

# Town of Prescott Valley



## Financial Trends Analysis

For Fiscal Years  
2004 - 2008

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January 2009



Prepared by  
Management Services Department

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## INTRODUCTION



### **PURPOSE**

This financial trends analysis provides the Town of Prescott Valley's (Town) citizens, elected officials, management, staff and other stakeholders with information regarding existing and potential organizational and financial problems that may impact the Town's future fiscal health. As a useful management tool, it combines budgetary and financial information with economic and demographic data to create a series of local government indicators that can be used to monitor changes in the Town's financial condition.

This analysis does not provide solutions to negative trends, nor does it provide a single number or index to measure the Town's financial condition. When all of the financial indicators are considered together, interested stakeholders can gain a better understanding of the Town's overall financial condition (e.g. similar to credit rating agency analysis). Using this trend analysis and the framework of the financial policies adopted by Town Council will enable management to strategically plan and budget, provide solutions to negative trends, and ultimately preserve the financial health of the Town.



## INTRODUCTION



### ORGANIZATION

This report contains an analysis of the financial trends for the Town for the five-year period of 2003/04 - 2007/08. By analyzing these trends, the financial condition of the Town can be monitored. Monitoring the financial condition allows Town officials to better understand the forces that affect the *financial condition* of the Town and the obstacles associated with measuring the financial condition. It will also allow officials to identify existing and emerging financial problems and develop action plans to remedy these problems.

The term *financial condition* has many meanings. From an accounting standpoint, it refers to the Town's ability to generate enough cash over thirty or sixty days to pay its bills (e.g. cash solvency). It also refers to the Town's ability to generate enough revenues over a normal budgetary period to meet its expenditures and not incur deficits (e.g. budgetary solvency). It also includes the ability of the Town in the long run to pay all costs of doing business, including those that are annually budgeted and those that appear only in years in which they must be paid (e.g. long-run solvency). Service level solvency refers to the ability of the Town to support municipal services at an adequate level.





## INTRODUCTION

collectively. A specific trend, if analyzed on its own, may provide a misleading representation of the Town's financial condition.

This report uses numerous indicators, covering separate issues including external revenue, fund balance, liquidity, unfunded liabilities and business activity. Town officials can use these indicators to achieve the following:

- Gain a better understanding of the government's financial condition.
- Identify existing and emerging problems before they reach serious proportions.
- Present a straightforward picture of the government's financial strengths and weaknesses.
- Introduce long-range considerations into the annual budgeting process.
- Provide a starting point for setting financial policies.

The financial factors are separated into specific trend indicators. The Town's financial policies, community needs and resources, and intergovernmental constraints are incorporated into the analysis. Certain environmental and organizational factors cannot be quantified and, therefore, are not part of this analysis.

## EXECUTIVE SUMMARY

The 2007/08 fiscal year saw the *national and state economies* continue to decline with the slowdown in the housing market. Slowing worker productivity and higher inflation were growing concerns as the fiscal year progressed. The national economy based on GDP (Gross Domestic Product) had been growing at a steady 3 percent from 2003/04 to 2006/07. However, this economic index trended downward in fiscal year 2007/08, further indicating a slowing economy expected to extend into 2008/09. Since economic performance tends to be cyclical in nature, there are short-term and long-term uncertainties that could have an impact on the strength and longevity of the current economic cycle as we head into 2008/09. These uncertainties include housing and construction markets, energy prices, inflation, changing interest rates, consumer confidence, job market and geopolitical activity.

Prescott Valley is continuing to grow, although at a decidedly slower pace than that seen over the last several years. Building permit activity demonstrated a 47% decline from fiscal year 2006/07. Building activity is projected to continue to post a decline in fiscal year 2008/09, demonstrating the severity of the housing market. This decline will provide economic challenges for Prescott Valley and its citizens, and presents significant challenges to properly manage current or new Town services and maintain existing infrastructure.

On October 30, 2007, the Town of Prescott Valley held an auction to sell effluent water interests. Water Property



## EXECUTIVE SUMMARY



Wal-Mart will be located in the Glassford Hill Marketplace complex and is projected to break ground in 2010. Crossroads has completed construction and several businesses have opened such as Sam's Club, Home Depot and Cracker Barrel. Hampton Inn opened as of November 2008 and Comfort Inn will continue construction into the 2008/09 fiscal year.

A new Town of Prescott Valley Public Library broke ground in January 2008 with partnership from Yavapai Community College using funding generated from \$15.9 million in Certificates of Participation issued December 2007. This facility will occupy 52,000 square feet with the space used not only for the library, but an auditorium, classrooms and offices. The building is planning to open July 2009.

Based on fiscal year 2007/08 and the outlook for 2008/09, guarded optimism best describes the Town of Prescott Valley's current economic prospects. Nationally and locally, the construction and housing industries have experienced a significant drop-off beginning at the end of calendar year 2005/06 and continuing into 2006/07 and 2007/08 from the record-breaking performances of the past few years. Current economic conditions allow the Town to maintain core services and to provide limited enhancements to existing service levels. However, prudent long-term fiscal planning dictates a conservative financial approach, focusing on the highest Council and citizen priorities. The challenge for the future is the Town's ability to absorb, within available resources, increasing operational costs (i.e. rising health insurance costs, utilities, infrastructure maintenance,



## EXECUTIVE SUMMARY

public safety, etc.) associated with a growing population base and increased demands for public services. The use of economic resources to fund future development will have an immediate impact on the Town's current resources as well. The budget for the 2008/09 year includes a conservative economic forecast and limited revenue growth. The Management Services staff will continue to monitor the Town's financial trends on an annual basis. If action is required to address unfavorable trends, the Director of Management Services will alert the Town Manager in a timely manner and bring forward strategic options for future consideration.

**Community Needs and Resources** – A growing population, is positively contributing to the Town's condition. However, increased inflation and the declining per capita income in 2007/08 offers concern as it negatively affects the citizens' ability to pay for goods and services as seen in the business activity indicator.

<b>Indicator</b>	<b>2006/07</b>	<b>2007/08</b>
Population	Positive	<b>Neutral</b>
Inflation	Positive	<b>Negative</b>
Residential Development	Negative	Negative
Business Activity	Positive	<b>Negative</b>
Personal Income	Neutral	<b>Negative</b>

**Revenues** – Operating revenues as well as sales tax revenues have begun to fall in 2007/08 due to the uncertainty in the economy. The decrease in per capita revenue is substantial indicating a slowdown from the pace seen over the last several years.

## EXECUTIVE SUMMARY



<b>Indicator</b>	<b>2006/07</b>	<b>2007/08</b>
Revenue per Capita	Positive	<b>Negative</b>
Restricted Revenues	Positive	Positive
Intergovernmental Revenues	Negative	Negative
Elastic Revenues	Positive	<b>Neutral</b>

**Expenditures** – The Town has experienced increased growth during the period measured and expenditures per capita have increased in the last three periods. The increase may be an indication that with the rising population there are more demands for provided services. This trend may reverse as we experience reduced revenues which restrict the ability for the Town to enhance services.

<b>Indicator</b>	<b>2006/07</b>	<b>2007/08</b>
Expenditures per Capita	Negative	Negative
Employees per Capita	Neutral	<b>Positive</b>
Fringe Benefits	Neutral	Neutral

**Operating Position** – The operating position indicators reflect an overall solid financial base. Enterprise funds show a decline in earnings in the last year due to increased depreciation, utilities, capital outlay, bond issuance costs and increased professional fees. Although the Town is gradually using more of its cash on hand, a majority of the fund balances are unreserved and undesignated. The percentage of current liabilities to cash and investments remains above industry averages and the Town’s liquidity is strong even with a slowed economy.



## EXECUTIVE SUMMARY



<b>Indicator</b>	<b>2006/07</b>	<b>2007/08</b>
General Fund Balance	Positive	Neutral
Enterprise Fund Earnings	Positive	Positive
Liquidity	Positive	Positive

**Debt Structure** – Currently the Town has the available funds to make payments for outstanding debt. However, if the economy does not rebound, the Town may have difficulties paying future scheduled debt payments due to decreased revenue collections. The increase in current liabilities and net direct debt per capita are primarily due to the new bond issues in 2007/08. Debt service decreased due to reductions in debt service payments and payments for new debt not being due in the current fiscal year.

<b>Indicator</b>	<b>2006/07</b>	<b>2007/08</b>
Current Liabilities	Negative	Negative
Net Direct Debt per Capita	Positive	<b>Neutral</b>
Debt Service	Neutral	Neutral
Excise Tax	Positive	Positive
Overlapping Debt	Neutral	<b>Negative</b>

**Contingent Liabilities** – The Pension Benefit Obligation-Arizona Public Safety Personnel Retirement System (APSPRS) experienced a decline beginning in fiscal year 2005/06 as a result of changing population demographics, expanded coverage needs and a downturn in the economy resulting in sharply lower returns on investments. The Pension Benefit Obligation-ICMA is one hundred percent funded.



## EXECUTIVE SUMMARY

<b>Indicator</b>	<b>2006/07</b>	<b>2007/08</b>
Pension Benefit-APSPRS	Negative	Negative
Pension Benefit-ICMA	Positive	Positive
Compensation Absences	Neutral	<b>Negative</b>

**Condition of Capital Plant** – The Town’s maintenance and replacement of capital assets has decreased only slightly over the measured period. This is due to the Town being proactive and replacing broken or obsolete assets regularly.

<b>Indicator</b>	<b>2006/07</b>	<b>2007/08</b>
Maintenance Effort	Positive	<b>Neutral</b>
Depreciation Expense	Neutral	Neutral



## SOURCES

The following information has been analyzed using the information and analysis suggestions as described in the ICMA publication Evaluating Financial Condition – A Handbook for Local Government and the Town’s Finance staff. Trend indicators are based primarily on the Town’s economic base.

The analytical techniques that are part of this evaluation system are similar to the analytical approaches used by the municipal credit rating industry. For example, certain indicators are adjusted for inflation, as measured by the Consumer Price Index (CPI), to yield constant dollars, thus representing the real growth or decline of the indicators. This technique can help the Town analyze and interpret key financial, economic and demographic trends and can provide management with information needed to improve the Town’s overall financial position and aid in the decision-making process.

In order to ensure validity and consistency of the indicators, most data is tied to data published in the Town’s Comprehensive Annual Financial Report (CAFR). In addition, many indicators relate directly to information required by municipal credit rating agencies. The rating agencies, bond buyers and other interested parties consider the annually audited and published CAFR as the most reliable financial information source for the Town. The Town presents its CAFR in accordance with Generally Accepted Accounting Principles (GAAP) and in a consistent format as promulgated by the Government Finance Officers Association (GFOA).

## **COMPREHENSIVE FINANCIAL POLICIES**



The following excerpts are from the Town-adopted financial policies and establish a framework for overall fiscal planning and management. They set forth guidelines against which current budgetary performance can be measured and proposals for future programs can be evaluated. Adopted financial policies reflect the Town's commitment to sound financial management and fiscal integrity to the credit rating industry and prospective investors (bond buyers). The financial policies also improve the Town's fiscal stability by helping Town officials plan fiscal strategy with a consistent approach. Adherence to adopted financial policies promotes sound financial management, which can lead to improvement in Town bond ratings and lower cost of capital. The Town is in compliance with the comprehensive financial policies adopted.

### **OPERATING MANAGEMENT POLICIES**

1. All departments will participate in the responsibility of meeting policy goals and ensuring long-term financial health. Future service plans and program initiatives will be developed to reflect current policy directives, projected resources and future service requirements.
2. Budgets for governmental fund types will be adopted on a basis of accounting consistent with Generally Accepted Accounting Principles (GAAP). The budget process is intended to weigh all competing requests for Town resources, within expected fiscal constraints. Requests for new, ongoing programs made outside the budget process will be discouraged. for new, ongoing programs made outside the budget process will be discouraged.



## COMPREHENSIVE FINANCIAL POLICIES

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3. The budget shall be adopted at the fund level. Budget development will use strategic multi-year fiscal planning, conservative revenue forecasts and modified zero-base expenditure analysis that requires every program to be justified annually in terms of meeting intended objectives (effectiveness criteria) and in terms of value received for dollars allocated (efficiency criteria). The process will include a diligent review of programs by the Town Manager and Town Council.
  4. Revenues will not be dedicated for specific purposes, unless required by law or Generally Accepted Accounting Principles (GAAP). The only exception is .33% of the transaction privilege taxes that have been dedicated to the Street Improvement Fund. All non-restricted revenues will be deposited in the General Fund and appropriated by the budget process. Special one-time revenue sources will be used to purchase non-recurring items like capital equipment or projects.
  5. Current revenues will fund current expenditures and a diversified and stable revenue system will be developed to protect programs from short-term fluctuations in any single revenue source.
  6. Addition of personnel will only be requested to meet program initiatives and policy directives; after service needs have been thoroughly examined and it is substantiated that additional staff will result in increased revenue or enhanced operating efficiencies. Personnel cost reductions will be achieved through attrition to the extent feasible.
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## COMPREHENSIVE FINANCIAL POLICIES

7. Utility (Water and Wastewater) user charges will reflect cost of service and will be established so that operating revenues are at least equal to operating expenditures. User fees and charges will be examined annually to ensure that they recover all direct and indirect costs of service and be approved by the Town Council.
8. All non-enterprise user fees and charges will be examined annually to determine the direct and indirect cost of service recovery rate. The acceptable recovery rate and any associated changes to user fees and charges will be approved by the Town Council.
9. Development impact fees, as permitted by State law, for capital expenses attributable to new development will be reviewed periodically to ensure that fees recover all direct and indirect development-related expenses and be approved by Town Council.
10. Capital equipment replacement will be accomplished through the use of a Replacement Fund. The amount transferred will be reviewed annually to ensure that charges to operating departments are sufficient for operation and replacement of vehicles and other computer equipment. Replacement costs will be based upon equipment lifecycle financial analysis.
11. Grant funding will be considered to leverage Town funds. Inconsistent and/or fluctuating grants should not be used to fund ongoing programs. Programs financed with grant monies will be budgeted in a separate fund, and the service program will be adjusted to reflect the level of available funding. In the event of reduced grant funding,



## **COMPREHENSIVE FINANCIAL POLICIES**



### **CAPITAL MANAGEMENT POLICIES**

15. A five-year Capital Improvement Plan will be developed and updated annually, including anticipated funding sources. Capital improvement projects are defined as infrastructure, land improvements, equipment purchases or construction projects which result in a capitalized asset costing more than \$25,000 and having a useful (depreciable) life of two years or more.
16. Proposed capital projects will be reviewed and prioritized by the Town Manager in discussion with the director of the department and overall consistency with the Town's goals and objectives. Financing sources will then be identified for the highest ranking projects.
17. Capital improvement lifecycle costs will be coordinated with the development of the operating budget. Future operating, maintenance and replacement costs associated with new capital improvements will be forecast, matched to available revenue sources and included in the operating budget.
18. A portion (.33 percent of the 2.33 percent) of the privilege tax revenue will be restricted for purposes of funding improvements to Robert Road, Navajo Drive, Lakeshore Drive and other priority roadways.

### **DEBT MANAGEMENT POLICIES**

19. The issuance of long-term debt is limited to capital projects and assets that the Town cannot finance from current revenues or resources.





## COMPREHENSIVE FINANCIAL POLICIES



by the project will be greater than the debt service requirements). The net revenues should not simply be positive over the life of the bonds, but must be positive each year within a reasonably short period (e.g., by the third year of debt service payments).

24. Town debt service costs (GO, MPC, HURF and Revenue Bond Debt) should not exceed 25% of the Town's operating revenue in order to control fixed costs and ensure expenditure flexibility. Improvement District (ID) and Community Facilities District (CFD) debt service is not included in this calculation because it is paid by district property owners and is not an obligation of the general citizenry. Separate criteria have been established regarding ID and CFD debt policies.
25. Improvement District (ID) and Community Facilities District (CFD) bonds shall be permitted only when there is a general Town benefit. Both ID and CFD bonds will be utilized only when it is expected that they will be issued for their full term. It is intended that ID and CFD bonds will be primarily issued for developments or existing neighborhoods desiring improvements to their property such as roads, water lines, sewer lines, streetlights, parks and drainage.
  - a. Improvement District debt will be permitted only when the full cash value of the property, as reported by the Assessor's Office, to debt ratio (prior to improvements being installed) is a minimum of 3/1 prior to issuance of debt and 5/1 or higher after



## COMPREHENSIVE FINANCIAL POLICIES



construction of improvements. Should the full cash value to debt ratio not meet the minimum requirements, property value may be determined by an appraisal paid for by the applicant and administered by the Town. In addition, the Town's cumulative improvement district debt will not exceed 15 percent of the Town's secondary assessed valuation. Bonds issued to finance improvement district projects will not have maturities longer than ten years.

- b. Community Facilities District debt will be permitted only when the full cash value of the property, as reported by the Assessor's Office, to debt ratio (prior to improvements being installed) is a minimum of 3/1 prior to issuance of debt and 5/1 or higher after construction of improvements. In addition, the Town's cumulative facilities district debt will not exceed 15 percent of the Town's secondary assessed valuation. The landowner/developer shall also contribute \$.30 in public infrastructure improvements of each dollar of public infrastructure improvement debt to be financed by the district.

26. Debt financing should not exceed the useful life of the infrastructure improvement with the average (weighted) bond maturities at or below ten years.

27. Utility rates will be set, at a minimum, to ensure the ratio of revenue to debt service meets our bond indenture requirement of 1.2:1. The Town goal will be to maintain a minimum ratio of utility revenue to debt service of 1.6:1



## COMPREHENSIVE FINANCIAL POLICIES

or greater, to ensure debt coverage in times of revenue fluctuations attributable to weather or other causes, and to ensure a balanced pay-as-you-go Capital Improvement Plan.

### RESERVE POLICIES

28. The Town will maintain a fund reserve for the General Fund to pay expenditures caused by unforeseen emergencies, for shortfall caused by revenue declines and to eliminate any short term borrowing for cash flow purposes. This reserve shall be maintained at an amount that represents 25% of general government (General and HURF Funds) operating expenditures.
29. The Town's General Fund will maintain a year-to-year "carryover balance" in an amount necessary to maintain adequate cash flow and to reduce the demand for short-term borrowing. The carry forward balance will equal 90 days of operating expenditures but not less than \$10,000,000.
30. A contingency account equal to five percent of annual general governmental (General and HURF Funds) operating expenditures will be maintained for unforeseen emergencies or catastrophic impacts to the Town. This account will be available for unanticipated and unbudgeted expenditures and will require the Town Council's approval. The purpose of this account is to provide some flexibility for unforeseen events without the necessity to spend from the Town's reserves.

## **COMPREHENSIVE FINANCIAL POLICIES**

- 31. Fleet Management Reserve will be maintained based upon lifecycle replacement plans to ensure adequate fund balance required for systematic replacement of fleet vehicles and operational contingencies. Operating departments will be charged for fleet operating costs per vehicle class and replacement costs spread over the useful life of the vehicles.

## **FINANCIAL REPORTING POLICIES**

- 32. Contingency and reserves funds in the Municipal Water and Wastewater utility operating funds should be equal to 90 days operating expenditures to meet unforeseen emergencies.
- 33. The Town's accounting, budgetary, and financial reporting systems will be maintained in conformance with all State and Federal laws, Generally Accepted Accounting Principles (GAAP), standards of the Governmental Accounting Standards Board (GASB) and the Government Finance Officers Association (GFOA).
- 34. An annual audit will be performed by an independent public accounting firm, with an audit opinion to be included with the Town's published Comprehensive Annual Financial Report (CAFR).
- 35. The Town's CAFR will be submitted to the GFOA Certification of Achievement for Excellence in Financial Reporting Program. The financial report should be in conformity with GAAP, demonstrate compliance with finance-related legal and contractual provisions, disclose

## COMPREHENSIVE FINANCIAL POLICIES



thoroughness and detail sufficiency, and minimize ambiguities and potentials for misleading inference.

36. The Town's CAFR will also be submitted to national repositories identified by the Nationally Recognized Municipal Securities Information Repository as a continuing commitment to disclose thoroughness to enable investors to make informed decisions.
37. The Town budget will be submitted to the GFOA Distinguished Budget Presentation Program. The budget should satisfy criteria as a financial and programmatic policy document, as a comprehensive financial plan, as an operations guide for all organizational units and as a communications device for all significant budgetary issues, trends and resource choices.
38. Financial systems will maintain internal controls to monitor revenues, expenditures and program performance on an ongoing basis.







## INTERGOVERNMENTAL CONSTRAINTS



The following is an overview of various intergovernmental constraints affecting Prescott Valley's operations.

### STATE-SHARED REVENUES

Prescott Valley receives a share of its monies collected by the State since cities and towns in Arizona are not permitted to levy an income tax. This year, Prescott Valley received in excess of \$12.9 million in shared revenues from the State, an increase of 4% over the previous year. Some money, such as State-Shared Sales Tax and State Income Tax, are unrestricted as to use. Other revenues, such as Highway User Fuel Tax and Local Transportation Assistance Funds, are restricted to transportation purposes only.

In addition to the restrictions on the use of these funds, there are also differing methods of distribution that impact Prescott Valley's revenue share. In some cases, United States Census figures are used to calculate revenue distribution. Other revenue distribution method calculations are based on the county in which the revenue originated.

State-Shared Income Tax receipts are received by the Town based on income earned two years prior to distribution. The State of Arizona income tax calculations are tied to the federal tax system and, therefore, fluctuations in federal income tax levels caused by economic downturns or tax cuts can negatively impact the State's income tax revenues. The distribution of the State Income Tax to Prescott Valley is projected to decrease in fiscal year 2008/09, as future receipts will be based on income earned during the







## COMMUNITY NEEDS & RESOURCES

Community Needs and Resources encompass various economic and demographic characteristics including population, employment, personal income, property value and business activity. These indicators describe and quantify a community's wealth and economic condition. They provide insight into the community's collective ability to generate revenue relative to the community's demand for public services such as public safety, capital improvements and social services.

Community Needs and Resources are all closely interrelated and affect each other in a continuous cycle of cause and effect. In addition, changes in these characteristics tend to be cumulative.

In addition to analyzing these indicators, the Town may also want to study more subjective issues, such as land-use characteristics, as they relate to the Town's ability to generate revenue and, therefore, provide convenient, efficient public services. Also important are the Town's plans and potential for future development. The diversification of the commercial and industrial tax base should be considered for its revenue-generating ability, employment-generating ability, vulnerability to economic cycles and relationships within the larger economic region.

## COMMUNITY NEEDS & RESOURCES



An examination of local economic and demographic characteristics can identify the following types of situations:

- A declining tax base and, correspondingly, the community's ability to pay for public services.
- A need to shift public service priorities because of demographic changes in the community.
- A need to shift public policies because of a loss in competitive advantage of the Town's businesses to surrounding communities or because of a surge in inflation or other changes in regional or national economic conditions.



## POPULATION



### **Description**

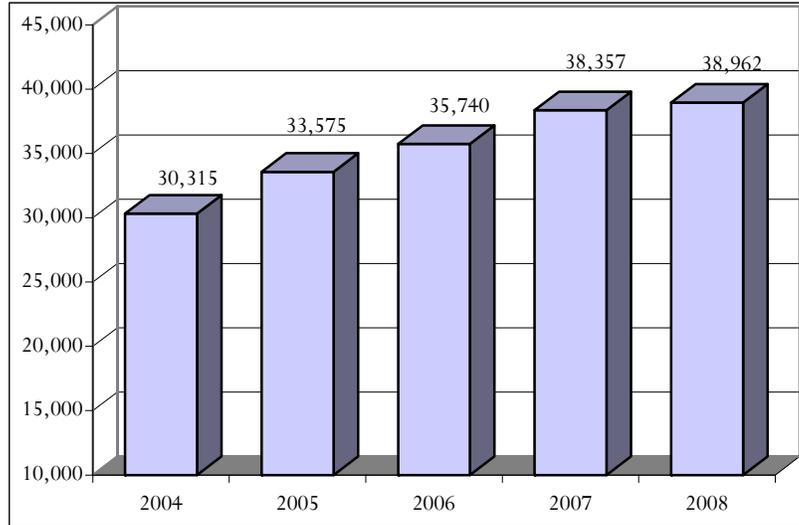
Although the exact relationship between population change and other economic and demographic factors is difficult to evaluate, it is important to realize the effects that both increases and decreases in population may have on a local government. An increase in population will create pressures for new capital outlay and higher levels of service which are offset by a proportionate increase in revenues. A decline in population would, at first glance, appear to relieve pressures for expenditures, because the population is getting smaller. But in practice, a local government faced with a declining population is rarely able to make reductions in expenditures that are proportional to the loss in a critical revenue stream.

### **Analysis**

The Town continues to experience population growth, although at a slower pace than fiscal years 2003/04 and 2004/05. The population growth seen over the past five years has contributed to the Town receiving a larger percentage of intergovernmental revenue; however, the increase in population can result in an increased demand for governmental services. Although there has been an increase in population, the downturn in the economy has resulted in decreased revenues instead of the expected increase due to the uncertainty in state shared revenues. In addition, the 2008/09 Transaction Privilege Tax collections are currently 9% lower than the prior fiscal year. This decline in revenues has put a strain on funding for current services as well as funding needs for any additional services.



## POPULATION



<u>Population</u>	FY	FY	FY	FY	FY
	2004	2005	2006	2007	2008
Population	30,315	33,575	35,740	38,357	38,962
% Change <sup>1</sup>	10.6%	10.8%	6.4%	7.3%	1.6%

Source: Arizona Department of Economic Security

<sup>1</sup> Calculation:  $\frac{\text{Current Year Population} - \text{Previous Year Population}}{\text{Previous Year Population}}$

## INFLATION



### **Description**

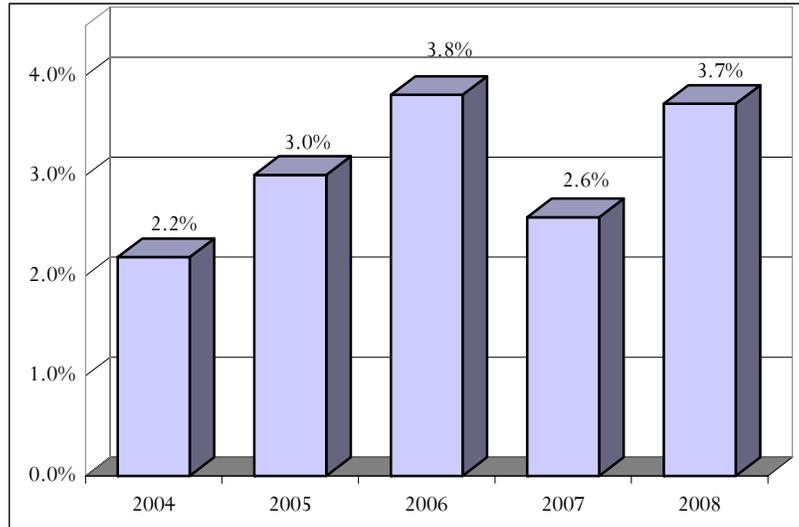
The Consumer Price Index (CPI) is one of the most widely recognized and used measures of the average change over time in the prices paid by consumers for goods and services. The CPI is based on a weighted average of prices for a variety of goods from eight different groups: food and beverages, housing, apparel, transportation, medical care, recreation, education and communication, and other goods and services (e.g., tobacco and smoking products, haircuts and other personal services). Stability in price level changes is generally beneficial and continued low rates of inflation indicate a positive trend.

### **Analysis**

The rate of inflation increased in fiscal year 2007/08 after a decline in the prior fiscal year. The economic downturn experienced in the last 18 months contributed to the rise in the inflation rate. A weakening housing market and higher oil prices resulted in increased prices for consumer goods and increased unemployment. This coupled with the sub-prime credit problems has resulted in the Federal Reserve Board taking action to stimulate the economy. Current economic forecasts suggest a continued weakening of the economy and decreased consumer confidence with a slow recovery beginning in fiscal year 2009/10; however, many factors play into inflation and this analysis is not intended to offer predictions.



## INFLATION



<u>Inflation</u>	FY	FY	FY	FY	FY
	2004	2005	2006	2007	2008
Consumer Price Index	186.1	191.7	199.0	204.1	211.7
Inflation Rate <sup>1</sup>	2.2%	3.0%	3.8%	2.6%	3.7%

Source: U.S. Bureau of Labor Statistics - CPI

Note: Consumer price index is presented using fiscal year averages

<sup>1</sup> Calculation: Current Year CPI - Prior Year CPI/Prior Year CPI

## RESIDENTIAL DEVELOPMENT

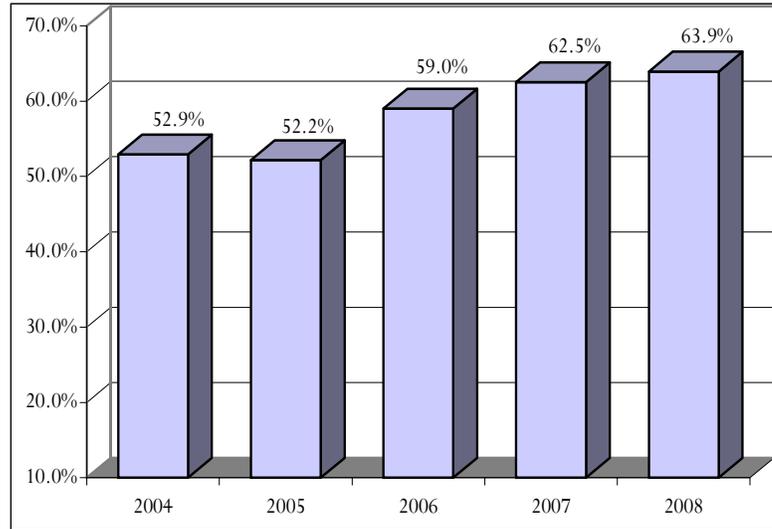
### Description

Generally, the net cost of servicing residential development is higher than the net cost of servicing commercial or industrial development. Under this set of circumstances, the ideal condition would be to have sufficient commercial and industrial development to more than offset the costs of the residential development. There are exceptions to this situation. For example, a high-density residential area occupied by middle-aged, wealthy families whose children have already left home, who are heavy consumers, and who look to the government for very few services, can generate more revenues than service costs.

### Analysis

Residential development as a percent of total property has trended upward since 2005. Since property values for the current year are calculated at the end of the previous calendar year, 2009 is expected to decline due to the devaluation of property values related to the troubled housing market. The Town has experienced a decrease in residential development due to the financial credit crisis and problems experienced in the banking industry within the home mortgage market. Commercial development has continued in the Town but at a much slower rate than in prior years. Because the cost of servicing residential development is generally greater than servicing commercial development, this may become a positive trend in the future. The type of development should be taken into consideration in forecasting service levels and the associated service costs.

## RESIDENTIAL DEVELOPMENT



<u>Residential Development</u>	Calendar Year				
(in thousands)	2004	2005	2006	2007	2008
Assessed Value					
Residential Property	\$ 96,603	\$ 113,740	\$ 152,864	\$ 206,616	\$ 278,908
Assessed Value					
All Properties	\$ 182,514	\$ 218,003	\$ 259,023	\$ 330,513	\$ 436,242
% Residential					
Development <sup>1</sup>	52.9%	52.2%	59.0%	62.5%	63.9%

Source: State and County Abstract of the Assessment Roll, State of Arizona, Department of Revenue and the Property Tax Rates and Assessed Values, Arizona Tax Research Foundation

<sup>1</sup> Calculation: Assessed Value Residential/Assessed Value All Property

## BUSINESS ACTIVITY



### Description

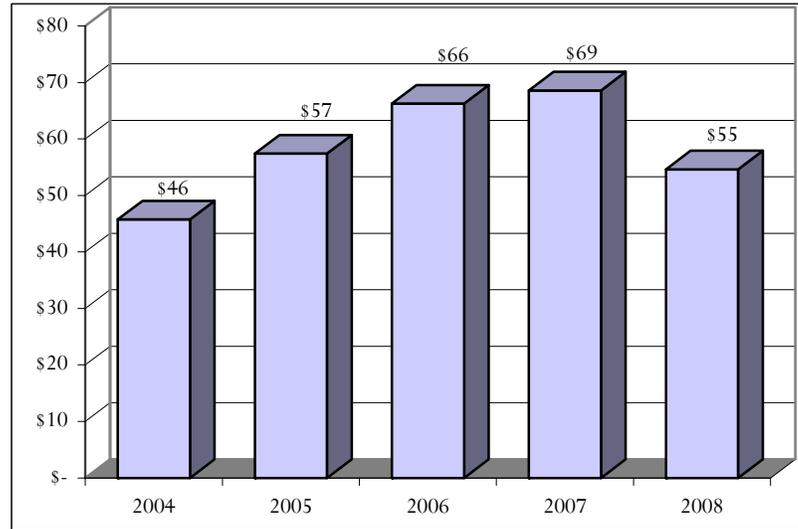
The level of business activity directly affects the Town's financial condition by revenue sources such as sales tax receipts; and indirectly to the extent that a change in business activity affects other demographic and economic areas such as employment base, personal income or property values. Changes in business activity also tend to be cumulative, causing a positive or negative impact on all related factors such as employment base, income and property value.

### Analysis

During the past four fiscal years, the Town has experienced an increase in overall sales tax collections. In 2007/08 however, sales tax collections decreased to below 2004/05 levels. The Town has several development agreements in place which allow for future sales tax rebates to fund infrastructure expansions. The figures shown in the following chart list total and net sales tax revenue. The sales tax revenue in the graph is the net revenue adjusted for rebates paid to the developers. The reduction in sales tax collections is related to the slow economic conditions currently faced nationwide. A reduction in revenues is expected to continue well into the next fiscal year due to the uncertainty of the economy. If this trend continues, it could have a negative effect on the Town's revenues and limit the Town's ability to pay for community services.



## BUSINESS ACTIVITY



<u>Business Activity</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Sales Tax Revenue	\$ 8,665	\$ 11,293	\$ 13,781	\$ 14,821	\$ 12,500
Rebated to Developers	152	288	600	819	934
Total Net Sales Tax	\$ 8,513	\$ 11,005	\$ 13,181	\$ 14,002	\$ 11,567
Consumer Price Index	186.1	191.7	199.0	204.1	211.7
Net Constant Dollar					
Sales Tax Revenue <sup>1</sup>	\$ 46	\$ 57	\$ 66	\$ 69	\$ 55
% Change Tax Rev <sup>2</sup>	11.1%	25.5%	15.4%	3.6%	-20.4%

Source: U.S. Bureau of Labor Statistics- CPI, Town of Prescott Valley Finance Division,  
 Fiscal year 2006/07 CAFR to 2007/08 - General Governmental Tax Revenues by Source -  
 Table 5, Demographic and Economic Statistics - Table 15  
 Fiscal years 2003/04 to 2005/06 - CAFR Changes in Net Assets - Table 2c, Demographic and  
 Economic Statistics - Table 16

<sup>1</sup> Calculation: Net Sales Tax/CPI

<sup>2</sup> Calculation: Current Year Net Constant Dollar Revenue - Prior Year Net Constant Dollar  
 Revenue/Prior Year Net Constant Dollar Revenue

## PERSONAL INCOME



### **Description**

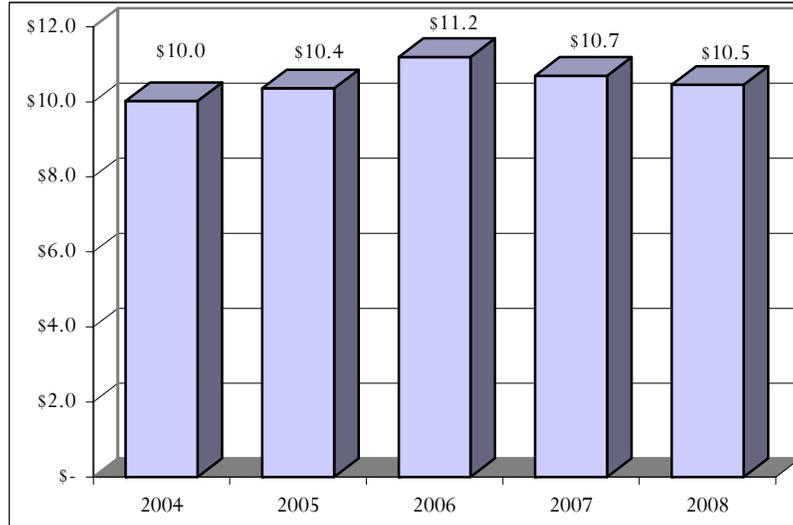
Personal income is one measure of a community's ability to pay taxes. Generally, the higher per capita income, the more property taxes, sales taxes, income taxes and business taxes the Town can generate. If income is distributed evenly, a higher per capita income will usually mean a lower dependency on government services, recreation and welfare. A decline in per capita income results in loss of consumer purchasing power and can provide advance notice that businesses, especially in the retail sector, will suffer a decline that can ripple through the rest of the Town's economy. Credit rating firms use per capita income as an important measure of a Town's ability to meet its financial obligations.

### **Analysis**

The community of Prescott Valley experienced an upward trend in its per capita personal income from 2003/04 to 2005/06. In fiscal year 2007/08, there was a decrease in the net constant dollar personal income. This indicates a loss of consumer purchasing power and can have a negative impact on the Town's revenue sources due to a decrease in consumer spending. The decline in spending with an increased population will not only place additional demands for services provided by the Town, but limit the ability for the Town to maintain those services.



## PERSONAL INCOME



Personal Income	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Per Capita Personal Income	\$ 18,646	\$ 19,858	\$ 22,282	\$ 21,836	\$ 22,133
Consumer Price Index	186.1	191.7	199.0	204.1	211.7
Population	30,315	33,575	35,740	38,357	38,962
Net Constant Dollar Personal Income (in thousands) <sup>1</sup>	\$ 10.0	\$ 10.4	\$ 11.2	\$ 10.7	\$ 10.5

Source: U.S. Bureau of Labor Statistics - CPI, Arizona Department of Economic Security, Fiscal year 2006/07 to 2007/08 CAFR - Demographic and Economic Statistics - Table 15, Fiscal year 2003/04 to 2005/06 CAFR - Demographic and Economic Statistics - Table 16

<sup>1</sup> Calculation: Per Capita Income\*Population/CPI/Population/10

## REVENUES

Revenue determines the capacity of the Town to provide services. Important issues to consider in revenue analysis are economic growth, diversity, reliability, flexibility and administration. Revenues should be growing at a rate equal to or greater than the combined effects of inflation and expenditures. Revenue should be sufficiently unrestricted to allow for necessary adjustments to changing economic and operational conditions. Revenue should be balanced between elastic and inelastic sources with respect to economic base and inflation while others should remain relatively constant. Revenue should be diversified by source so as not to be overly dependent on residential, commercial or industrial land uses, or external funding sources such as federal grants or discretionary state aid. User fees should be regularly reevaluated to cover full costs of services.

Analyzing the Town's revenue structure will help to identify the following types of problems:

- Deterioration of the revenue base.
- Internal procedures or legislative policies that may adversely affect revenue yields.
- Inefficiency in the collection and administration of revenue.
- Over dependence on obsolete or external revenue sources.

## REVENUES

- Changes in tax burden on various segments of the population.
- Lack of cost controls and poor revenue estimating practices.

Changes in revenue can be monitored by using the indicators detailed on the following pages.



## REVENUE PER CAPITA



### Description

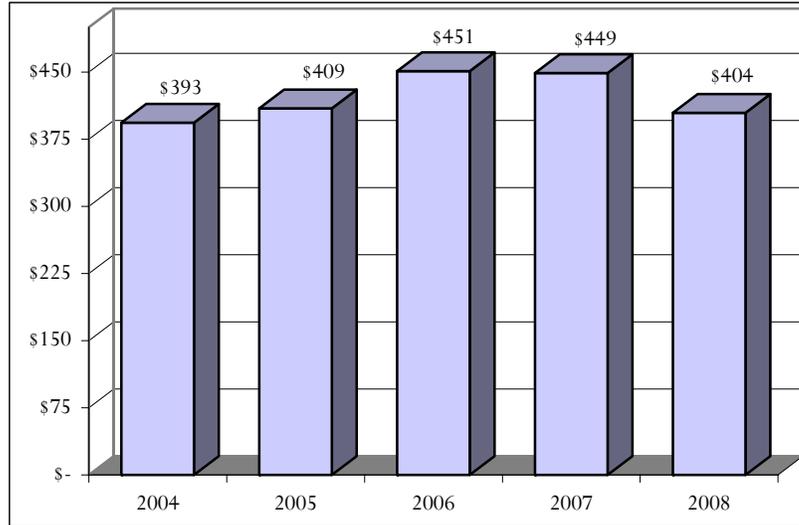
Per capita revenue illustrates operating revenue changes relative to population changes. Operating revenue is comprised of local taxes (transaction privilege, cable TV franchise, and light and power franchise taxes), intergovernmental taxes (state revenue sharing, auto lieu, state-shared sales tax and intergovernmental agreements), fines and forfeitures (court and library), licenses and permits (business licenses and building permits), charges for services (building, recreation and public safety), special assessments and property tax. As population increases, it might be expected that the need for services would increase proportionately and, therefore, the level of per capita revenue should remain at least constant in real terms. If per capita revenue is decreasing, it would be expected that the Town would be unable to maintain existing service levels unless it were to find new revenue sources or reduce expenditures.

### Analysis

In fiscal year 2007/08, the current economic conditions and increased inflation is a leading cause for the reduced growth in revenue per capita, which will also be a factor in 2008/09. Also, increased population with a lower revenue base caused a decline in this indicator. The revenue streams affected by the economic downturn include transaction privilege tax (down 16%), building permits (down 33%) and building charges for services (down 41%). A decline in revenue per capita could indicate the Town may have future difficulties in funding services for the growing community.



## REVENUE PER CAPITA



Revenue per Capita (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Operating Revenue	\$ 22,197	\$ 26,349	\$ 32,077	\$ 35,141	\$ 33,367
Consumer Price Index	186.1	191.7	199.0	204.1	211.7
Current Population	30,315	33,575	35,740	38,357	38,962
Net Constant Dollar Revenue Per Capita <sup>1</sup>	\$ 393	\$ 409	\$ 451	\$ 449	\$ 404
Revenue Per Capita (% change) <sup>2</sup>	-7.0%	4.1%	10.2%	-0.5%	-9.9%

Source: U.S. Bureau of Labor Statistics - CPI, Arizona Department of Economic Security.  
 Fiscal years 2003/04 to 2007/08 CAFR - Statement of Revenues, Expenditures and  
 Changes in Fund Balances - Governmental Funds

<sup>1</sup> Calculation: Operating Revenue/CPI/Population\*100,000

<sup>2</sup> Calculation: Current Year - Prior Year/Prior Year

Note: Does not include Community Facilities Districts

## RESTRICTED REVENUES



### Description

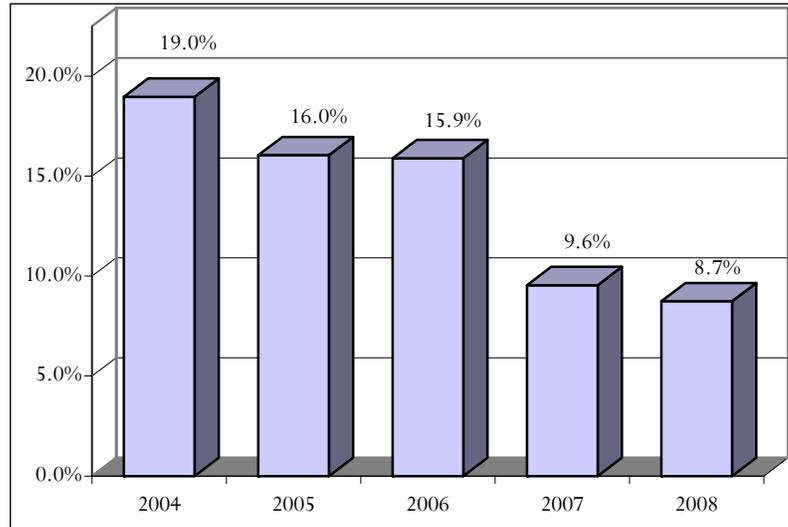
Restricted revenues are legally earmarked for a specific use, as may be required by state law, bond covenants or grant requirements. The Town's restricted revenues include grants, impact fees and developer contributions. As the percentage of restricted revenues increases, the Town loses its flexibility to respond to changing conditions. An over dependence on restricted revenues makes the Town's programs vulnerable to restrictions imposed by the funding agencies and may signal a future inability to maintain current service levels.

### Analysis

The percent of restricted revenues to operating revenue has declined during the past five fiscal years. Due to less building permits being issued, impact fee revenue fell 43% from 2006/07 to 2007/08. The decline in the percent of restricted operating revenue to operating revenue over the 2007/08 period was also caused by a 24% decrease in grants. Both of these revenue sources are directly affected by the current economic conditions. Restricted revenues have historically been used to fund infrastructure and enhance public safety. A decline in these revenues could delay needed infrastructure and protection for the growing community.



## RESTRICTED REVENUES



<u>Restricted Revenues</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Restricted Operating Rev.	\$ 4,211	\$ 4,229	\$ 5,100	\$ 3,356	\$ 2,917
Operating Revenue	\$ 22,197	\$ 26,349	\$ 32,077	\$ 35,141	\$ 33,367
% Restricted <sup>1</sup>	19.0%	16.0%	15.9%	9.6%	8.7%

Source: Fiscal years 2003/04 to 2007/08 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Government Funds

<sup>1</sup> Calculation: Restricted Operating Revenue/Operating Revenue

## INTERGOVERNMENTAL REVENUES



### Description

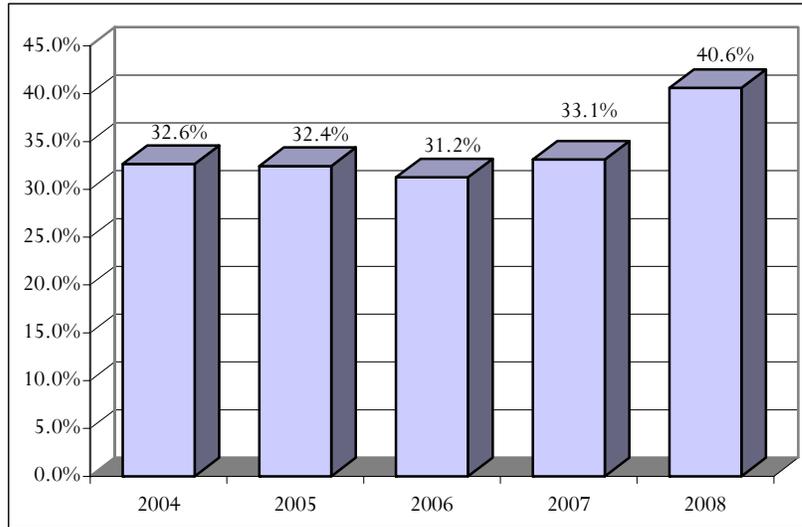
Intergovernmental revenues are received from other governmental entities. Intergovernmental revenues for the Town encompass state revenue sharing, auto lieu, state-shared sales tax, intergovernmental agreements and local governmental assistance fund. An over dependence on intergovernmental revenues can have an adverse impact on financial conditions due to restrictions or stipulations that the other governmental entities may attach to the revenue. During declining economic times, state and federal governments may withdraw or reduce payments to local governments. The overriding concern in analyzing intergovernmental revenues is to determine whether the Town is controlling its use of the revenues or whether these revenues are controlling the Town.

### Analysis

The warning trend for this indicator is an increasing amount of intergovernmental operating revenues as a percentage of operating revenues. The increase observed in fiscal year 2007/08 is primarily due to revenue received from Yavapai College for their portion of construction costs related to the Prescott Valley Public Library Building. In the fiscal year 2008/09, we will continue to receive revenue from Yavapai College for library construction costs. State shared revenues are expected to decline in 2008/09 and for future years due to the projected economic conditions. Reduced state shared revenues will have a negative effect on the Town's financial position and could limit the Town's ability to maintain current service levels.



## INTERGOVERNMENTAL REVENUES



<u>Intergovernmental Revenue</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Intergovernmental Rev.	\$ 7,245	\$ 8,547	\$ 10,023	\$ 11,634	\$ 13,548
Operating Revenue	\$ 22,197	\$ 26,349	\$ 32,077	\$ 35,141	\$ 33,367
% Intergovernmental <sup>1</sup>	32.6%	32.4%	31.2%	33.1%	40.6%

Source: Fiscal years 2003/04 to 2007/08 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Government Funds

<sup>1</sup> Calculation: Intergovernmental Revenues/Operating Revenue

## ELASTIC TAX REVENUES

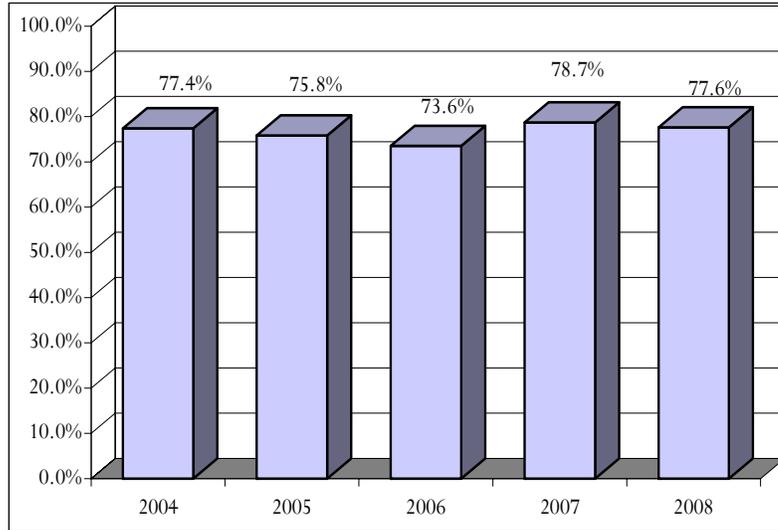
### Description

Elastic tax revenues are highly responsive to changes in the economy and inflation. As the economy grows and inflation increases, elastic revenues increase in approximately the same proportion, and vice versa. For example, sales tax revenues rise and fall with increases and decreases in retail sales and corresponding economic growth. Inelastic revenues, such as fixed license fees or user charges, are relatively unresponsive to changes in economic conditions unless there are business closures. The following Town revenues fall within the elastic revenue category: general sales tax, state-shared sales tax, state revenue sharing, auto lieu tax, highway user revenue fund tax (fuel tax) and local transportation assistance fund (portion of state lottery revenues).

### Analysis

The change in a municipality's elastic revenues as a percent of operating revenues can be attributed to the growth or decline of retail businesses and population. The decline in 2007/08 is a result of a reduction in all levels of taxes and revenues collected due to a slowed economy. These ratios are still well within the desired high range to keep pace with inflation which attributes to the higher prices government must pay for its services. The outlook for fiscal year 2008/09 is lowered elastic tax revenue in all tax categories. Since elastic tax revenues represent a significant portion of operating revenues, the percentages are not expected to change dramatically from year to year. The reduction in these taxes will hamper the Town in maintaining current infrastructure and will limit building any new infrastructure.

## ELASTIC TAX REVENUES



<u>Elastic Tax Revenues</u>	FY	FY	FY	FY	FY
(in thousands)	2004	2005	2006	2007	2008
Elastic Tax Revenues	\$ 17,179	\$ 19,980	\$ 23,596	\$ 27,648	\$ 25,899
Operating Revenue	\$ 22,197	\$ 26,349	\$ 32,077	\$ 35,141	\$ 33,367
% Elastic Tax Rev. <sup>1</sup>	77.4%	75.8%	73.6%	78.7%	77.6%

Source: Fiscal years 2003/04 to 2007/08 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Government Funds

<sup>1</sup> Calculation: Elastic Tax Revenues/Operating Revenue

## EXPENDITURES

Expenditures are an approximate measure of the Town's service output. Generally, the more the Town spends in constant dollars, the more service it is providing. These measures do not provide accountability for service delivery efficiency and effectiveness.

The first issue to consider is the expenditure growth rate to determine whether the Town is operating within its revenues. The Town makes every attempt to have a balanced budget, where expenditure growth matches revenue growth. The Town may plan additional capital expenditures in excess of revenues and use fund balances for these projects. The long-run balance between revenues and expenditures warrants separate attention. Common ways to create future problems where expenditures exceed revenues are to use reserve funds, defer maintenance on streets and buildings or by deferring funding of contingent liabilities. In each of these cases, the current budget remains balanced; however, the long-run budget is developing a deficit.

A second issue to consider is the level of mandatory or fixed costs. This is referred to as expenditure flexibility which is a measure of the Town's freedom to adjust its service levels to changing economic, political and social conditions. A town with a growing percentage of mandatory costs will find itself proportionately less able to make adjustments. As the percentage of debt service, grant matching requirements, pension benefits, State and Federal mandates, contractual agreements and commitments to existing capital



## EXPENDITURES PER CAPITA



### Description

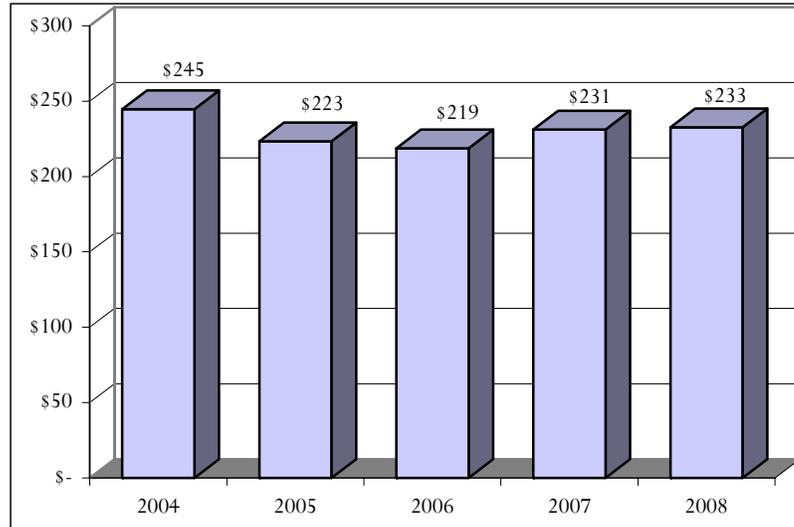
Per capita expenditures reflect changes in expenditures relative to changes in population. Increasing per capita expenditures may indicate that the cost of providing services is outstripping the Town's ability to pay, especially if spending is increasing faster than the Town's sales tax base. If the increase in spending is greater than would be expected from continued inflation and cannot be explained by the addition of new services, it can be an indicator of declining productivity.

### Analysis

The chart shows the cyclical nature of expenditures per capita - the shape of this chart typically demonstrates the same general shape as the Revenue per Capita chart seen on page 47, meaning that expenditure increases or decreases normally follow a similar trend as revenue changes. This is not the case with 2007/08 due to decreased revenue collections and increased expenditures. Expenditure changes tend to lag revenue changes (e.g. as revenues decline, expenditures may continue increasing until services can be adjusted to reflect the reduced revenue levels). Increases may be an indication that additional services are provided as the population increases. When revenues remain the same or decline, the expectation is that expenditures per capita would level out following the revenue trend. For 2007/08, operating expenditures grew 8% and operating revenues decreased 10%. Management must monitor this indicator closely because if this trend continues, the ability of the Town to maintain current service levels or expand for the growing population will be greatly hampered.



## EXPENDITURES PER CAPITA



<u>Expenditures per Capita</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Operating Expenditures	\$ 16,323	\$ 17,215	\$ 19,906	\$ 23,371	\$ 25,176
Consumer Price Index	186.1	191.7	199.0	204.1	211.7
Current Population	30,315	33,575	35,740	38,357	38,962
Depreciation	\$ 2,520	\$ 2,838	\$ 4,347	\$ 5,270	\$ 5,980
Constant Dollar					
Exp. per Capita <sup>1</sup>	\$ 245	\$ 223	\$ 219	\$ 231	\$ 233
Exp. per Capita (% change) <sup>2</sup>	-21.3%	-8.7%	-2.1%	5.7%	0.7%

Source: U.S. Bureau of Labor Statistics - CPI, Arizona Department of Economic Security,  
 Fiscal years 2003/04 to 2007/08 CAFR - Statement of Revenues, Expenditures and  
 Changes in Fund Balances - Governmental Funds  
 Fiscal years 2003/04 to 2007/08 CAFR - Combining Statement of Revenues,  
 Expenditures and Changes in Fund Balances - Nonmajor Governmental Funds  
 Fiscal years 2003/04 to 2007/08 CAFR Notes to Financial Statements - Section C.  
 Capital Assets

<sup>1</sup> Calculation: Operating Expenditures - Depreciation/CPI/Population\*100,000

<sup>2</sup> Calculation: Current Year - Prior Year/Prior Year

## EMPLOYEES PER CAPITA



### Description

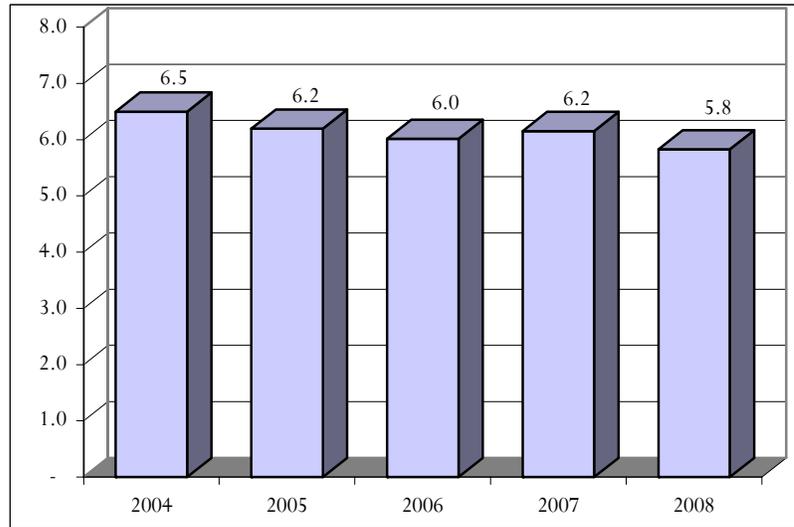
Personnel costs are a major portion of the Town's operating budget. Tracking changes in the number of employees to population is a means to measure changes in expenditures. An increase in employees to population may indicate that expenditures are rising faster than revenues, the Town is becoming more labor intensive or that productivity is declining. A decrease may be indicative of an insufficient number of employees on staff to provide increased or existing services and infrastructure maintenance to a growing community. This indicator needs to be evaluated in conjunction with other measurements (e.g. services provided, efficiency and effectiveness of service levels).

### Analysis

Full-time equivalents (FTE) include full-time, part-time and grant-funded employees. Although the Town has experienced increased growth during the period, employees per capita has decreased. For 2007/08, there was an 8.5% decrease in FTE which is attributed to the hiring freeze instituted by the Town to control expenditures. This calculation is not a measurement of types of service directly provided by Town staff (e.g. work that is contracted out, services provided by other government agencies or the private sector). The trend may suggest that the Town is providing increased service levels and productivity while not becoming more labor intensive. The most recent citizen satisfaction survey and employee workload should be reviewed in conjunction with this indicator.



## EMPLOYEES PER CAPITA



<u>Employees per Capita</u>	FY	FY	FY	FY	FY
	2004	2005	2006	2007	2008
Full-Time Staffing Equivalents	197	208	215	236	227
Current Population	30,315	33,575	35,740	38,357	38,962
Full-Time Staffing Equivalents (FTE) per Capita <sup>1</sup>	6.5	6.2	6.0	6.2	5.8

Source: Arizona Department of Economic Security,

Fiscal years 2003/04 to 2007/08 CAFR - Town Employee by Function - Table 17

<sup>1</sup> Calculation: FTE/Population\*1000

## FRINGE BENEFITS

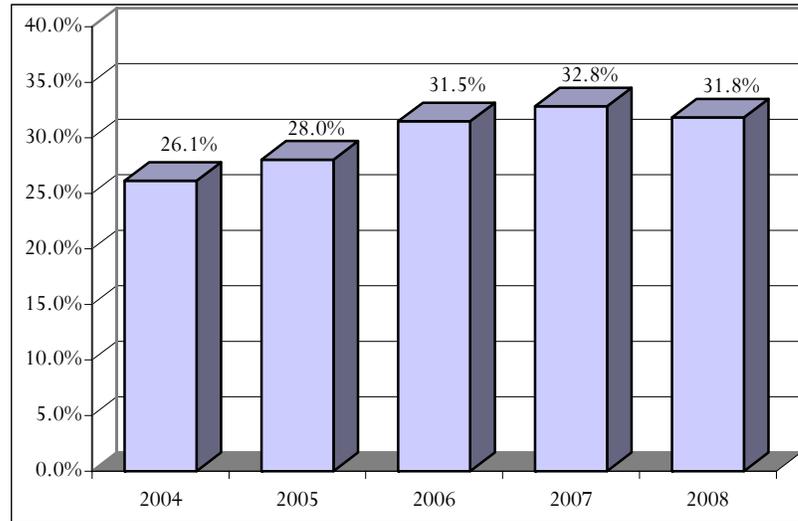
### Description

Fringe benefits comprise a significant portion of operating costs. Direct fringe benefits requiring an immediate cash outlay include retirement system contributions, worker's compensation, life and health insurance, tuition reimbursement and vehicle allowances. Indirect benefits, which include accumulated holiday, vacation and sick leave, do not require immediate cash outlay but may require paying the opportunity cost of not having the work done or paying others to do the work.

### Analysis

The increases over the years in fringe benefit expenditures were attributable to increased health care costs and retirement contributions as well as the addition of new employees. In 2005/06 the Town increased the employer retirement contribution rate from 7% to 12%. Health care premiums have remained stable for the 2006/07 and 2007/08 periods offset by increased worker's compensation rates. The Town's current percentage of fringe benefits to salaries and wages is lower than other state and local governments with the average rate reported by the U.S. Department of Labor - Bureau of Labor Statistics as 34.2% of salaries and wages. A factor in the decreased fringe benefit costs in 2007/08 is the reduction of 5.8 FTE staff. The addition of a Retirement Health Savings Account benefit in 2007/08, which the Town contributes 2% for all employees, added to the increased benefit expenditures from 2006/07 to 2007/08. The Town will be challenged to maintain this lower fringe benefit cost with continued rising health care costs which may be experienced in the future.

## FRINGE BENEFITS



<u>Fringe Benefits</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Fringe Benefit Expenditures	\$ 2,055	\$ 2,310	\$ 2,999	\$ 3,548	\$ 3,901
Salaries & Wages	\$ 7,865	\$ 8,239	\$ 9,524	\$ 10,806	\$ 12,257
% Fringe Benefits <sup>1</sup>	26.1%	28.0%	31.5%	32.8%	31.8%
Number of Employees	197	208	215	236	227

Source: Town of Prescott Valley Finance Division, Town of Prescott Valley Annual Budget,  
Fiscal years 2003/04 to 2007/08 CAFR - Town Employees by Function - Table 17

<sup>1</sup> Calculation: Fringe Benefits/Salaries & Wages

## OPERATING POSITION

Operating position refers to the Town's ability to balance its budget on a current basis, maintain reserves for emergencies and maintain sufficient cash to pay its bills on time.

During a typical year, a town will usually generate either an operating surplus, when revenues exceed expenditures or an operating deficit, when expenditures exceed revenues. An operating surplus or deficit may be created intentionally as a result of a conscious policy decision or may be created unintentionally because it is difficult to precisely forecast revenues and expenditures. When a deficit occurs, it is usually funded from accumulated fund balances; when a surplus occurs, it is usually dedicated to building prior years' fund balances or to funding future years' operations.

Reserves are built through the accumulation of operating surpluses. Reserves are maintained for the purposes of a financial cushion in the event of a loss of a revenue source, economic downturn, unanticipated expenditure demands due to natural disasters, insurance losses, need for large-scale capital expenditures or other non-recurring expenses or an uneven cash flow.

Sufficient cash or liquidity refers to the flow of cash in and out of the Town treasury. The Town receives many of its revenues in large installments at infrequent intervals during the year. It is to the Town's advantage to have excess liquidity or cash reserves as a cushion in the event of an

## OPERATING POSITION

● ● ● ● ● ● ● ● ● ● ● ● ● ● ● ● ● ●  
unexpected delay in receipt of revenues, an unexpected decline or loss of a revenue source or an unanticipated need to make a large expenditure.

An analysis of operating position can help identify the following situations:

- A pattern of operating deficits.
- A decline in reserves.
- A decline in liquidity.
- Ineffective revenue forecasting techniques.
- Ineffective budgetary controls.

Changes in operating position can be monitored by using the indicators detailed on the following pages.



## GENERAL FUND BALANCE



### Description

The level of fund balances may determine the Town's ability to withstand unexpected financial emergencies that may result from natural disasters, revenue shortfalls or steep rises in inflation. Fund balances may also determine the Town's ability to accumulate funds for large-scale purchases without having to borrow.

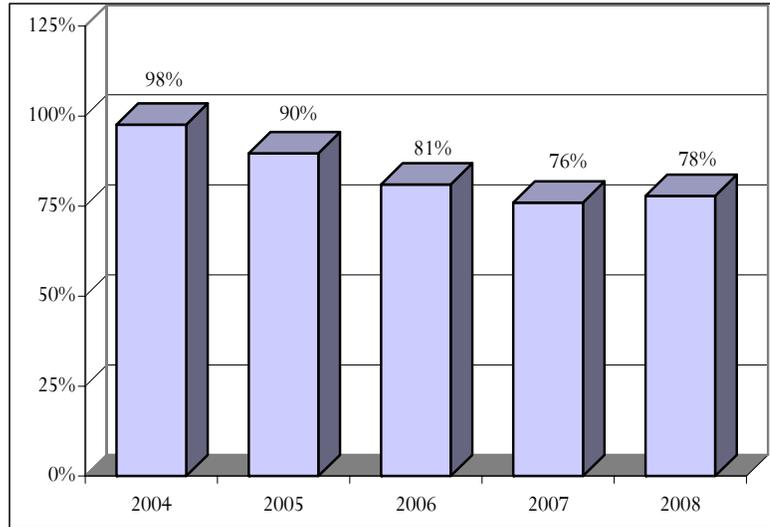
### Analysis

Prescott Valley's unrestricted fund balance as a percent of operating revenue has declined over the measured period with a slight increase in 2007/08 due to a reduction in budgeted expenditures as a result of an early recognition of slower revenue collections. This only becomes a negative trend when this decline is unplanned or if fund balances are dropping lower than is desirable. All fiscal years in the measured period have adopted an annual budget that planned for spending into fund balance. If the unreserved fund balance continues to decline, it could indicate the Town is experiencing financial stress.

The Town's financial policy states that the Town will maintain a general fund balance that represents at least 25% of the general government operating expenditures. Also, the carryover balance will equal at least 90 days of operating expenditures, and not be less than \$10 million. As of June 30, 2008, the Town had an unreserved and undesignated fund balance equal to 87% of the general government operating expenditures. In addition, the carryover balance was equivalent to 318 days of operating expenditures.



## GENERAL FUND BALANCE



<u>General Fund Balance</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
GF Unreserved/Undesignated Fund Balance	\$ 16,755	\$ 18,838	\$ 21,367	\$ 21,328	\$ 21,669
Total Operating Revenues General Fund Only	\$ 17,161	\$ 21,011	\$ 26,365	\$ 28,063	\$ 27,836
% Fund Balance <sup>1</sup>	98%	90%	81%	76%	78%

Source: Fiscal years 2003/04 to 2007/08 - CAFR Balance Sheet - Governmental Funds and  
Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds

<sup>1</sup> Calculation: Unreserved Fund Balance/Operating Revenue

## ENTERPRISE FUND EARNINGS



### **Description**

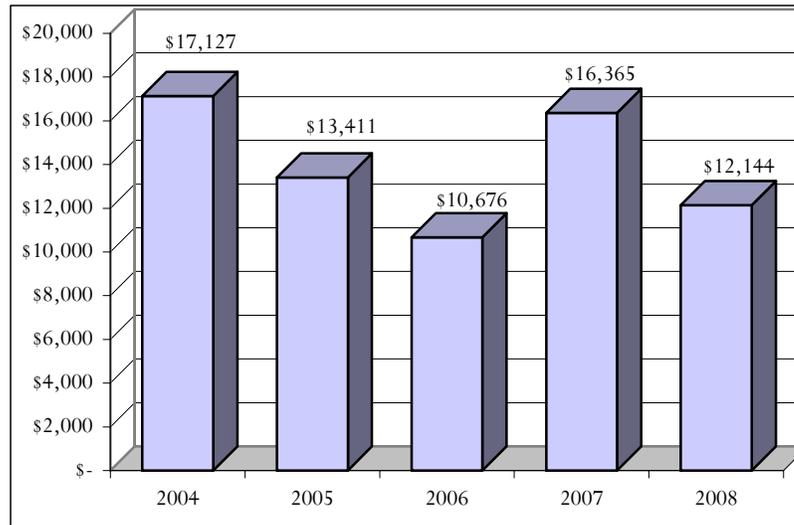
Enterprises are expected to function as if they were a commercial “for profit” entity and supported by user fees as opposed to a governmental “not for profit” entity supported by taxes. Moderate rate increases are included as part of the budget to offset increasing operational costs, mandated environmental standard compliance and capital assets attributable to repair and replacement of infrastructure as well as to maintain a net revenue ratio to remain in compliance with bond covenants and the Town financial policy. Positive operating results allow Enterprise Funds to stabilize rates even in years when large capital expenditures must be made (e.g. the construction of a new plant).

### **Analysis**

The Enterprise Funds for the Town are the Prescott Valley Water System and Wastewater funds. The separate entity of the Prescott Valley Water District was dissolved as of April 30, 2008 and consolidated into the Municipal Water System creating the Prescott Valley Water System. The declining profitability evidenced by the Enterprise Funds during the period of 2004/05 to 2005/06 revealed the need for a comprehensive evaluation of the rate structure resulting in volume rate increases in all three funds. The rate study was conducted during fiscal year 2006/07 and new rates were put into place October 2006, which contributed to the increase in profitability for these funds. In 2007/08 increased utilities and capital outlay as well as bond issuance costs, attributed to lower operating results which led to a rate study to be conducted in 2008/09. New rates became effective October 2008 which increased wastewater service by 3% and water service between 4% and 9%. These new rates will assist the Town in providing services for a growing population.



## ENTERPRISE FUND EARNINGS



<u>Enterprise Fund Earnings</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Enterprise Funds					
Operating Income(Loss)	\$ 685	\$ (105)	\$ (1,277)	\$ (550)	\$ (1,979)
Depreciation and Amortation	\$ 2,503	\$ 2,676	\$ 3,401	\$ 3,891	\$ 4,550
Consumer Price Index	186.1	191.7	199.0	204.1	211.7
Enterprise Funds Operating Results <sup>1</sup>	\$ 17,127	\$ 13,411	\$ 10,676	\$ 16,365	\$ 12,144

Source: U.S. Bureau of Labor Statistics - CPI,  
Fiscal years 2003/04 to 2007/08 CAFR - Statement of Revenues, Expenses & Changes in  
Fund Net Assets - Proprietary Funds

<sup>1</sup> Calculation: Operating Income(Loss) + Depreciation/CPI\*1000

Note: This graph includes Prescott Valley Water System, Wastewater and Water District.

## LIQUIDITY



### **Description**

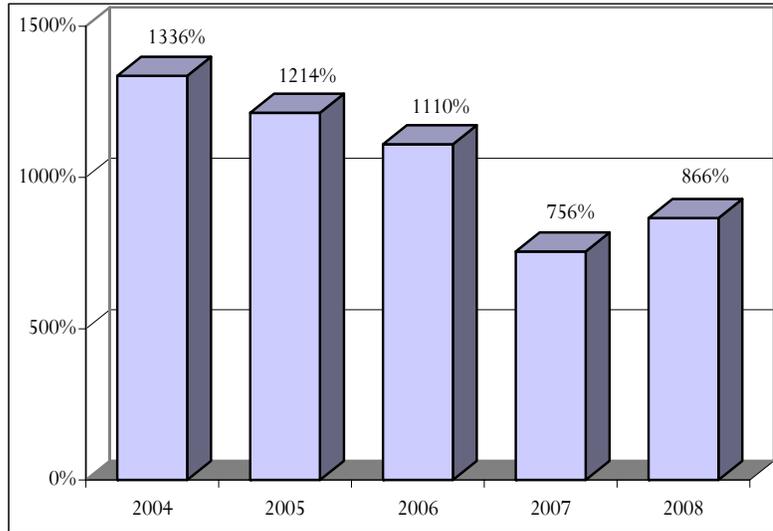
A measure of the Town's short-run financial condition is its cash position. Cash position includes cash on hand and in the bank, as well as other assets that can be easily converted to cash, such as short-term investments. The level of this type of cash is referred to as liquidity. Liquidity measures the Town's ability to pay its short-term obligations. Low or declining liquidity can indicate that the Town has overextended itself in the long term.

### **Analysis**

Liquidity is a controversial indicator, because the ratio changes constantly, depending on the time of year for receipt of revenues and the need for expenditures. The trend for fiscal years 2003/04 to 2006/07 is downward, which indicates that the Town is gradually using more of its cash on hand to meet the needs of the increasing population. In 2007/08, there is a slight increase due to conservative spending throughout the year. Per the International City/County Management Association handbook, if this ratio is less than one to one (or less than 100 percent), the commercial entity is considered to be facing liquidity problems. However, the percentage of current liabilities to cash and investments remains above industry averages, which indicates that the Town's ability to meet its short-term obligations is good.



## LIQUIDITY



<u>Liquidity</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Cash and Investments	\$ 13,810	\$ 15,533	\$ 20,462	\$ 21,567	\$ 34,287
Less Library Bond Proceeds	\$ -	\$ -	\$ -	\$ -	\$ 13,023
	\$ 13,810	\$ 15,533	\$ 20,462	\$ 21,567	\$ 21,264
Current Liabilities- General Fund Only	\$ 1,034	\$ 1,280	\$ 1,844	\$ 2,854	\$ 2,455
% Cash and Investments <sup>1</sup>	1336%	1214%	1110%	756%	866%

Source: Fiscal years 2003/04 to 2007/08 - CAFR Balance Sheet - Governmental Funds

<sup>1</sup> Calculation: Cash and Investments/Current Liabilities



## DEBT STRUCTURE

- Inadequacies in expenditure controls.
- Decreases in expenditure flexibility due to increased fixed costs in the form of debt service.
- Use of short-term debt to finance current operations.
- Existence of sudden large increases or decreases in future debt service.
- The amount of additional debt that the community can absorb.

Changes in debt structure can be monitored by using the indicators detailed on the following pages.



## CURRENT LIABILITIES



### Description

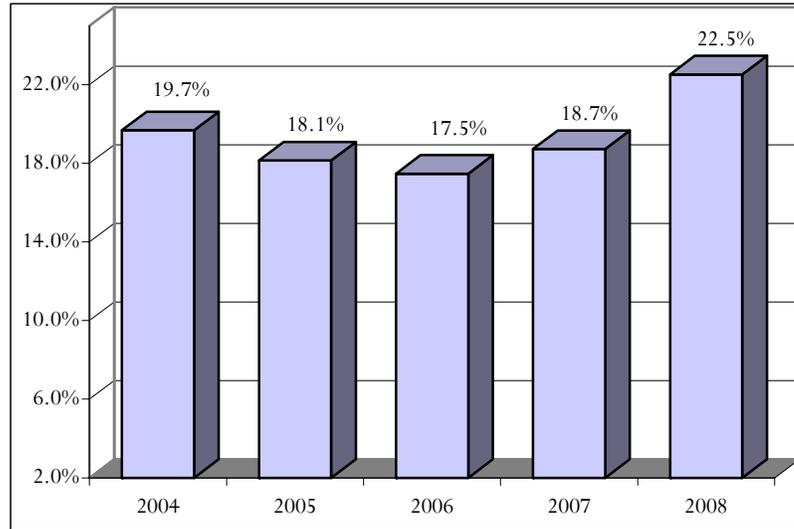
Governmental current liabilities are defined as the sum of all liabilities due at the end of the fiscal year, including short-term debt, current portion of long-term debt, accounts payable, accrued liabilities and other current liabilities. Current liabilities do not include Community Facilities Districts (CFD's) only Town obligated debt. Although short-term borrowing is an acceptable way to deal with uneven cash flow, an increasing amount of short-term debt outstanding at the end of successive years can indicate liquidity problems, deficit spending or both.

### Analysis

Current liabilities outstanding at the end of the year exceeding five percent of operating revenues and a two-year trend of increasing current liabilities outstanding at the end of the fiscal year is considered a negative trend. According to credit industry benchmarks, the Town has exceeded the five percent threshold for the past five years and has experienced increases over the last three years. This is primarily due to increases in debt service principal and interest payments on long-term debt associated with the Municipal Property Corporation. The increase from fiscal year 2005/06 to 2006/07 relates to a new \$5 million Water Infrastructure Finance Authority (WIFA) loan. The increase from 2006/07 to 2007/08 is due to the issue of the \$15.9 million bond for the Prescott Valley Public Library construction.



## CURRENT LIABILITIES



<u>Current Liabilities</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Current Liabilities	\$ 4,369	\$ 4,781	\$ 5,606	\$ 6,583	\$ 7,518
Operating Revenues	\$ 22,197	\$ 26,349	\$ 32,077	\$ 35,141	\$ 33,367
% Current Liabilities <sup>1</sup>	19.7%	18.1%	17.5%	18.7%	22.5%

Source: Fiscal years 2003/04 to 2007/08 - CAFR Statement of Net Assets - Governmental Activities

Fiscal years 2003/04 to 2007/08 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Governmental Funds

Fiscal years 2003/04 to 2007/08 CAFR - Notes Changes in Long-Term Liabilities

<sup>1</sup> Calculation: Current Liabilities/Operating Revenues

## NET DIRECT DEBT PER CAPITA



### **Description**

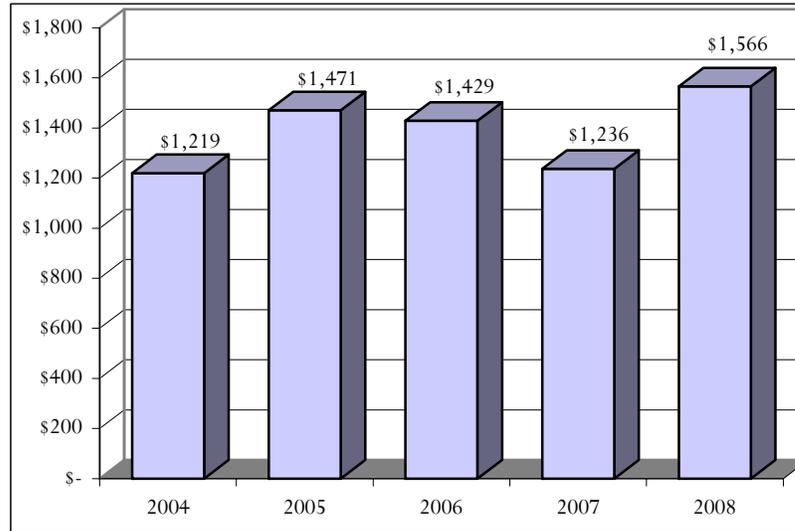
The per capita measure illustrates how the growth in debt is changing relative to population changes. As population increases it would be expected that capital needs and the associated long-term debt would also increase. If long-term debt is increasing in the face of a stabilizing or declining population, debt levels may be reaching or exceeding the Town's ability to pay. Net direct debt per capita does not include Community Facilities Districts (CFD's) only Town obligated debt.

### **Analysis**

Population has increased over the measured period and is projected to increase into the future. A growing town is expected to have associated debt burden to support its growing infrastructure needs. The 2004/05 increase was due to the issuance of \$14.3 million of Municipal Property Corporation debt to acquire additional water supply. During fiscal year 2005/06, the Town's total bonded debt decreased by approximately \$4.0 million. This decrease is attributable to the defeasance of \$1.2 million of Special Assessment debt and regularly scheduled debt service principal payments. For fiscal year 2006/07, no new long-term debt was acquired and debt decreased due to scheduled principal payments. In 2007/08, the increase is attributable to new debt being issued in the amount of \$15.9 million in bonds for the Prescott Valley Public Library construction. This calculation includes MPC, COP and Special Assessment debt and excludes Enterprise Fund bonded debt.



## NET DIRECT DEBT PER CAPITA



<u>Net Direct Debt Per Capita</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Net Direct Long-Term Debt	\$ 36,962	\$ 49,380	\$ 51,060	\$ 47,425	\$ 61,017
Population	30,315	33,575	35,740	38,357	38,962
Net Direct Debt Per Capita <sup>1</sup>	\$ 1,219	\$ 1,471	\$ 1,429	\$ 1,236	\$ 1,566

Source: Arizona Department of Economic Security,  
Fiscal years 2003/04 to 2007/08 CAFR - Notes Changes in Long-Term Liabilities

<sup>1</sup> Calculation: Net Direct Long-Term Debt/Population\*1,000

Note: Fiscal year 2005/06 has been restated due to a prior period adjustment found during the fiscal year 2006/07 audit.

## DEBT SERVICE



### Description

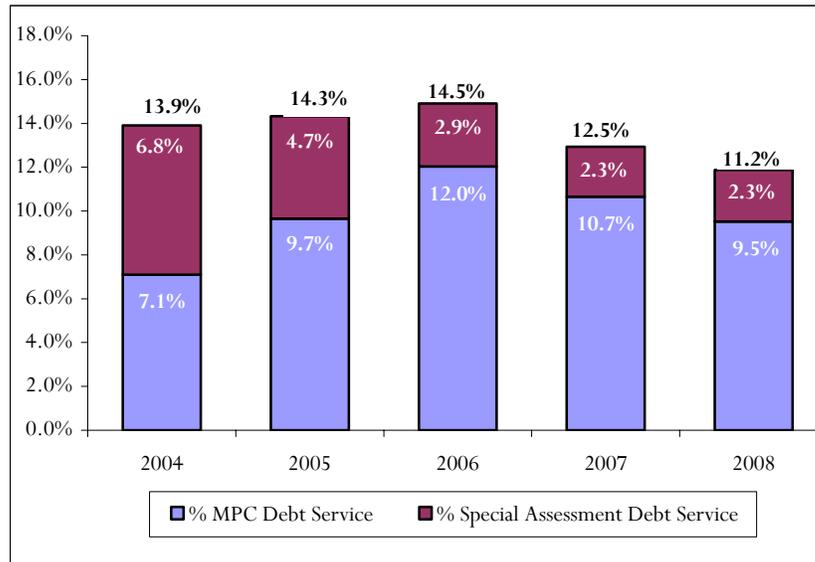
Debt service is defined as the amount of principal and interest that the Town must pay each year on net direct bonded long-term debt plus the interest it must pay on direct short-term debt. As the debt service increases, it adds to the Town's obligations and reduces the Town's expenditure flexibility. Debt service can be a major part of the Town's fixed costs and its increase may indicate excessive debt and fiscal strain.

### Analysis

The level of debt service as a percent of governmental fund operating revenues was on an upward climb from 2003/04 to 2005/06. The increases for 2003/04 to 2005/06 relate to higher scheduled debt service requirements on previous debt as well as new debt service requirements for the additional debt incurred for Water Importation Municipal Facilities Revenue Bonds. The decrease for 2006/07 and 2007/08 is due to a reduction in principal and interest for both MPC and Special Assessment bonds. The projection for 2008/09 will be an increase due to payments of newly issued bonds in 2007/08. According to the International City/County Management Association handbook, debt service on net direct debt exceeding 20% of operating revenue is considered a potential problem; 10% is considered acceptable. Per the Town's Financial Policy, debt service costs shall not exceed 25% of the Town's operating revenue so this rate is within limits.



## DEBT SERVICE



<u>Debt Service</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Governmental Debt Service	\$ 3,088	\$ 3,776	\$ 4,784	\$ 4,545	\$ 3,961
Operating Revenue	\$ 22,197	\$ 26,349	\$ 32,077	\$ 35,141	\$ 33,367
% Debt Service <sup>1</sup>	13.9%	14.3%	14.9%	12.9%	11.9%

Source: Fiscal years 2007/08 CAFR - Combining Statement of Revenues, Expenditures and Changes in Fund Balances - Nonmajor Governmental Funds (Special Assessments)  
 Fiscal years 2003/04 to 2007/08 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Governmental Funds

<sup>1</sup> Calculation: Debt Service/Operating Revenue

## EXCISE TAX



### **Description**

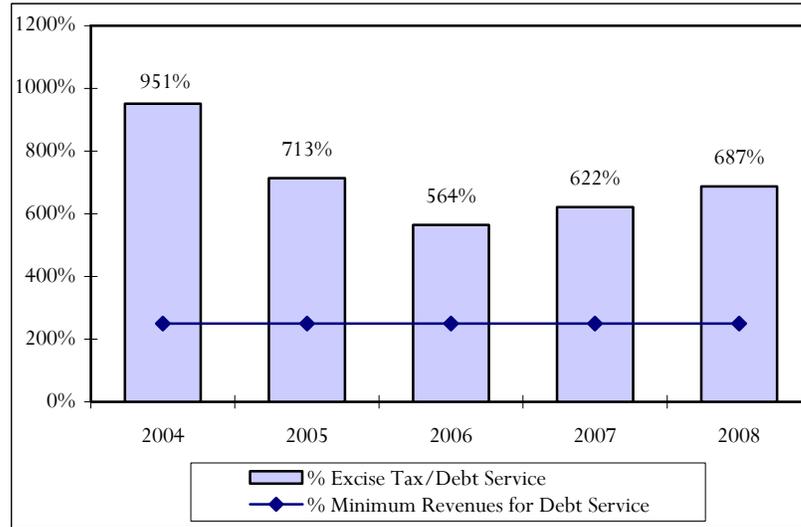
Excise taxes as a percent of debt service (MPC debt only) are presented as a measure of the Town's compliance with its bond indenture requirements. Excise tax is a tax levied on the manufacture, sale or consumption of certain (particular) non-essential goods or services (e.g. airline tickets, gasoline, alcohol, tobacco, etc). An excise tax is levied on a particular product in contrast to sales and use taxes, which are levied because sales occurred, rather than on the product purchased. For the Town, excise tax includes transaction privilege tax, franchise taxes, charges for services, state-shared revenues and fines and forfeitures.

### **Analysis**

Excise tax revenue has increased over the past four fiscal years with the exception of 2007/08 which declined 6% from the prior year due primarily to reduced transaction privilege tax collections. The percentage of excise tax with relation to MPC debt service increased for the year, but has more to do with the 15% decrease in debt service, attributable to a reduction in principal and interest payments, than revenues. Excise tax continues to exceed the minimum requirements of bond indentures which is two and one half times the debt service payments.



## EXCISE TAX



<u>Excise Tax</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Excise Tax	\$ 14,976	\$ 18,144	\$ 21,771	\$ 23,274	\$ 21,844
MPC Debt Service	\$ 1,575	\$ 2,543	\$ 3,859	\$ 3,743	\$ 3,180
% Excise Tax <sup>1</sup>	951%	713%	564%	622%	687%

Source: Town of Prescott Valley Financial Policies

Fiscal years 2003/04 to 2007/08 - Statement of Revenues, Expenditures and Changes in Fund Balances - Budget & Actual - GAAP Basis - General Fund and Streets Capital Improvement Fund

<sup>1</sup> Calculation: Excise Tax/Debt Service

Note: Minimum revenues for debt service are 2.5 times debt service obligations.

## OVERLAPPING DEBT



### **Description**

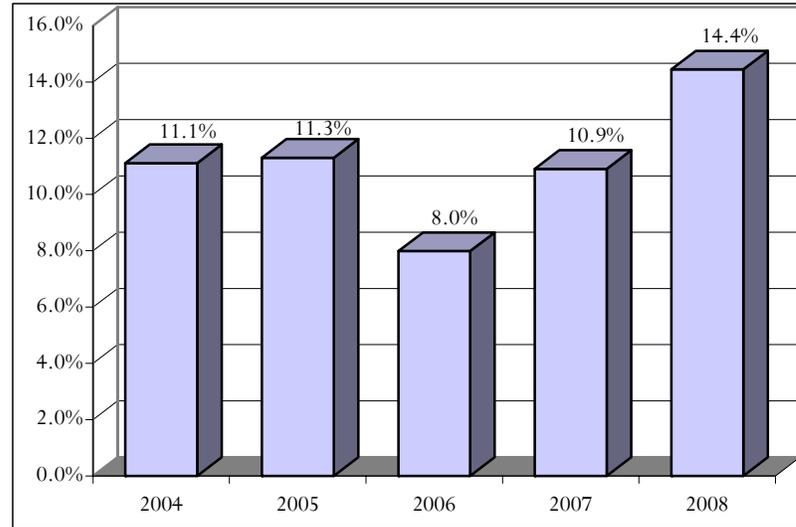
Overlapping debt is the net direct bonded debt of another jurisdiction that is issued against a tax base within all or part of the boundaries of the community. Examples of other jurisdictions are school districts and the County. The overlapping debt indicator measures the ability of the community's tax base to repay the debt of obligations issued by all of its governmental jurisdictions. Overlapping debt needs to be considered in assessing total indebtedness. Although the probability that the community of Prescott Valley would have to repay the debt may be slim, the potential exists.

### **Analysis**

The overlapping net debt as a percent of assessed valuation increased slightly for the period of 2004/05 reflecting an increase in both Yavapai Community College District and Humboldt Unified School District net debt outstanding. The decrease in fiscal year 2005/06 is due to the increase in assessed valuation even though net debt outstanding increased for Yavapai Community College District showing a positive trend as assessed value growth outstripped overlapping debt growth. For fiscal year 2006/07, both Yavapai Community College and Humboldt Unified School District increased their net debt outstanding considerably and this is offset by a sharp increase in assessed valuation. In 2007/08, the increase is due to Humboldt Unified School District increasing their debt by \$21 million with no increase reported by Yavapai Community College.



## OVERLAPPING DEBT



<u>Overlapping Debt</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Long-Term Overlapping Debt	\$ 20,292	\$ 24,652	\$ 20,686	\$ 36,073	\$ 63,019
Assessed Valuation	\$ 182,514	\$ 218,003	\$ 259,023	\$ 330,513	\$ 436,242
% Overlapping Debt <sup>1</sup>	11.1%	11.3%	8.0%	10.9%	14.4%

Source: State and County Abstract of the Assessment Roll, State of Arizona, Department of Revenue and the Property Tax Rates and Assessed Values, Arizona Tax Research Foundation, Fiscal year 2006/07 to 2007/08 CAFR - Statistical Section - Assessed and Est. Actual Value of Property - Table 12,  
 Fiscal year 2005/06 CAFR - Statistical Section - Assessed and Est. Actual Value of Property - Table 8,  
 Fiscal years 2003/04 to 2004/05 CAFR - Computation of Direct and Overlapping Debt - Table 12

<sup>1</sup> Calculation: Overlapping Debt/Assessed Valuation



## CONTINGENT LIABILITIES

A contingent liability is an existing condition or situation for which the ultimate disposition may not be known or does not have to be paid until a future year and for which reserves have been set aside. A contingent liability is similar to debt in that it represents a legal commitment to pay sometime in the future. Due to the potential magnitude, if these types of obligations are permitted to grow over a long period of time, they can have a significant impact on the Town's financial condition.

The contingent liabilities considered here are significant because they are not readily apparent in ordinary financial records, making it difficult to assess their relative impacts. Additionally, contingent liabilities build up gradually over time making it difficult to notice them until the problem is severe.

An analysis of the Town's contingent liabilities can reveal the following:

- An increase in the Town's pension liability.
- Inadequacies in pension plan contributions, pension systems assets and whether the investment earnings are keeping pace with the growth in benefits.
- An increasing amount of unused employee leave.
- Inadequacies of Town policies for payment of unused vacation and sick leave as compared to the Town's ability to pay.
- An increase in the amount of lawsuits and other claims against the Town.

## PENSION BENEFIT OBLIGATION PUBLIC SAFETY EMPLOYEES



### **Description**

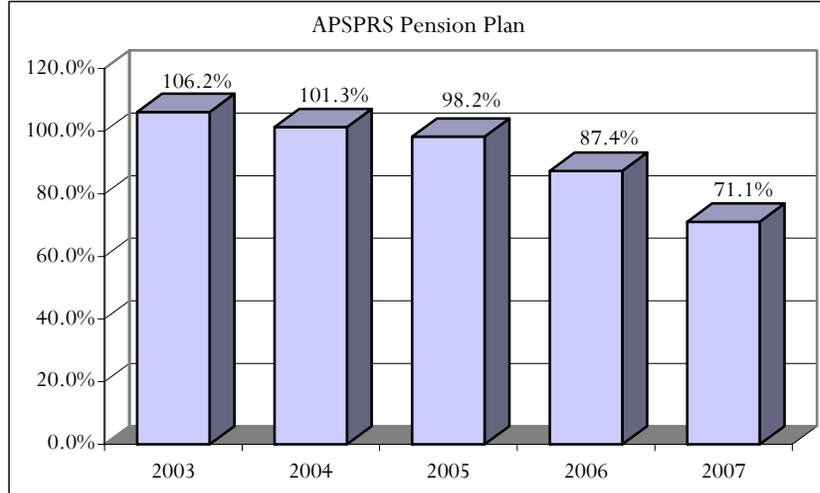
Pension plans represent a significant expenditure for the Town. There are two basic ways to fund the pension plans: (1) fund when benefits need to be paid (pay-as-you-go) or (2) fund as benefits accrue and reserve cash for when the benefits will have to be paid (full funding). The State of Arizona administers the pension plan for the public safety employees Arizona Public Safety Public Retirement System (APSPRS). This defined benefit pension plan provides retirement and disability benefits, annual cost-of-living adjustments and death benefits to plan members and beneficiaries. APSPRS members are required to contribute 7.65% of their annual salary. The Town is required to contribute at an actuarially determined rate. The rate for the year ended June 30, 2008 was 15.24% of annual covered payroll and the Town's annual pension cost of \$363,770 for APSPRS was equal to the Town's required and actual contributions.

### **Analysis**

Full funding of APSPRS has been a favorable trend over previous measured periods. The decline below 100% of APSPRS benefits funded in total, starting in fiscal year 2004/05 and continuing into 2006/07 can be attributed to a downturn in the economy, sharply lower returns on investments, expanded coverage needs and changing population demographics as average life expectancy increases. The decrease may also be attributable to an increased number of officers retiring. In light of this declining trend, increased contributions to the plans by employee and employer have been necessary to ensure full funding when the returns are less than 100%.



## PENSION BENEFIT OBLIGATION PUBLIC SAFETY EMPLOYEES



Pension Benefit Obligation

% of Pension Benefit Obligation Funded	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
Public Safety Retirement Plan (Police Employees)	106.2%	101.3%	98.2%	87.4%	71.1%

Source: Arizona Public Safety Personnel Retirement System report as of June 30, 2007  
Fiscal years 2003/04 to 2007/08 CAFR - Pension Plan Obligation Note

Note: Arizona Public Safety Personnel Retirement System report as of June 30, 2008 was not available when this analysis was completed.

## **PENSION BENEFIT OBLIGATION NON-PUBLIC SAFETY EMPLOYEES**



### **Description**

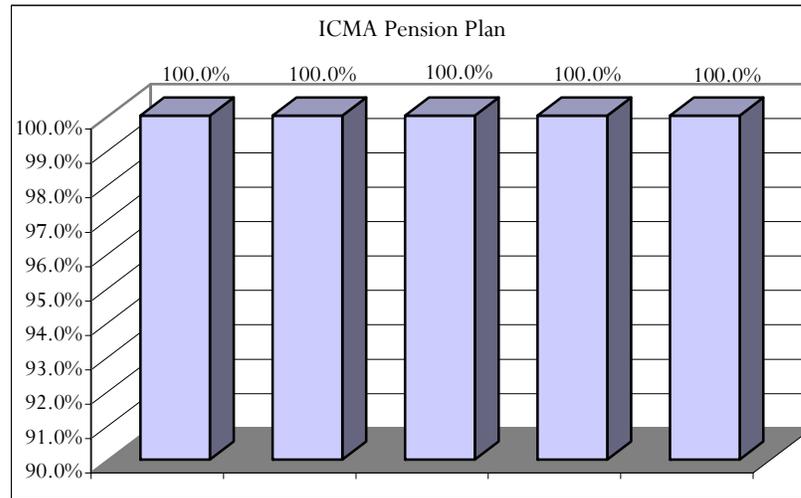
In lieu of participating in Social Security, the Town has a defined contribution plan created in accordance with Internal Revenue Code Section 401(a). The plan is available to all full-time employees of the Town, except sworn police personnel who are covered under the Arizona Public Safety Personnel Retirement System. In fiscal year 2007/08, the Town began a mandatory Retirement Health Savings Plan (RHS). The Town contributes 2% and employees contribute 1% of their salary.

### **Analysis**

The employee's contribution is one hundred percent (100%) funded at all times. The vesting schedule for the employer's contribution is twenty percent (20%) per year of service, thus employees are one hundred percent (100%) vested after five years of service. The ICMA defined contribution plan has been funded at one hundred percent over the measured periods.



## PENSION BENEFIT OBLIGATION NON-PUBLIC SAFETY EMPLOYEES



Pension Benefit Obligation

Percent of Pension Benefit Obligation Funded	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
ICMA (Other Employees)	100.0%	100.0%	100.0%	100.0%	100.0%

Source: Fiscal years 2003/04 to 2007/08 CAFR - Pension Plan Obligation Note



## ACCRUED COMPENSATED ABSENCES



### Description

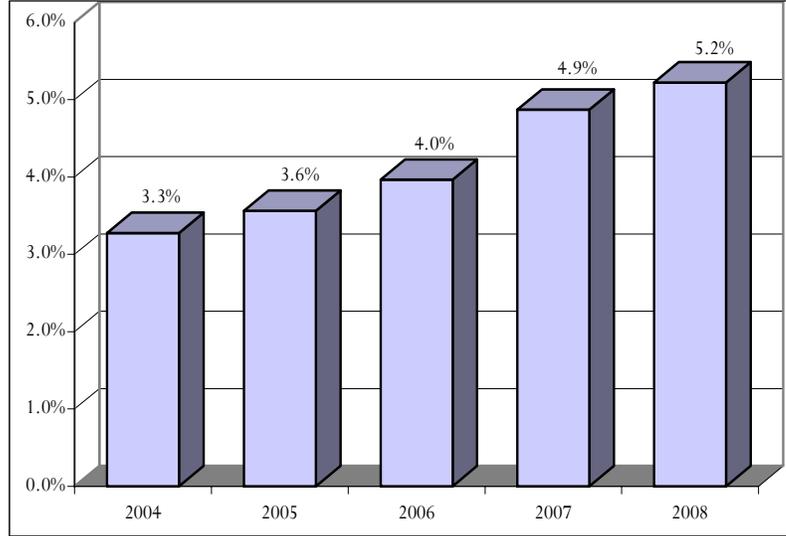
Accumulated unpaid general leave is accrued in governmental funds based on time of service and employee status. These accumulated employee benefits are payable to the employee, subject to certain limitations, and represent an unfunded, long-term liability to the Town.

### Analysis

The liability for compensated absences has remained constant over the prior four-year period. In fiscal year 2006/07 and 2007/08, there was an increase in compensated absences due primarily to an increase in employment and long-term employees earning a higher accrual rate.



## ACCRUED COMPENSATED ABSENCES



<u>Accrued Compensated Absences</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Compensated Absences	\$ 577	\$ 711	\$ 880	\$ 1,082	\$ 1,167
Unreserved Fund Balance	\$ 17,608	\$ 19,963	\$ 22,198	\$ 22,221	\$ 22,361
 % Compensated Absences <sup>1</sup>	3.3%	3.6%	4.0%	4.9%	5.2%

Source: Fiscal years 2003/04 to 2007/08 CAFR - Notes Changes in Long-Term Liabilities  
 Fiscal years 2003/04 to 2007/08 CAFR - Balance Sheet - Governmental Funds - Total  
 Unreserved (General Fund and HURF)

<sup>1</sup> Calculation: Compensated Absences/Unreserved Fund Balance

## CONDITION OF CAPITAL PLANT

Much of the Town's wealth is invested in its physical assets and infrastructure. If these assets are not maintained in good condition or if they are allowed to become obsolete, the result is often a decrease in the usefulness of the assets, an increase in the cost of maintaining and replacing them and a decrease in the attractiveness of the Town as a place to live or do business.

Many towns often defer maintenance and replacement because it is a relatively painless short-run method to reduce expenditures and ease current financial strain. Continued maintenance deferral, however, can create serious long-term problems that become exaggerated because of the large sums of money invested in capital facilities.

The following are some of the problems associated with continued deferred maintenance:

- Creation of safety hazards and other liability exposures.
- Reduction in the residential and business value of the Town.
- Decreased efficiency of equipment due to obsolescence and deferred maintenance.
- Increased costs of bringing the facility up to acceptable levels after continued maintenance deferral.

## CONDITION OF CAPITAL PLANT



- Creation of a large unfunded liability in the form of a backlog in maintenance that can result in accelerated deterioration.

The indicators detailed on the following pages can monitor changes in the condition of capital plant.



## MAINTENANCE EFFORT



### **Description**

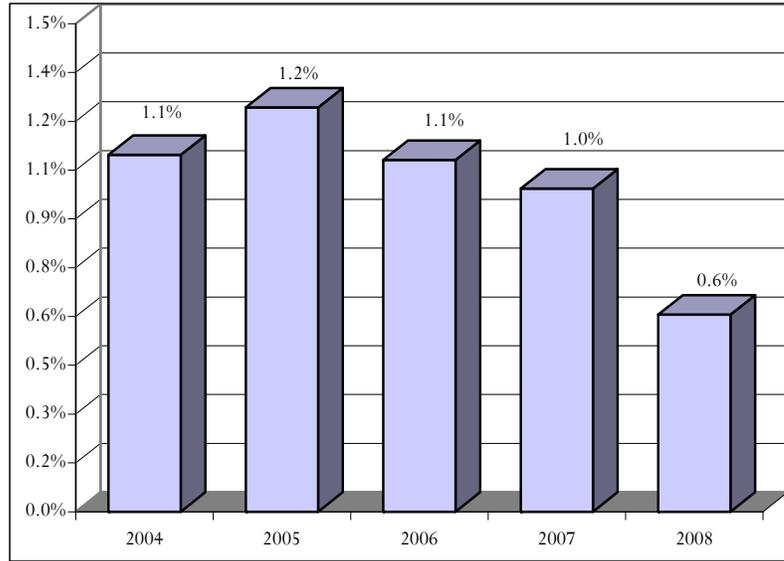
The condition of the Town's long-lived assets, such as buildings, is significant because of the tremendous cost and far-reaching consequence their decline can have on business activity, property values and operating expenditures. Deferral of maintenance on the assets and the subsequent deterioration can create a significant unfunded liability. Maintenance expenditures should remain relatively constant in relation to the cost and nature of assets maintained. If the ratio is declining it may be a sign that the Town's assets are deteriorating. This calculation excludes streets and other infrastructure and only focuses on building and building improvements.

### **Analysis**

Maintenance expenditures as a percent of building and improvement have decreased only slightly over the measured period. For the steady increase in population which the Town is experiencing, maintenance expenditures have remained stable. The Town replaces assets regularly as they break down or become obsolete. Building and improvements fixed asset acquisitions increased by 24% from fiscal year 2006/07 to 2007/08, attributing to the low level of maintenance required.



## MAINTENANCE EFFORT



<u>Maintenance Effort</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
Maintenance Expenditures	\$ 224	\$ 271	\$ 253	\$ 264	\$ 200
Building & Improvement Costs	\$ 20,421	\$ 21,815	\$ 23,398	\$ 26,587	\$ 33,025
 % Maintenance Expenditures <sup>1</sup>	1.1%	1.2%	1.1%	1.0%	0.6%

Source: Town of Prescott Valley Finance Division  
 Fiscal years 2003/04 to 2006/07 CAFR - Notes, Capital Assets Buildings and Improvements  
 Other Than Buildings  
<sup>1</sup> Calculation: Maintenance Expenditures/Building & Improvement Costs

## DEPRECIATION EXPENSE



### Description

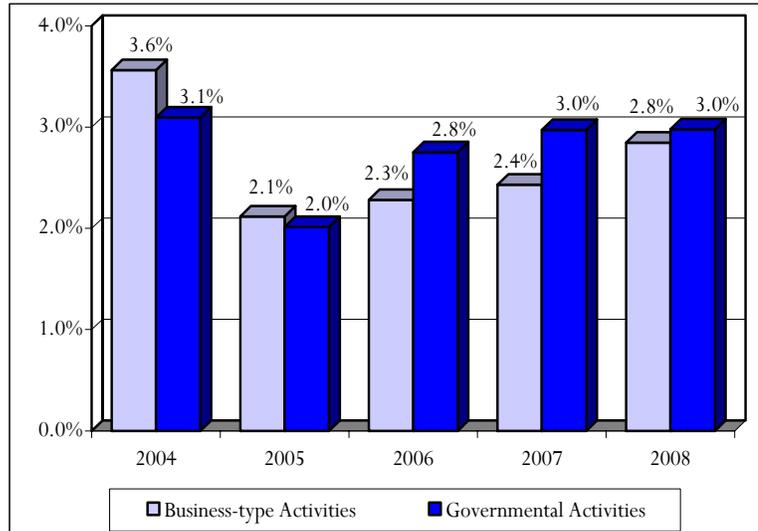
Depreciation is the mechanism by which cost is associated with the use of a fixed asset over its useful life. Depreciation should remain a relatively stable portion of asset cost assuming older assets, which are fully depreciated, are removed from service and replaced with newer assets. If depreciation costs start to decline as a portion of asset cost, the assets are probably being used beyond their useful lives, the estimated useful lives had been initially underestimated or the scale of operations was reduced.

### Analysis

Depreciation expense has remained a stable portion of fixed asset costs, which indicates that assets are being fully depreciated and replaced with newer assets on a timely basis. This will prevent a large expense, in any one year, to replace outdated assets. In fiscal year 2002/03, the Town was required to adopt Governmental Accounting Standards Board Statement No. 34 which required depreciation of all governmental assets. The significant increase in fixed assets for 2003/04 is attributable mainly to infrastructure contributed by developers.



## DEPRECIATION EXPENSE



<u>Depreciation Expense</u> (in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
<b>Business-Type Activities</b>					
Depreciation Expense	\$ 2,264	\$ 2,236	\$ 2,971	\$ 3,468	\$ 4,215
Fixed Asset Costs	\$ 63,516	\$ 105,568	\$ 130,243	\$ 142,640	\$ 148,084
% Depreciation Expense <sup>1</sup>	3.6%	2.1%	2.3%	2.4%	2.8%
<b>Governmental Activities</b>					
Depreciation Expense	\$ 2,520	\$ 2,838	\$ 4,347	\$ 5,270	\$ 5,980
Fixed Asset Costs	\$ 81,395	\$ 140,853	\$ 157,937	\$ 177,236	\$ 200,717
% Depreciation Expense <sup>1</sup>	3.1%	2.0%	2.8%	3.0%	3.0%

Sources: Fiscal years 2003/04 to 2007/08 CAFR - CAFR Notes to Financial Statements - Section C. Capital Assets

No. 34 at June 30, 2003, the Town is required to depreciate all governmental assets

<sup>1</sup> Calculation: Depreciation Expense/Fixed Asset Costs

Note: With the implementation of Governmental Accounting Standards Board Statement



TOWN OF PRESCOTT VALLEY