

City of Scotts Valley California



COMPREHENSIVE ANNUAL FINANCIAL REPORT For Fiscal Year Ended June 30, 2012

COMPREHENSIVE ANNUAL FINANCIAL REPORT

Of

**THE CITY OF SCOTTS VALLEY,
STATE OF CALIFORNIA**

For the Fiscal Year Ended June 30, 2012

**Stephen H. Ando
City Manager**

**CITY OF SCOTTS VALLEY
 COMPREHENSIVE ANNUAL FINANCIAL REPORT
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INTRODUCTORY SECTION

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CITY OF SCOTTS VALLEY

OFFICE OF THE CITY MANAGER

One Civic Center Drive . Scotts Valley . California . 95066
Phone (831) 440-5600 . Facsimile (831) 438-2793 . www.scottsvally.org

August 7, 2013

Honorable Mayor and City Council
City of Scotts Valley
One Civic Center Drive
Scotts Valley, CA 95066

SUBJECT: COMPREHENSIVE ANNUAL FINANCIAL REPORT - JUNE 30, 2012

Honorable Mayor and Council Members:

The Comprehensive Annual Financial Report for the City of Scotts Valley for the fiscal year ended June 30, 2012 is hereby submitted. The responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with City management. We believe the data, as presented, is accurate in all material respects and that it is presented in a manner designed to fairly set forth the financial position and results of operations of the City. All disclosures necessary to enable the reader to gain an understanding of the City's financial activity have been included. These statements have been audited by the City's independent auditor, C. G. Uhlenberg, LLP, who has issued an unqualified opinion thereon. The Auditors' report is also included.

In accordance with the guidelines recommended by the Government Finance Officers Association of the United States and Canada (GFOA), and the standards adopted by the Governmental Accounting Standards Board, the accompanying report consists of three parts:

- I. Introductory Section – Letter of Transmittal, List of Principal Officials and Organization Chart, Certificate of Achievement from the GFOA.
- II. Financial Section – Independent Auditors' Report, Government-wide Financial Statements, Fund Financial Statements, Notes to the Financial Statements followed by Required Supplementary Information and combining statements of the Non-major Fund Financial Statements.
- III. Statistical Section – Presenting ten year historical trends of financial and non-financial information.

Accounting principles, generally accepted in the United States of America, require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to compliment MD&A and should be read in conjunction with it. The City's MD&A can be found immediately following the report of the independent auditors.

REPORTING ENTITY AND SERVICES PROVIDED

The City of Scotts Valley is a general law city incorporated in 1966. It operates under a council-manager form of government and provides the following range of municipal services: police, parks, recreation, sanitary sewer, streets and roads, public improvements, planning and zoning, construction inspection, and general administrative services. The City provides its sanitary sewer services through its wastewater fund and its recreational programs through its recreation fund, both of which are intended to be funded through user fees.

This report includes all the funds of the City. The financial statements also include the accounts of the following separate legal entities:

- City of Scotts Valley Redevelopment Agency
- Scotts Valley Public Financing Authority

The accounts of these entities are blended into the City's financial statements in accordance with Governmental Accounting Standards Board Statement No. 14. Footnote 1 to the financial statements provides further information regarding these entities.

MAJOR INITIATIVES

During 2011 / 2012, the City accomplished the following:

- Issued \$4,460,000 of pension obligation bonds to pay off the City's side fund liability. This will save the City over \$1 million over 13 years.
- Woodside project was approved for 50 single family homes.
- Completed the upgrading of the City's Police Department Mobile Data Consoles (MDC) and records management system.
- Approved wastewater fee increase over five years.

The following are current and future projects:

- Complete the upgrading of our Police Department Mobile Data Consoles (MDC) and records management system.
- Relocation of existing propane fueling station out of the Town Center Project area.
- The Police Department is currently updating and improving their General Orders Manual.
- Two residential projects started: one with 46 units and one with 49 units.
- A 119-room hotel building.
- Comprehensive General Plan update.
- Submittal of a \$3.5 million federal grant application to the Economic Development Administration for infrastructure costs for the City's Town Center Project.

FINANCIAL POLICIES

The elimination of redevelopment agencies by the State of California will have a large impact on the City of Scotts Valley. The Scotts Valley Redevelopment Agency (Agency) did not have separate employees. Staff from the City also worked for the Agency and their salaries were allocated accordingly. Now, all salaries will be borne by the City's General Fund.

The City filed a lawsuit against the County of Santa Cruz regarding the amount of property taxes distributed to the City. In May 2009 the court ruled in the City's favor. The County has appealed this decision. In late October 2011 the Appellate Court affirmed in part and reversed in part the decision of the trial court. The County of Santa Cruz petitioned the State Supreme Court to consider the issues, but it declined to hear the case. The decision became final and the City will receive the back taxes, approximately \$2,175,000, over three years. The first payment was received in September, 2012.

FINANCIAL INFORMATION

Internal and Budgeting Controls: City Management is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the City are protected from loss, theft, or misuse and to ensure that adequate accounting data are compiled to allow for the preparation of financial statements in conformity with accounting principles generally accepted in the United States of America. The internal control structure is designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that: (1) the cost of controls should not exceed the benefits likely to be derived; and (2) the valuation of costs and benefits requires estimates and judgments by management.

In addition, the City maintains budgetary controls. The objective of these budgetary controls is to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the City Council. Activities of the General Fund, Special Revenue Funds, Debt Service Funds, Capital Projects Funds, Enterprise Funds, and Internal Service Funds are included in the annual appropriated budget. A Five-Year Financial Plan, or Capital Improvement Plan, is also adopted for the Capital Projects. The level of budgetary control (that is, the level at which expenditures cannot legally exceed the appropriated amount) is established by function and activity within an individual fund. See Note 1 to the financial statements for further information on budgets and budgetary accounting.

As demonstrated by the statements and schedules included in the Financial section of this report, the City continues to meet its responsibility for sound financial management.

ECONOMIC FACTORS

The City of Scotts Valley is located in Santa Cruz County, approximately 75 miles south of San Francisco. The unemployment rates for the City of Scotts Valley, the County of Santa Cruz, and the State of California as of June for the last five fiscal years are shown below. As reflective of the national economy, all three rates increased dramatically in 2009. However, Scotts Valley's 2012 rate is 52% lower than the County rate and 55% lower than the State rate.

<u>June 30,</u>	<u>Unemployment Rate</u>		
	<u>Scotts Valley</u>	<u>Santa Cruz County</u>	<u>California</u>
2008	2.6%	6.1%	7.0%
2009	4.7%	10.6%	11.6%
2010	5.4%	11.2%	12.2%
2011	5.5%	11.4%	12.1%
2012	4.8%	10.0%	10.6%

The average and median prices of single-family homes decreased substantially for the second straight year, another reflection of the national economy. Average prices have dropped 22% from five years ago. Property values do not have as much an impact on the City's property tax revenue as other cities in Santa Cruz County because the City is a low property tax city, which means that the City receives less than 7% of the assessed property taxes. Below is a table of the average and median sales prices of houses sold in Santa Cruz County as of June for each of the last five years.

<u>June 30,</u>	<u>Single-Family Homes</u>			
	<u>Average Price</u>	<u>Increase (Decrease) Over (Under) Prior Year</u>	<u>Median Price</u>	<u>Increase (Decrease) Over (Under) Prior Year</u>
2008	\$684,996	(23.0%)	\$610,000	(19.8%)
2009	569,814	(16.8%)	519,000	(14.9%)
2010	544,321	(4.5%)	503,750	(2.9%)
2011	627,248	15.2%	545,000	8.2%
2012	531,649	(15.2%)	495,000	(9.2%)

OTHER INFORMATION

Independent Audit: The Government Code requires an annual audit by independent certified public accountants selected by the City Council. This requirement has been complied with. The auditors' unqualified opinion has been included in the financial section of this report. The City is also required to undergo an annual single audit in conformity with the provisions of the Single Audit Act and the U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments and Non-Profit Organizations, unless exempt. The auditor's reports related specifically to the Single Audit Act are included in a separate Single Audit Report.

Awards: The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Scotts Valley for its comprehensive annual financial report for the fiscal year ended June 30, 2011. The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standard for preparation of state and local government financial reports.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report (CAFR), whose contents conform to program standards. Such CAFR must satisfy both accounting principles generally accepted in the United States of America and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. The City of Scotts Valley has received a Certificate of Achievement for the last nineteen consecutive years. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to GFOA.

There has been a change in the eligibility requirements for the Certificate of Award for Outstanding Financial Reporting from the California State Municipal Finance Officers (CSMFO) for Comprehensive Annual Financial Reports. If cities submit and receive the GFOA Certificate of Achievement for Excellence in Financial Reporting, they cannot apply for the CSMFO Certificate. Because the City of Scotts Valley receives the GFOA Certificate, the City no longer applies for the CSMFO Certificate.

ACKNOWLEDGMENTS

The preparation of this report could not have been accomplished without the productive and professional endeavors of Laurie Grundy and the Finance Department staff. I wish to express my appreciation to them.

In closing, the leadership and support of the City Council were essential to the preparation of this report.

Respectfully submitted,



Stephen H. Ando
City Manager

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LIST OF PRINCIPAL OFFICIALS

JUNE 30, 2012

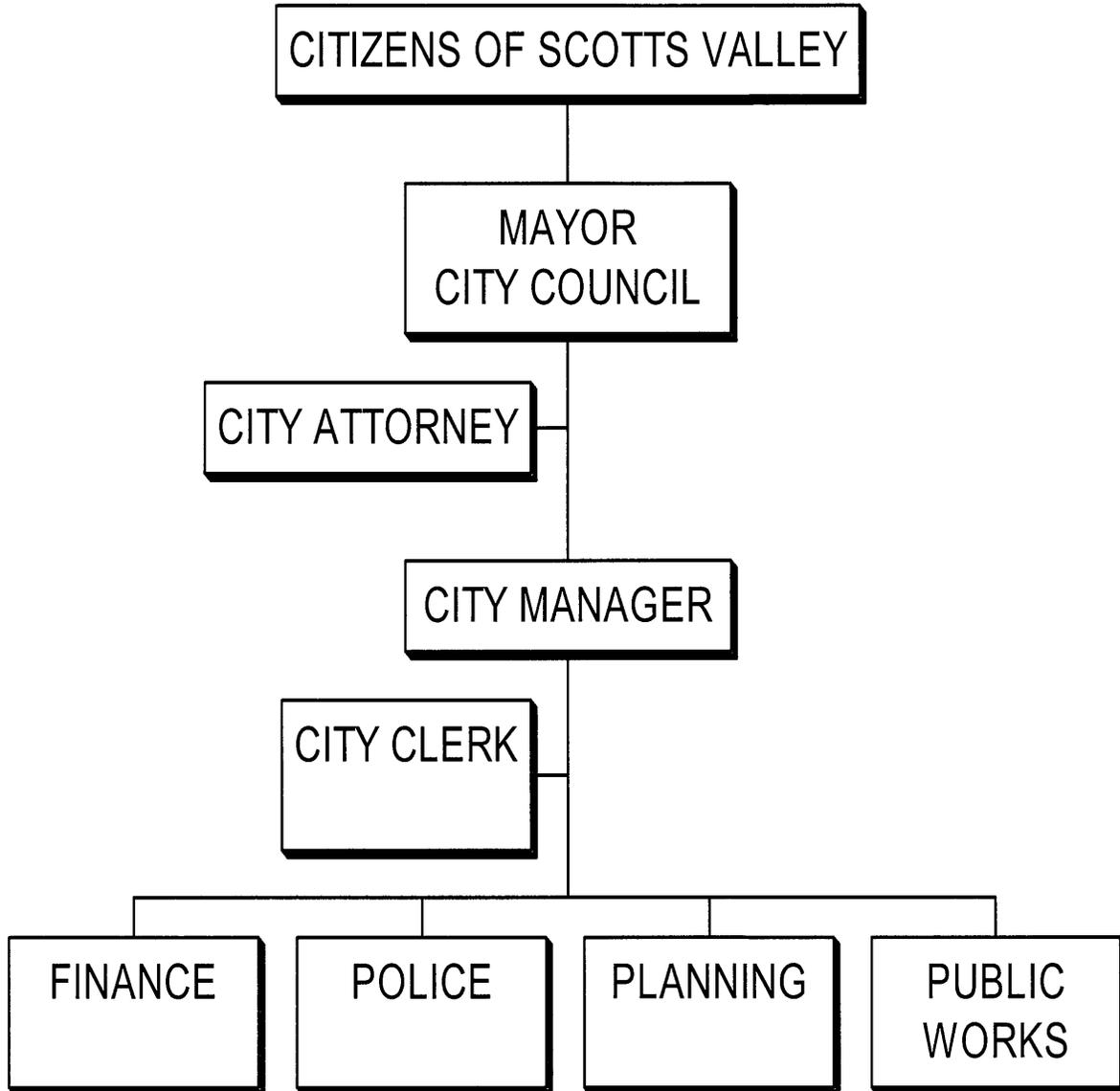
CITY COUNCIL MEMBERS

Donna Lind	Mayor
Randy Johnson	Vice Mayor
Stephany E. Aguilar	Councilmember
Dene Bustichi	Councilmember
Jim Reed	Councilmember

CHIEF ADMINISTRATIVE PERSONNEL

Stephen Ando	City Manager/ Finance Director
Kirsten Powell	City Attorney
Tracy Ferrara	City Clerk
John Weiss	Chief of Police
Ken Anderson	Director of Public Works / City Engineer
Corrie Kates	Community Development Dir / Deputy City Manager

CITY OF SCOTTS VALLEY
ORGANIZATION CHART



Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Scotts Valley
California

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2011

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



Linda C. Danison

President

Jeffrey R. Enow

Executive Director



FINANCIAL SECTION

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C. G. UHLENBERG LLP

CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

INDEPENDENT AUDITORS' REPORT

To the Members of City Council
City of Scotts Valley, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Scotts Valley, California (the "City") as of and for the year ended June 30, 2012, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City, as of June 30, 2012, and the respective changes in financial position, and, where applicable, cash flows thereof or the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 7, 2013, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information as listed in the Table of Contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic



financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's financial statements as a whole. The introductory section, combining and individual nonmajor fund financial statements, and statistical section, are presented for purposes of additional analysis and are not a required part of the financial statements. The combining and individual nonmajor fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

CG Uhlenberg LLP

August 7, 2013

Redwood City, California

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the City of Scotts Valley's annual financial report presents the City's discussion and analysis of its financial performance during the fiscal year ended June 30, 2012. Please read it in conjunction with the transmittal letter at the front of this report and the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

Two events during the year had a large impact on the financial statements. Per California law, redevelopment agencies were eliminated effective February 1, 2012. Therefore, only seven months of activity of the Scotts Valley Redevelopment Agency is presented in these financial statements. The effect of this is discussed further in this Management's Discussion and Analysis and in the footnotes to the financial statements. The other event was the issuance of \$4,460,000 in pension obligation bonds at the end of the fiscal year. The proceeds were used to pay off the side fund liability to the California Public Employees Retirement System.

The City's assets exceeded liabilities at June 30, 2012, by \$56,792,015. The current year change in net assets was a decrease of \$3,353,297. Of the total net assets, \$37,224,634 was invested in capital assets (net of related debt) and \$11,466,190 had restrictions on their use leaving \$8,101,191 as unrestricted. The current decrease in City net assets is a combination of the governmental activities decreasing \$2,360,474 and the business-type activities decreasing \$992,823.

As of June 30, 2012, the City's governmental funds (General Fund, special revenue funds, debt service funds, and capital project funds) had a combined fund balance of \$11,631,146, a decrease of \$1,158,468 from the previous year. This was primarily due to a decrease in the General Fund of \$1,361,784 before extraordinary loss. The General Fund was negatively affected by the elimination of redevelopment agencies. Of the total City governmental fund balance, \$7,515,172 was restricted, \$1,474,699 was assigned, and \$2,641,275 was unassigned.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of four parts: management's discussion and analysis (this section), the basic financial statements, required supplementary information, and an optional section that presents combining statement for non-major governmental funds. The basic financial statements include two kinds of statements that present different views of the City.

- The first two statements are government-wide financial statements that provide both long-term and short-term information about the City's overall financial status.
- The remaining statements are fund financial statements that focus on individual parts of the City government, reporting the City's operations in more detail than the government-wide statements.
 - The governmental funds statements tell how general government services such as public safety were financed in the short term as well as what remains for future spending.
 - Proprietary fund statements offer both short-term and long-term financial information about the activities the government operates like businesses, such as the sewer system.
 - Fiduciary fund statements provide information about the financial relationships (such as special assessment bond funds) in which the City acts solely as a trustee or agent for the benefit of others, to whom the resources in question belong.

OVERVIEW OF THE FINANCIAL STATEMENTS (continued)

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed information. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements. In addition to these required elements, the City included a section with combining statements that provide details about the City’s non major governmental funds, each of which are added together and presented in single columns in the basic financial statements.

Figure 1 below summarizes the major features of the City’s financial statements, including the portion of the City government they cover and the types of information they contain. The remainder of this overview section of management’s discussion and analysis explains the structure and contents of each of the statements.

Figure 1
Major Features of the City’s Government-wide and Fund Financial Statements

	<u>Government-wide Statements</u>	<u>Governmental Funds</u>	<u>Proprietary Funds</u>	<u>Fiduciary Funds</u>
Scope	Entire City government (except fiduciary funds) and the City’s component units	The activities of the City that are not proprietary or fiduciary	Activities the City operates similar to private businesses	Instances in which the City is the trustee or agent for someone else’s resources
Required financial statements	Statement of net assets Statement of activities	Balance sheet, Statement of revenues, expenditures, and changes in fund balances	Statement of net assets Statement of revenues, expenses, and changes in net assets Statement of cash flows	Statement of fiduciary net assets Statement of changes in fiduciary net assets
Accounting basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus	Accrual accounting and economic resources focus
Type of asset/liability information	All assets and liabilities, both financial and capital, and short-term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets included	All assets and liabilities, both financial and capital, and short-term and long-term	All assets and liabilities, both short-term and long-term
Type of inflow/outflow information	All revenues and expenses during the year, regardless of when cash is received or paid	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and payment is due during the year or soon thereafter	All revenues and expenses during the year, regardless of when cash is received or paid	All revenues and expenses during the year, regardless of when cash is received or paid

Government-wide Statement

The government-wide statements report information about the City as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the government’s assets and liabilities. All of the current year’s revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

OVERVIEW OF THE FINANCIAL STATEMENTS (continued)

The two government-wide statements report the City's net assets and how they have changed. Net assets (the difference between the City's assets and liabilities) is one way to measure the City's financial health, or position. Over time, increases or decreases in the City's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.

The government-wide financial statements of the City are divided into three categories:

- **Government activities:** Most of the City's basic services are included here, such as the police, public works, planning, building, park/street maintenance, and general administration. Various taxes, franchise fees, service charges, and investment earnings finance most of these activities.
- **Business-type activities:** The City charges fees to customers to help cover the cost of certain services it provides. The City's sewer system and recreation programs are included here.
- **Component units:** The City includes three other entities in its report - the Scotts Valley Redevelopment Agency, the Scotts Valley Public Financing Authority, and the Scotts Valley Parks and Recreation Advocates. Although legally separate, these "component units" are important because the City is financially accountable for them.

Fund Financial Statements

The fund financial statements provide more detailed information about the City's most significant funds, not the City as a whole. Funds are accounting devices that the City uses to keep track of specific sources of funding and spending for particular purposes. Some funds are required by State law and by bond covenants. The City Council establishes other funds to control and manage money for particular purposes such as capital project grant funds or to show that it is properly using certain restricted taxes such as gas tax revenues.

The City has three kinds of funds:

- **Government funds:** Most of the City's basic services are included in government funds, which focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, there is additional information at the bottom of the governmental funds statement, or on the subsequent page, that explains the relationship (or differences) between them.
- **Proprietary funds:** Services for which the City charges customers a fee are generally reported in proprietary funds. Proprietary funds, like the government-wide statements, provide both long- and short-term financial information. The City's enterprise funds (one type of proprietary fund) are the same as its business-type activities, but provide more detail and additional information, such as cash flows. Internal service funds (the other kind of proprietary fund) report activities that provide supplies and services for the City's other programs and activities, such as the City's dental insurance program.
- **Fiduciary funds:** The City is the trustee for some bondholders and fiduciary for others of the City's limited obligation improvement bonds associated with various special assessment districts within the City. The City is also responsible for other assets that, because of a trust arrangement, can be used for their intended purposes. All of the City's fiduciary activities are reported in a separate statement of fiduciary net assets and a statement of changes in fiduciary net assets. These activities are excluded from the City's government-wide financial statements because the City cannot use these assets to finance its operations.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

The following analysis pertains to the Government-wide statements as described above in the overview of the financial statements.

Net Assets: A condensed presentation of the City's net assets shown below totals \$56,792,015 as of June 30, 2012. This is a decrease of \$3,353,297, or 5.6%, from the previous year. It is a combination of a decrease in total assets of \$15,011,885 and a decrease in total liabilities of \$11,658,588. The full Statement of Net Assets can be seen on Page 15.

City of Scotts Valley Net Assets (in thousands of dollars)

	Governmental Activities		Business-type Activities		Total		Total Percent Change
	2012	2011	2012	2011	2012	2011	
Current and other assets	\$19,149	\$17,766	\$6,323	\$ 6,687	\$25,472	\$24,453	4.2%
Capital assets, net	33,013	48,444	14,717	15,317	47,730	63,761	(25.1%)
Total assets	52,162	66,210	21,040	22,004	73,202	88,214	(17.0%)
Long-term debt outstanding	12,010	22,304	429	330	12,439	22,634	(45.0%)
Other liabilities	3,636	5,029	335	405	3,971	5,434	(26.9%)
Total liabilities	15,646	27,333	764	735	16,410	28,068	(41.5%)
Net assets:							
Invested in capital assets, net or related debt	22,507	27,040	14,717	15,317	37,224	42,357	(12.1%)
Restricted	9,168	9,264	2,299	2,299	11,467	11,563	(0.8%)
Unrestricted	4,841	2,573	3,260	3,653	8,101	6,226	30.1%
Total net assets	\$36,516	\$38,877	\$20,276	\$21,269	\$56,792	\$60,146	(5.6%)

The main increases (decreases) in total assets were as follows:

Cash and Investments	(\$3,209,543)
Advances to Redevelopment Successor Agency	5,755,044
Cash and Investments with Fiscal Agents and Trustees	(1,034,124)
Capital Assets, net of depreciation	(16,030,159)

The decrease in cash is a combination of the General Fund (\$1,619,896) and the elimination of the Redevelopment Agency (\$970,196). As stated above, expenditures exceeded revenues in the General Fund. The remaining variances above all relate to the elimination of the Redevelopment Agency. In 2011 the advances to the Redevelopment Agency in the governmental activities offset and did not show in the City-wide statements. With the Redevelopment Agency being shown separately as a private purpose trust fund, the advances are now presented in the City-wide statements. The cash and investments with fiscal agents and trustees and the capital assets are also now shown in the private purpose trust fund rather than the City-wide statements.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (continued)

The main increases in total liabilities were as follows:

Accounts Payable	(\$1,049,605)
Long-Term Debt	(10,195,365)

The decrease in accounts payable relates to the remodel of an existing building into the Scotts Valley Branch Library. A large construction payment to the contractor was accrued at the end of fiscal year 2011 and was paid at the beginning of fiscal year 2012. The decrease in long-term debt once again relates to the elimination of the Redevelopment Agency which is now shown as a private purpose trust fund.

Changes in Net Assets: City-wide the change in net assets went from a decrease of \$672,663 in fiscal year 2011 to a decrease of \$3,333,456 in fiscal year 2012. This is a result of total revenues decreasing \$962,649, or 5.4%, and total expenses increasing \$1,698,144, or 9.2%. A further analysis is shown below.

	<u>2012</u>	<u>2011</u>	<u>Percent Change</u>
Program Revenues	\$ 4,478	\$ 6,279	(28.7%)
General Revenues	12,403	11,565	7.2%
Governmental Expenses	(15,532)	(14,668)	(5.8%)
Business-type Expenses	<u>(4,702)</u>	<u>(3,849)</u>	(22.2%)
Net Increase (Decrease)	<u>\$ (3,353)</u>	<u>\$ (673)</u>	(398.2%)

On the next page is a current and prior fiscal year recap of the changes in net assets. The full Statement of Activities can be seen on Page 16.

Revenues:

Program revenues decreased \$1,801,157, primarily in the governmental activities under Capital Grants and Contributions for Redevelopment. Capital grants are not consistent and can vary widely from year to year. Redevelopment decreased \$2,422,614 primarily from amounts received from the County of Santa Cruz for the Scotts Valley Branch Library Project. Starting in fiscal year 1997-98 per an agreement with the County of Santa Cruz, the Scotts Valley Redevelopment Agency began setting aside funds for a Scotts Valley Branch Library. The funds were held by the County. The Redevelopment Agency drew down those funds from the County as the construction of the Library progressed.

There were no material variances in program revenues for the business-type activities.

General revenues increased \$838,508. Of that amount, governmental activities decreased \$35,251 and business-type activities increased \$873,759. Although governmental activities decreased only \$35,251, there were large offsetting variances. Property taxes decreased \$3,534,004 due to the elimination of redevelopment agencies. "Transfers out" increased \$903,909 mainly due to transfers of pension obligation bond proceeds to the enterprise funds to pay off their side fund liabilities. The business-type activities increase is mainly due to the increase in "transfers in" of the pension obligation bond proceeds.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (continued)

**City of Scotts Valley
Change in Net Assets**
(in thousands of dollars)

	Governmental Activities		Business-type Activities		Total		Total Percent Change
	2012	2011	2012	2011	2012	2011	
Program revenues:							
Charges for services	\$879	\$551	\$2,447	\$2,512	\$3,326	\$3,063	8.6%
Operating grants	670	552	0	0	670	552	21.4%
Capital grants	344	2,645	137	20	481	2,665	(82.0%)
General revenues:							
Property tax	2,143	5,677	0	0	2,143	5,677	(62.3%)
Sales tax	1,887	2,108	0	0	1,887	2,108	(10.4%)
Other taxes	3,271	3,251	0	0	3,271	3,251	0.6%
Investment earnings	86	44	14	30	100	74	35.1%
Miscellaneous	450	454	0	0	450	454	(0.9%)
Extraordinary Item	4,553	0	0	0	4,553	0	n/a
Total revenues	14,283	15,282	2,598	2,562	16,881	17,844	(5.4%)
Expenses:							
General government	5,563	1,617	0	0	5,563	1,617	244.0%
Public safety	4,855	4,454	0	0	4,855	4,545	6.8%
Planning & building	1,186	1,178	0	0	1,186	1,178	0.7%
Public works	2,961	2,965	0	0	2,961	2,965	(0.1%)
Redevelopment	0	3,036	0	0	0	3,036	(100.0%)
Interest on debt	967	1,327	0	0	967	1,327	(27.1%)
Wastewater	0	0	3,291	2,767	3,291	2,767	18.9%
Recreation	0	0	1,411	1,082	1,411	1,082	30.4%
Total expenses	15,532	14,668	4,702	3,849	20,234	18,517	9.3%
Excess or (Deficiency)	(1,249)	614	(2,104)	(1,287)	(3,353)	(673)	(398.2%)
Transfers	(1,111)	(207)	1,111	207	0	0	
Change in Net Assets	(\$2,360)	\$407	(\$993)	(\$1,080)	(\$3,353)	(\$673)	(398.2%)

Net Cost of Services: The table on the next page presents the total cost of each of the City's governmental and business-type activities as well as each activity's net cost (total cost less fees generated by the activities and intergovernmental aid). The net cost shows the financial burden that was placed on the City's taxpayers by each of these functions.

For governmental activities, the total costs of \$15,532,610 were offset by charges for services (\$879,345), operating grants/contributions (\$670,329), and capital grants/contributions (\$344,033), bringing the net cost of services down to \$13,638,903. The large increase in general government, wastewater, and recreation relate to the payoff of the City's side fund liability with the Public Employees Retirement System (PERS). As mentioned at the beginning of this discussion and analysis, the City issued pension obligation bonds at near the end of the fiscal year. The proceeds from those bonds were used to pay off the side fund liability to the PERS. In 2003 PERS combined all entities with less than 100 employees for determining their retirement contribution rates. To account for the various funding status of the entities, PERS established a side fund for each agency which could either be a surplus or a deficit. Rather than pay off the deficit with annual contributions, the City paid it off with the bond proceeds. The side fund payoffs were \$3,497,982 in the general government, \$487,034 in wastewater, and \$290,248 in recreation. The low interest rates of the bonds will save the City approximately \$1.3 million over the next twelve years.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (continued)

City of Scotts Valley
Net Cost of Governmental and Business-Type Activities
(in thousands of dollars)

	Total Cost			Net Cost		
	of Services		Percent Change	of Services		Percent Change
	2012	2011		2012	2011	
General Government	\$5,563	\$1,617	244.0%	\$5,312	\$1,568	238.8%
Public Safety	4,855	4,545	6.8%	4,524	4,320	4.7%
Planning & Building	1,186	1,178	0.7%	795	896	(11.3%)
Public Works	2,961	2,965	(0.1%)	2,041	2,216	(7.9%)
Redevelopment	0	3,036	(100.0%)	0	593	(100.0%)
Interest on L-T Debt	967	1,327	(27.1%)	967	1,327	(27.1%)
Total	<u>\$15,532</u>	<u>\$14,668</u>	5.9%	<u>\$13,639</u>	<u>\$10,920</u>	24.9%
Wastewater	\$3,291	\$2,767	18.9%	\$1,518	\$1,088	39.5%
Recreation	1,411	1,082	30.4%	600	229	162.0%
Total	<u>\$4,702</u>	<u>\$3,849</u>	22.2%	<u>\$2,118</u>	<u>\$1,317</u>	60.8%

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The following analysis pertains to the fund financial statements as described above in the overview of the financial statements.

There are no restrictions, commitments, or other limitations that would significantly affect the availability of fund resources for the future.

To provide an overview of the City's funds, below is a table showing the increases and (decreases) to total assets, liabilities, revenues, and expenditures of the City fund types from fiscal year 2011 to 2012. The total revenues and expenditures do not include any "other financing sources (uses)."

	Increase (Decrease) from Prior Year			
	Assets	Liabilities	Revenues	Expenditures
General Fund	(\$3,580,503)	\$16,214	(\$523,904)	\$4,543,536
Special Rev Funds	(1,754,818)	22,415	(641,350)	(901,207)
Debt Service Funds	(1,707,044)	(4,284,501)	(2,575,234)	(3,472,670)
Capital Project Funds	(671,693)	(2,309,718)	(2,534,939)	(5,884,746)

The General Fund budget is discussed below under the "Budgetary Highlights".

The largest variances other than the General Fund are the assets, revenues, and expenditures in the Special Revenue Funds; assets, liabilities, revenues, and expenditures in both the Debt Service Funds and Capital Projects Funds.

The decrease in the Special Revenue Funds assets, revenues, and expenditures is due to the elimination of the Redevelopment Agency. There was only seven months of activity recorded for the Redevelopment Agency which was dissolved effective February 1, 2012. Adding to the deficit in expenditures was the former affordable housing fund of the Redevelopment Agency purchasing a parcel of undeveloped land in fiscal year 2011 for \$725,000. There were no land purchases in fiscal year 2012.

All of the decreases in the Debt Service Funds and the Capital Projects Funds are due to the elimination of the Redevelopment Agency. Adding to the large deficit in the Capital Projects Funds expenditures was \$5,823,170 of capital outlay costs in the Redevelopment Agency in fiscal year 2011 for the renovation of an existing building into the Scotts Valley Branch Library.

GENERAL FUND BUDGETARY HIGHLIGHTS

Total revenues were \$535,869 (8.1%) over budget. The main reason for this is due to three accounts being over budget: sales tax (\$202,720), transient occupancy tax (\$232,605), and cost reimbursements (\$181,833) from the Successor Agency. Sales tax is over budget mainly due to service stations and the increase in the price of gasoline. Transient occupancy tax is over budget mainly due to a new company taking over management of the Scotts Valley Hilton Hotel in January 2011. This has helped with the overall increase in transient occupancy tax for the City. With the elimination of redevelopment agencies the City now acts as the Successor Agency to the former redevelopment agency. The City is reimbursed for its administrative costs.

On the expenditure side, the General Fund was over the original budget by \$4,268,296. The main variance is in general government being \$3,679,703 over budget. As stated above, the City paid off its side fund liability to PERS. The General Fund portion was \$3,497,982. The funds for this were transferred in from the bond proceeds in the Pension Obligation Bond Fund. Other accounts related to salaries were over budget because of the elimination of the redevelopment agency. The salaries of the positions in the redevelopment agency were transferred to the General Fund.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets: A recap of the City's capital assets, net of accumulated depreciation, is shown in the table below. The City-wide decrease (net of depreciation) is \$16,030,159, or 25.1%. The governmental activities had capital assets additions of \$610,649. Current year depreciation of \$1,361,264 brought capital assets to a net decrease of \$750,615. The main capital asset additions were improvements to the Scotts Valley Branch Library (\$288,813) and purchase of a new computerized records management system in the Police Department (151,829). The business-type activities had capital assets additions of \$160,047 while depreciation of \$759,550 created a net decrease of \$599,503.

City of Scotts Valley Capital Assets, Net of Depreciation (in thousands of dollars)

	Governmental Activities		Business-type Activities		Total		Total Percent Change
	2012	2011	2012	2011	2012	2010	
Land	\$7,012	\$14,808	\$429	\$429	\$7,441	\$15,237	(51.2%)
Buildings & Improvements	3,093	9,633	2,163	2,295	5,256	11,928	(55.9%)
Equipment	734	885	477	468	1,211	1,353	(10.5%)
Infrastructure	21,938	22,887	11,517	12,042	33,455	34,929	(4.2%)
Outfall Agreement	0	0	80	83	80	83	(3.6%)
Construction in Progress	236	231	51	0	287	231	24.2%
Total	<u>\$33,013</u>	<u>\$48,444</u>	<u>\$14,717</u>	<u>\$15,317</u>	<u>\$47,730</u>	<u>\$63,761</u>	(25.1%)

More detailed information about the City's capital assets is presented in Note 4 to the financial statements.

Long-term Debt: A recap of the City's long-term debt is shown below. Total long-term debt decreased \$10,379,330, or 44.1%. The main changes during the year were annual debt service payments on long-term debt, the issuance of \$4,460,000 of pension obligation bonds, and increases in both accrued compensated absences and net OPEB obligation. The net OPEB obligation is an actuarially determined amount for Other Post Employment Benefits in accordance with GASB (Governmental Accounting Standards Board) Statement 45. More detailed information about the City's long-term debt is presented in Note 5 to the financial statements.

**City of Scotts Valley
Outstanding Debt**
(in thousands of dollars)

	Governmental Activities		Business-type Activities		Total		Total Percent Change
	2012	2011	2012	2011	2012	2011	
Certificates of Participation	\$6,046	\$7,154	\$ 0	\$ 0	\$6,046	\$7,154	(15.5%)
Pension Obligation Bonds	4,460	0	0	0	4,460	0	n/a
Installment Notes	0	125	0	0	0	125	(100.0%)
Tax Allocation Bonds	0	5,365	0	0	0	5,365	(100.0%)
Lease Revenue Bonds	0	8,760	0	0	0	8,760	(100.0%)
Accrued Comp							
Absences	832	748	175	175	1,007	923	9.1%
Net OPEB Obligation	<u>1,290</u>	<u>928</u>	<u>355</u>	<u>262</u>	<u>1,645</u>	<u>1,190</u>	38.2%
Total	<u>\$12,628</u>	<u>\$23,080</u>	<u>\$530</u>	<u>\$437</u>	<u>\$13,158</u>	<u>\$23,517</u>	(44.0%)

NEXT YEAR'S BUDGETS AND RATES

The City continues to have a hiring freeze. As positions become vacant, they are reviewed before deciding whether to fill the vacancy or not. The two exceptions are emergency dispatch and police officers. Police officer positions are capped at two vacancies. The 2012-13 General Fund expenditure budget was approved with a \$529,280 (6.5%) increase. This was due to the salaries previously budgeted in the Redevelopment Agency now being budgeted in the General Fund. This was offset by a revenue budget with a \$1,469,300 (22.1%) increase. The main new items in the revenue budget included a payment Santa Cruz County (\$725,000) due to the City winning its lawsuit for additional property taxes. In addition, administrative cost reimbursements (\$190,000) for the City acting as the Successor Agency to the former Redevelopment Agency were included in the 2012-13 budget.

CalPERS has provided the City with next year's rate and a projected 2012-13 rate. A recap of the retirement rates by fiscal year is shown below. The decrease effective in the 2012-13 fiscal year is due to the City issuing pension obligation bonds to pay off its side fund obligation. The savings from issuing these bonds is approximately \$1.3 million over the next twelve years.

Fiscal Year	Miscellaneous Group	Safety Group	
2009-10	16.176%	29.381%	Actual
2010-11	16.200%	29.500%	Actual
2011-12	20.258%	33.960%	Actual
2012-13	13.914%	23.681%	Actual
2013-14	14.166%	24.188%	Projected

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide the citizens, taxpayers, customers, investors, and creditors of Scotts Valley with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional information, contact the City of Scotts Valley Finance Department, 1 Civic Center Drive, Scotts Valley, CA 95066.