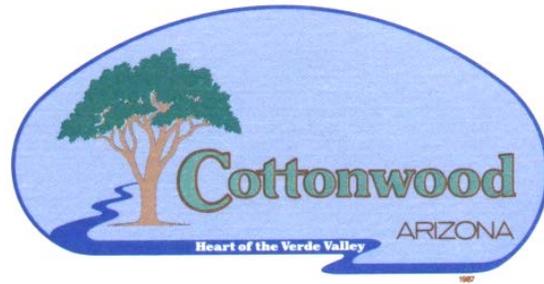


FY 2013 2nd Quarter Financial Report



City of Cottonwood

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City of Cottonwood
Fiscal Year 2013 – 2nd Quarter Report
For the period ending December 31, 2012

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EXECUTIVE SUMMARY

This is the City of Cottonwood quarterly summary of the financial activity for its major operating funds. It is reflective of activity through the period ending December 31, 2012 and it should be noted that the information presented within this document is unaudited. This report is presented only to be a guide to the fiscal health of the City of Cottonwood.

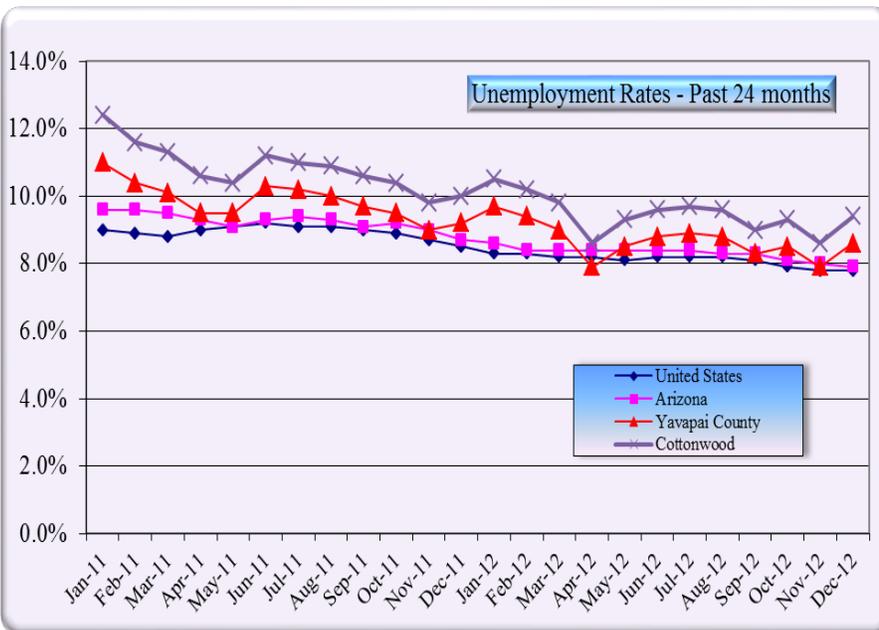
This report follows previous quarterly reporting format for consistency and easy reading. It contains a brief description of each of the City's major revenue sources and expenditure data by fund. A brief analysis of each is also presented, highlighting any issues or concerns. The executive section contains broad general data that affects the overall community.

Unemployment Data:

As we finish out the calendar year we can see in the chart to the right that the U.S. unemployment rate¹ has declined from the last quarter and has remained around the 7.8% mark. The State of Arizona² rate has also declined slightly to 7.9% from last quarter's 8.4%. Compared to this time last year the declines have been .7% and .8% for the U.S and Arizona, respectively.

Yavapai County³ on the other hand has seen its unemployment number increase to 8.6% from last quarter's 8.3%. The City of Cottonwood as also seen an increase in its numbers from last quarter's 9.0% to 9.4%. On the bright side of these unemployment numbers are both the county and the city are down .6% from last year at this time.

Monthly	United States	Arizona	Yavapai County	Cottonwood
Jan-11	9.0%	9.6%	11.0%	12.4%
Feb-11	8.9%	9.6%	10.4%	11.6%
Mar-11	8.8%	9.5%	10.1%	11.3%
Apr-11	9.0%	9.3%	9.5%	10.6%
May-11	9.1%	9.1%	9.5%	10.4%
Jun-11	9.2%	9.3%	10.3%	11.2%
Jul-11	9.1%	9.4%	10.2%	11.0%
Aug-11	9.1%	9.3%	10.0%	10.9%
Sep-11	9.0%	9.1%	9.7%	10.6%
Oct-11	8.9%	9.2%	9.5%	10.4%
Nov-11	8.7%	9.0%	9.0%	9.8%
Dec-11	8.5%	8.7%	9.2%	10.0%
Jan-12	8.3%	8.6%	9.7%	10.5%
Feb-12	8.3%	8.4%	9.4%	10.2%
Mar-12	8.2%	8.4%	9.0%	9.8%
Apr-12	8.2%	8.4%	7.9%	8.6%
May-12	8.1%	8.4%	8.5%	9.3%
Jun-12	8.2%	8.4%	8.8%	9.6%
Jul-12	8.2%	8.4%	8.9%	9.7%
Aug-12	8.2%	8.3%	8.8%	9.6%
Sep-12	8.1%	8.3%	8.3%	9.0%
Oct-12	7.9%	8.1%	8.5%	9.3%
Nov-12	7.8%	8.0%	7.9%	8.6%
Dec-12	7.8%	7.9%	8.6%	9.4%



The graph to the left shows that there have been some overall improvements in the unemployment numbers over the past 24 months. There is still, however, some uneasiness with the fluctuations in the overall unemployment statistics despite the improvements of the past few years.

When we look at the chart and the graph, however, it becomes obvious that the most improvement has been to our local economy with Cottonwood having a full 3% decline in unemployment over the past 24 month.

¹ United States - <http://data.bls.gov/pdq/SurveyOutputServlet>

² Arizona - http://data.bls.gov/PDQ/servlet/SurveyOutputServlet?data_tool=latest_numbers&series_id=LASST04000003

³ Yavapai County - <http://www.workforce.az.gov/pubs/labor/countylaus10+.pdf>

	Consolidated	
	Budget	2nd Qtr Actual
Revenues	\$29,157,525	\$13,034,114
Operating Expenditures	26,821,610	11,325,706
Capital Outlay	18,366,170	2,995,592
Debt Service	4,576,085	2,287,512
Revenues over (under) Expenditures	(20,606,340)	(3,574,696)
Other Funding Sources & Uses	4,261,015	(224,383)
Revenues & other funding sources & uses over (under) Expenditures	(16,345,325)	(3,799,079)
Beginning Fund Balance	21,182,709	21,182,709
Ending Fund Balance	\$4,837,384	\$17,383,630

The current fiscal situation of the City of Cottonwood is still relatively stable despite the slowly improving local economy. Much of credit for this goes to both the early increase in sales tax of 0.08¢, as well as our frugal city employees for their attention to departmental costs.

As you can see by the consolidated chart at the left, we are starting the fiscal year in moderately good overall shape. We will cover the condition of the other funds later in this document, some of which are still struggling and will require some careful monitoring.

The current operating revenues, though improving, are still not at the levels we would like to see. We are lacking some grant funding that may or may not come fruition. We do anticipate continued improvement in our revenues as the year progresses.

Operating expenditures are slightly below target as we complete the second fiscal quarter due to the city's conservative views on spending along with capital and grant projects that are currently in the works and not yet being expended. The conservation outlook is refreshing and we are expecting continued cost reductions for the remainder of the fiscal year.

As for capital equipment, most of the budgeted items are staggered throughout the fiscal year so as not to strain the different funds or create cash flow problems. Most of the capital outlay will be used before fiscal year end.

GENERAL FUND

As we complete the second fiscal quarter, the General Fund continues to struggle with a slowly improving local economy. The overall operating revenues were 5.3% below projections. This is 0.6% less than the previous quarter of 4.7%. Most of the shortages were due to grants, and lease financing not coming to fruition at this time. This is not uncommon and seems to happen every year because the City of Cottonwood budgets for any potential grant opportunity, as well as annual financing opportunities. These are a one-time revenue and not continuous throughout the year. Also realizing that if the grants do not come through, the expenditures associated with those grant will also not be occurring.

The City of Cottonwood has budgeted a use of about \$2.9M in reserves, however, with cost containment measures in place and some projects not started or completed during the fiscal year; the use of reserves will be limited.

	General Fund	
	Budget	2nd Qtr Actual
Revenues	\$16,408,310	\$7,348,997
Operating Expenditures	16,204,380	6,758,995
Capital Outlay	1,816,360	335,748
Debt Service	0	0
Revenues over (under) Expenditures	(1,612,430)	254,254
Other Funding Sources & Uses	(1,289,675)	(546,753)
Revenues & other funding sources & uses over (under) Expenditures	(2,902,105)	(292,499)
Beginning Fund Balance	6,426,945	6,426,945
Ending Fund Balance	\$3,524,840	\$6,134,446



Local sales tax:

This is the General Fund’s major source of funds at roughly over 52% of its regular operating revenue. The city monitors this revenue very closely for changes both positive and negative.

At the end of the second fiscal quarter our local sales tax up by 5.6% over last fiscal year for the same period. The City of Cottonwood is trending at about where we should be to hit our budgeted estimate of \$10.8M for the year. Currently we are at the highest ever for this period in time. Though this sounds like we are doing great, we need to be cognizant of the fact that the City losses in revenue have been substantial over the past five years. Local sales tax alone lost over \$3M in potential revenues.

Though increases are small it is a welcome change from past years and we are confident that improvement in our sales tax base will continue into the foreseeable future. The city’s General Fund continues to be in good shape due to the shift of all sales tax from other funds to the General Fund in order to keep it stable. As we enter the FY 2014 budget process we will endeavor to shift sales tax back to other funds over the next few years in order to replenish capital reserves and improve our financial position.

State Shared Sales Tax:

This revenue is sales tax collected by the state and distributed to all the incorporated communities based on the relationship of the local population to the total population of all incorporated cities & towns in the state. The State Shared Sales tax is currently coming in at about FY 2008 levels, which is an improvement from previous reports.

As a reminder; during these past hard economic times the city used much of its reserves to support the local economy by keeping construction jobs moving. The City also maintained or improved public



safety, protection of the environment through its conservation programs, and the overall quality of life of its citizens. Our continued success in managing our past, current and future fiscal matters is to the credit of our citizen’s support and the City personnel, who have taken on additional responsibilities, all the while core services have not deteriorate and recreational programming was immaterially affected.

SPECIAL REVENUE FUNDS

The Special Revenues Funds include the Highway User Revenue Fund (HURF) or Streets Fund, the Library Fund, Cemetery Fund, Airport Fund, and Grants Fund. Overall the Special Revenue Funds are performing as expected. Most of these funds are supported by the General Fund through transfers in. The HURF being the largest of the Special Revenue Funds, is the one we will concentrate on in these reports unless there is something of concern in the other funds.

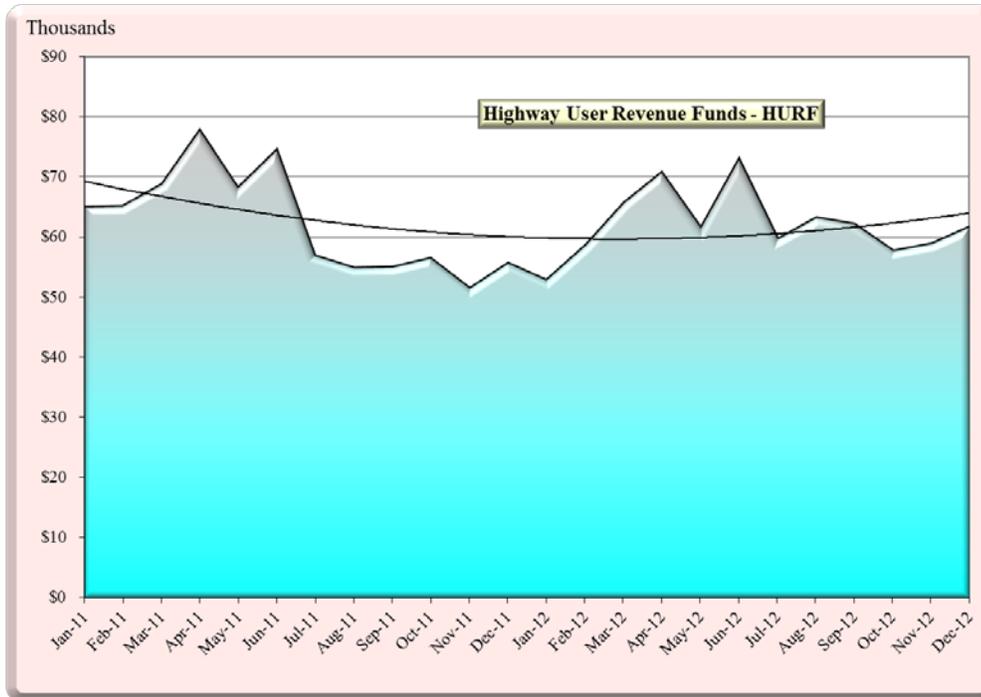
HURF Revenues:

HURF⁴ revenues are about at FY 2002 levels for the same period. Much of what is happening to this fund is due to the legislature, as it continues to take state HURF to support the Arizona Department of Public Safety and the Arizona Motor Vehicle Division. As you can see not much has changed recently.

This revenue has declined nearly 24.6% since 2007. Much of the loss is related to the state and its fiscal problems.

	Consolidated	
	Budget	2nd Qtr Actual
Revenues	\$2,402,700	\$546,670
Operating Expenditures	2,038,200	967,443
Capital Outlay	5,914,190	1,001,713
Debt Service	0	0
Revenues over (under) Expenditures	(5,549,690)	(1,422,486)
Other Funding Sources & Uses	5,550,690	361,448
Revenues & other funding sources & uses over (under) Expenditures	1,000	(1,061,037)
Beginning Fund Balance	(213,060)	(213,060)
Ending Fund Balance	(\$212,060)	(\$1,274,097)

Operating expenditures were at 52.5.0%, which is nearly 3% above where they should be at this time of year. Materials costs such as culverts, asphalt, and street signs are the main driver of this higher than normal trend. We will monitor this closely but we expect it to level out over the year.



Costs are mounting quickly as the West Mingus Avenue from Willard Street to SR 89A reconstruction project as it is nearing completion. As of the close of December this project is at \$910,218. Another project that has been in the works for some time is the 12th Street project from Fir St. to SR89A. Both these project are multimillion dollar projects and will more likely be financed through a bond or a Greater Arizona Development Authority (GADA) Loan.

The CAT/LYNX system is currently running about 6% below budget for this fiscal year. The Library is running about 4% below projections at the close of the 2nd fiscal quarter. All other special revenue funds are relatively small and subsidized by the General Fund. There are no significant items to report at this time.

⁴ The HURF funds streets maintenance, street construction.

CAPITAL PROJECTS

	Capital Improvements	
	Budget	2nd Qtr Actual
Revenues	\$475,000	\$93,659
Operating Expenditures	0	0
Capital Outlay	1,916,655	280,192
Debt Service	0	
Revenues over (under) Expenditures	(1,441,655)	(186,533)
Other Funding Sources & Uses	(3,600,000)	0
Revenues & other funding sources & uses over (under) Expenditures	(5,041,655)	(186,533)
Beginning Fund Balance	13,602,200	13,602,200
Ending Fund Balance	\$8,560,545	\$13,415,667

This fund continues to be in relatively good fiscal shape; however, this fund will be tapped into heavily over the past five years as the City has aggressively move forward with parking and street projects throughout the community. The City of Cottonwood continues to push large sums of monies into the local economy to keep local contractors working and construction projects moving forward.

Over the past five years it has been the City's priority to use these accumulated funds to assist in supporting the local economy. This support comes in the form of keeping construction jobs and trying to keep unemployment in the construction sector from climbing as it waits for the local and state economic base to improve. At the same time it is taking care of much need projects that need to be addressed.

The remaining reserves in this fund are anticipated to pay for the Wastewater Reclamation Facility at Riverfront Park, which will provide much needed reclaimed water to the area sport fields. It will also provide some of the financial support for a future City Hall and a Communications Center while a financing package can be arranged.

It should be noted that in the near future, the City of Cottonwood will need to replenish these reserves for potential needs just as it has in the recent past. As a note, the current Capital Improvements Fund was accumulated from excess 1% sales tax over nearly two decades.

Below are the major projects funded by these reserves for this fiscal year. Some of these costs are remaining from previous year's project, others are projects that are on the drawing board and are planned to begin construction later this fiscal year. Any projects that are not completed by year end will be rolled over into next fiscal year via the budget process.

	Adopted Budget		
		Y-T-D	% Used
Capital outlay:			
Investment Expenses		2,507	0.00%
Railroad Wash	225,000	0	0.00%
Capital Projects		671	0.00%
Architecture - City Hall	100,000	7,200	7.20%
Old Town Jail Remodel	5,000	24,898	497.96%
Old Court Bldg Remodel	60,000	3,610	6.02%
Old Town Parking & Rear Utility	144,555	134,604	93.12%
Riverfront Park Ramada Parking	108,600	81,912	75.43%
Fire Station 2 (GADA) Design	120,000	0	0.00%
Portal Signs COC		6	0.00%
Gardner Bldg Demo	55,000	0	0.00%
Rec Center Solar	598,500	16,824	2.81%
Communications Architecture	500,000	7,962	1.59%
Total Expenditures	1,916,655	280,192	14.62%

ENTERPRISE FUNDS

Both these funds were programmed to use some of their reserves during the course of the 2013 fiscal year. As you can see we are heavily depending on our reserves to make it through the fiscal year.

It is not uncommon for the wastewater system to take a loss since it has not raised rates for over a decade. The water system has also used some reserves despite showing some

improvement in its cash flow due to a rate increase in 2011. Unfortunately, its debt service coverage has dropped. The debt services coverage has become an issue with our bond holders who have stated a concern with the lack of rate increases to address the bond covenants.

Both these systems continue to be behind on their revenue generation. These funds are in need of a rate adjustment to compensate for the lack of rate increases, the effects of conservation and increasing costs to maintain the current level of service.

The city staff, along with some City Council members, and citizens from within the city limits and outside the city limits have resumed their meetings in preparation for an in-house rate study and possible adjustment.

	Enterprise Funds			
	Wastewater		Water	
	Budget	2nd Qtr Actual	Budget	2nd Qtr Actual
Revenues	1,341,905	673,277	\$6,390,085	\$3,302,173
Operating Expenditures	1,758,710	793,565	6,784,820	1,683,213
Capital Outlay	4,858,565	510,355	3,860,400	867,584
Debt Service	0	0	2,502,050	1,251,024
Revenues over (under)				
Expenditures	(5,275,370)	(630,644)	(6,757,185)	(499,647)
Other Funding Sources & Uses	3,600,000	0	0	0
Revenues & other funding sources & uses over (under)				
Expenditures	(\$1,675,370)	(\$630,644)	(\$6,757,185)	(\$499,647)

DEBT SERVICE FUNDS

	Debt Service	
	Budget	2nd Qtr Actual
Revenues	\$2,073,225	\$1,034,626
Operating Expenditures		1,036,488
Capital Outlay		
Debt Service	2,074,035	1,036,488
Revenues over (under)		
Expenditures	(810)	(1,038,349)
Other Funding Sources & Uses	0	0
Revenues & other funding sources & uses over (under)		
Expenditures	(810)	(1,861)
Beginning Fund Balance	1,237,020	1,237,020
Ending Fund Balance	\$1,236,210	\$1,235,159

This fund begins the year in good shape; with some sales taxes and a little interest income providing all of the revenues for this fund. Expenditures consist of principal and interest on loans and bond issues. Also included are any trustee fees assessed for managing the Debt Service Accounts.

As of June 1, 2008 the payment for the Recreation Center Bonds were transferred to the Debt Service accounts on recommendation from our independent auditors. The debt service for the Recreation Center is solely funded by sales tax revenues.

Currently, all water debt service is funded through user fees and other operational revenues, and therefore the debt service for the water utility is reflected in the enterprise fund.

This fund usually remains in very good shape.

BRIEF OVERVIEW

As we complete the first half of fiscal year 2013 we are seeing steady signs of improvement in our local economy. We are confident that the local economy will continue to strengthen, and we remain optimistic in our future planning. The City continues with its traditional fiscally conservative way of doing their everyday business. We are looking for ways to reduce costs, provide quality essential services, and protect staff. Cottonwood shall continue to maintain reasonable reserves for unforeseeable emergencies as is sensible.

The City will slowly begin to replenish its reserves in preparation for future downturns as well as improvement to its fiscal position.