

TOWN OF FOUNTAIN HILLS

TWENTY YEAR FINANCIAL OVERVIEW

June 14, 2005

(To be revised after completion of strategic plan December 2005)



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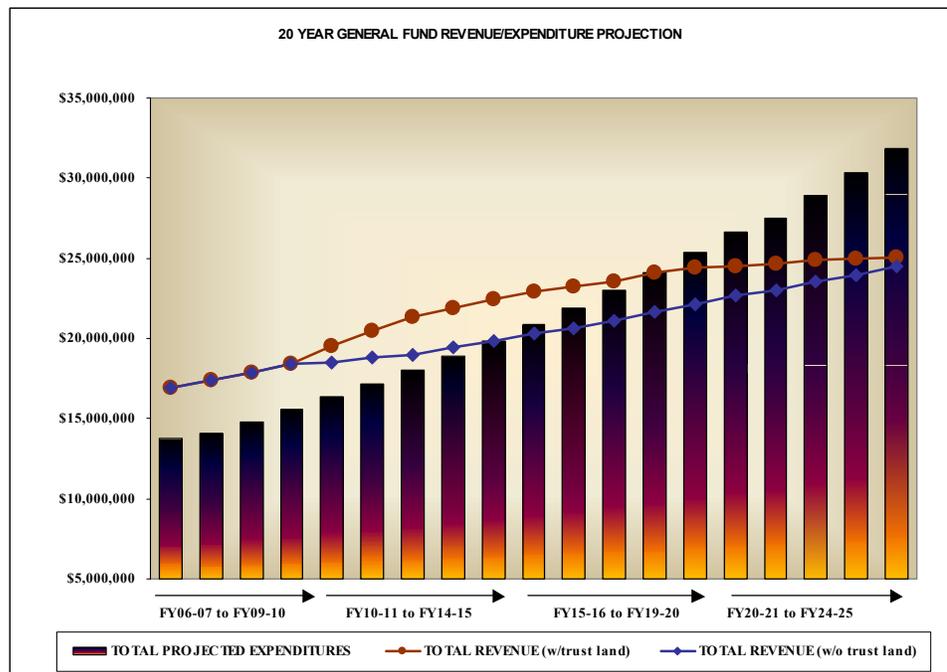
Fiscal Years 2006 - 2025

Introduction

Since incorporation the Town has enjoyed riding a wave of economic prosperity due to the explosive growth of the mid to late 1990's. The Town took advantage of the building boom and paved streets, built four new parks and a new Community Center/Library Museum, preserved 354 acres of open space, and provided many services to enhance the quality of life of the citizens of Fountain Hills. However, the ride ended with the economic slump of the early 2000's that has forced many cities and towns across the country to re-evaluate their financial future.

The financial future for Fountain Hills through FY2025 continues to be cautiously optimistic, with a heavy reliance on construction related revenues (construction sales tax, building permit fees) and state shared revenues. The projection for the next eight years provides sufficient resources to fund

the current level of ongoing operations without spending down the reserve balance but includes one-time revenue sources. The revenue projections are based on another five years of moderate growth in residential and commercial construction activity. However, by FY2013 the Town will have much less inventory of vacant land that



can generate sales tax revenue; additional revenue sources will need to be identified as construction revenue declines. Additionally, the projection assumes that Fountain Hills will lose share of state revenues to other surrounding communities that are experiencing explosive growth, beginning in FY2006-07 (the first year after the next mid-decade census).

Projects included in the CIP form the basis for appropriations in the annual budget and will affect the Town’s budget process ten to twenty years into the future. In order for the Town to prevent the deterioration of community infrastructure, continue to enhance the quality of life, and provide needed services to the citizens it is necessary for the government to identify the resources that will fund capital improvements each year. Finalization of the capital improvement plan will be completed through the strategic planning process.

Summary

Staff has prepared this report as part of an annual review process and as a blueprint for future capital budgeting and to assist residents to understand financial implications as part of the Town’s strategic plan. The plan is flexible to allow the public’s input through the strategic planning process, which may provide additional recommendations for other capital priorities or eliminate some projects. As the table below indicates if all proposed capital projects and the associated operating costs are approved, the cumulative shortfall is (\$59M) over the 20-year period including annexation of the state trust land.

SUMMARY OF CAPITAL PROJECT FINANCING

	FY06-10	FY11-15	FY16-20	FY21-25
	(in millions)			
Fund Balance Financing Potential	\$5.6	\$6.5	(\$4.7)	(\$33.7)
Surplus Revenues & Expenditures	\$12.3	\$5.3	(\$9.3)	(\$27.5)
ExciseTax Revenue	\$8.9	\$12.1	\$13.5	\$15.1
Development Fee Revenue	\$3.8	\$3.1	\$1.6	\$0.9
HURF Revenue	\$4.0	\$5.0	\$5.0	\$5.0
Less CIP Expenditures	(\$38.2)	(\$40.1)	(\$33.8)	(\$13.0)
Operating Cost increases from Capital Projects	(\$0.3)	(\$2.3)	(\$5.6)	(\$6.1)
CIP Funding Deficit including State Land	(\$3.9)	(\$10.3)	(\$33.3)	(\$59.3)
Remove State Land Revenue/Project	\$0.0	(\$10.1)	\$8.6	(\$6.3)
CIP Funding Deficit without State Land	(\$3.9)	(\$20.4)	(\$24.7)	(\$65.7)

What are Capital Improvements?

Capital improvements are the “bricks and mortar” of the Town – streets, dams, bridges, parks and parks buildings, one-time acquisitions of equipment over \$10,000, including municipal facilities such as the new Town Hall. Projects in the CIP generally cost more than \$10,000 and have a projected minimum life span of five (5) years.

Financial Plan

A financial trend analysis 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. The challenge is for the Town to absorb, within

available financial resources, increasing operational costs associated with an ever-increasing population but also include funding for capital projects.

Projecting revenues and expenditures over a twenty-year period is part science and part art – the further out the projection, the less reliable the estimate.

The revenue forecast assumes the following:

- The local sales tax rate remains at 2.6% over the twenty year period
- Future year revenue forecasts are based on statistical analysis and historical trends, taking into account a drop in revenue sharing from decreased population growth
- Revenues are based on “most likely” scenario
- The legislature will not reduce or eliminate state revenue sharing
- The residential and commercial activity will continue at a moderate pace until buildout
- Reserved fund balance is excluded as available resources
- One time revenues (construction related) are included as available resources
- The development fees are projected using the current rate

The projection of operating expenditures over the next twenty years assumes the following:

- An average inflation factor of 5% for each fiscal year
- No increase in level of services for FY2006 through FY2025
- The Target tax rebate is eliminated in FY07-08
- The forecast does not incorporate unanticipated policy changes or adjustments in spending priorities
- The capital project figures are based on current dollars
- Community Center bond payments are eliminated in FY20-21
- One time costs incurred in FY05-06 are removed before applying inflation factor

Many capital improvements and purchases of large pieces of equipment will be included in the operating budget on a “pay-as-you-go” basis. In our analysis recurring large equipment replacement expenses for new heavy equipment, street sweepers, and continuing costs such as street asphalt overlay are included in the capital projects budget. The operating budget is for costs associated with providing ongoing services such as police and fire protection, building inspection, parks and recreation activities, and street maintenance. Ongoing costs are tied to ongoing revenues (i.e., sales tax, user fees, intergovernmental revenues).

This first draft of the capital improvement plan includes costs for long-term capital projects, which add to the capital assets or infrastructure of the Town. These include new facilities, land, major infrastructure improvements on streets, etc. and include prioritization of which projects will be decided as part of the strategic plan process. Almost all potential projects include options from the first Town Hall are included in this report. The projects are usually financed on a long-term basis with revenue sources such as development fees, grants and intergovernmental sources. The Town has adopted a policy that considers pay-as-you-go financing to be the primary source of funding capital projects when possible.

Financial and planning considerations help staff identify projects that should be included in the annual CIP, and how those projects will be integrated into the Town’s annual budgeting process. Capital projects should support Council goals and the strategic plan objectives and be consistent with the Town’s General Plan. It should also prevent the deterioration of the Town’s existing infrastructure and protect its investment in parks, streets, and municipal buildings. Capital projects should provide all geographic areas of the Town with comparable quality and types of services.

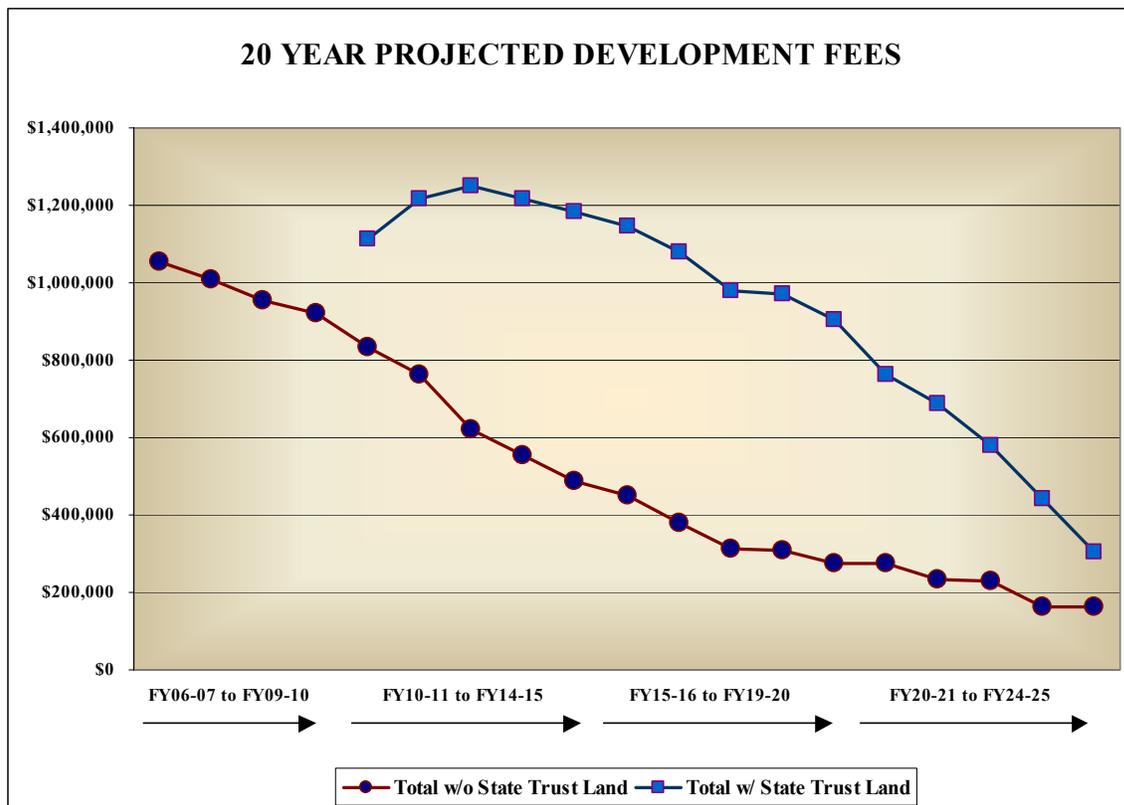
Financial Resources

In the past, operating revenue has been used to fund one-time projects, such as the Community Center. In the future, this revenue source will be in the form of a cash transfer from the General Fund of any surplus over operating costs to the Capital Projects fund for future projects.

The Excise Taxes (Local Sales Tax) are primarily used for general operating costs (2.2%). However, the remaining .4% is dedicated to specific purposes:

- Mountain bond debt payment (.2%)
- Civic center bond debt payment (.1%)
- Downtown development costs (.1%)

Development fees are collected from construction permits and are limited to specific projects for which they were created. These funds are categorized as General Government, Streets, Parks & Recreation, Law Enforcement and Open Space. The chart below highlights the decline in building permit activity over the next twenty years.



Bonds are issued in several forms. State law requires voters to authorize general obligation and revenue bonds by election. State law also authorizes other forms of debt to be issued without voter approval. These alternate financing sources include Municipal Property Corporation (MPC) bonds.

Grants are available for various types of projects through different sources and governmental agencies. If capital grants are included in the budget as a funding source, the project will not proceed until the grant is awarded. A grant-funded project may also require Town matching funds, which should also be clearly stated in the project description.

The twenty-year financial summary below (20 Year Capital Improvement Plan Resources and Expenses) summarizes the financing potential available, sources of revenue, proposed capital projects and the remaining capital projects balance (which is cumulative). Available HURF (Highway User Revenue Fund) resources are based on the average expenditures for major road maintenance within the streets budget.

	FY06-10	FY11-15	FY16-20	FY21-25
<u>General Fund</u>				
Gen Govt Capital Financing Potential from Fund Balance	\$2.8	\$0.0	\$4.1	(\$8.8)
Remaining Capital Projects Balance	\$0.0	\$4.1	(\$8.8)	(\$36.7)
Add State Trust Land Revenue	\$0.0	\$10.1	\$12.4	\$6.3
New Capital Projects Balance	\$0.0	\$14.2	\$3.6	(\$30.4)
<u>Excise Tax Fund</u>				
Mountain Bonds Fin Potential	\$0.1	\$1.0	\$2.2	\$7.5
Remaining Balance	\$1.0	\$2.2	\$7.5	\$13.7
Civic Center Bonds Fin Potential	\$0.2	\$0.3	\$0.7	\$1.6
Remaining Balance	\$0.3	\$0.7	\$1.6	\$4.7
Downtown Development Fin Potential	\$0.5	\$0.5	\$2.9	\$5.6
Remaining Capital Projects Balance	\$0.5	\$2.9	\$5.6	\$8.7
<u>Development Fees</u>				
Parks & Rec Financing Potential	\$0.5	\$0.0	(\$19.4)	(\$37.9)
Remaining Capital Projects Balance	\$0.0	(\$19.4)	(\$37.9)	(\$37.6)
Open Space Financing Potential	\$1.5	\$0.3	\$0.5	\$1.1
Remaining Capital Projects Balance	\$0.3	\$0.5	\$1.1	\$1.4
<u>Streets and Highways (HURF)</u>				
Street Capital Financing Potential	\$0.0	(\$5.8)	(\$8.1)	(\$9.1)
Remaining Capital Projects Balance	(\$5.8)	(\$8.1)	(\$9.1)	(\$13.8)
TOTAL	(\$3.6)	(\$7.0)	(\$27.7)	(\$53.2)

As the Town approaches buildout the available resources from construction related activity will begin to decline in FY08-09 with a deficit projected for FY14-15. If the state trust land is annexed into Fountain Hills the Town construction related revenue will prolong the deficit until FY18-19. The mountain bond payments will be eliminated in FY16-17 and Civic Center bond

payments will be eliminated in FY19-20. These bond payments are funded from local sales tax revenues that were dedicated by the Council for this specific purpose.

Improving The Long Term Financial Picture

The following options to improve the scenario above will be presented for consideration following adoption of the strategic plan:

1. Eliminate major capital projects - this solution, although easily accomplished, would have a cumulative negative impact on the Town infrastructure. This could create a significant future financial burden for Fountain Hills' citizens as well as increased liability with insufficient maintenance. Fountain Hills has a reputation of one of the "World's Ten Best Places to Live" and that should be valued. Prioritizing capital projects will be determined during the strategic plan process.
2. A review of the current development fee structure is being performed to align the cost of the capital projects with the resources. This will be repeated every five years.
3. Revenue enhancements – additional sources of revenue (other than issuing debt) are a primary property tax, liquor license permit fees, updating the planning and zoning fees, revising the license fees, etc.

Once the strategic plan is adopted, this report will be updated to reflect the citizen's priorities and long-term solutions will need to be considered at that time. Council approval of this 20-year financial and capital improvement plan at that time does not appropriate the proposed capital projects; however, the plan does demonstrate to the public the Town's commitment to financial planning for the future.