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CALL TO ORDER

[Time: 00:00:00]

Mayor Ortega: We will resume the Work Study portion of our meeting as agendized. At this point I do want to point out that our City Council is all present, the Charter Officers are present, and we are ready to proceed with the information from our City Treasurer on the year-end financial report for 2021-2022. Please proceed.

1. FISCAL YEAR END 2022 FINANCIAL REPORT

[Time Stamp: 00:00:24)

City Treasurer Sonia Andrews: Than you Mayor. Thank you, council. This presentation is our year-end financial report for fiscal year 22. Next slide.

Our fiscal year 22 ended on June 30th. It takes a couple months to perform all the year-end closings to produce preliminary results and so we presented those preliminary results for the General Fund to Council on August 26th. It then takes another three months to go through the audit process and complete the year-end report. The audit was completed on October 26 and presented to the Audit Committee in November. On December 16, the auditors presented their audit report to Council and tonight’s presentation is the last step in our year-end process. Next slide.

Before I begin, I want to mention that our fiscal year 22 report has been submitted to the GFOA for the Excellence in Financial Reporting Award. Like the Mayor mentioned earlier, this is the 50th consecutive

year that we have submitted for this award and it is a milestone that we are incredibly proud of and I'd like to recognize and thank our accounting director Anna Henthorn, our accounting managers Sarah Delgado and Chris Downey. They're here in the audience and the accounting team for this accomplishment which comes with much hard and work and dedication. Next slide.
So I will be highlighting numbers from my year-end report and also helping you understand what it says about the city's financial health. The audited annual financial report is a very important document. Aside from being the City's official audited financial statement, it provides a lot of detailed information about the City's finances and is used by our bond rating agencies lenders and investors to assess our financial health. Next slide.

In order to understand what the financial report is saying about the City's financial health, we look at three areas. First, we look at financial conditions – do our revenues cover expenditures to maintain our service levels. Are we spending within our means? Do we have strong cash balances and liquidity to pay our bills or do we have cash flow problems? Is our balance sheet strong? We look at financial capacity. Do we have a manageable debt burden on our long-term liabilities? Or are we over leveraged. Do we have the ability to finance and fund our capital needs without shifting that burden to the future. And finally, we look at financial resiliency. Do we have sufficient and adequate reserves and budget flexibility to handle economic downturns and unforeseen events without straining our finances and having to use our operating money.

Our year-end report for fiscal year 22 I'm happy to report shows that the city of Scottsdale is financially healthy and strong. And let me go over some numbers to show that. Next slide.

So first of all our financial condition for fiscal year 22, our operating revenues adequately covered our operating expenditures across pretty much all funds. Let's take a look at the general fund first. Next slide.

So the General Fund is our primary operating fund. We collected 37.6 million or 26 percent more in sales tax than we expected. Sales tax is the largest source of revenues in the General Fund. Now as I've discussed earlier in previous presentations, we can't get too excited about t his because the excess tax collection is due to the federal government's stimulus actions that supercharged the economy creating what we call the pandemic spending spree. And this is not unique to Scottsdale. It is happening across all cities in the nation. And then you add inflation, that drives up the prices. Most cities are experiencing excess tax collections like us so we do not expect this to continue each year. And we look at these excesses as one-time revenues. However we did get that in fiscal year 22. We also received 14.6 million from the American Rescue Plan Act. Those are the stimulus funds allocated to us which we used for some public safety expenditures and that allowed us to free up some of our General Fund dollars for other one-time needs.

On the expenditure side in the General Fund, we made a one-time 40 million dollar additional payment to pay down our Public Safety pension liability. Without that 40 million dollars, our General Fund operating expense is actually less than the 400 million you see there. Okay, next slide.

The next group of funds are our other governmental funds. Those are our dedicated revenue funds where the revenues are either legally restricted by State statute or by voter approval. Next slide.

Let's look at those. These are major categories of other governmental funds. We have a lot of smaller other governmental funds, but these are our major categories with all of these funds. Our transportation tax fund, Preserve tax fund, tourism fund, and our GO bond debt service fund. We saw positive revenue growth and our revenues adequately covered expenditures. Now I wanted to make a comment on the Preserve tax fund, which is the second two bars and the second column. The Preserve taxes collected are used for debt service. We typically do not see such a large excess of revenues over expenditures. Only during the last two years with this pandemic spending spree, did we see such an excess. If we go into a recession, the Preserve tax revenues may dip below the expenditures. And unlike our transportation tax fund and our tourism fund where we can reduce expenditures in response to reduced revenues, in the Preserve tax fund, the expenditures have fixed debt service and we won't be able to reduce expenditures in response. So we maintain reserves to ensure that we have enough tax collections to pay our debt. So when we have years of excess like that in the Preserve tax fund, we typically put in those reserves to ensure future years we can cover out of that service. Next slide.

The last group of funds is our enterprise funds. And these are our business type operations that are 100 percent fee supported. They do not rely on the General Fund and they're not subsidized by tax dollars or General Fund. Next slide.

Now these are enterprise operations and this slide shows the net operating income or actually loss in the sewer fund, which I'll talk about a little bit later. For fiscal year 22, we had positive net operating income in all our funds except the sewer fund operating income is operating revenues minus operating expenses, which includes depreciation expense. So for the sewer fund, what this is telling us is that our sewer rates are generating enough revenues to cover out-of-pocket expenses and we're able to pay our bills to maintain our system, but it is not sufficient to cover depreciation expense which is the rate at which our assets of depreciation and eventually depreciating and eventually needing to be replaced. We are working on our utility rate adjustments right now for next fiscal year and we will make sure that our proposed rates that we bring forward to Council will cover not only just that out-of-pocket expense, but also future replacement for our capital assets as well. But otherwise our water fund is healthy with an 18 percent operating margin. Solid waste and airport funds are also healthy with positive operating margins. Next slide.

[Time Stamp: 00:09:05]

Now on to our balance sheet. Our balance sheet for fiscal year 22 is strong and we also improved our balance sheet a little bit on the short-term assets. Mostly cash, we increased that from 1.3 billion to 1.4 billion mostly due to the excess sales tax collections. Next is our long-term assets. There are capital assets that increased by a hundred million from 6.1 billion to 6.2 billion. We'll talk a little bit more about that later. Liabilities decreased by 200 million to 1.5 billion. So overall we improved our net position, which is like our equity, by about 300 million. So capital assets and investment in our infrastructure is the largest asset and component of our balance sheet. 6.2 billion in netbook value of capital assets. Next slide.

56 of that netbook value of our capital assets is in the land that we own. Most of it is that open space which is our Preserve and also our street right-of-way. And netbook value is not market value. Network value is original cost or donated value. We don't depreciate land, so as you can see, we have an incredibly priceless valuable asset in the land that we own and the open space that we have. The other large categories of assets is our water and sewer systems and our street and storm drain systems. Our buildings and other assets are not as significant. Next slide.

Onto our liabilities. Our main long-term liabilities are our pension liabilities. And our debt with our pension liabilities actually decreased by a hundred and twelve million last year from 421.6 million to 309.6 million mainly due to the strong investment earnings in those plans in 2021. ASRS is the retirement plan for non-public safety employees. PSPRS is the public safety retirement plan. Now these PSPRS numbers – the decrease you see here does not reflect the 40 million extra payment we made, so we actually expect the liability to go down even further once that extra payment is factored into the actuarial calculations. So what this really shows you is that with a good investment year and good investment return, the pension liabilities can actually go down quite a but. But on the flip side, if there's a bad investment year and negative returns, that could really increase our pension liabilities. Next slide.

That is our other long-term liability. We maintain a very manageable debt profile with 832 million outstanding at June 30, 2022. Our larges debt outstanding are our Preserve debt and our water sewer debt. Preserve debt, as you know, is repaid from the Preserve taxes. Water sewer debt is repaid from water sewer rates. So our two largest debt balances do not rely on the General Fund. As you can see, we have only issued 48 million in the Bond 2019 debt. We haven't issued the whole 319 million yet. We issue that as we go along. In terms of how we construct the projects, we will be issuing more to Bond 2019 and water sewer debt this year. Next slide.

And this slide just shows you how much the significant capacity we have available to us to issue more GO debt if needed. The state statute limits the GO debt that we can issue. Under the six percent statutory limit, we still have 519 million more of capacity. Under the 20 percent statutory limit, we have 1.3 billion in capacity. We have plenty of capacity to issue debt without having to shift burden to the future. And all this debt, if we have to issue it, requires voter approval. We cannot just go out and issue it without voter approval. Next slide.

So we talked about financial condition of our revenues covering expenditures, our strong balance sheet and financial capacity. Our debt is manageable debt. And the final thing is financial resiliency which is the third indicator of our financial health. Financial resiliency is having enough reserves and budget flexibility to respond to economic downturns and unexpected events and as we talked about, as you know, we increased our policy reserves last year. So I'm happy to report that as of June 30, 2022, we met our new policy reserves as shown on this slide in our General Fund. Without stabilization emergency reserves, we have 83.2 million. That might sound like a very large number that's only 25 percent, or three months, of our operating expenses. In water and sewer, we have 67.2 million in reserves, that's also three months of operating expenses plus two percent of asset book value. That's because of the incredibly valuable assets in our water and sewer systems that we have to protect and ensure we have the money to respond to any emergencies. We have 46.1 million in debt service reserves and 7 million in other operating reserves. Next slide.

[Time Stamp: 00:14:44]

And this is my final slide. Finally, we maintained our AAA bond rating throughout fiscal year 22. A triple A bond rating is the highest rating that we can achieve. Rating agencies look for economic and revenue growth. They look for strong balance sheets. They look for manageable debt and liabilities. And they also look for strong financial management policies and practices. So I want to comment that the city's financial strength is not something that was achieved overnight, but rather through years of consistent and outstanding financial and budget management by Council and staff. So thank you Council for your strong financial leadership.

And so to conclude, our fiscal year 22 report shows that the city is in strong financial position heading into 2023 and 2024. However, as the City Treasurer, I must say that as we head into 23/24, we will be dealing with cost increases, inflation reduced consumer spending and probably a recession labor market challenges. Whatever challenges we have, at least we're starting off in a financially strong position and we believe that we can manage through the financial challenges we will be facing moving forward. So thank you and I can answer any questions that you may have.

Mayor Ortega: Well thank you very much and let's proceed to Councilwoman Whitehead.

[Time Stamp: 00:16:12]

Councilwoman Whitehead: I thank our City Treasurer team. This has been That was a really big change and it was one that you initiated – these reserves and I'm just really pleased with the financial position we're in, so thank you.

Mayor Ortega: Councilmember Graham.

Councilmember Graham: Sonia, thank you very much for the presentation. I would put some questions up in the next slide. I would cross them all out because you answered them. For our annual audit, we got a management letter. Is that right? Were there any comments for material weaknesses?

City Treasurer Sonia Andrews: Mayor, Councilmember Graham, I'm going to ask our accounting director to answer because I don't remember. There was nothing of significant substance, but I think there was some comments on that, so I'll have her come respond.

Accounting Director Anna Henthorn: Thank you. Hi there, Anna Henthorn, I'm the accounting director. The comment that we received was related to our purchasing card controls. There was some deficiencies in the oversight.

Councilmember Graham: Can you say a little more about that Anna?

Accounting Director Anna Henthorn: Yea, so there was – one of the samples that they selected, they did not the appropriate approvals from the supervisors to authorize those Procards. They were not done timely. So the approvals happened, but not early enough.

Councilmember Graham: Okay, but they did happen at some point by the appropriate person?

Accounting Director Anna Henthorn: That is correct.

Councilmember Graham: Was that considered a material weakness or significant deficiency that was considered – if it was not can you remind me how that was written --

Accounting Director Anna Henthorn: -- not significant deficiency, there was no issues with the financial statements. It was just on the internal controls.

Councilmember Graham: In those management letters, there's also other comments that they don't have to include in the management letter. But can you talk about them with management, were there any other comments that they brought up that did not –- included in the management letter --

Accounting Director Anna Henthorn: Okay, just a moment. Sorry.

Councilmember Graham: I apologize if you weren't totally ready. That's okay.

Accounting Director Anna Henthorn: Sorry, is this such a large packet.

Councilmember Graham: Maybe you could send it to us if you can't find it.

Accounting Director Anna Henthorn: We did provide this in the December meeting where the audit results were provided, so yes we can definitely – well this wouldn't actually probably be and that it would be more verbal communications and other comments for like improvements for operations and internal controls. Usually they provided all of that, but I'll definitely make sure that we provide the management letter to you. Well the management letter and the additional comments.

Councilmember Graham: Yes, can you send to the full council and mayor?

Accounting Director Anna Henthorn: Yes, absolutely.

[Time Stamp: 00:19:16]

Councilmember Graham: Okay a couple more questions. Sonia, how many weeks, and thank you Anna, how many weeks of operating expenses do you like to have of cash on hand.

City Treasurer Sonia Andrews: Mayor, Councilmember Graham. It is a little bit complicated question. We have about 800 million in cash and we have our operating needs vary depending on our debt payments. And you know so we have cash flow projections that we work with our investment advisor to ensure our available liquidity and availability to meet debt service and operating requirements are in our short-term portfolio. And then we have long-term portfolio where we invest the cash more long term

Councilmember Graham: Okay, I was just curious. If there is no magic answer, but I just interested in your philosophy and I'll sit down with you more and talk about that. Because I know that if we have too much cash sitting around and its not getting to work for us, we're not getting a return for taxpayers, but it's very basic isn't it.

City Treasurer Sonia Andrews: We don't have a policy where we – there is a lot of cash required for operations that we maintain and it's the whole cash management program that we have ensures that we have the liquidity and the –

Councilmember Graham: Oh I'm not concerned with liquidity, sufficient liquidity, I'm just concerned maybe there's too much liquidity. If we could put some to use making sure it's still working, just kind of your philosophy about cash management. But we don't have to talk more about that. My other last question, then that'll be the end of it, I promise Mayor. We have a – you said we have 2.7 billion dollars of depreciable assets.

City Treasurer Sonia Andrews: Can you repeat the question?

Councilmember Graham: We have 2.7 billion dollars of depreciable assets, do you have a percentage or a benchmark that you think we should be investing in our fixed assets to make sure we don't have a structural deficit? It's okay, if you – year, we can talk about it more, it's just some questions that came to mind.

City Treasurer Sonia Andrews: Sure, absolutely, Okay so our capital asset – each of our capital assets programs have studies that we do. So for example with our water and sewer program, through our rate study, the rate study incorporates the needed investment in those capital assets. The impact fee and the master plans and all those studies that we do that's how we determine how much we need to invest in those assets to maintain those assets. And there are somehow they're all interconnected in how we set our rates and how we determine the finances for the City.

Councilmember Graham: Very good. Well thank you for indulging me and we'll talk more about it when we have our meetings and we'll share with the resto the council. And I thank you, appreciate you for coming to the podi7um answering my questions. And Mr. Mayor thank you for allowing me to ask those questions.

Mayor Ortega: Excellent, I have just two comments. First of all the refinancing of certain notes and so forth is authorized by the Council every step of the way. And I think we let you test the market this coming quarter. Secondly the financial advisors, and as I understand it, two sort of like checkbook and an investment group that is expiring with Wells Fargo and a subsidiary spin off of them, so we'll have a chance to rebid that and see where the performance or lack of has been there. It tends to be a pretty solid relationship and there are several that can meet those kinds of fiduciary. I want to say not strength, but just to be able to be valuable partners with the City. So that's so to speak the checkbook and just like the CDs that we tend to manage in our own life, right? Especially with growing kids, you know that's got to be working for you.

Councilmember Graham: I think this council or the city has like an 850 credit score. We're pretty close to it right?

[Time stamp: 00:22:47]

Mayor Ortega: We're doing very well. With that, I don't see any other hands up. I look forward as we move forward. And this is the only work study item. With that I would request a motion to adjourn our work study.

Move to adjourn.

Mayor Ortega: I had a second from Mr. Graham. Accordingly ,please record your vote. We are adjourned. Thank you.