

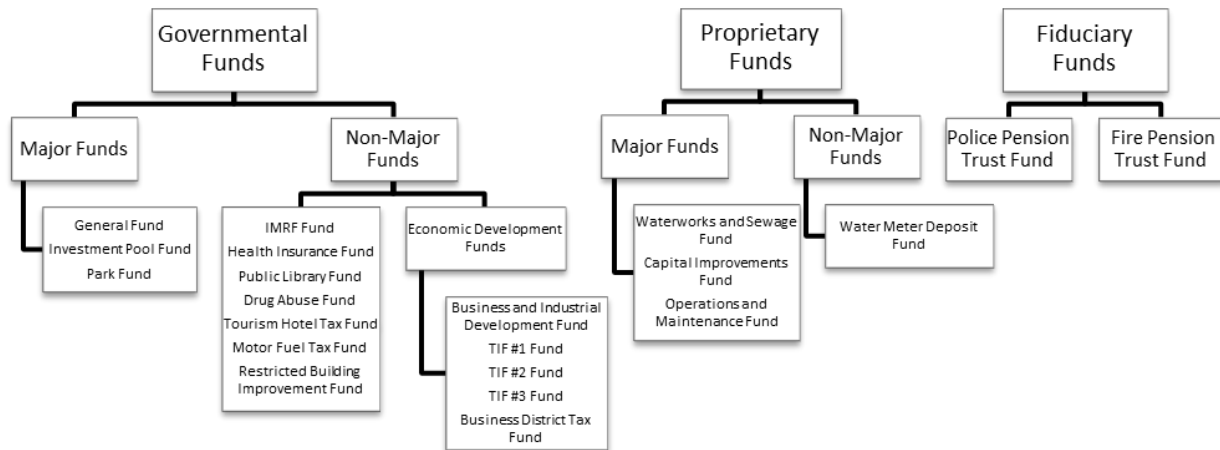


## Management Discussion and Analysis For the Fiscal Year Ended December 31, 2018

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, 2018. 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 all that is 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, Emergency Management, 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 is more like a business. Consumption of water and discharge of sewage is billed at a rate that generates 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 the 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 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.

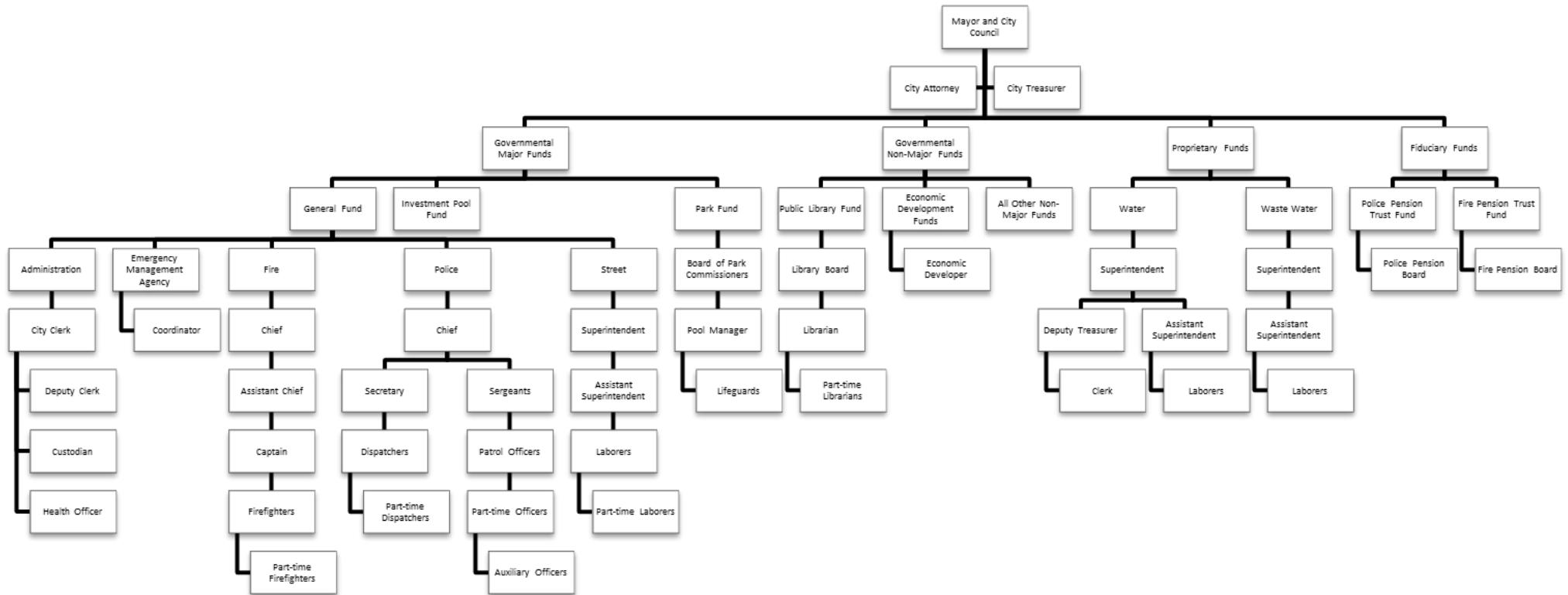
The Public Library Fund provides for the operation of the Du Quoin Public Library. The City accounts for the Library's funds, but does not manage them. The Library Board is responsible for levying their own Real Estate taxes, preparing their own budget, and approving expenditures.

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 (RLF) 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. The City returned its RLF cash balance of \$153,219 to the State in February, 2019.

The City's structure can be reduced further as illustrated on the following page.



## Financial Highlights

For the year ended December 31, 2018, revenues across all funds totaled \$8,717,116. Expenditures totaled \$8,150,361, resulting in a total net change in fund balance of \$566,755<sup>1</sup>. 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 \$410,653<sup>2</sup>. 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 expenditures<sup>3</sup>. In 2017, 2016, and 2015, the total net change in fund balance was \$191,322, (\$44,257), and \$311,975, respectively. From 2015 through 2018, the collective total net change in fund balance was \$1,025,795 versus (\$1,410,203) for the preceding four years ending in 2014.

Using the modified accrual basis of accounting, General Fund revenues increased from \$3,657,380 in 2017 to \$3,975,088 in 2018 for an increase of \$317,708 or 8.7%. Taxes and Intergovernmental revenues collectively increased \$212,346 or 6.2%. There was also an increase of Grant Income of \$93,662. Expenditures increased slightly. They increased from \$3,798,419 in 2017 to \$3,883,825 in 2018 for an increase of \$85,406 or 2.2% due to an increase in Public Safety and Capital Outlay expenditures of \$82,415 and \$63,750, respectively. The larger growth in General Fund revenues relative to the smaller growth in expenditures resulted in a surplus of \$91,263<sup>4</sup>.

Using the cash basis of accounting, General Fund revenues were \$3,939,516 against expenditures of \$3,880,528 for a surplus of \$58,988. There was budget variances of \$158,413 on revenues and (\$211,792) on expenditures. The better than expected revenues were mostly due to overages of \$41,495 in Taxes and \$78,662 in Grant Income. Expenditures were worse than expected mostly due to overages of (\$39,560) in Wages, (\$48,836) in Health Insurance, and (\$35,719) in Maintenance<sup>5</sup>.

Investment Pool Fund had revenues of \$111,606 and expenditures of \$0 for a surplus of \$111,606. The Fund had a revenues variance of \$18,721 from the budget due to Video Gaming Tax and Interest Income being over budget by \$17,521 and \$1,200, respectively. Video Gaming Tax increased \$4,257 or 4% year over year<sup>6</sup>.

Park Fund had revenues of \$162,198 versus expenditures of \$118,928 for a surplus of \$43,270. This surplus was largely due to total revenues variance of \$10,065 and Utilities expenditure variance of \$9,624. This Fund continues to provide for the City's pool and parks that many families use and enjoy<sup>7</sup>.

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<sup>1</sup> See pages 21, 24, and 27

<sup>2</sup> See page 18

<sup>3</sup> See page 22

<sup>4</sup> See page 21

<sup>5</sup> See pages 67-74

<sup>6</sup> See page 75

<sup>7</sup> See page 76

Major Proprietary Funds revenues decreased from \$2,954,683 in 2017 to \$2,833,356 in 2018 for a decrease of \$121,327 or 4.1%. This drop in revenues was largely due to Grant Income of \$208,712 in 2017 to rehabilitate the Grant Way lift station. Expenditures went the other direction. They increased from \$2,635,918 in 2017 to \$2,795,133 in 2018 for an increase of 6%. For 2018, Major Proprietary Funds net income was \$14,487. For comparison, net income from 2015 through 2017 was \$166,472, \$99,276, and \$276,541, respectively<sup>8</sup>.

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 2018, the Police Pension Board requested \$274,395. The City levied \$274,395 and received \$272,177. The Fire Pension Board requested \$265,367. The City levied \$285,214 and received \$282,891. The Police and Fire Pension Funds are 51.6% and 42.6% funded, respectively<sup>9</sup>.

Restricted Funds continue to be used constructively and for the purposes that they were intended for. The following Restricted Funds had a surplus in 2018: Business and Industrial Development, IMRF, Public Library, Drug Abuse, Tourism/Hotel Tax, TIF #2, TIF #3, Business District Tax, and Motor Fuel Tax Funds. The following had a deficit: Health Insurance, TIF #1, and Restricted Building Improvement Funds. The Restricted Funds collectively had a surplus of \$319,130. The largest contributor was the Business District Tax Fund of \$144,285. Cash balances for the Restricted Funds have grown \$880,245 or 157.4% since 2015.

The Economic Development Funds continue to assist businesses, provide for public projects, and perpetually grow. In 2018, TIF Funds provided for six new and 12 existing redevelopment agreements. Four of the six new agreements provided \$44,550 in roof repair and replacement assistance. The other two new agreements provided \$20,498 in solar panels and land acquisition. They also provided for the development of a public commons area at 110 and 112 East Main Street. TIF Funds had combined revenues of \$253,176 versus expenditures of \$194,161 for a surplus of \$59,015. Combined TIF revenues were \$81,670 more than 2017 due to an Industrial Park land sale of \$83,112 to Chester Construction Supply. The land sale proceeds will be used to extend water and sewer mains to their development in 2019.

Business District Tax Fund had revenues of \$378,743 and expenditures of \$234,458 for a surplus of \$144,285. Revenues were \$194,920 more than 2017 due to the Illinois Department of Revenue assessing all businesses in the Business District the correct sales tax rate. In 2018, this Fund provided for two new and five existing redevelopment agreements. The two new agreements provided \$24,000 to Abundant Storage and \$17,500 to Porter's Storage and RV. The City also prepaid \$54,911 to Fenton's Custom and Collision to fulfill the remainder of that redevelopment agreement.

Business and Industrial Development Fund had revenues of \$2,449 versus expenditures of \$0 for a surplus of \$2,449. All revenues were generated through interest income from existing loans and there was no new activity for the year.

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<sup>8</sup> See page 24

<sup>9</sup> See page 59

## **2019 Budget**

The 2019 Budget has budgeted revenues and expenditures of \$9,232,543 and \$8,975,843, respectively for a budgeted surplus of \$256,700. This is an increase in budgeted revenues and expenditures of \$601,625 and \$653,474, respectively from 2018. There are surpluses budgeted in General, Park, IMRF, Restricted Building Improvements, Major Proprietary, Business District Tax, and Investment Pool Funds. There are deficits budgeted in Health Insurance, Motor Fuel Tax, and TIF Funds.

The significant increase in budgeted revenues from 2018 is mostly due to anticipated State Grants of \$272,915 and an increase of Business District Sales Tax of \$215,718. There are also smaller budgeted revenue increases in Income Tax of \$33,149, Utility Tax of \$18,988, Towing Fees of \$16,400, and Water Revenues of \$42,506. All of these revenue sources sum to a budgeted increase of \$599,676. All other large revenue sources such as Property and Sales Taxes are expected to be constant or decrease slightly.

In regards to budgeted expenditures, labor costs are expected to increase by \$147,337 due to Fire and Police pensions, health insurance, and pay raises. Fire and Police pensions contribute \$62,811 to the labor costs increase due to the Illinois Department of Insurance making changes to their actuarial assumptions such as decreasing investment returns and increasing life expectancy. The City decided to absorb this pension shortfall, rather than levy more property taxes. Health insurance premiums are expected to increase by 10%, and dental, vision, and life insurance premiums are expected to increase by 7.6%. All insurance renews on May 1, 2019. Hourly wage rates are set to increase by \$0.41 for Firefighters and \$0.54 for all other full-time employees. Annual property, liability, and workers' compensation insurance premiums are set to decrease from \$280,780 in 2018 to \$176,579 in 2019. IMRF employer contribution rates are also set to decrease from 12.18% of employee earnings in 2018 to 8.44% in 2019. All other budgeted expenditures such as fuel, maintenance, and utilities are expected to remain stable.

The 2019 Budget contains the following planned capital expenditures: \$152,065 for water and sewer main extensions in the Industrial Park, \$94,030 for water main replacement on South Madison Street, \$35,000 for a squad car, \$20,000 for down payment on a dump truck, and \$5,250 for the City's grant portion of a trailer hauler truck. Planned capital expenditures total \$306,345, which is up from \$134,100 in 2018.

## **Future Financial Strategies**

### **Governmental Funds**

General Fund continues to be unstable and difficult to balance due to the large percentage of revenues used for salaries and benefits. This metric continues to flirt with 80% despite solid revenues and numerous labor cost cutting efforts. These efforts include generating over \$250,000 in health insurance savings and slashing annual liability insurance from \$422,000 to \$163,000. Other efforts include reducing the number of full-time positions through attrition, adding more part-time positions, and negotiating responsible labor contracts that provide for wage rate resets and individual health insurance contributions.

If growth in salary and benefit expenditures exceeds growth in revenues, expenditures on capital converges to zero. Ultimately, a trap situation occurs where 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 situation leads to a downward spiral. The City is investing more in productive capital to prevent a downward spiral. Administration invested in accounting software and hardware to fully integrate with its existing utility management software. This technology upgrade brings accounts payable, counter receipts, general ledger, payroll, and utility management into one software suite, which provides for more accountability, automation, and features. New features include electronic counter receipts and purchase orders, and utility payments via automated clearing house (ACH) and phone. Police have also invested in productive capital such as: body cameras to reconcile conflicting narratives, mobile data centers to produce electronic tickets and reports, and smartphones to produce evidence and use as a reference. These investments make labor more productive, and more must be done.

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 also help slow this labor trend some.

Department Supervisors must also 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 must re-evaluate, re-think, and re-negotiate its intergovernmental agreements and relationships to ensure that they add value and reciprocity to the City's taxpayers. This is especially the case as the City's first responders are responding to Perry County's calls as they cope with financial reality. The City has no statutory obligation to do so and should only do so if it is beneficial to its taxpayer.

The City must continue to leverage its Economic Development Funds and grants to spark private business investment and further develop infrastructure in support of. An example of this is the development of Chester Construction Supply and the Industrial Park railroad spur. This development will result in the Industrial Park being linked to the North American railroad system, which could initiate more private business investment. The City must also continue to promote and support events that draw regional crowds like the State Fair, Holiday Lights, NubAbility, and Special Olympics. These two strategies expand the tax base and thus tax receipts, which tempers inclinations to increase taxes and thus erode the tax base.

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 2019 Proprietary Funds Budget does include 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 financial activities 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, 2018 was compiled by Budget and Finance Director Andrew Croessman.

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Andrew Croessman, Budget and Finance Director