Town of Prescott Valley

Financial Trends Analysis

For Fiscal Years
2005 - 2009

December 2009

Prescott Valley
Where Opportunity Lives

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

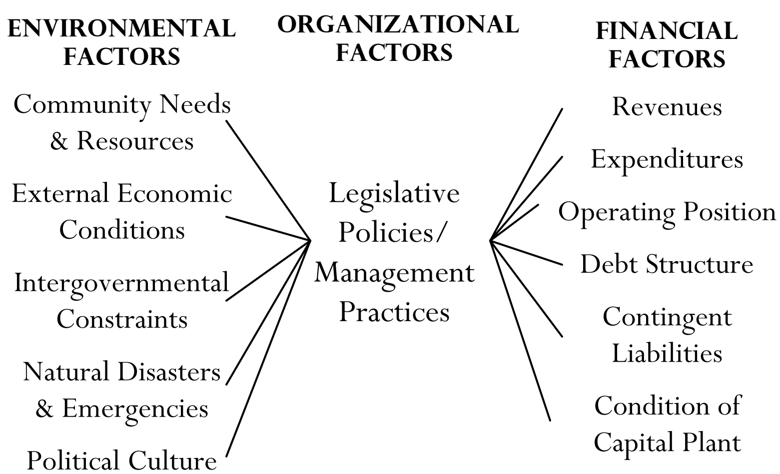
This report contains an analysis of the financial trends for the Town for the five-year period of 2004/05 - 2008/09. By analyzing these trends, the financial condition of the Town can be monitored. Monitoring the financial condition allows Town officials to better understand the forces that affect the *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

The analysis, as designed by the International City/ County Management Association (ICMA), encompasses three primary factors that affect the Town's financial condition: environmental factors, organizational factors and financial factors. These factors are divided into twelve categories that influence financial conditions. As the chart below illustrates, the factors are arranged as inputs and outputs to each other representing cause-and-effect relationships. The factors are interrelated and, taken collectively, represent an inventory of considerations when evaluating financial conditions.

FINANCIAL CONDITION FACTORS



Evaluating a government's financial condition is a complex process. For this reason, the trend information, whether positive, negative or neutral, should be viewed 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 revenues, 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 2008/09 fiscal year saw the *national and state economies* continue to decline with the slowdown in the housing market and rising unemployment. Governments continued to struggle to balance their budgets under declining revenues results. 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 and 2008/09. The third calendar quarter of 2009 showed an increase for GDP at a 3.5% annualized rate. This has been the first sign that the economic recession has ended, but there continues to be concerns about the economy and our weak labor market. Unemployment rates pushed up to an eye-catching 10.2 percent. 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 2009/10. These uncertainties include housing and construction markets, energy prices, inflation, consumer confidence, job market and geopolitical activity.

Arizona has been hard hit by the recession and is currently considered the third weakest economy in the United States. The state is ranked in last place among the states for job growth and the real estate market continues to struggle through this tough economic time. The state economy is currently feeling the effects of some signs of economic expansion, but the recovery will be at a very slow pace. Arizona will continue to experience rising unemployment and economic growth will be anemic at best. The state's expenditures continue to rise with falling revenues, setting the stage for future budget cuts and expected tax increases.

EXECUTIVE SUMMARY

Consensus forecasts call for a sluggish recovery due to tight credit markets and reduced consumer spending until consumer confidence in the recovery is well established. The return to robust growth in the state could be as long as 2011 or 2012.

Prescott Valley's growth leveled out with building permit activity remaining relatively the same as last year, but still at a 47% decline from fiscal year 2006/07. Building activity is projected to remain at these levels in fiscal year 2009/10, continuing the negative impact on the local economy in the housing and construction markets. This decline will provide economic challenges for Prescott Valley and its citizens, and will require prudent management of available Town resources to provide current or new Town services and maintain existing infrastructure.

Crossroads retail development was completed and several businesses opened such as Sam's Club, Home Depot, Cracker Barrel and Hobby Lobby. Other developments within Prescott Valley include Hampton Inn and Comfort Inn which opened during 2008/09. The new business additions in this area should increase revenues for the Town in future years. Fry's Supermarket recently expanded their business in the Glassford Hill Marketplace complex while Wal-Mart is projected to break ground in 2010/11. Developments for two new apartment complexes are also under construction or in the planning stage.

Executive Summary

A new Town of Prescott Valley Public Library was completed in October 2009 using funding generated from $15.9 million in Certificates of Participation issued December 2007. Yavapai Community College and Northern Arizona University will utilize a portion of this space for classrooms. This facility will occupy 52,000 square feet with the space used not only for the library, but an auditorium, classrooms and offices.

Based on fiscal year 2008/09 and the outlook for 2009/10, 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 through 2008/09 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, public safety, etc.) associated with the current population base and continued 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.

EXECUTIVE SUMMARY

The budget for the 2009/10 year includes a conservative economic forecast and reduced revenues projections from the prior year. 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 – The declining population in the area is a result of the weak economy and declining jobs in construction and housing. This also results in reduced tax receipts as spending in the Town is decreased. Inflation has declined which has a positive effect by keeping prices for goods at lower levels. Declines in residential development, business activity and personal income are currently having a negative effect on the Town's condition. Concerns in these areas will continue until the local economy experiences a rebound from the 2008 recession. Indicators in the current fiscal year are showing some signs of economic expansion, but there are many concerns on the stability and sustainability of any substantial economic rebound at this time.

Indicator	**2007/08**	**2008/09**
Population	Neutral	**Negative**
Inflation	Negative	**Neutral**
Residential Development	Negative	Negative
Business Activity	Negative	Negative
Personal Income	Negative	Negative

EXECUTIVE SUMMARY

Revenues – Operating revenues as well as sales tax revenues continue to fall in 2008/09 due to the downturn in the economy. The decrease in per capita revenues is substantial and is now at the level experienced in 2004/05. Restricted revenues are down substantially due to lower building permits and impact fees. Intergovernmental revenues carry future risk in revenues because of the current down economy which affects revenues from income tax and state-shared revenues received by the Town on a delayed basis.

Indicator	2007/08	2008/09
Revenues per Capita	Negative	Negative
Restricted Revenues	Positive	Positive
Intergovernmental Revenues	Negative	Negative
Elastic Revenues	Neutral	Neutral

Expenditures – The Town has experienced increased expenditures per capita during the past five periods. The Town's population and revenues have decreased in the recent periods. Expenditure changes tend to lag changes in revenue. This trend should be reversed as we experience reduced revenues which restrict the ability for the Town to enhance or maintain current services levels, or the Town will have to use fund balances for operating expenditures. The Town has taken measures to reduce costs in the past two fiscal years by implementing a hiring freeze and cost reduction controls.

Indicator	2007/08	2008/09
Expenditures per Capita	Negative	Negative
Employees per Capita	Positive	Positive
Fringe Benefits	Neutral	Neutral

EXECUTIVE SUMMARY

Operating Position – The operating position indicators reflect an overall solid financial base. Enterprise funds show an increase in earnings in the last year due to increased rates implemented in October of 2008 and reduced administrative expenses. 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.

Indicator	**2007/08**	**2008/09**
General Fund Balance	Neutral	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 to reduce service levels to enable payments of debt service. Current liabilities decreased $700K at the end of the year. Net direct debt per capita decreased due to debt service payments made during 2008/09. Debt service increased due to new bonds issued for the new library construction offset by debt service payments in the current fiscal year.

Indicator	**2007/08**	**2008/09**
Current Liabilities	Negative	Negative
Net Direct Debt per Capita	Neutral	Neutral
Debt Service	Neutral	Neutral
Excise Tax	Positive	Positive
Overlapping Debt	Negative	**Neutral**

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 Town has experienced increased funding needs for the pension obligation for the past five periods. The Defined Contribution Benefit Obligation-ICMA is one hundred percent funded.

Indicator	2007/08	2008/09
Pension Benefit-APSPRS	Negative	Negative
Defined Contribution Benefit-ICMA	Positive	Positive
Compensation Absences	Negative	Negative

Condition of Capital Plant – The Town's maintenance and replacement of capital assets increased slightly during 2008/09. This is due to the Town being proactive in the maintenance of buildings and infrastructure and regularly replacing broken or obsolete assets.

Indicator	2007/08	2008/09
Maintenance Effort	Neutral	Neutral
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.
3. The budget shall be adopted at the fund level. Budget

development will use strategic multi-year fiscal planning, conservative revenues forecasts and modified zero-base expenditure analysis that require 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 revenues 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 revenues system will be developed to protect programs from short-term fluctuations in any single revenues 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 revenues or enhanced operating efficiencies. Personnel cost reductions will be achieved through attrition to the extent feasible.

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,

Town resources will be substituted only after all program priorities and alternatives are considered during the budget process.

12. Alternative means of service delivery will be evaluated to ensure that quality services are provided to our citizens at the most competitive and economical cost. Departments, in cooperation with the Town Manager, will identify all activities that could be provided by another source and review options/alternatives to current service delivery. The review of service delivery alternatives and the need for the service will be performed annually or on an "opportunity" basis.

13. Cash and investment programs will be maintained in accordance with the Town Charter and the adopted investment policy and will ensure that proper controls and safeguards are maintained. Town funds will be managed in a prudent and diligent manner with an emphasis on safety of principal, liquidity and financial return on principal, in that order.

14. The Town will follow an aggressive and consistent policy of collecting revenues to the limit of our ability with sensitivity to individuals' circumstances. Collection policy goal will be for all adjusted uncollectible accounts to be no more than .5% of the total Town revenues being adjusted for bad debts annually.

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 revenues will be restricted for purposes of funding improvements for street and roadway projects such as the Lakeshore Drive improvements.

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.

20. The Town will seek to maintain and, if possible, improve our current bond rating in order to minimize borrowing costs and preserve access to credit.

21. An analysis showing how the new issue combined with current debt impacts the Town's debt capacity and conformance with Town debt policies will accompany every future bond issue proposal.

22. General Obligation (GO) debt, which is supported by property tax revenues and grows in proportion to the Town's assessed valuation and/or property tax rate increases, will be utilized as authorized by voters. Other types of voter-approved debt (e.g., water, sewer and HURF) may also be utilized when they are supported by dedicated revenue sources (e.g., fees and user charges).

23. Municipal Property Corporation (MPC) and contractual debt, which is non-voter approved, will be utilized only when a dedicated revenue source (e.g., transaction privilege taxes, State-shared revenues) can be identified to pay debt service expenses. The following considerations will be made to the question of pledging of project (facility) revenues towards debt service requirements:

    a. The project requires monies not available from other sources.

    b. Matching fund monies are available which may be lost if not applied for in a timely manner.

    c. Catastrophic conditions.

    d. The project to be financed will generate net positive revenues (i.e., the additional tax revenues generated 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 Revenues Bond Debt) should not exceed 25% of the Town's operating revenues 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 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 revenues to debt service meets our bond indenture requirement of 1.2:1. The Town goal will be to maintain a minimum ratio of utility revenues to debt service of

1.6:1 or greater, to ensure debt coverage in times of revenues 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.

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 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.

Prescott Valley

Prescott Valley

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 revenues for General Fund intergovernmental taxes, Highway Use Fuel Tax (HURF), and Local Transportation Assistance Funds (LTAF) in excess of $17.2 million in shared revenues from the State. This is an increase of 5% 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 HURF and LTAF revenues, 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 revenues share. In some cases, United States Census figures are used to calculate revenues distribution. Other revenues distribution method calculations are based on the county in which the revenues 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 2009/10, as future receipts will be based on income earned during the economic downturn of fiscal year 2007/08. Also, because of lower than expected state-wide revenues, State-Shared Sales Tax receipts to the Town are projected to decrease in fiscal year 2009/10.

RESTRICTED REVENUES

Restricted revenues is legally earmarked for specific use as may be required by State law, bond covenants or grant requirements. For example, the State of Arizona requires that gas tax revenues be used only for street maintenance or construction. 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 dictates by the funding agencies and may signal a future inability to at least maintain current service levels.

REPORTING REQUIREMENTS

State law requires that the Town establish at least two funds – the General Fund for recording "general" Town operations and the Highway User Revenues Fund (HURF), which records the monies received from highway user revenues. In addition to these requirements, additional funds are established to respond to reporting requirements for federal grants, bond rating agencies and regulatory accounting agencies.

PRESCOTT VALLEY

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 revenues 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. 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 revenues 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 revenues-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.

Prescott Valley

Population

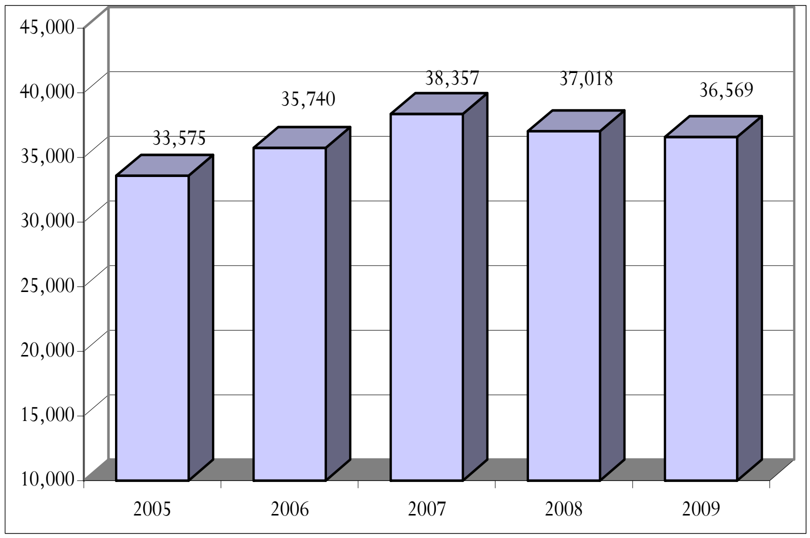
Description

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 has experienced a population decline in the last two years by 4.7%. The population decline seen over the past two years is related to the downturn in economic conditions in the region. The construction industry has dramatically declined, creating a reduction of jobs in the area. Businesses have struggled in this economy and some have closed their doors while others have contracted to remain open with reduced revenues. This has contributed to loss of jobs and potentially to the decline in population. This decline tends to have a negative effect on revenues for the Town and adverse effects on employment, income, housing and business activity. The economy and housing market seem to have reached bottom which could lead to a recovery in the economy over the next year. This could reverse the negative population trend in the region.

Population



Population	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Population	33,575	35,740	38,357	37,018	36,569
% Change[1]	10.8%	6.4%	7.3%	-3.5%	-1.2%

Source: Arizona Department of Economic Security

[1] Calculation: (Current Year Population - Previous Year Population)/Previous Year Population

INFLATION

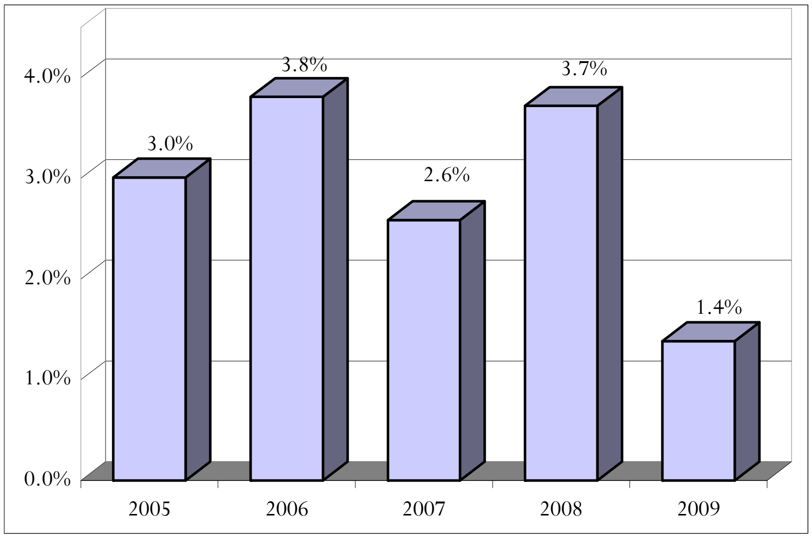
Description

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 decreased in fiscal year 2008/09 after an increase in the prior fiscal year. The Federal Reserve Board has kept interest rates low in an attempt to stimulate the economy. Low inflation helps prevent costs from rising faster than consumers' paychecks, allowing them to buy more with each dollar. Low inflation also increases incentives for shop owners to increase their inventories. However, with the decline in jobs, the increase in the unemployment rate, the unwillingness of financial institutions to lend and consumers' willingness to borrow may temper consumer spending, necessary for a robust recovery. Many factors play into inflation and this analysis is not intended to offer predictions.

INFLATION



Inflation	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Consumer Price Index	191.7	199.0	204.1	211.7	214.7
Inflation Rate [1]	3.0%	3.8%	2.6%	3.7%	1.4%

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

Note: Consumer Price Index is presented using fiscal year averages

[1] Calculation: (Current Year CPI - Prior Year CPI)/Prior Year CPI

Residential Development

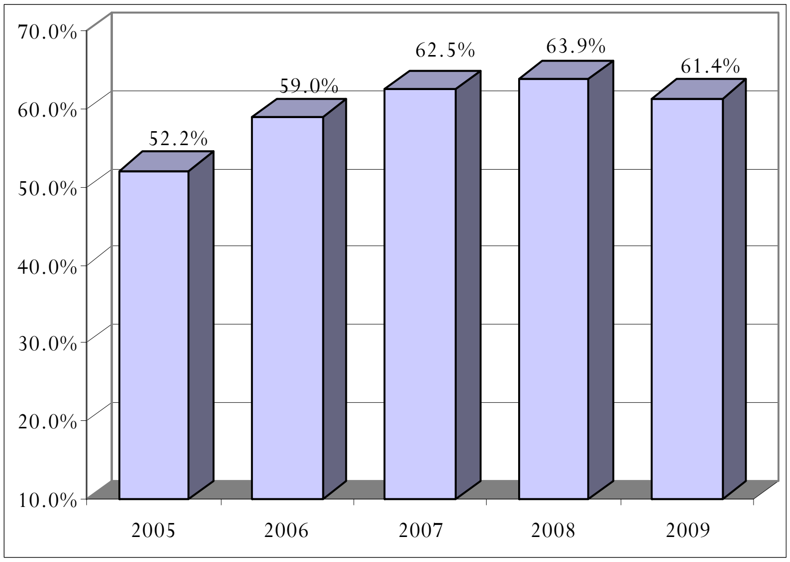
Description

Generally, the net cost of servicing residential development is higher than the net cost of servicing commercial or industrial development. 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 trended down slightly in 2009. Part of this decline is related 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. The housing market has recently seen some improvements and sales have increased with the help of the Federal government stimulus package. These improvements need to be sustained to fully recover in residential development. 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



Residential Development (in thousands)	Calendar Year 2005	2006	2007	2008	2009
Assessed Value Residential Property	$ 113,740	$ 152,864	$ 206,616	$ 278,908	$ 256,518
Assessed Value All Properties	$ 218,003	$ 259,023	$ 330,513	$ 436,242	$ 417,511
% Residential Development [1]	52.2%	59.0%	62.5%	63.9%	61.4%

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

[1] Calculation: Assessed Value Residential/Assessed Value All Property

Business Activity

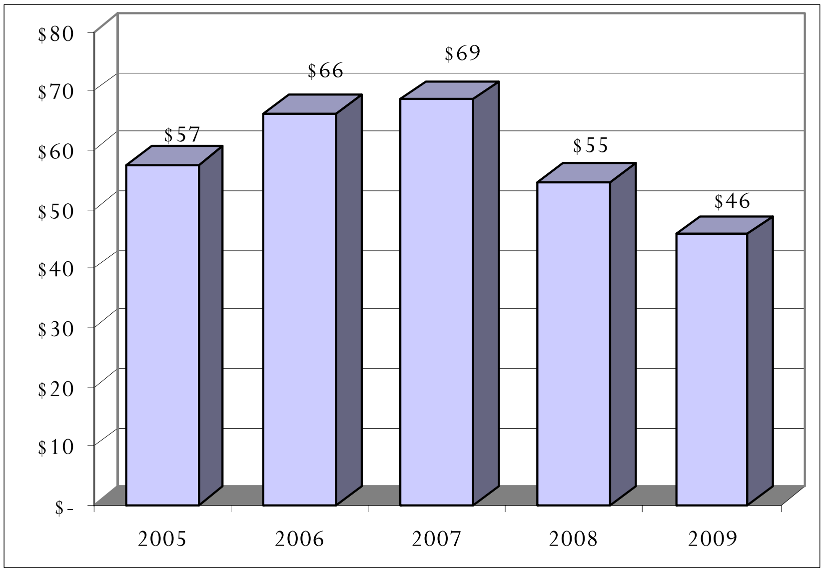
Description

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

In the last two fiscal years the Town has experienced a decrease in gross and net sales tax collections. Our current year net collections is equivalent to the level experienced in 2003/04. 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 revenues. The sales tax revenues in the graph is the net revenues adjusted for rebates paid to the developers. The reduction in sales tax collections is related to the slow economic conditions currently faced nationwide. Uncertainty still remains as to when the economy will recover and when revenues will return to a positive trend. If the negative trend continues, it will have a negative effect on the Town's revenues and limit the Town's ability to pay for community services.

BUSINESS ACTIVITY



Business Activity (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Sales Tax Revenues	$ 11,293	$ 13,781	$ 14,821	$ 12,500	$ 11,172
Rebated to Developers	288	600	819	934	1,340
Total Net Sales Tax	$ 11,005	$ 13,181	$ 14,002	$ 11,566	$ 9,832
Consumer Price Index	191.7	199.0	204.1	211.7	214.7
Net Constant Dollar					
Sales Tax Revenues [1]	$ 57	$ 66	$ 69	$ 55	$ 46
% Change Tax Revenues [2]	25.5%	15.4%	3.6%	-20.4%	-16.2%

Source: U.S. Bureau of Labor Statistics- CPI, Town of Prescott Valley Finance Division,
Fiscal year 2005/06 CAFR to 2008/09 - General Governmental Tax Revenues by Source - Table 5, Demographic and Economic Statistics - Table 15
Fiscal years 2004/05 to 2005/06 - CAFR Changes in Net Assets - Table 2c, Demographic and Economic Statistics - Table 16

[1] Calculation: Net Sales Tax/CPI

[2] Calculation: (Current Year Net Constant Dollar Revenues - Prior Year Net Constant Dollar Revenues)/Prior Year Net Constant Dollar Revenues

PERSONAL INCOME

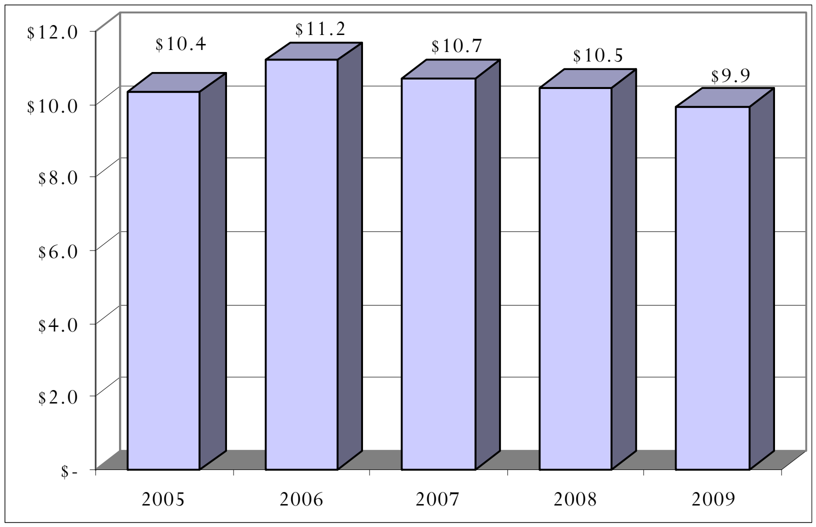
Description

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

Prescott Valley has experienced a downward trend in its per capita personal income for the last three fiscal years. This downward trend is related to the economic conditions faced regionally and nationally. This indicates a loss of consumer purchasing power and has had a negative impact on the Town's revenue sources due to decreases in consumer spending. The Town may also experience an increase in demand for services as families in the community face loss of jobs and uncertainty of future income. Businesses struggle with reduced revenues as consumers reduce spending. This may 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 2005		FY 2006		FY 2007		FY 2008		FY 2009
Per Capita Personal Income	$	19,858	$	22,282	$	21,836	$	22,133	$	21,317
Consumer Price Index		191.7		199.0		204.1		211.7		214.7
Population		33,575		35,740		38,357		37,018		36,569
Net Constant Dollar Personal Income (in thousands) [1]	$	10.4	$	11.2	$	10.7	$	10.5	$	9.9

Source: U.S. Bureau of Labor Statistics - CPI, Arizona Department of Economic Security,
Fiscal year 2006/07 to 2008/09 CAFR - Demographic and Economic Statistics - Table 15 ,
Fiscal year 2004/05 to 2005/06 CAFR - Demographic and Economic Statistics - Table 16

[1] Calculation: Per Capita Personal Income/CPI/10

Revenues

Revenues determine the capability of the Town to provide services. Important issues to consider in revenues 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. Revenues should be sufficiently unrestricted to allow for necessary adjustments to changing economic and operational conditions. Revenues should be balanced between elastic and inelastic sources with respect to economic base and inflation while others should remain relatively constant. Revenues 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 revenues structure will help to identify the following types of problems:

- Deterioration of the revenues base.
- Internal procedures or legislative policies that may adversely affect revenue yields.
- Inefficiency in the collection and administration of revenues.
- 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 revenues can be monitored by using the indicators detailed on the following pages.

Prescott Valley

Revenues per Capita

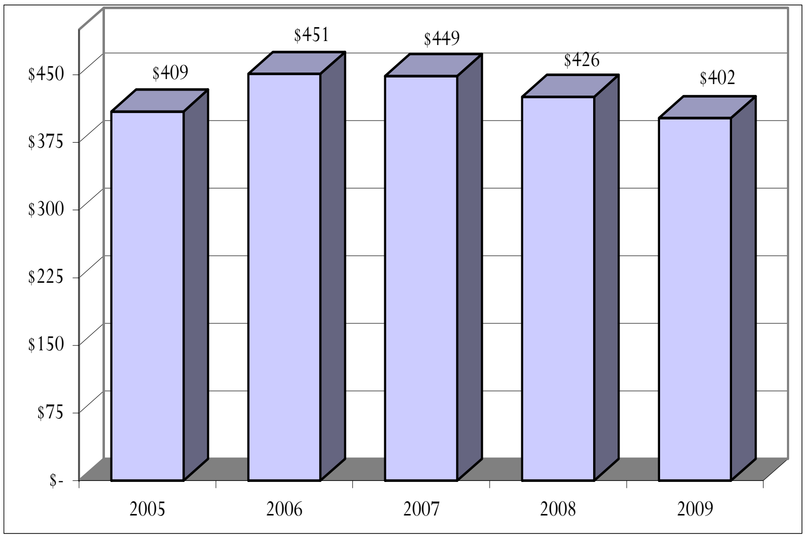
Description

Per capita revenues illustrates operating revenue changes relative to population changes. Operating revenues are comprised of local taxes (transaction privilege, cable TV franchise, and light and power franchise taxes), intergovernmental taxes (state revenues 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 revenues should remain at least constant in real terms. If per capita revenues are 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 2008/09, revenues per capita decreased 5.6 % from the prior year primarily due to the current economic conditions. The revenue streams affected by the economic downturn include transaction privilege tax (down 10%), building permits (down 33%), building charges for services (down 37%) and special assessments (down 11%). Recreation fees were up 10% and court fines up 16%. FY 2009/10 will also be affected by the downturn. A decline in revenues per capita could indicate the Town may have future difficulties in funding services for the community.

Revenues per Capita



Revenues per Capita (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Operating Revenues	$ 26,349	$ 32,077	$ 35,141	$ 33,367	$ 31,560
Consumer Price Index	191.7	199.0	204.1	211.7	214.7
Current Population	33,575	35,740	38,357	37,018	36,569
Net Constant Dollar Revenues Per Capita [1]	$ 409	$ 451	$ 449	$ 426	$ 402
Revenues Per Capita (% change) [2]	4.0%	10.2%	-0.5%	-5.1%	-5.6%

Source: U.S. Bureau of Labor Statistics - CPI, Arizona Department of Economic Security.
Fiscal years 2004/05 to 2008/09 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Governmental Funds

[1] Calculation: Operating Revenues/CPI/Population*100,000

[2] Calculation: (Current Year - Prior Year)/Prior Year

Note: Does not include Community Facilities Districts

RESTRICTED REVENUES

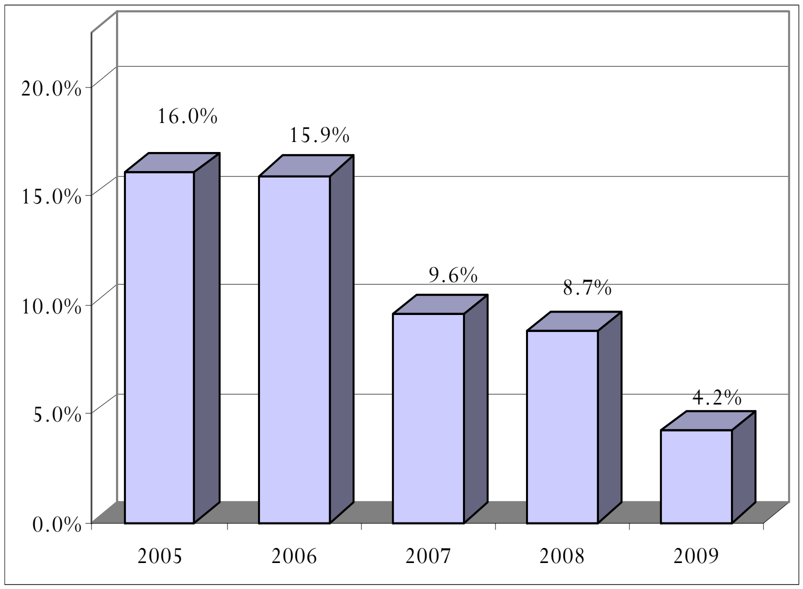
Description

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 revenues has declined during the past five fiscal years. Due to fewer building permits being issued, impact fee revenues fell 38% from 2007/08 to 2008/09. In addition, developer revenues declined $1.2 million, of which $640,000 represented a 2007/08 one time charge, allowing outsiders to connect to Southside CFD No. 1 facilities, and the balance from an increase in property tax revenues which offset the developers' contributions. 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 community.

Restricted Revenues



Restricted Revenues (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Restricted Operating Revenues	$ 4,229	$ 5,100	$ 3,356	$ 2,917	$ 1,320
Operating Revenues	$ 26,349	$ 32,077	$ 35,141	$ 33,367	$ 31,560
% Restricted [1]	16.0%	15.9%	9.6%	8.7%	4.2%

Source: Fiscal years 2004/05 to 2008/09 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Government Funds

[1] Calculation: Restricted Operating Revenues/Operating Revenues

Intergovernmental Revenues

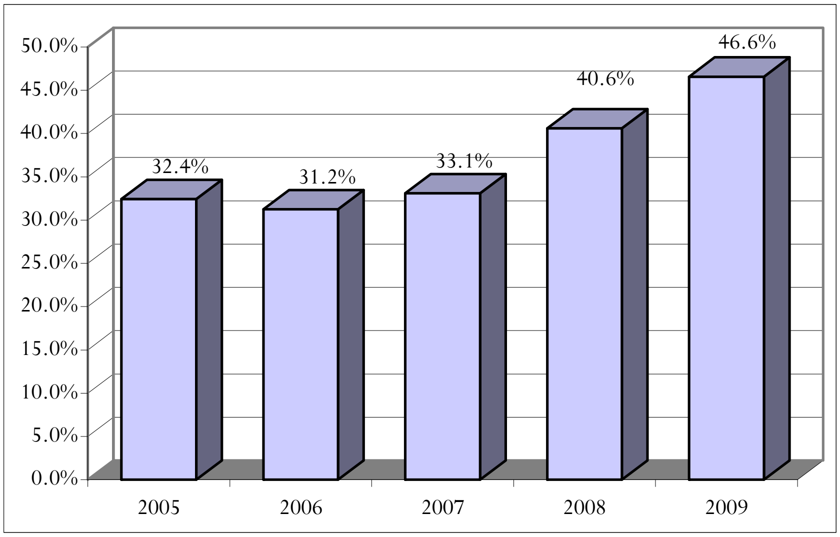
Description

Intergovernmental revenues are received from other governmental entities. Intergovernmental revenues for the Town encompass state revenues 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 revenues. During declining economic times, state and federal governments may withdraw or reduce payments to local governments.

Analysis

The warning trend for this indicator is an increasing amount of intergovernmental operating revenues as a percentage of operating revenues. Fiscal year 2008/09 continued to see an increase in these revenues primarily due to $2.1 million received from Yavapai College for their portion of construction costs related to the Prescott Valley Public Library Building. The balance of these revenues from Yavapai College will be received in FY 2009/10. State sales tax revenues declined $400,000 from the prior year due to economic conditions and are projected to further decline in 2009/10. Other state revenues remained fairly constant in 2008/09, but are also expected to decline during the current year. 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



Intergovernmental Revenues (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Intergovernmental Revenues	$ 8,547	$ 10,023	$ 11,634	$ 13,548	$ 14,699
Operating Revenues	$ 26,349	$ 32,077	$ 35,141	$ 33,367	$ 31,560
% Intergovernmental [1]	32.4%	31.2%	33.1%	40.6%	46.6%

Source: Fiscal years 2004/05 to 2008/09 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Government Funds

[1] Calculation: Intergovernmental Revenues/Operating Revenues

Elastic Tax Revenues

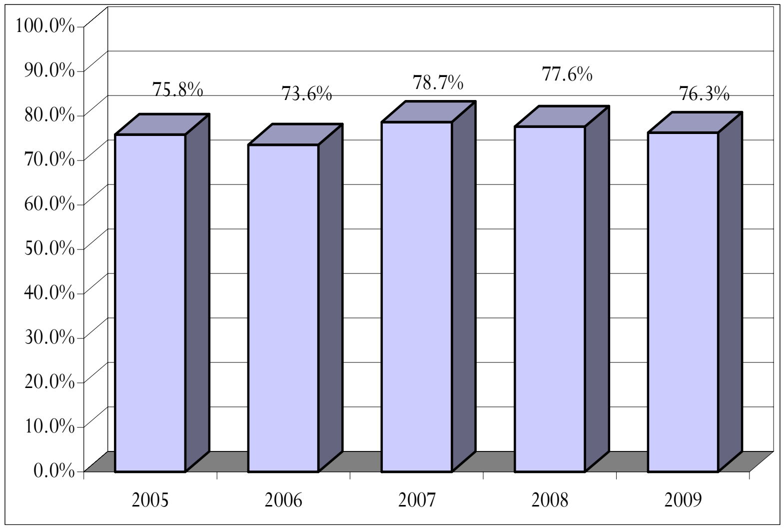
Description

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 revenues category: general sales tax, state-shared sales tax, state revenues sharing, auto lieu tax, highway user revenues 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. In spite of a slowed economy, elastic revenues declined less than 1% in 2008/09. 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 2009/10 is lowered elastic tax revenues 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



Elastic Tax Revenues (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Elastic Tax Revenues	$ 19,980	$ 23,596	$ 27,648	$ 25,899	$ 24,066
Operating Revenues	$ 26,349	$ 32,077	$ 35,141	$ 33,367	$ 31,560
% Elastic Tax Rev. [1]	75.8%	73.6%	78.7%	77.6%	76.3%

Source: Fiscal years 2004/05 to 2008/09 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Government Funds

[1] Calculation: Elastic Tax Revenues/Operating Revenues

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 increase, the flexibility to make spending decisions decreases.

Ideally, the Town will have an expenditure growth rate that does not exceed its revenue growth rate and will have maximum spending flexibility to adjust to changing conditions. Analyzing the Town's expenditure profile will help to identify the following types of problems:

- Excessive growth of overall expenditures as compared to revenue growth or growth in community wealth (personal and business income).
- An undesired increase in fixed costs.
- Ineffective budgetary controls.
- A decline in personnel productivity.
- Excessive growth in programs that create future expenditure liabilities.

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

EXPENDITURES PER CAPITA

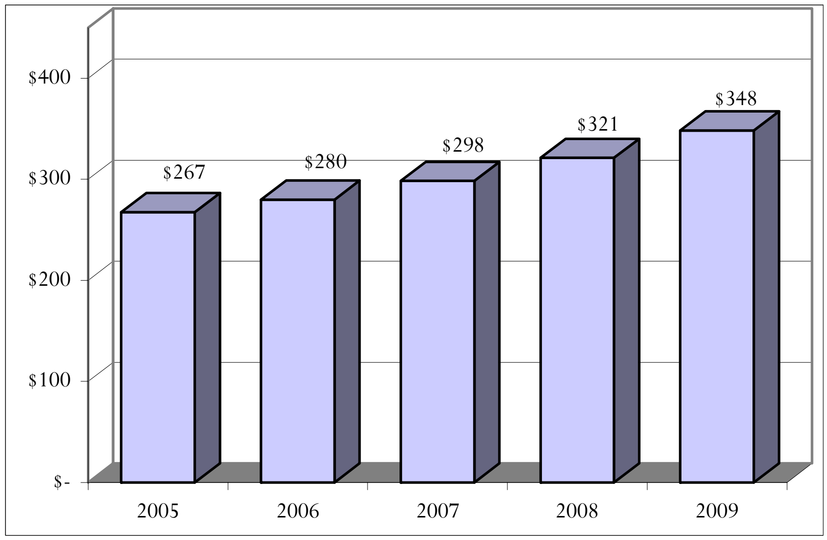
Description

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 a continued trend of increased costs per capita since FY2005/06. Expenditure increases or decreases normally follow a similar trend as revenues change. The Town has experienced declining revenues for the past three years while expenditures have continued to increase. Expenditure changes will tend to lag revenue changes (e.g. as revenues decline, expenditures may continue increasing until services can be adjusted to reflect the reduced revenues levels). Under these economic conditions, to balance revenues and expenditures, either expenditures have to be decreased or revenues increased. Another alternative would be to use fund balances to cover operating expenditures. For 2008/09, operating expenditures grew 8% and operating revenues decreased 10%. Management has taken steps through reduced spending and a hiring freeze to reverse the trend for expenditures. Continued monitoring of this indicator is required because if this trend continues, the ability of the Town to provide adequate service levels for the community will be greatly hampered.

EXPENDITURES PER CAPITA



Expenditures per Capita (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Operating Expenditures	$ 17,215	$ 19,906	$ 23,371	$ 25,176	$ 27,347
Consumer Price Index	191.7	199.0	204.1	211.7	214.7
Current Population	33,575	35,740	38,357	37,018	36,569
Constant Dollar					
Expenditures per Capita [1]	$ 267	$ 280	$ 298	$ 321	$ 348
(% change) [2]	9.3%	4.6%	6.6%	7.6%	8.5%

Source: U.S. Bureau of Labor Statistics - CPI, Arizona Department of Economic Security,
Fiscal years 2004/05 to 2008/09 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Governmental Funds
Fiscal years 2004/05 to 2008/09 CAFR - Combining Statement of Revenues, Expenditures and Changes in Fund Balances - Nonmajor Governmental Funds

[1] Calculation: Operating Expenditures/CPI/Population*100,000

[2] Calculation: (Current Year - Prior Year)/Prior Year

Employees per Capita

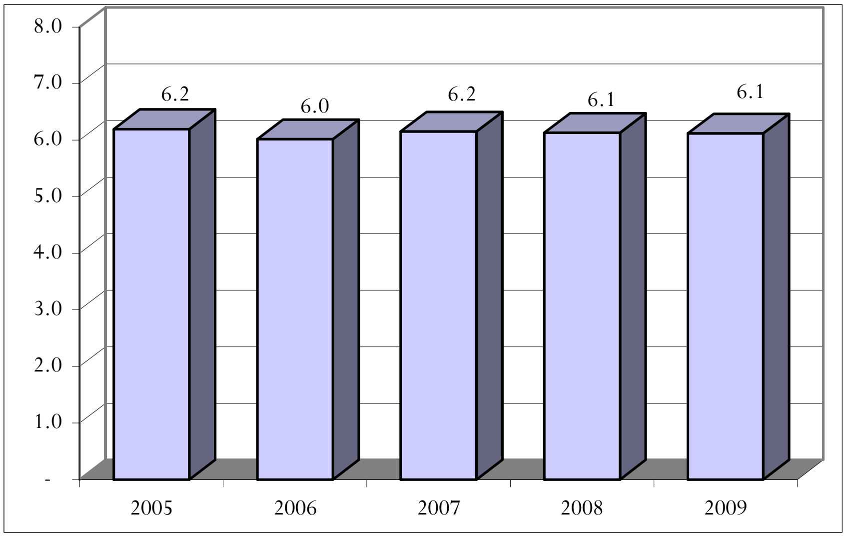
Description

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. This information could be confirmed after the next citizen satisfaction survey and comparing it with the survey taken in 2007.

EMPLOYEES PER CAPITA



Employees per Capita	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Full-Time Staffing Equivalents	208	215	236	227	224
Current Population	33,575	35,740	38,357	37,018	36,569
Full-Time Staffing Equivalents (FTE) per Capita [1]	6.2	6.0	6.2	6.1	6.1

Source: Arizona Department of Economic Security,
Fiscal years 2004/05 to 2008/09 CAFR - Town Employee by Function - Table 17

[1] Calculation: Full-Time Staffing Equivalents/Population*1000

FRINGE BENEFITS

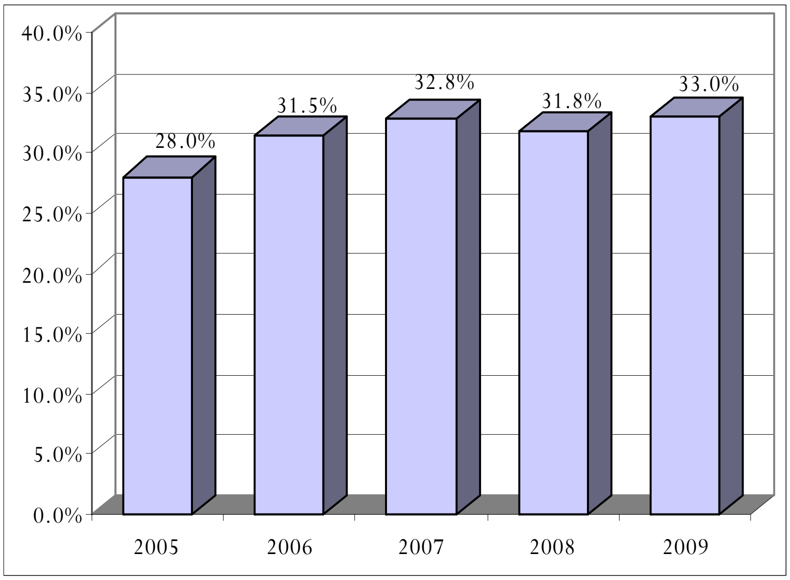
Description

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 primarily attributable to increased retirement contributions offset by a small reduction of employees and lower worker's compensation costs. In 2005/06 the Town increased the employer retirement contribution rate from 7% to 12%. Health care premiums have remained stable for the past three years. In 2008/09 there was a reduction of 3 FTE staff while the annual salaries and wages remained level. The increase in benefits for the current year is attributed to contributions to the Arizona Public Safety Personnel Retirement System (APSPRS). The contributions increased by $260,000 over the prior year. This was offset by lower worker's compensation costs and lower contribution costs for ICMA and health insurance paid by the Town. The cost reduction measures and hiring freeze currently in place should enable the Town to reduce the salaries and benefit cost in the future until the economy recovers.

Fringe Benefits



Fringe Benefits (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Fringe Benefit Expenditures	$ 2,310	$ 2,999	$ 3,548	$ 3,901	$ 4,049
Salaries & Wages	$ 8,239	$ 9,524	$ 10,806	$ 12,257	$ 12,257
% Fringe Benefits [1]	28.0%	31.5%	32.8%	31.8%	33.0%
Number of Employees	208	215	236	227	224

Source: Town of Prescott Valley Finance Division, Town of Prescott Valley Annual Budget, Fiscal years 2004/05 to 2008/09 CAFR - Town Employees by Function - Table 17

[1] 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 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

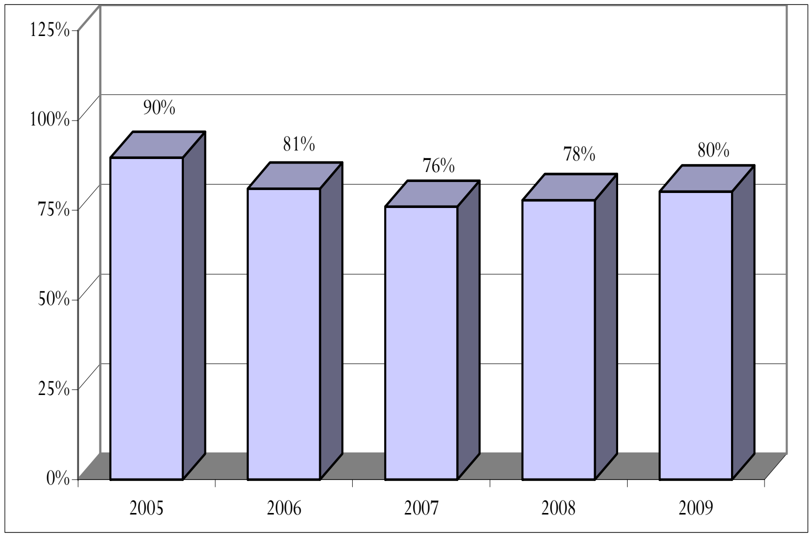
The level of fund balances may determine the Town's ability to withstand unexpected financial emergencies that may result from natural disasters, revenue shortfalls or steep rises in inflation. Fund balances may also determine the Town's ability to accumulate funds for large-scale purchases without having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

Analysis

Prescott Valley's unrestricted fund balance as a percent of operating revenues had declined for the first three years of the measured period with a slight increase beginning in 2007/08 and continuing through 2008/09. This increase is due to a reduction in budgeted expenditures as a result of an early recognition of slower revenues 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.

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, 2009, the Town had an unreserved and undesignated fund balance equal to 86% of the general government operating expenditures. In addition, the carryover balance was equivalent to 310 days of operating expenditures.

GENERAL FUND BALANCE



General Fund Balance (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
GF Unreserved/Undesignated Fund Balance	$ 18,838	$ 21,367	$ 21,328	$ 21,669	$ 22,710
Total Operating Revenues General Fund Only	$ 21,011	$ 26,365	$ 28,063	$ 27,836	$ 28,302
% Fund Balance [1]	90%	81%	76%	78%	80%

Source: Fiscal years 2004/05 to 2008/09 - CAFR Balance Sheet - Governmental Funds and Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds

[1] Calculation: Unreserved Fund Balance/Operating Revenues

Enterprise Fund Earnings

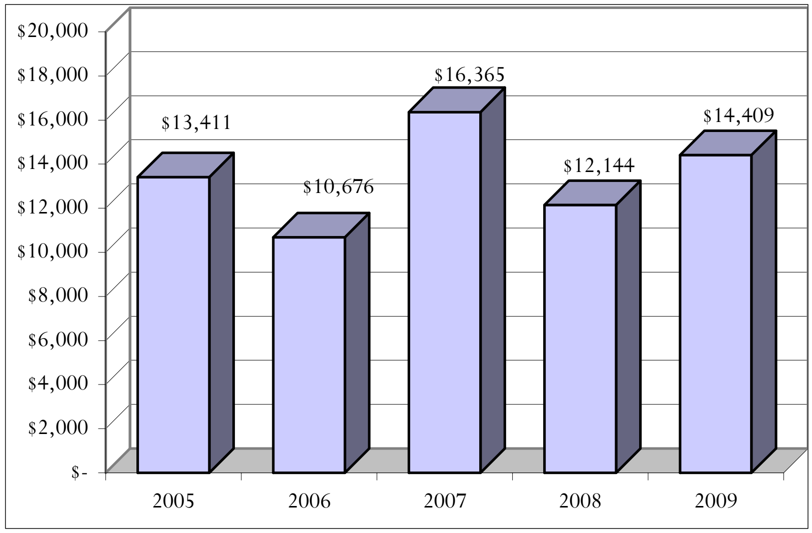
Description

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 revenues 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. 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%. During FY 2008/09 the number of Water System customers decreased by 80 or .4% and consumption decreased by 182.6 million gallons or 9.9%. In addition, operating expenditures declined $445,000, primarily from reduced administrative expenses. Effective November 1, 2009, there will be a 3% rate increase in wastewater service and a 9% water increase for those customers north of Hwy 89A.

ENTERPRISE FUND EARNINGS



Enterprise Fund Earnings (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Enterprise Funds Operating Losses	$ (105)	$ (1,277)	$ (550)	$ (1,979)	$ (1,508)
Depreciation and Amortation	$ 2,676	$ 3,401	$ 3,891	$ 4,550	$ 4,601
Consumer Price Index	191.7	199.0	204.1	211.7	214.7
Enterprise Funds Operating Results [1]	$ 13,411	$ 10,676	$ 16,365	$ 12,144	$ 14,409

Source: U.S. Bureau of Labor Statistics - CPI, Fiscal years 2004/05 to 2008/09 CAFR - Statement of Revenues, Expenditures & Changes in Fund Net Assest - Enterprise Funds

[1] Calculation: (Operating Losses + Depreciation)/CPI*1000

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

LIQUIDITY

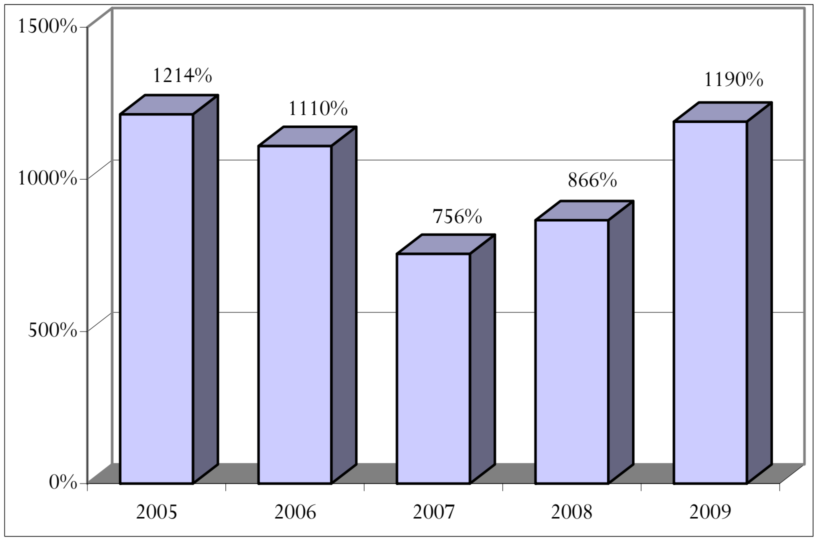
Description

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 was downward, which indicates that the Town was gradually using more of its cash on hand to meet the needs of the increasing population. Starting in 2007/08 and continuing through 2008/09 there is an increase in liquidity due to conservative spending. This conservative spending trend will continue throughout 2009/10 in response to the weakened economy. 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



Liquidity (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Cash and Investments	$ 15,533	$ 20,462	$ 21,567	$ 34,287	$ 24,665
Less Library Bond Proceeds	$ -	$ -	$ -	$ 13,023	$ 2,530
	$ 15,533	$ 20,462	$ 21,567	$ 21,264	$ 22,135
Current Liabilities- General Fund Only	$ 1,280	$ 1,844	$ 2,854	$ 2,455	$ 1,860
% Cash and Investments [1]	1214%	1110%	756%	866%	1190%

Source: Fiscal years 2004/05 to 2008/09 - CAFR Balance Sheet - Governmental Funds

[1] Calculation: Cash and Investments/Current Liabilities

Debt Structure

Debt structure is important because debt is an explicit expenditure obligation that must be satisfied when due. Debt can be an effective tool to finance capital improvements and to smooth out short-term revenue flows; however, its misuse can cause serious financial problems. Even a temporary inability to repay debt can result in a reduction of the Town's credit rating, increased borrowing costs and loss of autonomy to state and other regulatory bodies.

The Town's most common forms of long-term debt are Municipal Property Corporation (MPC), Certificates of Participation (COP), special assessment and revenue bonds. When the Town issues debt for capital projects, it must ensure that aggregate outstanding debt does not exceed the community's ability to pay debt service as measured by the property value or personal or business income.

Under the most favorable circumstances, the Town's debt should be proportionate in size and growth to the Town's tax base. It should not extend past the useful life of the facilities which it finances, be used to balance the operating budget, require repayment schedules that put excessive burdens on operating expenditures or be so high as to jeopardize the Town's credit rating.

Debt Structure

An examination of the Town's debt structure can reveal the following conditions:

- Inadequacies in cash management procedures.
- 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

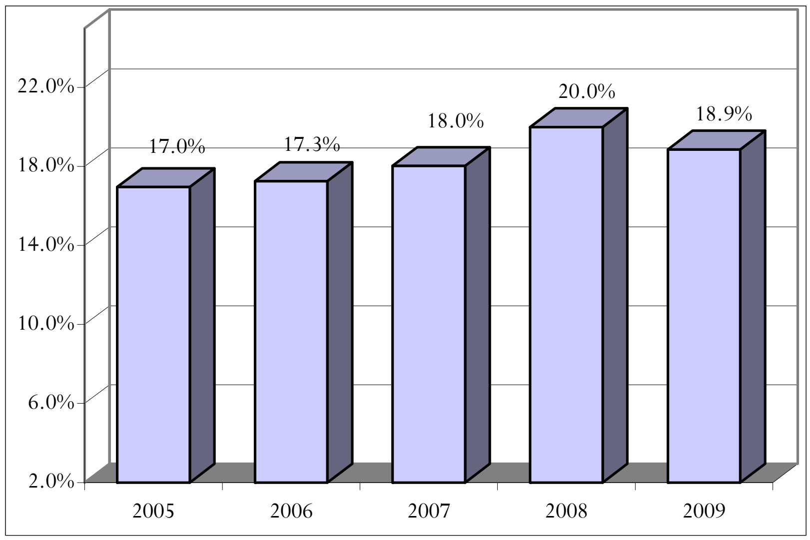
Description

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 (CFDs), 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 is considered a negative trend. According to credit industry benchmarks, the Town has exceeded the five percent threshold for the past five years, primarily due to increases in debt service principal and interest payments on long-term debt associated with the Municipal Property Corporation. FY 2008/09 saw a decrease in current liabilities from the prior year by $700K. This is primarily due to a decrease in accounts payable in the General Fund (amount fluctuates at any given time).

CURRENT LIABILITIES



Current Liabilities (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Current Liabilities	$ 4,470	$ 5,538	$ 6,338	$ 6,675	$ 5,956
Operating Revenues	$ 26,349	$ 32,077	$ 35,141	$ 33,367	$ 31,560
% Current Liabilities [1]	17.0%	17.3%	18.0%	20.0%	18.9%

Source: Fiscal years 2004/05 to 2008/09 - CAFR Statement of Net Assets - Governmental Activities
Fiscal years 2004/05 to 2008/09 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Governmental Funds
Fiscal years 2004/05 to 2008/09 CAFR - Notes Changes in Long-Term Liabilities
[1] Calculation: Current Liabilities/Operating Revenues

NET DIRECT DEBT PER CAPITA

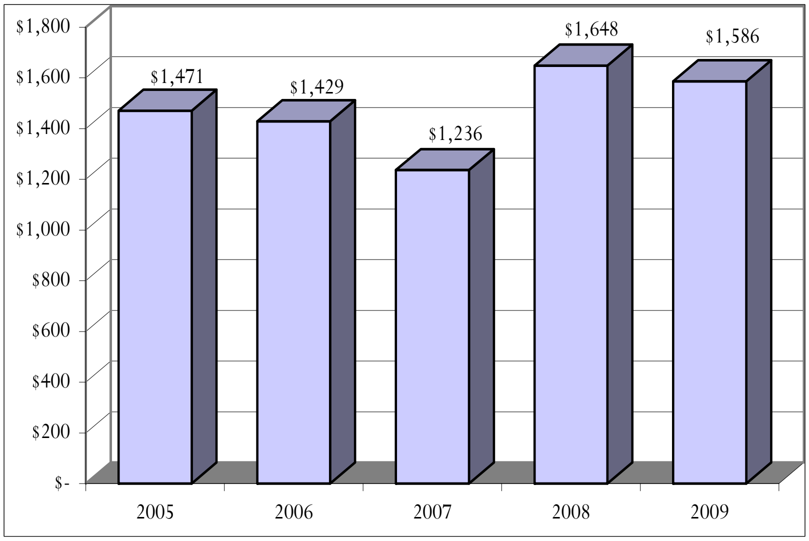
Description

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 (CFDs), only Town-obligated debt.

Analysis

Population has decreased 1% from the prior fiscal year, most likely due to the slowed economy, and can be expected to increase as the economy recovers. 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 MPC debt to acquire additional water supply. During fiscal year 2005/06, the Town's total bonded debt decreased by approximately $4.0 million, 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 was attributable to new debt being issued in the amount of $15.9 million in bonds for the public library construction. For fiscal year 2008/09, no new long-term debt was acquired and debt decreased due to scheduled principal payments. This calculation includes MPC, COP and Special Assessment debt and excludes Enterprise Fund bonded debt.

NET DIRECT DEBT PER CAPITA



Net Direct Debt Per Capita (in thousands - except population)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Net Direct Long-Term Debt	$ 49,380	$ 51,060	$ 47,425	$ 61,017	$ 58,003
Population	33,575	35,740	38,357	37,018	36,569
Net Direct Debt Per Capita [1]	$ 1,471	$ 1,429	$ 1,236	$ 1,648	$ 1,586

Source: Arizona Department of Economic Security, Fiscal years 2004/05 to 2008/09 CAFR - Notes Changes in Long-Term Liabilities

[1] 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

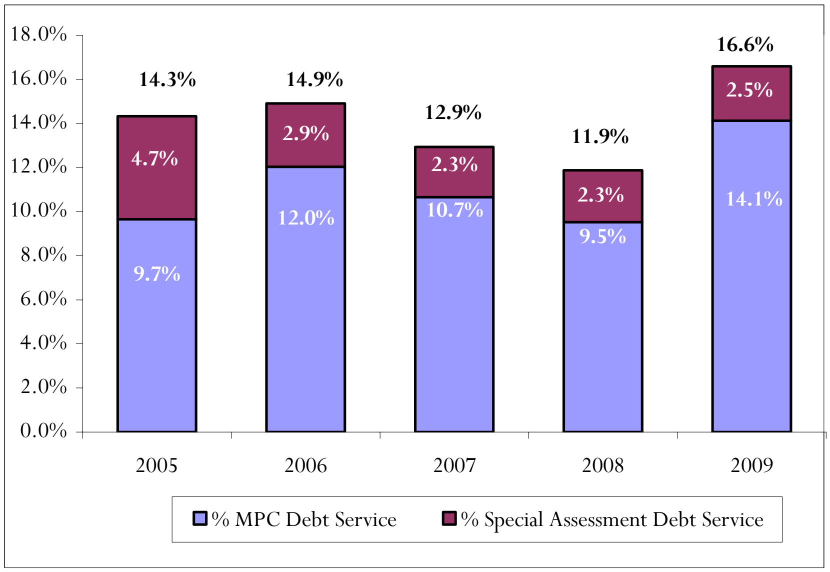
Description

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 Revenues 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. FY 2008/09 saw an increase of $1.3 million due to payments of bonds issued in 2007/08 associated with the library construction. According to the International City/County Management Association handbook, debt service on net direct debt exceeding 20% of operating revenues 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 revenues, so this rate is within limits.

DEBT SERVICE



Debt Service (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Governmental Debt Service	$ 3,776	$ 4,784	$ 4,545	$ 3,961	$ 5,238
Operating Revenues	$ 26,349	$ 32,077	$ 35,141	$ 33,367	$ 31,560
% Debt Service [1]	14.3%	14.9%	12.9%	11.9%	16.6%

Source: Fiscal years 2007/08 to 2008/09 CAFR - Combining Statement of Revenues, Expenditures and Changes in Fund Balances - Nonmajor Governmental Funds (Special Assessments)
Fiscal years 2004/05 to 2006/07 CAFR - Statement of Revenues, Expenditures and Changes in Fund Balances - Governmental Funds

[1] Calculation: Debt Service/Operating Revenues

Excise Tax

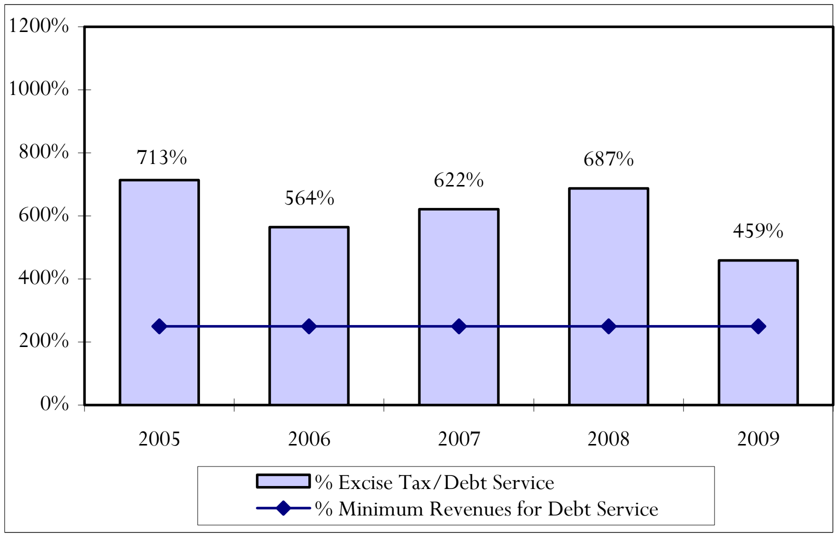
Description

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 revenues decreased 6% in FY 2007/08 and 6% in FY 2008/09 due primarily to reduced transaction privilege tax collections. In 2007/08 the percentage of excise tax with relation to MPC debt service increased, but had more to do with the 15% decrease in debt service, attributable to a reduction in principal and interest payments, than revenues. For FY 2008/09, the percentage of excise tax with relation to MPC debt service decreased, attributable to both a $1.4 million decrease in revenues and a $1.3 million increase in MPC debt service. Excise tax continues to exceed the minimum requirements of bond indentures which is two and one half times the debt service payments.

EXCISE TAX



Excise Tax (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Excise Tax	$ 18,144	$ 21,771	$ 23,274	$ 21,844	$ 20,446
MPC Debt Service	$ 2,543	$ 3,859	$ 3,743	$ 3,180	$ 4,458
% Excise Tax [1]	713%	564%	622%	687%	459%

Source: Town of Prescott Valley Financial Policies
Fiscal years 2005/06 to 2008/09 - Statement of Revenues, Expenditures and Changes in Fund Balances - Budget & Actual - GAAP Basis - General Fund and Streets Capital Improvement Fund

[1] Calculation: Excise Tax/Debt Service

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

OVERLAPPING DEBT

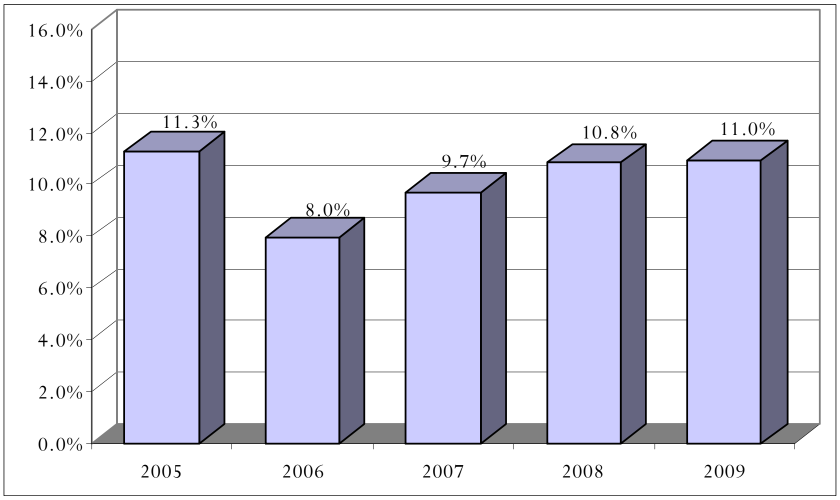
Description

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. Overlapping debt does not include Community Facilities Districts (CFDs).

Analysis

The overlapping net debt as a percent of assessed valuation decreased in fiscal year 2005/06 due to the increase in assessed valuation, even though net debt outstanding increased for Yavapai Community College (YCC). For fiscal year 2006/07, both YCC and Humboldt Unified School District (HUSD) increased their net debt outstanding considerably and this was offset by a sharp increase in assessed valuation. In 2007/08 the increase is due to HUSD increasing their debt by $21 million with no increase reported by YCC. For FY 2008/09 the assessed valuation remained fairly constant with the prior year. YCC decreased its net debt by $5 million while HUSD's net debt remained equal to the prior year. The assessed valuation for both YCC and HUSD decreased from the prior year and can be expected to maintain this trend for FY 2009/10.

OVERLAPPING DEBT



Overlapping Debt (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Long-Term					
Overlapping Debt	$ 24,652	$ 20,686	$ 31,990	$ 47,298	$ 45,721
Assessed Valuation	$ 218,003	$ 259,023	$ 330,513	$ 436,242	$ 417,511
% Overlapping Debt [1]	11.3%	8.0%	9.7%	10.8%	11.0%

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 2007/08 to 2008/09 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 year 2004/05 CAFR - Computation of Direct and Overlapping Debt - Table 12

[1] Calculation: Overlapping Debt/Assessed Valuation

Prescott Valley

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

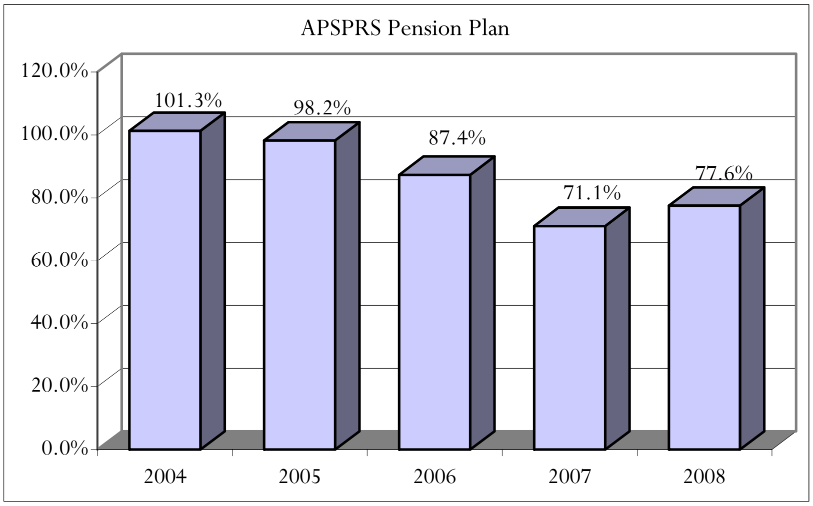
Description

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, 2009 was 13.45% of annual covered payroll and the Town's annual pension cost of $645,946 for APSPRS was equal to the Town's required and actual contributions.

Analysis

The decline below 100% of APSPRS benefits funded in total, starting in fiscal year 2004/05 and continuing into 2007/08 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 2004	FY 2005	FY 2006	FY 2007	FY 2008
Public Safety Retirement Plan (Police Employees)	101.3%	98.2%	87.4%	71.1%	77.6%

Source: Arizona Public Safety Personnel Retirement System report as of June 30, 2008
Fiscal years 2003/04 to 2008/09 CAFR - Pension Plan Obligation Note

Note: Arizona Public Safety Personnel Retirement System report as of June 30, 2009 was not available when this analysis was completed.

DEFINED CONTRIBUTION PLAN OBLIGATION NON-PUBLIC SAFETY

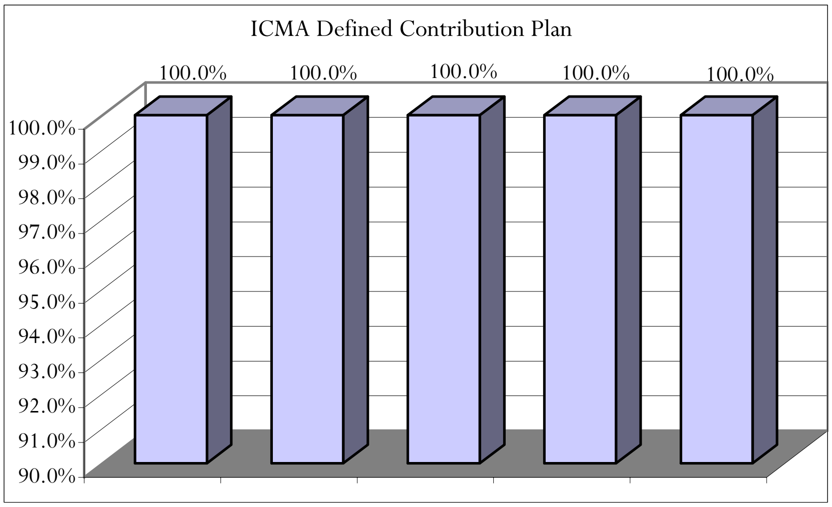
Description

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.

DEFINED CONTRIBUTION PLAN OBLIGATION NON-PUBLIC SAFETY



<u>Defined Contribution Obligation</u>

Percent of Defined Contributioı Obligation Funded	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
ICMA (Other Employees)	100.0%	100.0%	100.0%	100.0%	100.0%

Source: Fiscal years 2004/05 to 2008/09 CAFR - Pension Plan Obligation Note

Compensated Absences

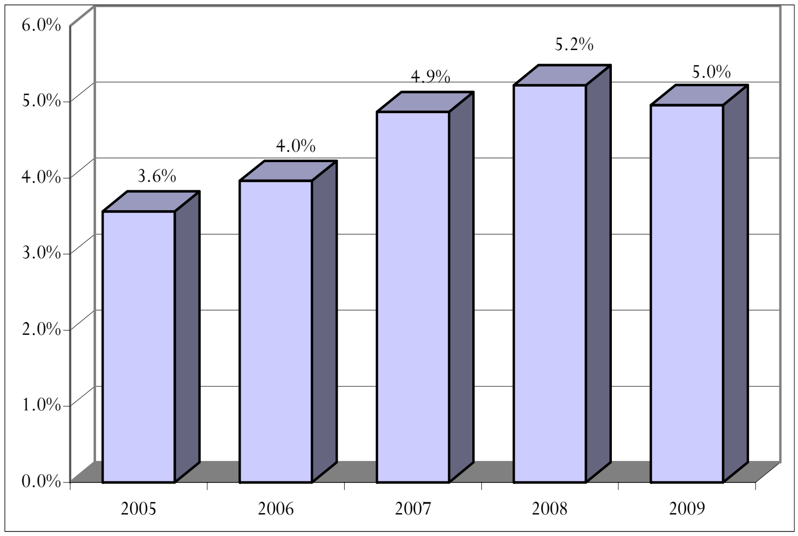
Description

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 five-year period. The trend had been increasing through 2007/08 due primarily to an increase in employment and long-term employees earning a higher accrual rate. In 2008/09 compensated absences decreased due to the effects of a hiring freeze implemented to reduce costs during the downturn in the economy.

COMPENSATED ABSENCES



Compensated Absences (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Compensated Absences	$ 711	$ 880	$ 1,082	$ 1,167	$ 1,179
Unreserved Fund Balance	$ 19,963	$ 22,198	$ 22,221	$ 22,361	$ 23,778
% Compensated Absences [1]	3.6%	4.0%	4.9%	5.2%	5.0%

Source: Fiscal years 2004/05 to 2008/09 CAFR - Notes Changes in Long-Term Liabilities
Fiscal years 2004/05 to 2008/09 CAFR - Balance Sheet - Governmental Funds - Total Unreserved (General Fund and HURF)

[1] 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

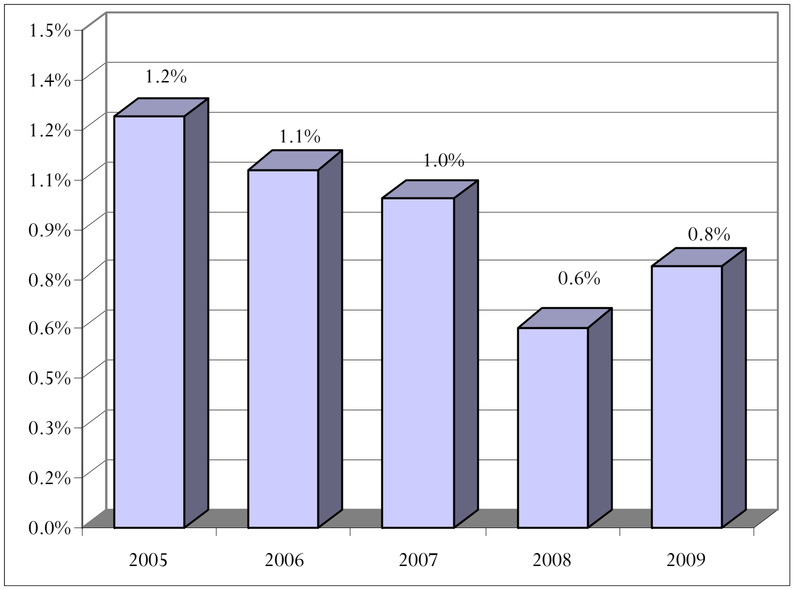
Description

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 increased slightly in 2008/09. The downward trend experienced in the prior years can be attributed to adding new building and building improvements for the Town. The Town replaces assets regularly as they break down or become obsolete. Building and improvements fixed asset acquisitions increased by 24% in the fiscal year 2007/08, but only added 2.6% in 2008/09. The slight increase in maintenance costs can be attributed to the lower additions for building and building improvements.

MAINTENANCE EFFORT



Maintenance Effort (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Maintenance Expenditures	$ 271	$ 253	$ 264	$ 200	$ 268
Building & Improvement Costs	$ 21,815	$ 23,398	$ 26,587	$ 33,025	$ 33,885
% Maintenance Expenditures [1]	1.2%	1.1%	1.0%	0.6%	0.8%

Source: Town of Prescott Valley Finance Division
Fiscal years 2004/05 to 2008/09 CAFR - Notes, Capital Assets Buildings and Improvements Other Than Buildings

[1] Calculation: Maintenance Expenditures/Building & Improvement Costs

DEPRECIATION EXPENSE

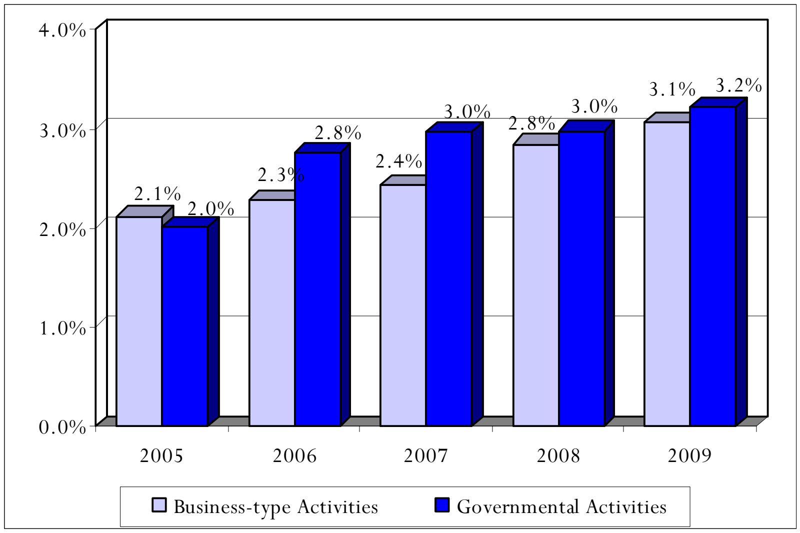
Description

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 costs, 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 rate of increase in fixed assets for 2008/09 was reduced and is attributable mainly to reduced capital spending due to the current economic conditions. Capital projects will be limited in the future until improved economic conditions and increased revenues are experienced by the Town.

DEPRECIATION EXPENSE



Depreciation Expense (in thousands)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Business-Type Activities					
Depreciation Expense	$ 2,236	$ 2,971	$ 3,468	$ 4,215	$ 4,648
Fixed Assets	$ 105,568	$ 130,243	$ 142,640	$ 148,084	$ 149,153
% Depreciation Expense [1]	2.1%	2.3%	2.4%	2.8%	3.1%
Governmental Activities					
Depreciation Expense	$ 2,838	$ 4,347	$ 5,270	$ 5,980	$ 6,708
Fixed Assets	$ 140,853	$ 157,937	$ 177,236	$ 200,717	$ 208,203
% Depreciation Expense [1]	2.0%	2.8%	3.0%	3.0%	3.2%

Sources: Fiscal years 2004/05 to 2008/09 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

[1] Calculation: Depreciation Expense/Fixed Assets

Note: With the implementation of Governmental Accounting Standards Board Statement

TOWN OF PRESCOTT VALLEY