



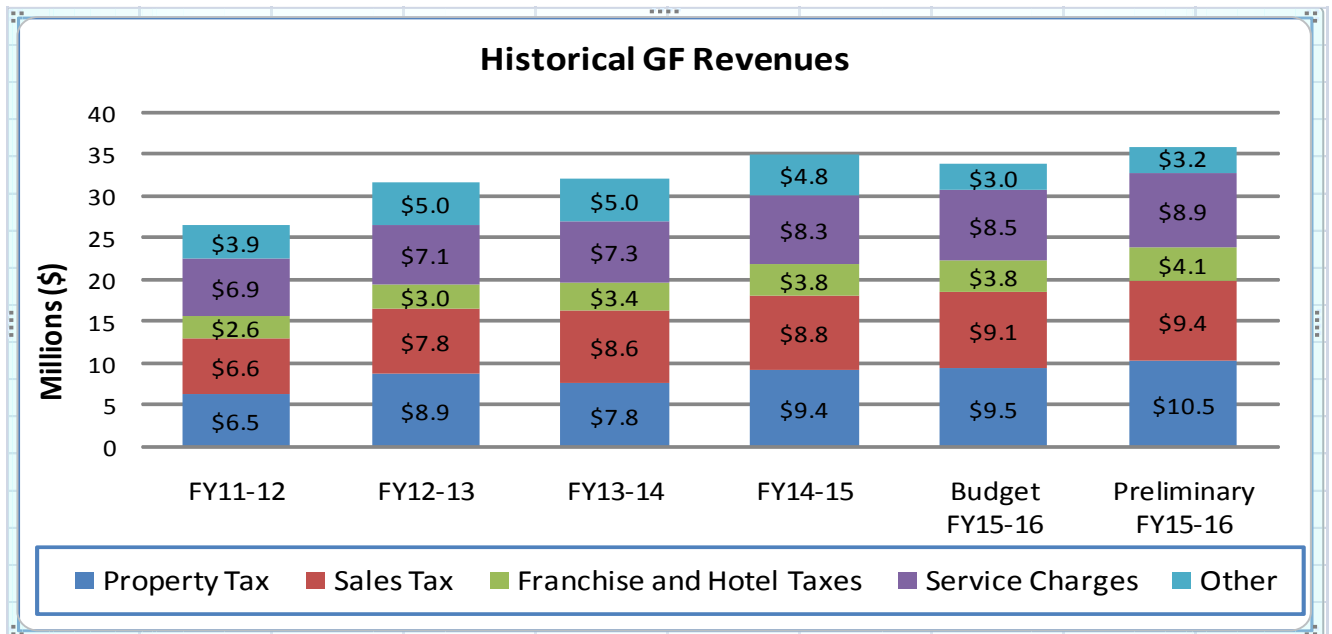
**CITY OF MORGAN HILL, CALIFORNIA
FINANCIAL STATEMENT ANALYSIS - FISCAL YEAR 2015-16 UNAUDITED
FOR THE MONTH ENDED JUNE 2016 – 100% OF YEAR COMPLETE**

- General Fund** – The preliminary total revenues for the fiscal year exceeded the adopted budget by approximately \$2.1 million. The biggest contributors for the increase came from all four major revenue categories: property tax, sales tax, recreation services, and Transient Occupancy Tax (TOT). Property tax, excluding property transfer tax, received for the fiscal year is approximately \$10.0 million, exceeded the budgeted amount by approximately \$1.0 million, and is 7% or about \$674,000 more than prior fiscal year. The increase is primarily due to new housing units and restoration of Prop 8 temporary reduction. Sales tax, including public safety sales tax received for the fiscal year is approximately \$9.4 million, an all-time high for the city, and is 7% or about \$647,000 more than last fiscal year.

The small category of business licenses has exceeded the budgeted amount at \$190,756 for the fiscal year. Business license renewal payments are usually received in July. Franchise tax revenue totaled approximately \$1.8 million or 8% higher than last fiscal year.

For the TOT (hotel tax), the amount received through twelve months ended June 30, 2016 exceeds budgeted amount by approximately \$292,000, also an all-time high for the city, and is 11% above the amount received last fiscal year. With no new capacity having been built in the City in recent years, the hotel tax revenue surge by definition is due to a combination of increased room rates and increased occupancy levels.

The chart below shows historical General Fund revenues by major revenue category from FY11-12 through FY14-15 Actual, FY15-16 Budget, and Preliminary FY15-16 Actual.



Preliminary year end General Fund expenditures and encumbrances came in under budget, totaling 94% of budgeted appropriations.

- Community Services** - The Community Services Department’s recreation operations, as reflected in the schedule presented on page 4 of the Monthly Financial and Investments Reports, shows a minimal impact to the General Fund of approximately \$18,000 for the year. The amount is much better than the budgeted net impact to the general fund of approximately \$733,000, primarily due to



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the increases in the number of members and the higher membership fee implemented in January 2015 coupled with conservative spending. Any net impact from the recreation operations at the end of the fiscal year increases (decreases) reserves in the General Fund.

Due to longstanding governmental accounting and budgeting convention, the City's recreation operations are not charged for indirect costs (known in Morgan Hill as "General Fund Administration") from the central services departments of City Attorney, City Manager, and Administrative Services. The City's other governmental funds, such as Community Development, and the proprietary funds, such as Water and Wastewater, and the Information Services Fund, are assessed such charges through the City's indirect cost allocation plan, prepared in compliance with the Federal government's OMB Circular No. A-87, which mandates certain calculation and cost allocation practices that must be followed in order to qualify for Federal grant funding, but which also represent best practice for non-grant funded City operations like utilities and information services.

- **Community Development Fund** – Preliminary revenues for the fiscal year totaled \$4.0 million, a decrease of 18% or approximately \$909,000 from the prior fiscal year partially due to lower contractual services revenue. Expenditures and encumbrances totaled \$5.2 million or approximately 92% of budgeted appropriation. Without the outstanding encumbrances, however, expenditures for the fiscal year amounted to \$4.9 million versus \$4.6 million in prior fiscal year primarily due to large ticket items undertaken such as the General Plan Update and purchase and implementation of the new permitting system, TRAKiT. The fund ended the fiscal year with an operating deficit of approximately \$0.9 million and a fund balance of approximately \$2.6 million or 48% of adopted FY16-17 appropriation, including carry-over encumbrances. Though it is still in excess of the Council's 30% reserve level policy, the fund is forecasted to continue to be structurally imbalanced requiring significant use of reserves in subsequent years. To address this issue, the Community Development Department is in the process of completing an updated fee study with plans to present to City Council an updated fee schedule in fall 2016.
- **Debt Service Funds** – Preliminary expenditures for the fiscal year totaled \$941,630. The first half of the year payment includes both interest and principal, while the second half of the year the payment will include interest only. Debt service payments were all scheduled when the bonds were issued, and are budgeted for in the months delineated in the underlying bond documents.
- **Successor Agency to the Former Redevelopment Agency Fund** - The Successor Agency continues down the path of meeting its debt and long range property management plan obligations through the Recognized Obligation Payment Schedule (ROPS) process, and in spending bond proceeds for the redevelopment of the downtown area. Preliminary CIP costs for the fiscal year totaled \$15.2 million mostly for the construction of the parking structure.

From a fiscal policy perspective, Successor Agency revenues and most expenditures simply represent the fulfillment of remaining enforceable obligations of the former redevelopment agency, expenditures which are ultimately controlled by the Oversight Board and the State Department of Finance, rather than by the City Council as governing body of the Successor Agency. The Successor Agency has been relegated by the California accounting profession to the status of a "private purpose trust fund" in the City's audited financial statements, which denotes that it is not included on the City's own books. One policy area where Fund 250 Successor Agency expenditures are relevant is capital spending from remaining bond proceeds of the original 2008 redevelopment bonds, which were refunded in November 2013.



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- Sewer Operations** – Revenues from Sewer Operations for the fiscal year totaled \$9.9 million. Expenditures and outstanding encumbrances through June 30, 2016 totaled \$11.4 million, which includes a \$4.0 million transfer of excess funds over the Council-adopted reserve policy to the System Replacement and Rate Stabilization Funds per Sewer Revenue Adjustment approved by City Council in January. To date, the impact of the drought and mandatory water conservation to the Sewer Operations Fund has been nominal because sewer service charges to residential consumers are established by measuring water consumption based on the three lowest months of water consumption in a year. The table below shows historical Sewer Operations revenues and expenditures from FY11-12 through FY14-15 Actual, FY15-16 Budget, and Preliminary FY15-16 Actual.

(amount in millions)	FY11-12	FY12-13	FY13-14	FY14-15	Budget FY15-16	Preliminary FY15-16
Revenues	8.0	9.7	9.4	10.3	9.9	9.9
Expenditures	8.3	9.0	8.6	8.8	13.9	11.4
Operating Margin	(0.3)	0.7	0.8	1.5	(4.0)	(1.5)
Operating Margin without Encumbrances	(0.3)	0.7	0.8	1.5	(4.0)	(1.5)

- Water Operations** – Water Operations includes Utility Billing, Water Conservation, and Water Operations. Preliminary revenues from Water Operations for the fiscal year totaled \$8.4 million, approximately \$444,000 or 5% less than a year ago at this time. Water sales revenues for the fiscal year totaled \$7.3 million, a decrease of approximately \$613,000 or 8% compared to prior fiscal year. The continued revenue shortfall is a result of water conservation efforts being met by the community and consequently driving down water consumption. Water Operations expenditures, including outstanding encumbrances for the fiscal year totaled \$10.0 million or 3% better than budgeted appropriation. Without the encumbrances, however, the expenditures amounted to \$9.7 million. The difference between revenues and expenditures, excluding outstanding encumbrances, is a net deficit of approximately \$1.3 million to Water Operations Fund, better than budgeted deficit of approximately \$1.6 million primarily due to the Water Revenue Adjustment recently approved by Council in January, Council savings initiated from bonds refunding, and a reduction in expenditures after the budget was adopted. The table below shows Water Operations revenues and expenditures from FY11-12 through FY14-15 Actual, FY15-16 Budget, and Preliminary FY15-16 Actual.

(amount in millions)	FY11-12	FY12-13	FY13-14	FY14-15	Budget FY15-16	Preliminary FY15-16
Revenues	9.8	10.2	12.2	8.8	8.6	8.4
Expenditures	8.3	9.1	12.1	9.3	10.4	10.0
Operating Margin	1.5	1.1	0.1	(0.5)	(1.8)	(1.6)
Operating Margin without Encumbrances	1.5	1.1	0.1	(0.5)	(1.6)	(1.3)

- Investments** - There were three securities called and three securities purchased during the month of June 2016. Total interest earnings received on investments were \$134,000 during the month.