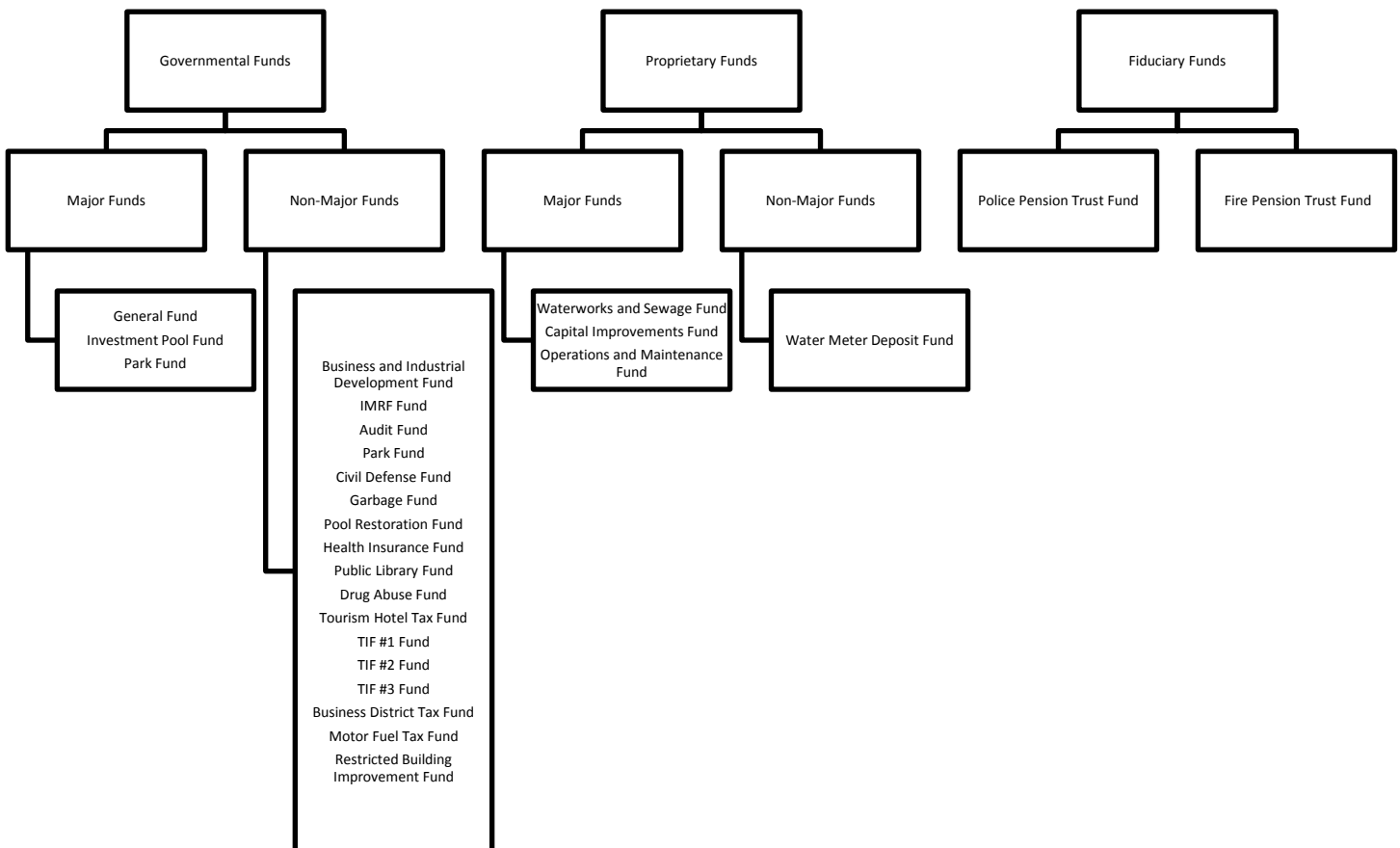


Management Discussion and Analysis For the Fiscal Year Ended December 31, 2017

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, 2017. 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. Governmental Funds account for tax supported. Proprietary Funds account for business activities such as providing water. Fiduciary Funds account for investments managed by the Police and Fire Pension Boards to provide pension plans to retired employees. 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, Investment Pool, and Park 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. Roughly 90% of the funding for these Departments is provided by Home Rule and Municipal sales taxes, Income, Local Use, Personal Property Replacement, Phone, and Utility taxes. The remainder is funded by smaller sources of revenue collected by the City such as Franchise, Liquor License and Permit fees, and fines.

The Investment Pool Fund consists of three savings accounts for contingencies. One account is funded by Video Gaming tax and the other two by interest only.

The Park Fund provides for the operation and maintenance of the City swimming pool, and Keyes and Pettiford Parks. It shares many of the same revenue sources as the General Fund plus some smaller sources such as swimming pool admissions and concessions.

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 smaller in size and scope than the Major Funds. They are used only for specific purposes within the City's operations, which could be one-time grants or projects, or continuing activities that have a particular purpose. They are as follows.

The City has created four Restricted Funds since 2015: the Pool Restoration, Health Insurance, Restricted Building Improvement, and Water and Sewer Infrastructure Funds. 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 Health Insurance Fund was created in 2017 when the City switched insurance carriers for its group health plan. This change resulted in annual savings north of \$200,000 which funds it. The Fund can be used for self-insuring differences in plan benefit levels and mitigating premium increases so long as the balance is greater than \$156,000.

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 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, Civil Defense, and Garbage Funds are Restricted Fund extensions of the General Fund as they share the same revenue sources. These funds provide for the preparation of the City's audit, 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, Concerts in the Park, and the Fall Festival.

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. The City originates and collects on these loans, and reports to the State. The State has announced that it will dissolve this program by the end of 2018.

Financial Highlights

For the year ended December 31, 2017, revenues across all funds totaled \$8,236,048. Expenditures totaled \$8,044,726, resulting in a total net change in fund balance of \$191,322¹. 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 (\$127,679)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 defers expenditures³. In 2016 and 2015, the total net change in fund balance was (\$44,257) and \$311,975, respectively.

Using the modified accrual basis of accounting, General Fund revenues decreased from \$4,326,598 in 2016 to \$3,657,380 in 2017 for a decrease of \$669,218 or 15.5%. Taxes and Intergovernmental revenues collectively decreased \$580,102 or 14.5%. Expenditures fell as well. They decreased from \$4,296,191 in 2016 to \$3,798,419 in 2017 for a decrease of \$497,772 or 11.6%. However, the decrease in General Fund revenues outpaced expenditures resulting in a deficiency of (\$141,039)⁴. In 2016 and 2015, the General Fund had excess revenues of \$30,407 and \$99,095, respectively.

Using the cash basis of accounting, General Fund budgeted revenues were \$3,786,677 against budgeted expenditures of \$3,853,115 for 2017, resulting in a variance of \$34,454 and \$53,410, respectively. A positive variance on both revenues and expenditures resulted in excess revenues of \$21,426 versus a budgeted deficiency of (\$66,438). This surplus is mostly attributed to deferring \$72,005 of planned Capital Outlay expenditures⁵.

Investment Pool Fund had revenues of \$106,218 and expenditures of \$0 for a surplus of \$106,218. The Fund had a variance of \$12,894 from the budget. Almost all of this pleasant surprise was due to Video Gaming tax being over budget by \$12,190. This tax increased \$16,057 or 18.0% from 2016.

Park Fund had revenues of \$135,538 versus expenditures of \$118,003 for a surplus of \$17,535. This surplus was largely due to a \$15,225 variance in Intergovernmental revenues. It is also worthwhile to note a prior period adjustment of \$507,379 which is the Du Quoin Unit School District #300 receivable that was moved from the General to Park Fund. This fund continues to provide for the City's parks and pool.

Major Proprietary Funds revenues increased from \$2,679,908 in 2016 to \$2,954,683 in 2017 for an increase of \$274,775 or 10.3%. This jump in revenues was largely due to Grant Income of \$208,712 to rehabilitate the Grant Way lift station. Expenditures also increased. They increased from \$2,571,611 in 2016 to \$2,635,918 in 2017 for an increase of 2.5%. For 2017, Major Proprietary Funds net income was \$276,541. For comparison, net income was \$99,276 in 2016 and \$166,472 in 2015.

¹ See pages 20 and 23

² See page 17

³ See page 21

⁴ See page 20

⁵ See page 66

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 2017, the Police Pension Board requested \$294,545. The City levied \$294,545 and received \$295,468. The Fire Pension Board requested \$259,691. The City levied \$285,214 and received \$289,083. The City also provided \$6,326 of its Personal Property Replacement Tax to further support the Fire Pension Fund. The Police and Fire Pension Funds are 54% and 45% funded, respectively.

Restricted Funds continue to be used constructively and for the purposes that they were intended for. The following Restricted Funds had a positive change in fund balance: Business and Industrial Development, IMRF, Garbage, Health Insurance, TIF #2, TIF #3, and Business District Tax Funds. The following had a negative change in fund balance: Audit, Civil Defense, Pool Restoration, Public Library, Drug Abuse, Tourism/Hotel Tax, TIF #1, Motor Fuel Tax, and Restricted Building Improvement Funds. The Restricted Funds collectively had a positive change in fund balance of \$27,415. The largest contributor was the Health Insurance Fund of \$111,385. Cash balances for the Restricted Funds have grown \$332,864 or 59.5% since 2015.

The Economic Development Funds continue to assist businesses, provide for public projects, and perpetually grow. In 2017, TIF Funds provided for one new and 12 existing redevelopment agreements. The new agreement provided \$15,000 of assistance to B&J True Value Power Equipment. They also provided the Du Quoin Community Development Corporation (DCDC) the means to acquire property at 110 and 112 East Main Street to develop a downtown commons area. TIF Funds had combined revenues of \$171,506 versus expenditures of \$137,907 for a surplus of \$33,599.

Business District Tax Fund had revenues of \$183,823 and expenditures of \$165,259 for a surplus of \$18,564. In 2017, this Fund provided for one new and four existing redevelopment agreements. The new agreement provided \$58,500 to Scoop Foods, Inc. to open a Save A Lot grocery store. The City also used roughly \$15,000 from this Fund to enlarge the drain culvert under the south entrance to the Southtowne Shopping Center.

Business and Industrial Development Fund had revenues of \$1,825 versus expenditures of \$40 for a surplus of \$1,785. There was not much activity for the year.

2018 Budget

The 2018 Budget has budgeted revenues and expenditures of \$8,629,202 and \$8,222,869, respectively for a budgeted surplus of \$406,333. This is a decrease in budgeted revenues and expenditures of \$165,867 and \$173,239, respectively from 2017. There are surpluses budgeted in General, Park, IMRF, Major Proprietary, Business District Tax, and Investment Pool Funds. There are deficits budgeted in Health Insurance, Restricted Building Improvements, and Motor Fuel Tax Funds.

It is expected that Home Rule and Municipal sales taxes will collectively decrease by \$11,067 or 0.4% from 2017 actuals. The assumption is that these sales taxes will revert to the trend prior to 2017. It is also expected that Personal Property Replacement Tax will decrease by \$11,485 or 22.3% from 2017 actuals as the State diverts more for its own purposes. Water revenues are

expected to increase by 1.4% from 2017 actuals due to rate increases. In regards to expenditures, it is expected that wage rates will increase by 2.4% due to labor contracts, health insurance costs will increase by 10%, and fuel, utility, and workers' compensation insurance costs will stay constant.

The 2018 Budget contains the following planned capital expenditures: \$35,000 for a squad car, \$5,000 for body cameras, \$20,000 for down payment on dump truck, \$6,000 for a computer server, \$4,100 for meter reading equipment, \$24,000 for a pickup truck, \$30,000 for lift station upgrades, and \$10,000 for a lawn mower. Planned capital expenditures total \$134,100, which is up from \$128,000 in 2017.

Future Financial Strategies

Governmental Funds

General Fund continues to be unstable and difficult to balance. The same problem persists, which is the percentage of revenues used for salaries and benefits. This statistic was 78.96% in 2017, which is the third highest reading since 2000. Even worse is that three of the highest readings were in the past four years, and the 2017 reading was when the City experienced solid revenues and cut health insurance costs by over \$150,000. The picture is clear. If growth in salary and benefit expenditures continues to exceed growth in revenues, expenditures on capital will converge to zero; the resulting effect is a trap. Year after year, the City pays more for labor that is less productive as it does not generate the savings to invest in capital to complement its labor to make it more productive. This is counter intuitive.

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 continue to 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 and aspires to be more aggressive in making additional payments towards debt principal, but has not had the cash flow to do so. However, the 2018 Proprietary Funds Budget includes an appropriation of \$30,578 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. The City is currently analyzing the costs and benefits of automated meter reading and monitoring systems.

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.

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, 2017 was compiled by City Clerk Andrew Croessman.

Andrew Croessman, Budget and Finance Director