

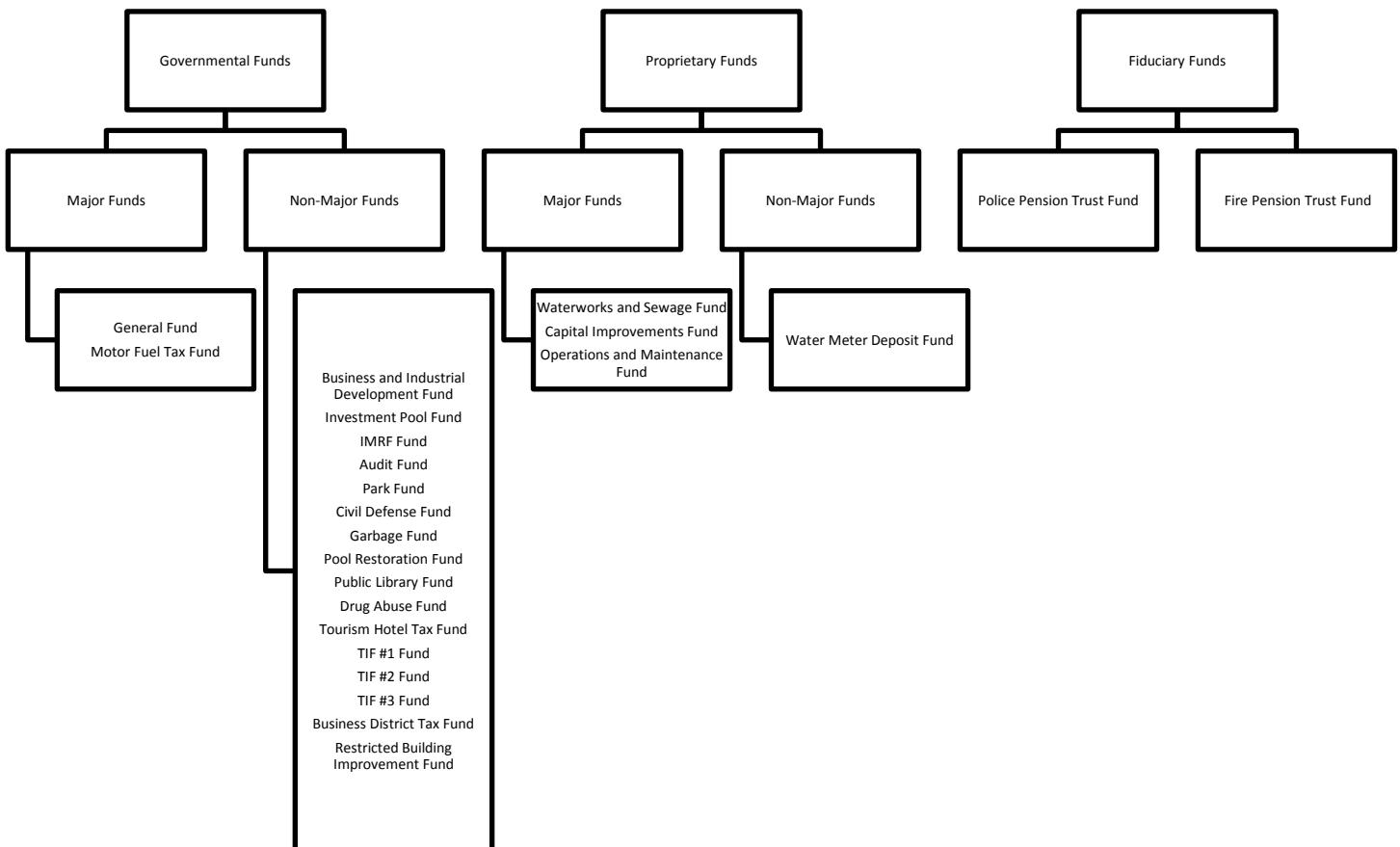


Management Discussion and Analysis
For the Fiscal Year Ended December 31, 2016

The City Council of the City of Du Quoin, Illinois offers this overview and analysis of the financial activities of the City for the fiscal year ended December 31, 2016. We encourage readers to consider the information in conjunction with the accompanying accounting information.

Financial Structure and Organization

The City’s financial activity happens in three main fund types, Governmental, Proprietary, and Fiduciary Funds. The former two of three fund types can be further reduced to Major and Non-Major or Restricted Funds. Major Funds support general operations of the City, whereas, Non-Major or Restricted Funds support specific purposes. The City’s financial structure can be illustrated as follows.



Major Governmental Funds includes the General and Motor Fuel Tax Funds. The General Fund provides for the Administration, Fire, Police, and Street Departments. These departments are mostly funded through collection of local and state taxes. Home Rule and Municipal sales taxes, Real Estate, Income, Local Use, Personal Property Replacement, Phone, Utility, and Video Gaming taxes account for roughly 90% of the funding for these departments. The remainder is funded by smaller sources of revenue collected by the City such as Franchise, Liquor License and Permit fees, and fines. The Motor Fuel Tax Fund is used to construct and maintain the City's streets. It is funded by a state tax on gasoline.

Major Proprietary Funds support the Water Department and Waste Water Treatment Plant. This division of the City's operations acts like a private business. Consumption of water and discharge of sewage is billed at a rate to generate enough revenue to cover the cost of supplying these services. Leachate Processing and Water Tap charges, and Reconnection fees also compliment Water and Sewer receipts.

Fiduciary Funds is the last of three main fund types. It includes the Police and Fire Pension Trust Funds that provide for pension benefits. They are funded by employer and employee contributions. Employer contributions are made by levying real estate taxes.

The next subset of funds is the Non-Major or Restricted Funds. These funds are only used for specific purposes within the City's operations. They can be one-time grants or projects, or continuing activities that have a particular purpose. They are as follows.

The City has created three Restricted Funds since 2015, which are the Restricted Building Improvement, Pool Restoration, and Water and Sewer Infrastructure Funds. The Restricted Building Improvement Fund housed loan proceeds of \$225,000 to replace the roof, tuck-point, and paint City Hall. The residual amount from completing these projects remains for future building needs. The Pool Restoration Fund was a savings fund used to renovate the City Pool in fall 2016. Its revenues were from donations, fundraisers, and an annual receivable from Du Quoin Unit School District #300 of \$39,029. This receivable is the result of a renegotiated intergovernmental agreement. In December, 2016 the City rolled the Pool Restoration Fund into the Restricted Park and Pool Fund. It is still funded by the annual receivable of \$39,029. The purpose of this fund was to establish a non-taxing Park District that funds future expansion, improvement, and repair of park and pool facilities. The Water and Sewer Infrastructure Fund is another savings fund to be used for the expansion, improvement, and repair of the City's Water and Sewer systems. It is funded by a portion of the service charge on all bills.

The Audit, Park, Civil Defense, and Garbage Funds are Restricted Fund extensions of the General Fund as they use the same revenue sources. These funds provide for the

preparation of the City's audit, park and pool operations, Emergency Management Agency, and garbage collection. They are not included in Major Governmental Funds because the City levied Real Estate taxes at one time to fund them.

The Drug Abuse Fund supports the Police Department through fines collected from drug and drunken driving arrests. This fund purchases most of the City's Police cars.

The Hotel Tax Fund is a pass through to fund activities of the Du Quoin Tourism Commission such as Holiday Lights.

The Public Library Fund provides for the operation of the Du Quoin Public Library. The City accounts for the Library's funds, but does not manage them. The Library Board is responsible for levying their own Real Estate taxes, preparing their own budget, and approving expenditures.

Lastly, there is a collective set of Restricted Funds whose purpose is to support economic development in the City. This set is referred to as the Economic Development Funds, and is comprised of Tax Increment Financing (TIF) Districts 1, 2, and 3, the Business Development District, and the Revolving Loan Fund. Each TIF District has an established area with a base assessed valuation. As properties develop with TIF assistance, the equalized assessed valuation (EAV) of those properties increases. The difference between the increased EAV and the base generate additional property tax revenues to be used in the TIF District. These revenues can be used to reimburse businesses for redevelopment projects and to fund public infrastructure projects in the TIF District. The Business Development District is established along the Route 51 corridor and generates revenues through the imposition of a half cent sales tax. This revenue is used to create new businesses, expand existing businesses, and to fund public infrastructure projects in the Business District. The Revolving Loan Fund was initially capitalized by the Illinois Department of Commerce and Economic Opportunity, and provides low interest loans to new and existing businesses in the City.

Financial Highlights

For the year ended December 31, 2016, revenues across all funds totaled \$8,574,865. Expenditures totaled \$8,619,122, resulting in a total net change in fund balance of (\$44,257)¹. An alternative measure of the City's financial position is reported in the Statement of Activities. According to this measure, the total change in net position is (\$266,518)². The difference between the two measures is due to fund balance reports capital outlays as expenditures, uses bond proceeds as current financial resources, and

¹ See pages 19 and 22

² See page 16

defers expenditures³. In 2015, revenues were \$9,115,885 versus expenditures of \$8,803,910, resulting in a total net change in fund balance of \$311,975.

General Fund revenues decreased from \$4,691,165 in 2015 to \$4,326,598 in 2016 for a decrease of \$364,567 or 7.77%. This decrease is largely accounted for by a decrease in Intergovernmental revenues and Grant income of \$116,909 and \$313,660, respectively. However, expenditures fell as well. They decreased from \$4,592,070 in 2015 to \$4,296,191 in 2016 for a decrease of \$295,879 or 6.44%. For 2016, General Fund revenues exceeded expenditures by \$30,407. In 2015, the difference was \$99,095.

General Fund budgeted revenues were \$4,114,245 against budgeted expenditures of \$4,124,916, resulting in a variance of \$212,353 and (\$171,275), respectively for 2016. This variance in revenues was largely a function of a late surge in sales taxes, a greater than expected reimbursement from Motor Fuel Tax Fund for labor and equipment, fines and assessments, entering into an intergovernmental agreement with the State of Illinois for the Fairgrounds, and other income. These five items were \$181,130.55 or 85.3% of the variance. In regards to expenditures, variance was mostly due to salaries and benefits, payment of one third of Home Rule sales tax to School District #300, professional services, building maintenance, and other expenses. These five items were (\$230,706.29) or 134.7% of the variance. There was savings in other expenditure items to arrive at (\$171,275).

Motor Fuel Tax Fund had revenues of \$155,736 versus expenditures of \$182,797 for a deficit of \$27,061. This fund continues to support the City's road maintenance program and there is nothing to note about the deficit.

Major Proprietary Funds revenues increased from \$2,619,165 in 2015 to \$2,679,908 in 2016 for an increase of \$60,743 or 2.32%. Expenditures fell from \$2,676,270 in 2015 to \$2,571,611 in 2016 for a decrease of \$104,659 or 3.91%. For 2016, Major Proprietary Funds net income was \$99,276. In 2015, net income was \$166,472.

The City continues to support the Fiduciary Funds by levying real estate taxes by the full or greater amount requested by the Police and Fire Pension Boards. The Illinois Department of Insurance determines these amounts to get the Pension Funds 90% funded by 2040. For 2016, the Police Pension Board requested \$260,507. The City levied \$260,507 and received \$241,407. The Fire Pension Board requested \$249,283. The City levied \$292,293 and received \$276,882. The Police and Fire Pension Funds are 54% and 43% funded, respectively.

Restricted Funds continue to be used constructively and for the purposes that they were intended for. The following Restricted Funds had surpluses: Investment Pool, IMRF,

³ See page 20

Audit, Garbage, Pool Restoration, and Drug Abuse Funds. The following had deficits: Business and Industrial Development, Park, Civil Defense, Public Library, Tourism Hotel Tax, TIFs #1, 2, and 3, Business District Tax, and Restricted Building Improvement Funds. Park and Restricted Building Improvement Funds had the largest deficits of \$147,512 and \$73,131, respectively. An explanation is necessary.

Park Fund was debited with capital outlay of \$137,292 in 2016 for the City Pool renovation. However, Pool Restoration Fund was credited with revenues in 2015 and 2016 to cover the cost for this project. The explanation is similar for the Restricted Building Improvement Fund. In 2015, the City received loan proceeds of \$225,000 to roof, tuck-point, and paint City Hall. These proceeds were spent in 2015 and 2016 to complete this project.

The Economic Development Funds continue to assist businesses, provide for public projects, and perpetually grow. In 2016, TIF Funds provided for five new and 11 existing redevelopment agreements. The five new agreements provided assistance to Kim's Family Health Clinic, Baked by Gene, The Jimmy, Inc. Laundromat, Down Here Christian Gift Shop, and Slainte Real Estate LLC, owner of the former Cookie Factory. They also provided the Du Quoin Community Development Corporation (DCDC) the means to redevelop property at 101 East Main Street for the benefit of Jones and Son Gun Shop. Lastly, TIF Funds assisted in public improvements including the resurfacing of South Washington Street from Main Street to Poplar Street, replacement of sidewalks in front of City Hall, and extension of public utilities for the benefit of the new laundromat. TIF Funds had combined revenues of \$164,493 versus expenditures of \$204,005 for a deficit of \$39,512. Business District Tax Fund had revenues of \$179,781 and expenditures of \$205,736 for a deficit of \$25,955. This deficit was due to using \$49,382 to prematurely pay off a redevelopment agreement with Chip Banks Chevrolet Buick. Business and Industrial Development Fund had revenues of \$17,505 versus expenditures of \$41,403 for a deficit of \$23,898. There was not much activity for the year other than a \$41,387 expense for the local share of grant for the Main Street sidewalks project.

2017 Budget

The 2017 Budget has budgeted revenues and expenditures of \$8,795,069 and \$8,396,108, respectively for a budgeted surplus of \$398,961. This is an increase in budgeted revenues and expenditures of \$498,685 and \$61,340, respectively from 2016. There are surpluses budgeted in Major Proprietary, Business District Tax, and Investment Pool Funds. There are deficits budgeted in General, Civil Defense, and Revolving Loan Funds.

It is expected that Home Rule and Municipal sales taxes will increase by 6% to 7% from 2016 actuals and stay constant from 2015 actuals. The assumption is that these sales

taxes will revert to the trend prior to 2016. This is in spite of the School's additional 1% sales tax imposed that may push families to shop elsewhere. It is expected that Water revenues will increase by 5% from 2016 actuals due to rate increases and meter change outs. In regards to expenditures, it is expected that health insurance costs will increase by 7% to 10%, fuel and utility costs will stay constant, and workers' compensation insurance costs will decrease.

The 2017 Budget contains the following planned capital expenditures: \$19,000 for accounting software, \$60,000 for two squad cars, \$34,000 for dump truck, and \$15,000 for Waste Water Treatment Plant operating system. Planned capital expenditures total \$128,000, which is up from \$98,500 in 2016.

Future Financial Strategies

Governmental Funds

General Fund is just as unstable as it was in 2015. The same problem persists, which is the percentage of revenues used for salaries and benefits. This statistic was 78.43% in 2016. The only year it was greater since 2000 was in 2014 at 84.57%, which was partly due to \$370,423 less in revenues. It has traditionally ranged from 72% to 74%. From 2000 to 2016, insurance and pension expenditures had an alarming average annual growth rate of 7.17% and 12.25%, respectively. When these expenditures are combined with salaries, the growth rate is 5.15%. This exceeds revenues growth rate of 4.63%, which is partly attributed to Real Estate tax revenues growth rate of 10.47%. If growth in salary and benefit expenditures continues to exceed growth in revenues, expenditures on capital will converge to zero. The effect of this would be a less productive labor force as it would not be complimented with sufficient capital. This is counter intuitive. For example, there could be situations where two workers are sharing a truck.

The City will be bidding out health insurance and other benefits in an effort to get lower rates. The big constraints here are the collective bargaining agreements and the Affordable Care Act. In addition, Department Supervisors must continue to analyze their shift schedules and distribute employees across shifts in a manner that maximizes productivity and minimizes overtime. These efforts will help slow this trend some.

Second, Department Supervisors are the front lines against expenditures. They must authorize purchases in accordance with their budgets and ensure that purchases made are good value to the City. There are now better controls in place that requires pre-approval to spend if Supervisors do not take this responsibility seriously.

The City continues to make debt payments on time. For 2017, Major Governmental Funds debt payments will total \$83,852, which has decreased from \$92,945 in 2016. These payments are for the City Hall roof and a Fire truck. The City aspires to be more

aggressive in making additional payments towards debt principal, but has not had the cash flow to do so. However, the 2017 Proprietary Funds Budget includes an appropriation of \$61,200 for additional debt payments.

Proprietary Funds

Proprietary Funds must continue to get savings through investments. The City replaced some of its master and commercial meters at the end of 2016. Those efforts have yielded average water usage increases over 10%. These marginal revenues can then be used to replace depreciated capital assets in the water and sewer system, and at the Waste Water Treatment Plant. This program must continue.

Second, the City has raised water rates to mimic when Rend Lake Water Conservancy District raises their water supply rates. By moving in lockstep with their rates, the City's budget and its customers' budgets are not jolted. Furthermore, the City is funneling a portion of water and sewer receipts into a Restricted Infrastructure Fund. This will better position the City for future infrastructure needs and ensure delivery of quality water to its customers.

The City continues to chase grants for water and sewer infrastructure projects. The City had success at the end of 2016 when the Delta Regional Authority awarded over \$200,000 to renovate the Grant Way lift station. Construction is expected to start August 2017.

Requests for Information

This financial report was created to provide a basic overview of the City of Du Quoin's for those interested. Any questions concerning the information provided in this report or requests for additional financial information should be addressed to the City Clerk's Office at 302 East Poplar Street, Du Quoin, Illinois 62832.

Management's Discussion and Analysis for the City of Du Quoin for the fiscal year ended December 31, 2016 was compiled by City Clerk Andrew Croessman.

Andrew Croessman, Budget and Finance Director