt to changed circumstances that arise from a change in legal requirements, a change in law, or a change in the identity, nature, status, or type of operations of the District, if, but only if, (1) the agreement, as so amended, would have permitted underwriters to purchase or sell Bonds in the initial primary offering 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 (2) either (a) the holders of a majority in aggregate principal amount of the outstanding Bonds consent or (b) any qualified person unaffiliated with the District (such as nationally recognized bond counsel) determines that the amendment will not materially impair the interests of the holders and beneficial owners of the Bonds. If the District amends its agreement, it has agreed to include with the financial information and operating data next 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 information and operating data so provided.

Compliance with Prior Undertakings

The District has complied in all material respects with its continuing disclosure agreements in accordance with the Rule.

OTHER INFORMATION

Ratings

Standard & Poor's Ratings Group ("S&P") has assigned its municipal rating of "_____" to the Bonds by virtue of the guarantee of the Texas Permanent School Fund on the Bonds. An explanation of the rating may be obtained from S&P. The rating reflects only the views of S&P and the District makes no representation as to the appropriateness of the rating. There is no assurance that such ratings will continue for any given period of time or that it will not be revised downward or withdrawn entirely by S&P in the judgment of S&P circumstances so warrant. Any such downward revision or withdrawal by such rating may have an adverse effect on the market price of the Bonds. (See "THE PERMANENT SCHOOL FUND GUARANTEE PROGRAM" herein.)

No Litigation Certificate

The District will furnish to the Underwriters a certificate, dated as of the date of delivery of the Bonds, executed by an authorized officer of the District, to the effect that, except as disclosed in this Official Statement, no litigation of any nature has been filed or is then pending or threatened, either in state or federal courts, contesting or attacking the Bonds; restraining or enjoining the issuance, execution or delivery of the Bonds; affecting the provisions made for the payment of or security for the Bonds; in any manner questioning the authority or proceedings for the issuance, execution, or delivery of the Bonds; or affecting the validity of the Bonds.

Registration and Qualification of Bonds for Sale

No registration statement relating to the Bonds has been filed with the Securities and Exchange Commission under the federal Securities Act of 1933, as amended, in reliance upon the exemption provided thereunder by Section 3(a)(2); and the Bonds have not been 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 other jurisdiction in which the Bonds may be sold, assigned, pledged hypothecated or otherwise transferred. This disclaimer of responsibility for registration and 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 in such other jurisdictions.

The Bonds as Legal Investments in Texas

Under the Texas Public Security Procedures Act (Texas Government Code, Chapter 1201, as amended), the Bonds (1) are negotiable instruments, (2) are investment securities to which Chapter 8 of the Texas Business and Commerce Code applies, and (3) are legal and authorized investments for (A) an insurance company, (B) a fiduciary or trustee, or (C) a sinking fund of a municipality or other political subdivision or public agency of the State of Texas. The Bonds are eligible to secure deposits of any public funds of the State, its agencies and political subdivisions, and are legal security for those deposits to the extent of their market value. 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, as amended, Texas Government Code, requires the Bonds to be assigned a rating of not less than "A" or its equivalent as to investment quality by a national rating agency. (See "Rating" above). 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 District has made no investigation of other laws, rules, regulations or investment criteria which might apply to such institutions or entities or which might limit the suitability of the Bonds for any of the foregoing purposes or limit the authority of such institutions or entities to purchase or invest in the Bonds for such purposes. The District has made no review of laws in other states to determine whether the Bonds are legal investments for various institutions in those states.

Legal Matters

The delivery of the Bonds is subject to the approving opinion 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 opinions of Andrews Kurth LLP, Bond Counsel to the District ("Bond Counsel"), in substantially the form attached as APPENDIX C. In connection with the issuance of the Bonds, Bond Counsel has represented only the District. The legal fee to be paid Bond Counsel for services rendered in connection with the issuance of the Bonds is contingent upon the sale and delivery of the Bonds. Bond Counsel only represents the issuer in connection with the issuance of the Bonds.

Bond Counsel has reviewed the statements and information contained in the Official Statement under the captions and sub-captions "THE BONDS" (except for the information under the sub-captions "Yield on CABs," "Book-Entry-Only System," "Bondholders' Remedies" and "Sources and Uses of Funds," as to which no opinion is expressed) and "CONTINUING DISCLOSURE OF INFORMATION" (except for the information under the sub-caption "Compliance With Prior Undertakings," as to which no opinion is expressed) and Bond Counsel is of the opinion that the statements and information contained therein fairly and accurately reflect the provisions of the Order; further, Bond Counsel has reviewed the statements and information contained in the Official Statement under the captions and sub-captions "STATE AND LOCAL FUNDING OF SCHOOL DISTRICTS IN TEXAS," "CURRENT PUBLIC SCHOOL FINANCE SYSTEM," (except for the information under "Possible Effects of Wealth Transfer Provisions on the District's Financial Condition," as to which no opinion is expressed) "TAX RATE LIMITATIONS," "TAX MATTERS," "TAX TREATMENT OF ORIGINAL ISSUE DISCOUNT AND PREMIUM BONDS," "QUALIFIED TAX-EXEMPT OBLIGATIONS" "OTHER INFORMATION – Legal Matters" "OTHER INFORMATION – Registration and Qualification of Bonds for Sale" and "OTHER INFORMATION – The Bonds as Legal Investments in Texas" and Bond Counsel is of the opinion that the statements and information contained therein are correct as to matters of law. Bond Counsel has not independently verified any of the factual information contained in this Official Statement nor have they conducted an investigation of the affairs of the District for the purpose of passing upon the accuracy or completeness of this Official Statement. No person is entitled to rely upon such firm's limited participation as an assumption of responsibility for, or an expression of opinion of any kind with regard to, the accuracy or completeness of any of the information contained herein. Certain legal matters will be passed upon for the Underwriters by their counsel, Petruska & Associates, A Professional Limited Liability Company whose fee for services rendered is contingent upon the sale and delivery of the Bonds.

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.

Financial Advisor

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

Coastal has reviewed the information in this Official Statement in accordance with its responsibilities to the District and, as applicable, to investors under federal securities laws as applied to the facts and circumstances of this transaction, but Coastal does not guarantee the accuracy or completeness of such information.

Underwriting

The Bonds are being purchased by the Underwriters pursuant to a bond purchase agreement with the District, at a price of \$ _____, which reflects the par amount of the Bonds, less an underwriting discount (including underwriting expenses) of \$ _____, plus a net premium of \$ _____, plus accrued interest on the Bonds to the date of initial delivery.

The Underwriters’ obligation to purchase the Bonds is subject to certain conditions precedent, and they will be obligated to purchase all of the Bonds if any of the Bonds are purchased. The District has no control over the price at which the Bonds are subsequently sold and the initial yields at which the Bonds will be priced and reoffered will be established by and will be the responsibility of the Underwriters. The Bonds may be offered and sold to certain dealers and others at prices lower than such public offering prices, and such public prices may be changed from time to time, by the Underwriters.

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

MISCELLANEOUS

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.

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 Underwriters.

This Official Statement will be approved by the Board of Trustees of the District for distribution in accordance with the provisions of SEC's Rule 15c2-12, as amended.

DIBOLL INDEPENDENT SCHOOL DISTRICT

President, Board of Trustees

ATTEST:

Secretary, Board of Trustees

SCHEDULE I - TABLE OF ACCRETED VALUES OF CAPITAL APPRECIATION BONDS

The following schedule is calculated based on yields as of the date of sale, and is included for information purposes only. The accreted values may not reflect market values in the secondary market from time to time, if any.

Date	Capital Appreciation Bonds 2/15/2028 @ 4.55%
6/8/2010	\$ 2,256.30
8/15/2010	2,275.25
2/15/2011	2,327.05
8/15/2011	2,379.95
2/15/2012	2,434.10
8/15/2012	2,489.50
2/15/2013	2,546.15
8/15/2013	2,604.05
2/15/2014	2,663.30
8/15/2014	2,723.90
2/15/2015	2,785.85
8/15/2015	2,849.25
2/15/2016	2,914.05
8/15/2016	2,980.35
2/15/2017	3,048.15
8/15/2017	3,117.50
2/15/2018	3,188.45
8/15/2018	3,260.95
2/15/2019	3,335.15
8/15/2019	3,411.05
2/15/2020	3,488.65
8/15/2020	3,568.00
2/15/2021	3,649.15
8/15/2021	3,732.20
2/15/2022	3,817.10
8/15/2022	3,903.95
2/15/2023	3,992.75
8/15/2023	4,083.60
2/15/2024	4,176.50
8/15/2024	4,271.50
2/15/2025	4,368.70
8/15/2025	4,468.05
2/15/2026	4,569.70
8/15/2026	4,673.70
2/15/2027	4,780.00
8/15/2027	4,888.75
2/15/2028	5,000.00

APPENDIX A
INFORMATION REGARDING THE DISTRICT

TABLE 1 - VALUATION, EXEMPTIONS AND TAX-SUPPORTED DEBT**District Direct Debt**

2009 Certified Taxable Valuation (100% of Estimated Market Value)	\$ 263,921,662
Outstanding Limited Tax Debt (March 1 , 2010)	\$ 3,037,039
Outstanding Unlimited Tax Debt (March 1 , 2010)	5,730,000
Plus: U/L Tax School Building Bonds, Series 2010A	<u>11,039,595</u> ^(a)
Total Direct Debt	\$ <u>16,769,595</u>
As a % of Assessed Valuation	6.35%

^(a) Preliminary, subject to change.**TABLE 2 - TAXABLE ASSESSED VALUATIONS BY CATEGORY ^(a)**

	<u>Tax Year 2009</u>	<u>Tax Year 2008</u>	<u>Tax Year 2007</u>	<u>Tax Year 2006</u>	<u>Tax Year 2005</u>
Real Property	\$ 329,447,275	\$ 187,661,850	\$ 293,273,233	\$ 262,342,729	\$ 287,475,380
Personal Property	<u>107,225,232</u>	<u>123,973,582</u>	<u>122,591,323</u>	<u>113,199,608</u>	<u>86,148,641</u>
Gross Value	\$ <u>436,672,507</u>	\$ <u>311,635,432</u>	\$ <u>415,864,556</u>	\$ <u>375,542,337</u>	\$ <u>373,624,021</u>
Less Exemptions	<u>172,750,845</u>	<u>41,553,054</u>	<u>143,255,083</u>	<u>122,440,883</u>	<u>115,632,935</u>
Net Taxable Value	\$ <u>263,921,662</u>	\$ <u>270,082,378</u>	\$ <u>272,609,473</u>	\$ <u>253,101,454</u>	\$ <u>257,991,086</u>

^(a) Values may differ from those shown elsewhere in the document due to subsequent additions, deletions, and adjustments to the tax rolls.

Source: Angelina County Appraisal District.

TABLE 3 - TAX RATE, LEVY AND COLLECTION HISTORY; TAX RATE DISTRIBUTION

Fiscal Year End	Tax Year	Taxable Assessed Valuation ^(a)	Tax Rate	Tax Levy	Percent Collected	
					Current	Total ^(b)
2004	2003	\$ 232,981,640	\$ 1.5550	\$ 3,622,865	97.49%	99.23%
2005	2004	254,298,174	1.4800	3,763,613	97.25%	98.83%
2006	2005	256,690,811	1.5000	3,850,362	97.56%	100.41%
2007	2006	251,800,866	1.3700	3,449,672	98.36%	100.76%
2008	2007	269,541,472	1.0400	2,803,231	98.15%	101.41%
2009	2008	269,180,359	1.0400	2,756,300	98.53%	100.30%
2010	2009	263,921,662	1.0400	2,744,785	(In process of Collection)	

^(a) Net of exemptions. Assessed valuations do not include adjustments in supplemental rolls made after the end of each fiscal year.^(b) Excludes penalties and interest.**Tax Rate Distribution (Tax Year)**

	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>
Maintenance	\$ 1.0400	\$ 1.0400	\$ 1.0400	\$ 1.3700	\$ 1.5000
Debt Service	-	-	-	-	-
Total	\$ <u>1.0400</u>	\$ <u>1.0400</u>	\$ <u>1.0400</u>	\$ <u>1.3700</u>	\$ <u>1.5000</u>

TABLE 4 - TEN LARGEST TAXPAYERS

<u>Name</u>	<u>2009 Net Taxable Assessed Valuation</u>	<u>% of Total 2009 Assessed Valuation</u>
TEMPLE INLAND FPC	\$ 48,538,321	18.39%
TIN INC	30,064,819	11.39%
HEXICON SPECIALTY CHEMICALS	8,171,210	3.10%
CONSOLIDATED COMM. OF TEXAS CO	6,067,500	2.30%
ONCOR ELECTRIC DELIVERY CO.	5,417,710	2.05%
CROWN PINE TIMBER 1 LP	5,289,892	2.00%
ATCO STRUCTURES	2,917,083	1.11%
LUFKIN INDUSTRIES	2,863,080	1.08%
UNION PACIFIC RAILROAD Co	2,863,030	1.08%
NATURAL GAS PIPELINE	2,754,670	1.04%
	\$ 114,947,315	43.55%

TABLE 5 - TAX ADEQUACY ^{(a) (b)}

Estimated Average Annual Debt Service Requirements (2010-2026):	\$ 962,851
\$0.3840 per \$100 AV against the 2009 Taxable AV, at 95% collection, produces	\$ 962,861
Estimated Maximum Annual Debt Service Requirements (2026):	\$ 1,109,413
\$0.4425 per \$100 AV against the 2009 Taxable AV, at 95% collection, produces	\$ 1,109,424

^(a) Includes the Bonds. Preliminary, subject to change.

TABLE 6 - ESTIMATED OVERLAPPING DEBT

The following summary of estimated outstanding ad valorem tax bonds of taxing entities in the District was compiled from a variety of sources listed below. No representation is made with respect to the accuracy or completeness of information obtained from sources other than the District. Furthermore, certain entities listed below may have issued substantial amounts of bonds since the dates shown in this table and may have capital improvement programs requiring the issuance of substantial amounts of additional bonds. Sources include: Texas Municipal Reports compiled and published by the Municipal Advisory Council of Texas, and the Angelina County Appraisal District.

<u>Taxing Jurisdiction</u>	<u>Total Debt ^(a)</u>	<u>Estimated % Overlapping</u>	<u>As Of</u>	<u>Overlapping Debt</u>
Angelina Co.	\$ 11,063,640	8.83%	6/30/08	\$ 976,919
Angelina Co. JCD	23,099,326	8.83%	4/1/09	2,039,670
Diboll, City of	3,865,000	100.00%	7/31/09	<u>3,865,000</u>
Estimated Overlapping Debt				\$ 6,881,590
The District	\$ 16,769,595 ^(b)	100.00%		<u>16,769,595 ^(b)</u>
Total Direct & Estimated Overlapping Debt				\$ 23,651,185
As a % of 2009 Taxable Assessed Valuation				8.96%

^(a) Gross debt.

^(b) Includes the Bonds. Preliminary, subject to change.

TABLE 7 - PRO FORMA TAX SUPPORTED DEBT SERVICE REQUIREMENTS

FYE 31-Aug	Outstanding Debt Service	U/L Tax School Building Bonds, Series 2010 ^(a)			Total Debt Service ^(c)
		Principal	Interest ^(b)	Total	
2010	\$ 28,408	\$ -	\$ -	\$ -	\$ 28,408
2011	55,581	25,000	571,099	596,099	651,680
2012	400,581	-	473,430	473,430	874,011
2013	410,581	-	473,430	473,430	884,011
2014	415,581	-	473,430	473,430	889,011
2015	420,581	-	473,430	473,430	894,011
2016	425,581	-	473,430	473,430	899,011
2017	430,581	-	473,430	473,430	904,011
2018	435,581	-	473,430	473,430	909,011
2019	435,581	-	473,430	473,430	909,011
2020	440,581	-	473,430	473,430	914,011
2021	445,581	-	473,430	473,430	919,011
2022	450,581	-	473,430	473,430	924,011
2023	455,581	-	473,430	473,430	929,011
2024	460,581	-	473,430	473,430	934,011
2025	465,581	-	473,430	473,430	939,011
2026	470,581	-	473,430	473,430	944,011
2027	-	645,000	460,530	1,105,530	1,105,530
2028	-	54,595	1,053,035	1,107,630	1,107,630
2029	-	675,000	434,130	1,109,130	1,109,130
2030	-	700,000	406,630	1,106,630	1,106,630
2031	-	730,000	377,574	1,107,574	1,107,574
2032	-	760,000	345,988	1,105,988	1,105,988
2033	-	795,000	312,564	1,107,564	1,107,564
2034	-	830,000	278,033	1,108,033	1,108,033
2035	-	865,000	241,798	1,106,798	1,106,798
2036	-	905,000	202,838	1,107,838	1,107,838
2037	-	945,000	161,213	1,106,213	1,106,213
2038	-	990,000	117,675	1,107,675	1,107,675
2039	-	1,035,000	72,113	1,107,113	1,107,113
2040	-	1,085,000	24,413	1,109,413	1,109,413
	<u>\$ 6,647,704</u>	<u>\$ 11,039,595</u>	<u>\$ 12,161,079</u>	<u>\$ 23,200,674</u>	<u>\$ 29,848,378</u>

Estimated Average Annual Debt Service Requirements (2010-2026): \$ 962,851
 Estimated Maximum Annual Debt Service Requirements (2026): \$ 1,109,413

^(a) Preliminary, subject to change.

^(b) Interest calculated at market rates for illustration purposes.

^(c) Total debt service does not include any federal subsidy on the Bonds.

TABLE 8 - AUTHORIZED BUT UNISSUED UNLIMITED TAX BONDS

<u>Date Authorized</u>	<u>Purpose</u>	<u>Amount Authorized</u>	<u>Heretofore Issued</u>	<u>The Bonds</u>	<u>Authorized But Unissued</u>
November 3, 2009	School Building	\$ 22,500,000	\$ 5,730,000	\$ 11,039,595	\$ 5,730,405 ^(a)

^(a) The District will receive the full \$22,500,000 into the Project Fund and therefore this amount is not available to be issued..

TABLE 9 - INTEREST AND SINKING FUND BUDGET PROJECTION

Tax Supported Debt Service Requirements, FYE August 31, 2011 ^(a)		\$ 651,680
Estimated Debt Service Fund, August 31, 2010	\$ 46,247	
Capitalized Interest/Cash Deposit	-	
Estimated Interest and Sinking Fund Tax Levy @ 95%	1,078,120 ^(b)	1,124,367
Estimated Balance, August 31, 2011		\$ 472,687

^(a) Includes the Bonds. Preliminary. subject to change.

^(b) Assumes and I&S tax rate of \$0.43.

TABLE 10 - GENERAL FUND REVENUES AND EXPENDITURE HISTORY ^(a)

For Fiscal Year Ended August 31

	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>
REVENUES					
Local and Intermediate Sources	\$ 3,246,209	\$ 3,374,475	\$ 4,142,437	\$ 4,702,836	\$ 4,145,716
State Program Revenues	9,377,541	9,247,118	8,331,479	8,141,236	8,509,243
Federal Program Revenues	77,047	75,726	68,709	56,470	-
Total Revenues	<u>\$ 12,700,797</u>	<u>\$ 12,697,319</u>	<u>\$ 12,542,625</u>	<u>\$ 12,900,542</u>	<u>\$ 12,654,959</u>
EXPENDITURES					
Instruction	\$ 6,934,677	\$ 7,312,177	\$ 6,382,960	\$ 6,608,389	\$ 6,030,320
Instructional Resources and Media	350,113	365,212	298,963	305,291	289,707
Curriculum & Staff Dev.	44,461	35,265	70,279	60,689	64,301
Instructional Leadership	211,890	178,232	282,579	290,105	217,928
School Leadership	756,431	748,499	782,556	853,552	820,562
Guidance, Counsel & Evaluation. Serv.	269,495	280,310	413,380	356,356	239,115
Health Services	112,738	115,932	110,550	108,564	101,254
Student (Pupil) Transportation	481,521	516,596	675,953	443,300	507,422
Extracurricular Activities	515,951	499,355	534,402	477,131	460,624
General Administration	596,586	583,075	487,192	597,078	482,765
Plant Maintenance and Operations	1,693,328	1,694,293	1,807,471	1,724,524	1,502,267
Security and Monitoring Services	19,023	27,614	68,413	75,016	61,094
Data Processing Services	328,752	337,762	370,811	349,141	344,884
Community Service	59,445	79,790	69,682	92,009	80,625
Principal on Long-Term Debt	321,100	332,930	332,331	359,780	223,387
Interest on long-term debt	37,092	50,345	50,231	47,245	50,304
Bond issuance costs and fees	2,841	1,491	2,110	308	1,399
Capital Outlay	-	143,268	470,184	1,953,430	121,348
Pmts related to Shared Serv. Arrang.	63,250	56,050	59,840	495,529	488,445
Pmts to Juvenile Justice Alt. Ed. Prog.	-	-	-	-	-
Total Expenditures	<u>\$ 12,798,694</u>	<u>\$ 13,358,196</u>	<u>\$ 13,269,887</u>	<u>\$ 15,197,437</u>	<u>\$ 12,087,751</u>
Excess (Deficiency) Rev. Over Exp.	\$ (97,897)	\$ (660,877)	\$ (727,262)	\$ (2,296,895)	\$ 567,208
Operating Transfers Out	-	(336,698)	-	(46,529)	-
Operating Transfers In	-	336,698	-	-	-
Other (Uses)	-	(164,850)	-	-	-
Excess (Deficiency) of Rev. and Other Resources Over Exp. and Other Uses	<u>\$ (97,897)</u>	<u>\$ (825,727)</u>	<u>\$ (727,262)</u>	<u>\$ (2,343,424)</u>	<u>\$ 567,208</u>
Fund Balance - Sept. 1 (Beginning)	\$ 2,819,904 ^(b)	\$ 3,634,631	\$ 4,361,893	\$ 6,705,317	\$ 6,138,109
Increase (Decrease) in Fund Balance	-	-	-	-	-
Fund Balance - August 31 (Ending)	<u>\$ 2,722,007</u>	<u>\$ 2,808,904</u>	<u>\$ 3,634,631</u>	<u>\$ 4,361,893</u>	<u>\$ 6,705,317</u>

^(a) Source: District's audited financial reports. See "APPENDIX B - Audited Financial Statements."

^(b) Per page 31 of the year ended August 31, 2009 audited financial statements.

APPENDIX B

**EXCERPTS FROM THE DISTRICT'S
AUDITED FINANCIAL REPORT**

**For Year Ended
August 31, 2009**

**DIBOLL
INDEPENDENT SCHOOL DISTRICT**

ANNUAL FINANCIAL REPORT

FOR THE YEAR ENDED AUGUST 31, 2009

Introductory Section

Diboll Independent School District
Annual Financial Report
For The Year Ended August 31, 2009

TABLE OF CONTENTS

	<u>Page</u>	<u>Exhibit</u>
INTRODUCTORY SECTION		
Certificate of Board.....	1	
FINANCIAL SECTION		
Independent Auditor's Report on Financial Statements.....	2	
Management's Discussion and Analysis (Required Supplementary Information).....	4	
<u>Basic Financial Statements</u>		
Government-wide Financial Statements:		
Statement of Net Assets.....	14	A-1
Statement of Activities.....	15	B-1
Fund Financial Statements:		
Balance Sheet - Governmental Funds.....	16	C-1
Reconciliation of the Governmental Funds		
Balance Sheet to the Statement of Net Assets.....	17	C-1R
Statement of Revenues, Expenditures, and Changes in		
Fund Balances - Governmental Funds.....	18	C-2
Reconciliation of the Statement of Revenues, Expenditures, and Changes in		
Fund Balances of Governmental Funds to the Statement of Activities.....	19	C-3
Statement of Fiduciary Net Assets - Fiduciary Funds.....	20	E-1
Notes to the Financial Statements	21	
<u>Required Supplementary Information:</u>		
Budgetary Comparison Schedules:		
General Fund.....	31	G-1
National School Breakfast and Lunch Program.....	32	G-2
<u>Combining Statements as Supplementary Information:</u>		
Combining Balance Sheet - All Nonmajor Governmental Funds.....	33	H-1
Combining Statement of Revenues, Expenditures and Changes in		
Fund Balances - All Nonmajor Governmental Funds.....	34	H-2
<u>Special Revenue Funds:</u>		
Combining Balance Sheet - Nonmajor Special Revenue Funds.....	35	H-3
Combining Statement of Revenues, Expenditures and Changes		
in Fund Balances - Nonmajor Special Revenue Funds.....	39	H-4
<u>Fiduciary Funds:</u>		
Agency Funds:		
Combining Statement of Fiduciary Assets and Liabilities.....	46	H-5

Diboll Independent School District
 Annual Financial Report
 For The Year Ended August 31, 2009

TABLE OF CONTENTS

	<u>Page</u>	<u>Exhibit</u>
 OTHER SUPPLEMENTARY INFORMATION SECTION		
Schedule of Delinquent Taxes Receivable.....	47	J-1
Indirect Cost Computation Schedule	49	J-2
Fund Balance and Cash Flow Calculation Worksheet (Unaudited)-General Fund.....	50	J-3
Schedule of Loans.....	51	J-4
Budgetary Comparison Schedules Required by the Texas Education Agency: Debt Service Fund.....	53	J-5
Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	54	
Report on Compliance with Requirements Applicable To each Major Program and Internal Control over Compliance In Accordance With OMB Circular A-133.....	56	
Schedule of Findings and Questioned Costs	58	
Summary Schedule of Prior Audit Findings.....	59	
Schedule of Expenditures of Federal Awards	60	K-1
Notes to the Schedule of Expenditures of Federal Awards.....	61	
Schedule of Required Responses to Selected School First Indicators.....	62	K-2

CERTIFICATE OF BOARD

Diboll Independent School District
Name of School District

Angelina
County

003-905
Co.-Dist. Number

We, the undersigned, certify that the attached annual financial reports of the above named school district were reviewed and (check one) _____approved _____disapproved for the year ended August 31, 2009, at a meeting of the board of trustees of such school district on the ____ day of _____, _____.

Signature of Board Secretary

Signature of Board President

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

Financial Section

JOHN R. PECHACEK, CPA
P.O. Box 549
Bellville, Texas 77418-0549

Independent Auditor's Report on Financial Statements

Board of Trustees
Diboll Independent School District
401 Dennis
Diboll, Texas 75941

Members of the Board of Trustees:

I have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Diboll Independent School District as of and for the year ended August 31, 2009, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Diboll Independent School District's management. My responsibility is to express opinions on these financial statements based on my audit.

I conducted my 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 I 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 significant estimates made by management, as well as evaluating the overall financial statement presentation. I believe that my audit provides a reasonable basis for my opinions.

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Diboll Independent School District as of August 31, 2009, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

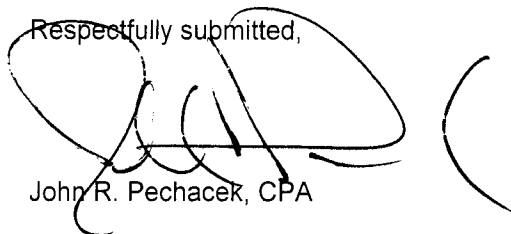
In accordance with *Government Auditing Standards*, I have also issued my report dated February 24, 2010, on my consideration of Diboll Independent School District's internal control over financial reporting and on my tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of my 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 my audit.

The Management's Discussion and Analysis and the budgetary comparison information identified as Required Supplementary Information in the table of contents are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. I have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, I did not audit the information and express no opinion on it.

**Diboll Independent School District
Independent Auditor's Report on Financial Statements
Page 2 of 2**

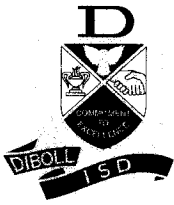
My audit was performed for the purpose of forming opinions on the financial statements which collectively comprise the Diboll Independent School District's basic financial statements. The accompanying schedule of expenditures of federal awards required by U. S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations* and the combining financial statements and supporting schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. This information, except for that portion marked "unaudited" on which I express no opinion, has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in my opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "John R. Pechacek", is written over a horizontal line. To the right of the signature is a large, hand-drawn left curly parenthesis "(".

John R. Pechacek, CPA

February 24, 2010



DIBOLL INDEPENDENT SCHOOL DISTRICT

P.O. BOX 550 • DIBOLL, TEXAS 75941 • 936/829-4718 • FAX 936/829-5558

Board of Trustees
Diboll Independent School District
Diboll, Texas

MANAGEMENT'S DISCUSSION AND ANALYSIS

Members of the Board:

We are pleased to submit to you the accompanying financial statements for the Diboll Independent School District as of and for the fiscal year ended August 31, 2009. These statements have been prepared in accordance with Governmental Accounting Standards Board (GASB) Statement Number 34.

This discussion and analysis of the Diboll Independent School District's financial performance provides an overview of the District's financial activities for the fiscal year ended August 31, 2009. It should be read in conjunction with the District's financial statements, which begin on page 14 of this report.

FINANCIAL HIGHLIGHTS

- The District's total combined net assets at August 31, 2009 were \$14,937,690.
- For the fiscal year ended August 31, 2009, the District's total expenses were \$902,833 more than the \$16,055,395 generated from ad valorem tax collections, State foundation program entitlements and other grants and miscellaneous revenues.
- The General Fund reported a fund balance of \$2,722,007 at August 31, 2009.
- The Debt Service Fund reported a fund balance of \$46,247 at August 31, 2009.
- The Capital Projects Fund reported a fund balance of \$335,717 at August 31, 2009.
- The District's long-term debt decreased by a total of \$321,099 during the year.

**Diboll Independent School District
MANAGEMENT'S DISCUSSION AND ANALYSIS**

OVERVIEW OF THE FINANCIAL STATEMENTS

The annual report consists of three parts – *Management's Discussion and Analysis* (this section), the *Basic Financial Statements*, and *Required Supplemental Information*. The basic financial statements include two kinds of statements that present different views of the District.

- The first two statements are *government-wide financial statements* that provide both *long-term* and *short-term* information about the District's overall financial status.
- The remaining statements are *fund financial statements* that focus on *individual parts* of the government, reporting the District's operations in more detail than the government-wide statements.
- The *governmental funds* statements tell how *general government* services were financed in the *short term* as well as what remains for future spending.
- *Fiduciary fund* statements provide information about the financial relationships in which the District acts solely as a trustee or *agent* for the benefit of others, to whom the fiduciary resources belong. This fund includes student activity funds.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The notes to the financial statements are followed by a section entitled *Required Supplementary Information* that further explains and supports the information in the financial statements.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The government-wide statements report information about the District as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the government's assets and liabilities. All of the current period's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the District's net assets and how they have changed. The net asset balance is the difference between the District's assets and liabilities and is one way to measure the District's financial health or *position*.

- Over time, increases or decreases in the District's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the District, one needs to consider additional non-financial factors such as changes in the District's tax base, staffing patterns, enrollment and attendance.

Diboll Independent School District MANAGEMENT'S DISCUSSION AND ANALYSIS

The government-wide financial statements of the District include the *Governmental activities*. Most of the District's basic services such as instruction, extracurricular activities, curriculum and staff development, health services, general administration and plant operation and maintenance are included in *Governmental activities*. Locally assessed property taxes, together with State Foundation Program entitlements, which are based upon student enrollment and attendance, finance most of the government activities.

FUND FINANCIAL STATEMENTS

The fund financial statements provide more detailed information about the District's most significant *funds* – not the District as a whole. Funds are simply accounting devices that are used to keep track of specific sources of funding and spending for particular purposes.

- Some funds are required by State law and other funds are mandated by bond agreements or bond covenants.
- The Board of Trustees establishes other funds to control and manage money set aside for particular purposes or to show that the District is properly using certain taxes and grants.
- Other funds are used to account for assets held by the District in a custodial capacity – these assets do not belong to the District but the District is responsible to properly account for them.

The District has the following kinds of fund:

- *Governmental Funds* – Most of the District's basic services are included in governmental funds, which focus on (1) how *cash and other financial assets* that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental fund statements provide a detailed *short-term* view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the District's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds statement, or on the subsequent page, that explain the relationship (or differences) between them.
- *Fiduciary funds* – the District serves as the trustee, or *fiduciary*, for certain funds such as student activity funds. The District is responsible for ensuring that the assets reported in these funds are used for their intended purposes. All of the District's fiduciary activities are reported in a separate statement of fiduciary net assets and a statement of changes in fiduciary net assets. We exclude these activities from the District's government-wide financial statements because the District cannot use these assets to finance its governmental operations.

**Diboll Independent School District
MANAGEMENT'S DISCUSSION AND ANALYSIS**

FINANCIAL ANALYSIS OF THE DISTRICT AS A WHOLE

The District's combined net assets were \$14,937,690 at August 31, 2009. *Table 1* focuses on the net assets while *Table 2* shows the revenues and expenses that changed the net asset balance during the fiscal year ended August 31, 2009.

**Table 1
Net Assets**

Description	Governmental Activities		Total Percentage Change
	2009	2008	2009-2008
Current Assets	\$ 4,426,161	\$ 4,705,502	-5.94%
Capital Assets	14,494,885	15,422,257	-6.01%
Total Assets	18,921,046	20,127,759	-6.00%
Current Liabilities	1,247,334	1,261,197	-1.10%
Long-Term Liabilities	2,736,022	3,037,039	-9.91%
Total Liabilities	3,983,356	4,298,236	-7.33%
Net Assets:			
Invested in Capital Assets	11,427,178	12,011,179	-4.86%
Restricted (1)	858,658	873,155	-1.66%
Unrestricted	2,651,854	2,945,189	-9.96%
Total Net Assets	\$ 14,937,690	\$ 15,829,523	-5.63%

Notes to Table 1

(1) A Summary of Restricted Net Assets are as follows:

	2009	2008
Restricted for State and Federal Programs	\$ 342,764	\$ 371,561
Restricted for Debt Service	45,404	43,593
Restricted for Capital Projects	335,717	333,766
Restricted for Campus Activities	134,773	124,235
Total Restricted Net Assets	\$ 858,658	\$ 873,155

**Diboll Independent School District
MANAGEMENT'S DISCUSSION AND ANALYSIS**

**Table 2
Changes in Net Assets**

Description	Governmental Activities		Total Percentage Change 2009-2008
	2009	2008	
Program Revenues			
Charges for Service	\$ 667,979	\$ 423,248	57.82%
Operating Grants and Contributions	3,661,188	3,255,823	12.45%
General Revenues -			
Property Taxes	2,807,809	2,862,660	-1.92%
State Foundation Program	9,037,237	8,885,733	1.71%
Investment Earnings	38,592	170,263	-77.33%
Other Revenues	335,856	372,232	-9.77%
Total Revenues	<u>16,548,661</u>	<u>15,969,959</u>	<u>3.62%</u>
Program Expenditures:			
Instruction	\$ 8,967,434	\$ 9,499,709	-5.60%
Instructional Resources and Media Services	382,907	402,724	-4.92%
Curriculum and Staff Development	131,431	53,217	146.97%
Instructional Leadership	247,655	252,323	-1.85%
School Leadership	770,490	754,873	2.07%
Guidance and Counseling	509,125	477,278	6.67%
Health Services	123,451	117,042	5.48%
Student Transportation	605,736	593,822	2.01%
Food Services	1,172,702	1,217,090	-3.65%
Extracurricular Activities	903,616	538,322	67.86%
General Administration	651,894	600,356	8.58%
Plant Operating and Maintenance	1,797,199	1,719,780	4.50%
Security and Monitoring Services	22,607	29,639	-23.73%
Data Processing Services	330,240	338,852	-2.54%
Community Services	260,829	141,429	84.42%
Interest on Debt / Issuance Costs & Fees on Debt	17,662	51,836	-65.93%
Capital Outlay	-	7,411	-100.00%
Payments Related to Shared Service Arrangements	63,250	56,050	12.85%
Total Expenses	<u>16,958,228</u>	<u>16,851,753</u>	<u>0.63%</u>
Excess (Deficiency) Before Other Resources and Uses and Transfers	(409,567)	(881,794)	-53.55%
Other Resources (Uses)	(493,266)	-	-
Transfers In (Out)	-	-	-
Increase (Decrease) in Net Assets	<u>\$ (902,833)</u>	<u>\$ (881,794)</u>	<u>2.39%</u>

**Diboll Independent School District
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Governmental Activities

Significant factors affecting the decrease of \$902,833 in net assets included:

- Revenues for the District increased by approximately \$578,700, or 3.62%, while expenses increased by approximately \$105,000, or .63%.
- Investment earnings decreased approximately \$130,000, or 77.33% during the 2009 fiscal year.
- Charges for services revenue increased approximately \$245,000, or 57.82%.
- The District deleted \$493,266 of fixed assets in order to report the appropriate totals.

Cost of District's Functions

The District records its expenses in various cost centers of "functions" in accordance with the requirements of the Texas Education Agency. *Table 3* presents the cost of each of the functions with the largest expense totals with that function's net costs (total cost less fees and grants that are directly attributable to that function). The net cost of each function reflects what was funded primarily from state foundation program and tax revenues.

**Table 3
Total and Net Cost of Selected District Functions**

Description	Total Cost of Services		Net Cost of Services		
	2009	2008	2009	2008	% Change
Instruction	\$ 8,967,434	\$ 9,499,709	\$ 6,800,302	\$ 7,422,427	-8.38%
Plant Main. and Operation	1,797,199	1,719,780	1,739,234	1,709,516	1.74%
School Leadership	770,490	754,873	757,638	750,248	0.99%
Food Service	1,172,702	1,217,090	82,394	204,669	-59.74%
Guidance and Counseling	509,125	477,278	293,772	279,954	4.94%

FINANCIAL ANALYSIS OF THE DISTRICT'S FUNDS

At the close of the fiscal year ending August 31, 2009, the District's combined governmental funds (as presented in the balance sheet, Exhibit C-1 on page 16 of this report) reported a combined fund balance of \$3,390,382. This compares to a combined fund balance of \$3,693,059 at August 31, 2008.

Diboll Independent School District MANAGEMENT'S DISCUSSION AND ANALYSIS

Budgetary Highlights

In accordance with State law and generally accepted accounting standards, the District prepares an annual budget for the General Fund, the Food Service Special Revenue Fund, and for the Debt Service Fund. The District budgets the Capital Projects Fund for each *project*, which normally cover multiple years. Special Revenue Funds have budgets approved by the funding agency and are amended throughout the year as required.

During the period ended August 31, 2009, the District amended its budget as required by State law and to reflect current levels of revenue and anticipated expenses. The District was able to keep expenditures below the budgeted level in the General Fund, Food Service Fund and Debt Service Fund. Rising operating costs caused the District to significantly amend the Function 51 (Plant Maintenance and Operations) budget in the General Fund, however, the District still managed to spend well below the final budget amount.

Actual revenues fell short of the revenue budget by \$225,628 and the expense budget exceeded actual expenses by \$464,248.

The Food Service Fund experienced a negative overall budget variance of \$60,877. Actual revenues were \$79,783 less than budgeted revenues, while expenditures were \$18,906 below budgeted expenditures.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

Capital assets are generally defined as those items that have useful lives of two years or more and have an initial cost or valued (if donated) of an amount determined by the Board. During the fiscal year ended August 31, 2009, the District used a capitalization threshold of \$5,000, which means that all capital type assets, including library books, with a cost or initial value of less than \$5,000, were not included in the capital assets inventory.

At August 31, 2009, the District had a total of \$22,562,542 invested in capital assets such as land, buildings, vehicles and equipment (*see Table 4*). During the year, the District deleted \$493,266 of capital assets to correct differences in the financial statements and district records.

Table 4 shows the classifications of capital assets together with the District's accumulated cost and depreciation of those assets.

**Diboll Independent School District
MANAGEMENT'S DISCUSSION AND ANALYSIS**

**Table 4
Capital Assets and Depreciation**

Asset Description	Governmental Activities		Total Percentage Change
	2009	2008	2009-2008
Land	\$ 1,089,694	\$ 1,089,694	0.00%
Construction in Progress	-	2,076,666	-100.00%
Buildings and Improvements	19,027,071	17,573,091	8.27%
Vehicles	1,189,046	1,070,319	11.09%
Equipment	1,256,731	1,080,682	16.29%
Total Historical Cost	22,562,542	22,890,452	-1.43%
Accumulated Depreciation	8,067,657	7,468,195	8.03%
Net Capital Assets	\$ 14,494,885	\$ 15,422,257	-6.01%

Notes to Table 4 –

More detailed information about the District's capital assets can be found in the notes to the financial statements on page 26.

Long-Term Debt

At August 31, 2009, the District had three loan issues outstanding of which the unpaid principal totaled \$3,060,832.

The District does not have the policy of paying for unused, accumulated sick leave for qualified employees upon their death or retirement.

Table 5 summarizes the District's outstanding debt at August 31, 2009. More detailed information regarding the District's debt obligations is presented in the notes to the financial statements on pages 27 and 28.

**Table 5
Analysis of Debt**

Description of Debt Outstanding	Governmental Activities		Total Percentage Change
	2009	2008	2009-2008
Loans Payable	\$ 3,060,832	\$ 3,381,932	-9.49%
Bonds Payable	-	-	0.00%
Total Debt Outstanding	\$ 3,060,832	\$ 3,381,932	-9.49%

ECONOMIC FACTORS AND THE NEXT YEAR'S BUDGETS

Economic Factors

The following factors were considered in establishing the District's budget for 2009-2010:

- Student enrollment for the 2009-2010 is expected to be unchanged compared to the 2008-2009 school year. The refined average daily attendance is projected to remain constant as well compared to the 2008-2009 school year.
- Property values for ad valorem tax purposes have declined slightly compared to 2008-2009.
- The District has maintained the same tax rate of \$1.04 for 2009-2010 as in 2008-2009.
- No new programs were added and no significant changes to existing programs occurred during the current year and no significant changes are planned for 2009-2010.

Next Year's Budget

- The District's general fund operating expenditures are budgeted to increase \$592,392 or 5% in comparison to \$12,798,694 of actual expenditures incurred in 2008-2009. Revenues are budgeted to increase \$690,289 compared to actual revenues in 2008-2009. The Board approved a balanced budget of revenue and expenditures for 2009-2010.
- The food service fund operating expenditures are budgeted to decrease \$222,479 or 17% in comparison to \$1,286,479 of actual expenditures incurred in 2008-2009. Revenues are budgeted to decrease \$78,613 compared to actual revenues in 2008-2009.

District officials anticipate that the fund balance for the general fund will not materially change for 2009-2010 compared to 2008-2009.

**Diboll Independent School District
MANAGEMENT'S DISCUSSION AND ANALYSIS**

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, students and creditors with a general fund overview of the District's finances and to demonstrate the District's commitment to accountability for the money it receives. If you have questions about this report or need additional financial information, contact Kevin Mathis, Asst. Superintendent at (936) 829-4718.

Basic Financial Statements

DIBOLL INDEPENDENT SCHOOL DISTRICT

STATEMENT OF NET ASSETS

AUGUST 31, 2009

Data Control Codes	1	Governmental Activities
ASSETS:		
1110	Cash and Cash Equivalents	\$ 3,753,149
1225	Property Taxes Receivable (Net)	120,131
1240	Due from Other Governments	504,578
1250	Accrued Interest	20,589
1290	Other Receivables (Net)	21,213
1300	Inventories	4,815
1410	Deferred Expenses	1,686
Capital Assets:		
1510	Land	1,089,694
1520	Buildings and Improvements, Net	12,207,521
1530	Furniture and Equipment, Net	1,197,670
1000	Total Assets	<u>18,921,046</u>
LIABILITIES:		
2110	Accounts Payable	84,837
2120	Short-Term Debt Payable	324,810
2140	Interest Payable	6,875
2165	Accrued Liabilities	465,559
2300	Unearned Revenue	365,253
Noncurrent Liabilities:		
2502	Due in More Than One Year	2,736,022
2000	Total Liabilities	<u>3,983,356</u>
NET ASSETS		
3200	Invested in Capital Assets, Net of Related Debt	11,427,178
Restricted For:		
3820	Federal and State Programs	342,764
3850	Debt Service	45,404
3860	Capital Projects	335,717
3870	Campus Activities	134,773
3900	Unrestricted	2,651,854
3000	Total Net Assets	<u>\$ 14,937,690</u>

The accompanying notes are an integral part of this statement.

DIBOLL INDEPENDENT SCHOOL DISTRICT

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED AUGUST 31, 2009

Data Control Codes	Functions/Programs	1	3	4	Net (Expense) Revenue and Changes in Net Assets
		Expenses	Charges for Services	Program Revenues Operating Grants and Contributions	Governmental Activities
	Governmental Activities:				
11	Instruction	\$ 8,967,434	\$ 36,875	\$ 2,130,257	\$ (6,800,302)
12	Instructional Resources and Media Services	382,907	--	27,297	(355,610)
13	Curriculum and Staff Development	131,431	--	83,857	(47,574)
21	Instructional Leadership	247,655	--	37,152	(210,503)
23	School Leadership	770,490	--	12,852	(757,638)
31	Guidance, Counseling, & Evaluation Services	509,125	--	215,353	(293,772)
33	Health Services	123,451	--	10,587	(112,864)
34	Student Transportation	605,736	--	10,934	(594,802)
35	Food Service	1,172,702	233,935	856,373	(82,394)
36	Cocurricular/Extracurricular Activities	903,616	397,169	32,711	(473,736)
41	General Administration	651,894	--	47,951	(603,943)
51	Plant Maintenance and Operations	1,797,199	--	57,965	(1,739,234)
52	Security and Monitoring Services	22,607	--	817	(21,790)
53	Data Processing Services	330,240	--	2,152	(328,088)
61	Community Services	260,829	--	134,400	(126,429)
72	Interest on Long-term Debt	14,821	--	116	(14,705)
73	Bond Issuance Costs and Fees	2,841	--	--	(2,841)
93	Payments Related to Shared Services Arrangements	63,250	--	414	(62,836)
TG	Total Governmental Activities	16,958,228	667,979	3,661,188	(12,629,061)
TP	Total Primary Government	\$ 16,958,228	\$ 667,979	\$ 3,661,188	(12,629,061)
	General Revenues:				
MT	Property Taxes, Levied for General Purposes				2,806,681
DT	Property Taxes, Levied for Debt Service				1,128
IE	Investment Earnings				38,592
GC	Grants and Contributions Not Restricted to Specific Programs				9,037,237
MI	Miscellaneous				335,856
	Special and Extraordinary Items:				
S2	Special Item Outflow				(493,266)
TR	Total General Revenues				11,726,228
CN	Change in Net Assets				(902,833)
NB	Net Assets - Beginning				15,840,523
NE	Net Assets - Ending				\$ 14,937,690

The accompanying notes are an integral part of this statement.

DIBOLL INDEPENDENT SCHOOL DISTRICT

BALANCE SHEET - GOVERNMENTAL FUNDS

AUGUST 31, 2009

Data Control Codes	10 General Fund	24 National School Breakfast/Lunch Program	Other Governmental Funds	98 Total Governmental Funds	
ASSETS:					
1110	Cash and Cash Equivalents	\$ 2,945,565	\$ 287,166	\$ 520,418	\$ 3,753,149
1225	Taxes Receivable, Net	119,190	--	941	120,131
1240	Due from Other Governments	334,284	92,057	78,237	504,578
1250	Accrued Interest	20,589	--	--	20,589
1260	Due from Other Funds	275,002	16,424	318	291,744
1290	Other Receivables	--	--	21,213	21,213
1300	Inventories	4,815	--	--	4,815
1410	Deferred Expenditures	1,686	--	--	1,686
1000	Total Assets	\$ 3,701,131	\$ 395,647	\$ 621,127	\$ 4,717,905
LIABILITIES:					
Current Liabilities:					
2110	Accounts Payable	\$ 54,388	\$ 27,634	\$ 2,815	\$ 84,837
2120	Short-Term Debt Payable	91,535	--	--	91,535
2150	Payroll Deductions & Withholdings	594	--	--	594
2160	Accrued Wages Payable	355,091	18,339	--	373,430
2170	Due to Other Funds	--	266,564	25,180	291,744
2300	Unearned Revenue	477,516	6,926	941	485,383
2000	Total Liabilities	979,124	319,463	28,936	1,327,523
FUND BALANCES:					
Reserved Fund Balances:					
3420	Debt Service	--	--	46,247	46,247
3450	Reserve for Food Service	--	76,184	--	76,184
3490	Other Reserves of Fund Balance	--	--	210,227	210,227
Designated Fund Balance:					
3510	Construction	--	--	335,717	335,717
3600	Unreserved	2,722,007	--	--	2,722,007
3000	Total Fund Balances	2,722,007	76,184	592,191	3,390,382
4000	Total Liabilities and Fund Balances	\$ 3,701,131	\$ 395,647	\$ 621,127	\$ 4,717,905

The accompanying notes are an integral part of this statement.

DIBOLL INDEPENDENT SCHOOL DISTRICT

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS
AUGUST 31, 2009

Total fund balances - governmental funds balance sheet	\$ 3,390,382
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not reported in the funds.	14,494,885
Property taxes receivable unavailable to pay for current period expenditures are deferred in the funds.	120,130
Payables for notes which are not due in the current period are not reported in the funds.	(3,060,832)
Other long-term liabilities which are not due and payable in the current period are not reported in the funds.	<u>(6,875)</u>
Net assets of governmental activities - statement of net assets	<u>\$ 14,937,690</u>

The accompanying notes are an integral part of this statement.

DIBOLL INDEPENDENT SCHOOL DISTRICT

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES

IN FUND BALANCES - GOVERNMENTAL FUNDS

FOR THE YEAR ENDED AUGUST 31, 2009

Data Control Codes	10 General Fund	24 National School Breakfast/Lunch Program	Other Governmental Funds	98 Total Governmental Funds
REVENUES:				
5700 <i>Local and Intermediate Sources</i>	\$ 3,246,209	\$ 243,488	\$ 376,694	\$ 3,866,391
5800 <i>State Program Revenues</i>	9,377,541	6,874	668,971	10,053,386
5900 <i>Federal Program Revenues</i>	77,047	892,251	1,675,741	2,645,039
5020 Total Revenues	<u>12,700,797</u>	<u>1,142,613</u>	<u>2,721,406</u>	<u>16,564,816</u>
EXPENDITURES:				
Current:				
0011 <i>Instruction</i>	6,934,677	--	1,749,921	8,684,598
0012 <i>Instructional Resources and Media Services</i>	350,113	--	25,005	375,118
0013 <i>Curriculum and Staff Development</i>	44,461	--	84,262	128,723
0021 <i>Instructional Leadership</i>	211,890	--	35,765	247,655
0023 <i>School Leadership</i>	756,431	--	7,899	764,330
0031 <i>Guidance, Counseling, & Evaluation Services</i>	269,495	--	238,551	508,046
0033 <i>Health Services</i>	112,738	--	9,849	122,587
0034 <i>Student Transportation</i>	481,521	--	11,552	493,073
0035 <i>Food Service</i>	--	1,232,374	18,993	1,251,367
0036 <i>Cocurricular/Extracurricular Activities</i>	515,951	--	351,155	867,106
0041 <i>General Administration</i>	596,586	105	43,943	640,634
0051 <i>Plant Maintenance and Operations</i>	1,693,328	54,000	3,304	1,750,632
0052 <i>Security and Monitoring Services</i>	19,023	--	737	19,760
0053 <i>Data Processing Services</i>	328,752	--	--	328,752
0061 <i>Community Services</i>	59,445	--	201,384	260,829
0071 <i>Principal on Long-term Debt</i>	321,100	--	--	321,100
0072 <i>Interest on Long-term Debt</i>	37,092	--	--	37,092
0073 <i>Bond Issuance Costs and Fees</i>	2,841	--	--	2,841
0093 <i>Payments to Shared Service Arrangements</i>	63,250	--	--	63,250
6030 Total Expenditures	<u>12,798,694</u>	<u>1,286,479</u>	<u>2,782,320</u>	<u>16,867,493</u>
1100 Excess (Deficiency) of Revenues Over (Under)				
1100 Expenditures	(97,897)	(143,866)	(60,914)	(302,677)
1200 Net Change in Fund Balances	<u>(97,897)</u>	<u>(143,866)</u>	<u>(60,914)</u>	<u>(302,677)</u>
0100 Fund Balances - Beginning	2,819,904	220,050	653,105	3,693,059
3000 Fund Balances - Ending	<u>\$ 2,722,007</u>	<u>\$ 76,184</u>	<u>\$ 592,191</u>	<u>\$ 3,390,382</u>

The accompanying notes are an integral part of this statement.

DIBOLL INDEPENDENT SCHOOL DISTRICT

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED AUGUST 31, 2009

Net change in fund balances - total governmental funds	\$ (302,677)
Amounts reported for governmental activities in the statement of activities ("SOA") are different because:	
Capital outlays are not reported as expenses in the SOA.	184,249
The depreciation of capital assets used in governmental activities is not reported in the funds.	(618,355)
Trade-in or disposal of capital assets decrease net assets in the SOA but not in the funds.	(493,266)
Certain property tax revenues are deferred in the funds. This is the change in these amounts this year.	(16,152)
Repayment of loan principal is an expenditure in the funds but is not an expense in the SOA.	321,099
(Increase) decrease in accrued interest from beginning of period to end of period.	22,271
Rounding difference	<u>(3)</u>
Change in net assets of governmental activities - statement of activities	<u>\$ (902,833)</u>

The accompanying notes are an integral part of this statement.

DIBOLL INDEPENDENT SCHOOL DISTRICT

STATEMENT OF FIDUCIARY NET ASSETS

FIDUCIARY FUNDS

AUGUST 31, 2009

Data Control Codes		Agency Funds
ASSETS:		
1110	Cash and Cash Equivalents	\$ 5,003
1000	Total Assets	<u>\$ 5,003</u>
LIABILITIES:		
Current Liabilities:		
2190	Due to Student Groups	\$ 5,003
2000	Total Liabilities	<u>5,003</u>
NET ASSETS		
3000	Total Net Assets	<u>\$ --</u>

The accompanying notes are an integral part of this statement.

DIBOLL INDEPENDENT SCHOOL DISTRICT

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED AUGUST 31, 2009

A. Summary of Significant Accounting Policies

The basic financial statements of Diboll Independent School District (the "District") have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP") applicable to governmental units in conjunction with the Texas Education Agency's Financial Accountability System Resource Guide ("Resource Guide"). The Governmental Accounting Standards Board ("GASB") is the accepted standard setting body for establishing governmental accounting and financial reporting principles.

1. Reporting Entity

The Board of School Trustees ("Board"), a seven-member group, has governance responsibilities over all activities related to public elementary and secondary education within the jurisdiction of the District. The Board is elected by the public and has the exclusive power and duty to govern and oversee the management of the public schools of the District. All powers and duties not specifically delegated by statute to the Texas Education Agency ("TEA") or to the State Board of Education are reserved for the Board, and the TEA may not substitute its judgment for the lawful exercise of those powers and duties by the Board. The District receives funding from local, state and federal government sources and must comply with the requirements of those funding entities. However, the District is not included in any other governmental "reporting entity" as defined by the GASB in its Statement No. 14, "The Financial Reporting Entity," as revised by GASB Statement No.39, and there are no component units included within the reporting entity.

2. Basis of Presentation, Basis of Accounting

a. Basis of Presentation

Government-wide Financial Statements: The statement of net assets and the statement of activities include the financial activities of the overall government, except for fiduciary activities. Eliminations have been made to minimize the double-counting of internal activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other nonexchange transactions.

The statement of activities presents a comparison between direct expenses and program revenues for each function of the District's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. The District does not allocate indirect expenses in the statement of activities. Program revenues include (a) fees, fines, and charges paid by the recipients of goods or services offered by the programs and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

Fund Financial Statements: The fund financial statements provide information about the District's funds, with separate statements presented for each fund category. The emphasis of fund financial statements is on major governmental funds, each displayed in a separate column. All remaining governmental funds are aggregated and reported as nonmajor funds.

The District reports the following major governmental funds:

General Fund: This is the District's primary operating fund. It accounts for all financial resources of the District except those required to be accounted for in another fund.

Food Service Fund: This fund is used to account for the revenues and expenditures related to the operation of the Child Nutrition Program. This fund is legally required to be budgeted.

DIBOLL INDEPENDENT SCHOOL DISTRICT

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED AUGUST 31, 2009

In addition, the District reports the following fund types:

Capital Projects Fund: This fund is used to account for revenues and expenditures related to projects financed by the proceeds of long term debt or for capital projects otherwise mandated to be accounted for in this fund. This fund is not required to be budgeted on an annual basis.

Special Revenue Funds: These funds are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for specified purposes.

Debt Service Fund: This fund is used to account for the re-payment of bonded debt which is approved by the voters of the District. This fund is legally required to be budgeted.

Agency Funds: These funds are used to report student activity funds and other resources held in a purely custodial capacity (assets equal liabilities). Agency funds typically involve only the receipt, temporary investment, and remittance of fiduciary resources to individuals, private organizations, or other governments.

Fiduciary funds are reported in the fiduciary fund financial statements. However, because their assets are held in a trustee or agent capacity and are therefore not available to support District programs, these funds are not included in the government-wide statements.

b. **Measurement Focus, Basis of Accounting**

Government-wide and Fiduciary Fund Financial Statements: These financial statements are reported using the economic resources measurement focus. They are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Nonexchange transactions, in which the District gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, grants, entitlements, and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants, entitlements, and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

Governmental Fund Financial Statements: Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. The District does not consider revenues collected after its year-end to be available in the current period. Revenues from local sources consist primarily of property taxes. Property tax revenues and revenues received from the State are recognized under the susceptible-to-accrual concept. Miscellaneous revenues are recorded as revenue when received in cash because they are generally not measurable until actually received. Investment earnings are recorded as earned, since they are both measurable and available. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures to the extent they have matured. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term debt and acquisitions under capital leases are reported as other financing sources.

When the District incurs an expenditure or expense for which both restricted and unrestricted resources may be used, it is the District's policy to use restricted resources first, then unrestricted resources.

DIBOLL INDEPENDENT SCHOOL DISTRICT

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED AUGUST 31, 2009

3. Financial Statement Amounts

a. Property Taxes

Property taxes are levied by October 1 on the assessed value listed as of the prior January 1 for all real and business personal property in conformity with Subtitle E, Texas Property Tax Code. Taxes are due on receipt of the tax bill and are delinquent if not paid before February 1 of the year following the year in which imposed. On January 1 of each year, a tax lien attaches to property to secure the payment of all taxes, penalties, and interest ultimately imposed. Property tax revenues are considered available when they become due or past due and receivable within the current period.

Allowances for uncollectible tax receivables within the General and Debt Service Funds are based upon historical experience in collecting property taxes. Uncollectible personal property taxes are periodically reviewed and written off, but the District is prohibited from writing off real property taxes without specific statutory authority from the Texas Legislature.

b. Inventories and Prepaid Items

The District records purchases of supplies as expenditures, utilizing the purchase method of accounting for inventory in accordance with the Resource Guide.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items.

c. Capital Assets

Purchased or constructed capital assets are reported at cost or estimated historical cost. Donated fixed assets are recorded at their estimated fair value at the date of the donation. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized. A capitalization threshold of \$5,000 is used.

Capital assets are being depreciated using the straight-line method over the following estimated useful lives:

<u>Asset Class</u>	<u>Estimated Useful Lives</u>
Buildings	40
Building Improvements	20
Vehicles	5-10
Equipment	3-15

d. Receivable and Payable Balances

The District believes that sufficient detail of receivable and payable balances is provided in the financial statements to avoid the obscuring of significant components by aggregation. Therefore, no disclosure is provided which disaggregates those balances.

There are no significant receivables which are not scheduled for collection within one year of year end.

DIBOLL INDEPENDENT SCHOOL DISTRICT

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED AUGUST 31, 2009

e. Interfund Activity

Interfund activity results from loans, services provided, reimbursements or transfers between funds. Loans are reported as interfund receivables and payables as appropriate and are subject to elimination upon consolidation. Services provided, deemed to be at market or near market rates, are treated as revenues and expenditures or expenses. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers In and Transfers Out are netted and presented as a single "Transfers" line on the government-wide statement of activities. Similarly, interfund receivables and payables are netted and presented as a single "Internal Balances" line of the government-wide statement of net assets.

f. Use of Estimates

The preparation of financial statements in conformity with GAAP requires the use of management's estimates.

g. Data Control Codes

Data Control Codes appear in the rows and above the columns of certain financial statements. The TEA requires the display of these codes in the financial statements filed with TEA in order to insure accuracy in building a statewide database for policy development and funding plans.

B. Deposits and Investments

The District's funds are required to be deposited and invested under the terms of a depository contract. The depository bank deposits for safekeeping and trust with the District's agent bank approved pledged securities in an amount sufficient to protect District funds on a day-to-day basis during the period of the contract. The pledge of approved securities is waived only to the extent of the depository bank's dollar amount of Federal Deposit Insurance Corporation ("FDIC") insurance.

1. Cash Deposits:

At August 31, 2009, the carrying amount of the District's deposits (cash, certificates of deposit, and interest-bearing savings accounts included in temporary investments) was \$3,758,155 and the bank balance was \$3,937,266. The District's cash deposits at August 31, 2009 and during the year ended August 31, 2009, were entirely covered by FDIC insurance or by pledged collateral held by the District's agent bank in the District's name.

2. Investments:

The District is required by Government Code Chapter 2256, The Public Funds Investment Act, to adopt, implement, and publicize an investment policy. That policy must address the following areas: (1) safety of principal and liquidity, (2) portfolio diversification, (3) allowable investments, (4) acceptable risk levels, (5) expected rates of return, (6) maximum allowable stated maturity of portfolio investments, (7) maximum average dollar-weighted maturity allowed based on the stated maturity date for the portfolio, (8) investment staff quality and capabilities, and (9) bid solicitation preferences for certificates of deposit.

The Public Funds Investment Act ("Act") requires an annual audit of investment practices. Audit procedures in this area conducted as a part of the audit of the basic financial statements disclosed that in the areas of investment practices, management reports and establishment of appropriate policies, the District adhered to the requirements of the Act. Additionally, investment practices of the District were in accordance with local policies.

The Act determines the types of investments which are allowable for the District. These include, with certain restrictions, 1) obligations of the U.S. Treasury, U.S. agencies, and the State of Texas, 2) certificates of deposit, 3) certain municipal securities, 4) securities lending program, 5) repurchase agreements, 6) bankers acceptances, 7) mutual funds, 8) investment pools, 9) guaranteed investment contracts, and 10) commercial paper.

DIBOLL INDEPENDENT SCHOOL DISTRICT

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED AUGUST 31, 2009

The District's investments at August 31, 2009 are shown below.

<u>Investment or Investment Type</u>	<u>Maturity</u>	<u>Fair Value</u>
Lonestar Investment Pool	N/A	\$ 2,937,135
First Bank & Trust Govt. Obigs	N/A	246,156
Total Investments		<u>\$ 3,183,291</u>

* - These investments are accounted for as Cash and Cash Equivalents on A-1.

3. Analysis of Specific Deposit and Investment Risks

GASB Statement No. 40 requires a determination as to whether the District was exposed to the following specific investment risks at year end and if so, the reporting of certain related disclosures:

a. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The ratings of securities by nationally recognized rating agencies are designed to give an indication of credit risk. At year end, the District was not significantly exposed to credit risk.

At August 31, 2009, the District's investments, other than those which are obligations of or guaranteed by the U. S. Government, are rated as to credit quality as follows:

<u>Investment or Investment Type</u>	<u>Administrator</u>	<u>Rating</u>
Lonestar Investment Pool	First Public LLC	AAAm

b. Custodial Credit Risk

Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized, collateralized with securities held by the pledging financial institution, or collateralized with securities held by the pledging financial institution's trust department or agent but not in the District's name.

Investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the government, and are held by either the counterparty or the counterparty's trust department or agent but not in the District's name.

At year end, the District was not exposed to custodial credit risk.

c. Concentration of Credit Risk

This risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. At year end, the District was not exposed to concentration of credit risk.

d. Interest Rate Risk

This is the risk that changes in interest rates will adversely affect the fair value of an investment. At year end, the District was not exposed to interest rate risk.

e. Foreign Currency Risk

This is the risk that exchange rates will adversely affect the fair value of an investment. At year end, the District was not exposed to foreign currency risk.

DIBOLL INDEPENDENT SCHOOL DISTRICT

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED AUGUST 31, 2009

Investment Accounting Policy

The District's general policy is to report money market investments and short-term participating interest-earning investment contracts at amortized cost and to report nonparticipating interest-earning investment contracts using a cost-based measure. However, if the fair value of an investment is significantly affected by the impairment of the credit standing of the issuer or by other factors, it is reported at fair value. All other investments are reported at fair value unless a legal contract exists which guarantees a higher value. The term "short-term" refers to investments which have a remaining term of one year or less at time of purchase. The term "nonparticipating" means that the investment's value does not vary with market interest rate changes. Nonnegotiable certificates of deposit are examples of nonparticipating interest-earning investment contracts.

Public Funds Investment Pools

Public funds investment pools in Texas ("Pools") are established under the authority of the Interlocal Cooperation Act, Chapter 79 of the Texas Government Code, and are subject to the provisions of the Public Funds Investment Act (the "Act"), Chapter 2256 of the Texas Government Code. In addition to other provisions of the Act designed to promote liquidity and safety of principal, the Act requires Pools to: 1) have an advisory board composed of participants in the pool and other persons who do not have a business relationship with the pool and are qualified to advise the pool; 2) maintain a continuous rating of no lower than AAA or AAA-m or an equivalent rating by at least one nationally recognized rating service; and 3) maintain the market value of its underlying investment portfolio within one half of one percent of the value of its shares.

The District's investments in Pools are reported at an amount determined by the fair value per share of the pool's underlying portfolio, unless the pool is 2a7-like, in which case they are reported at share value. A 2a7-like pool is one which is not registered with the Securities and Exchange Commission ("SEC") as an investment company, but nevertheless has a policy that it will, and does, operate in a manner consistent with the SEC's Rule 2a7 of the Investment Company Act of 1940.

C. Capital Assets

Capital asset activity for the year ended August 31, 2009, was as follows:

	Beginning Balances	Increases	Decreases	Ending Balances
<u>Governmental activities:</u>				
<i>Capital assets not being depreciated:</i>				
Land	\$ 1,089,694	\$ --	\$ --	\$ 1,089,694
Construction in progress	2,076,666	--	2,076,666	--
Total capital assets not being depreciated	<u>3,166,360</u>	<u>--</u>	<u>2,076,666</u>	<u>1,089,694</u>
<i>Capital assets being depreciated:</i>				
Buildings and improvements	17,573,091	1,472,880	18,900	19,027,071
Equipment	1,080,682	176,049	--	1,256,731
Vehicles	1,070,319	118,727	--	1,189,046
Total capital assets being depreciated	<u>19,724,092</u>	<u>1,767,656</u>	<u>18,900</u>	<u>21,472,848</u>
Less accumulated depreciation for:				
Buildings and improvements	(6,483,733)	(354,717)	(18,900)	(6,819,550)
Equipment	(374,623)	(86,049)	--	(460,672)
Vehicles	(609,839)	(177,596)	--	(787,435)
Total accumulated depreciation	<u>(7,468,195)</u>	<u>(618,362)</u>	<u>(18,900)</u>	<u>(8,067,657)</u>
Total capital assets being depreciated, net	<u>12,255,897</u>	<u>1,149,294</u>	<u>--</u>	<u>13,405,191</u>
Governmental activities capital assets, net	<u>\$ 15,422,257</u>	<u>\$ 1,149,294</u>	<u>\$ 2,076,666</u>	<u>\$ 14,494,885</u>

DIBOLL INDEPENDENT SCHOOL DISTRICT

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED AUGUST 31, 2009

Depreciation was charged to functions as follows:

Instruction	\$ 282,836
Instructional Resources and Media Services	7,789
Curriculum and Staff Development	2,708
School Leadership	6,160
Guidance, Counseling, & Evaluation Services	1,079
Health Services	864
Student Transportation	112,663
Food Services	95,684
Extracurricular Activities	36,510
General Administration	11,260
Plant Maintenance and Operations	56,467
Security and Monitoring Services	2,847
Data Processing Services	1,488
	\$ 618,355

D. Interfund Balances and Activities

1. Due To and From Other Funds

Balances due to and due from other funds at August 31, 2009, consisted of the following:

Due To Fund	Due From Fund	Amount	Purpose
General Fund	Food Service Fund	\$ 266,564	Short-term loans
General Fund	Summer Feeding	8,438	Short-term loans
Food Service Fund	Summer Feeding	16,424	Short-term loans
Capital Projects Fund	Debt Service Fund	318	Short-term loans
	Other Balances	--	
	Total	\$ 291,744	

All amounts due are scheduled to be repaid within one year.

E. Long-Term Obligations

The District has entered into a continuing disclosure undertaking to provide Annual Reports and Material Event Notices to the State Information Depository of Texas, which is the Municipal Advisory Council. This information is required under SEC Rule 15c2-12 to enable investors to analyze the financial condition and operations of the District.

1. Long-Term Obligation Activity

Long-term obligations include debt and other long-term liabilities. Changes in long-term obligations for the year ended August 31, 2009, are as follows:

	Beginning Balance	Increases	Decreases	Ending Balance	Amounts Due Within One Year
Governmental activities:					
QZAB Notes Payable	\$ 3,059,085	\$ --	\$ 246,140	\$ 2,812,946	\$ 269,933
Maintenance Tax Notes	322,847	--	74,960	247,887	78,670
Total governmental activities	\$ 3,381,932	\$ --	\$ 321,099	\$ 3,060,832	\$ 348,604

DIBOLL INDEPENDENT SCHOOL DISTRICT

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED AUGUST 31, 2009

I. Retiree Health Care Plan

1. Plan Description

The District contributes to the Texas Public School Retired Employees Group Insurance Program (TRS-Care), a cost-sharing multiple-employer defined benefit postemployment health care plan administered by the Teacher Retirement System of Texas (TRS). TRS-Care Retired Plan 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 TRS issues a publicly available financial report that includes financial statements and required supplementary information for TRS-Care. That report may be obtained by visiting the TRS web site at www.trs.state.tx.us, by writing to the Communications Department of the Teacher Retirement System of Texas at 1000 Red River Street, Austin, Texas 78701, or by calling 1-800-223-8778.

2. 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 2009, 2008 and 2007. 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 August 31, 2009, 2008, and 2007, the State's contributions to TRS-Care were \$13,074, \$12,908, and \$12,074, respectively, the active member contributions were \$66,260, \$63,940, and \$64,945, respectively, and the District's contributions were \$56,066, \$54,103, and \$54,954, respectively, which equaled the required contributions each year.

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003, which was effective January 1, 2006, established prescription drug coverage for Medicare beneficiaries known as Medicare Part D. One of the provisions of Medicare Part D allows for the Texas Public School Retired Employee Group Insurance Program (TRS-Care) to receive retiree drug subsidy payments from the federal government to offset certain prescription drug expenditures for eligible TRS-Care participants. For the fiscal years ended August 31, 2009, 2008, and 2007, the subsidy payments received by TRS-Care on behalf of the District were \$23,417, \$24,013, and \$22,607, respectively.

J. Employee Health Care Coverage

During the year ended August 31, 2009, employees of the District were covered by a health insurance plan (the Plan). The District paid premiums of \$150 per month per employee to the Plan. Employees, at their option, authorized payroll withholdings to pay premiums for dependents. All premiums were paid to a third party administrator, acting on behalf of the licensed insurer. The Plan was authorized by Section 21.922, Texas Education Code and was documented by contractual agreement.

The contract between the District and the third party administrator is renewable September 1, 2009, and terms of coverage and premium costs are included in the contractual provisions.

DIBOLL INDEPENDENT SCHOOL DISTRICT

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED AUGUST 31, 2009

K. Commitments and Contingencies

1. Contingencies

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

2. Litigation

No reportable litigation was pending against the District at August 31, 2009.

L. Workers' Compensation

During the year ended August 31, 2009, employees of the District were covered by a worker compensation plan in accordance with an interlocal agreement between the District and the Deep East Texas Workers' Compensation Insurance Fund (the "Fund"). The Fund is responsible for all compensation and other benefits required of the District as required by the Workers Compensation Law of the State of Texas, Chapter 504, Texas Labor Code. In addition to the worker compensation coverage, employers' liability is covered up to the following policy limits: \$500,000 Bodily Injury by accident - each accident; \$500,000 Bodily Injury by disease - each employee; and \$500,000 Bodily Injury by disease - policy limit.

M. Special Item

During the year ended August 31, 2009, the District deleted \$493,266 in fixed assets from the books in order to tie the financial statements to the Districts fixed asset listing. In prior years, Construction in Progress was inadvertently overbooked compared to actual capital outlay costs.

APPENDIX C

FORM OF BOND COUNSEL'S OPINION

June __, 2010

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

DIBOLL INDEPENDENT SCHOOL DISTRICT UNLIMITED TAX SCHOOL BUILDING BONDS, SERIES 2010, dated June 1, 2010, in the aggregate principal amount of \$_____ maturing on February 15 in each year from 20__ through 20__, inclusive. The Bonds are issuable in fully registered form only, in denominations of \$5,000 or integral multiples thereof, 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 and with respect to the exclusion of interest on the Bonds from gross income under federal income tax law. In such capacity we have examined the Constitution and laws of the State of Texas; federal income tax law; and a transcript of certain certified proceedings pertaining to the issuance of the Bonds, 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. R-1.

WE HAVE NOT BEEN REQUESTED to examine, and have not investigated or verified, any original proceedings, records, data or other material, but have relied upon the transcript of certified proceedings. We have not assumed any responsibility with respect to the financial condition or capabilities of the 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 as follows:

- (1) The transcript of certified proceedings evidences complete legal authority for the issuance of the Bonds in full compliance with the Constitution and laws of the State of Texas presently in effect; the Bonds constitute valid and legally binding obligations of the 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; and

- (2) The Bonds are payable, both as to principal and interest, from the receipts of an annual ad valorem tax levied, without legal limit as to rate or amount, upon taxable property located within the District, which taxes have been pledged irrevocably to pay the principal of and interest on the Bonds.

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

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

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

COASTAL SECURITIES, INC.

Financial Advisor to the District