



BOROUGH OF STATE COLLEGE

FINANCIAL TREND MONITORING SYSTEM

August 1, 2011

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FINANCIAL TREND MONITORING

EXECUTIVE SUMMARY

trend has been identified as a key indicator

<u>INDICATORS</u>			
COMMUNITY			
Population			NEUTRAL
Age Cohorts			NEUTRAL
REVENUES			
General Fund Revenue			FAVORABLE
General Fund Revenue (constant dollars)			NEUTRAL
General Fund Revenue per capita			NEUTRAL
Real Estate Tax Revenue			FAVORABLE
Real Estate Tax Revenue (constant dollars)			FAVORABLE
Assessed Valuation			ALERT
Earned Income Tax Revenue			NEUTRAL
Earned Income Tax Revenue (constant dollars)			UNFAVORABLE
Earned Income Tax Revenue per capita			UNFAVORABLE
EXPENDITURES			
General Fund Expenditures			NEUTRAL
General Fund Expenditures (constant dollars)			NEUTRAL
General Fund Expenditures per capita			NEUTRAL
OPERATING POSITION			
General Fund Operating Performance			FAVORABLE
Unreserved General Fund Balance			FAVORABLE
DEBT STRUCTURE			
Outstanding Debt by Fund			NEUTRAL
Outstanding General Fund Debt per capita			FAVORABLE
General Fund Debt Service-% of Revenues			FAVORABLE

<u>Performance Indicators</u>	
	= trend is an indicator of positive financial health
	= trend is an indicator of negative financial health
	= trend is neither positive nor negative
	= trend should be analyzed in greater detail and action taken

Borough of State College

FINANCIAL TREND MONITORING SYSTEM

Introduction

A government's financial condition can be broadly defined as its ability to finance the services it provides to its citizens on a continuing basis. More specifically, financial condition refers to a government's ability to maintain existing services levels; withstand local and regional economic disruptions; and meet the demands of natural growth, decline and change. Evaluating a government's financial condition is a complex process that involves analyzing a variety of factors, some of which are difficult to quantify. The relationship between these factors adds to the complexity of the task. To facilitate the evaluation process, the International City/County Management Association (ICMA), in collaboration with the Government Finance Officers Association (GFOA) and other groups, developed the Financial Trend Monitoring System (FTMS.) The FTMS is a management tool that identifies key factors affecting financial condition and arranges them to enable objective measurement and analysis. A series of financial indicators were created which, when plotted over a period of time, can be used to monitor changes in financial condition and alert a government to future problems. Review and analysis of these trends is very helpful in understanding financial condition. The FTMS does not provide a single number, rating, or index to measure a government's financial health. Rather, it provides flags to identify existing and emerging financial problems, gives clues to their causes, and provides time to develop actions to remedy the problems.

Overview

While State College is viewed as a financially healthy community, an objective review and analysis of the factors impacting our financial condition is important in identifying trends and planning for the Borough's future. The Ad Hoc Tax Study Committee appointed to study the Borough's tax structure in 2005 discussed the need for this kind of data to assist with long range financial planning and decision making. Finance staff, with the assistance of an intern, implemented this project in 2008. Staff first reviewed the thirty-six financial indicators which comprise the FTMS. The following fifteen indicators were selected for use in monitoring changes in the Borough's financial condition:

Community

Population
Population Age Cohorts

Revenues

General Fund Revenue
General Fund Revenue Per Capita
Real Estate Tax Revenue
Assessed Valuation
Earned Income Tax Revenue
Earned Income Tax Revenue Per Capita

Expenditures

General Fund Expenditures
General Fund Expenditures Per Capita

Operating Position

General Fund Operating Performance
Unreserved General Fund Balances

Debt Structure

Total Outstanding Debt by Fund
Outstanding General Fund Debt Per Capita
General Fund Debt Service as a Percentage of General Fund Revenues

Data necessary to plot ten year trends for these indicators was gathered from a variety of local, regional, state and national sources. Graphs were prepared to visually illustrate the trend for each indicator. This data formed a baseline to be reviewed on an annual basis so that monitoring of the Borough's financial condition is an on-going process. The first FTMS report was presented to Council in August, 2008 and it has been updated annually since that time.

This report presents the Borough's financial trend data for the period 2001 through 2010. Further review and analysis of the trends can enhance our financial management and decision-making processes. It will help us answer questions such as: Can the Borough continue to pay for the services it is now providing? Are there sufficient reserves available for financing emergencies or unforeseen contingencies? Is there adequate financial flexibility to allow the Borough to adjust to change?

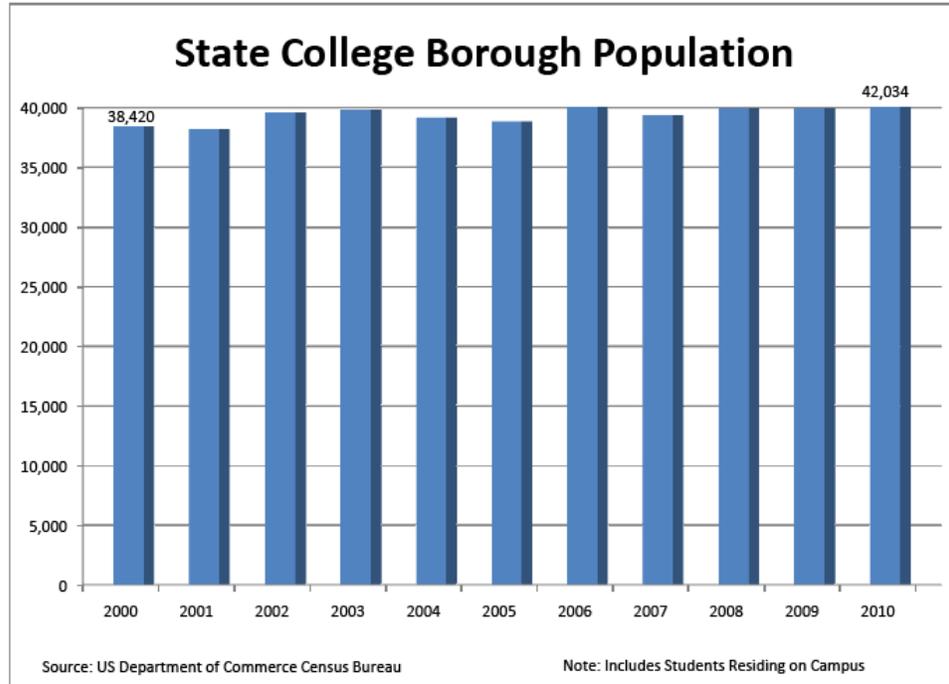
Discussion of the Indicators and Trend Data for 2001-2010

Community

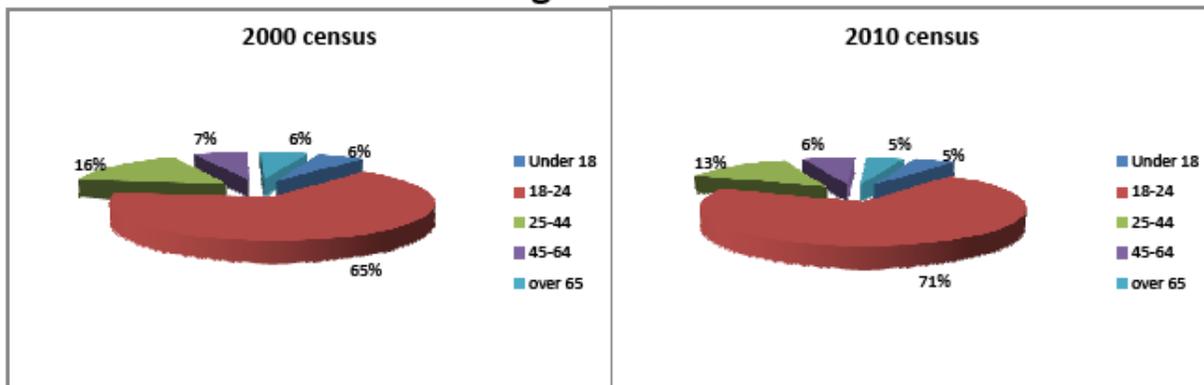
Population/Age Cohorts

During the period 2000-2010, the Borough's population has fluctuated, but grew by about 3,600 persons, or 9.4%. With the exception of the actual data for census years 2000 and 2010, the population figures shown are annual estimates furnished by the U. S. Census Bureau, and include Penn State

students living on campus. The age cohort data is available only for census years 2000 and 2010 and cannot be trended annually. For comparative purposes, the 2000 and 2010 age cohort data is shown to illustrate that the age 18-24 segment has accounted for most of the Borough's population growth in the past decade.



**State College Borough Population
Age Cohorts**

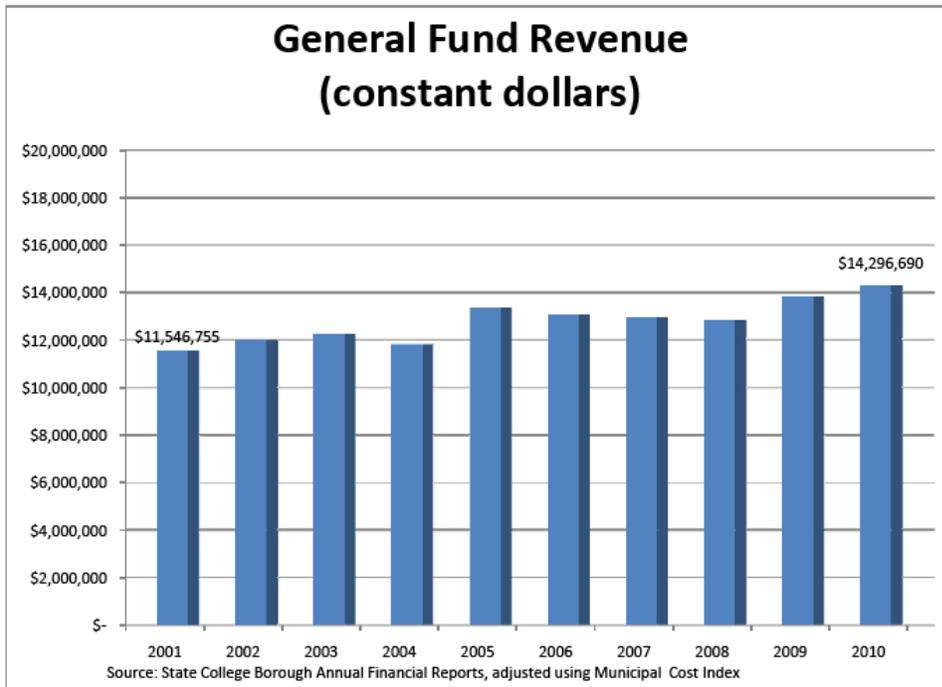
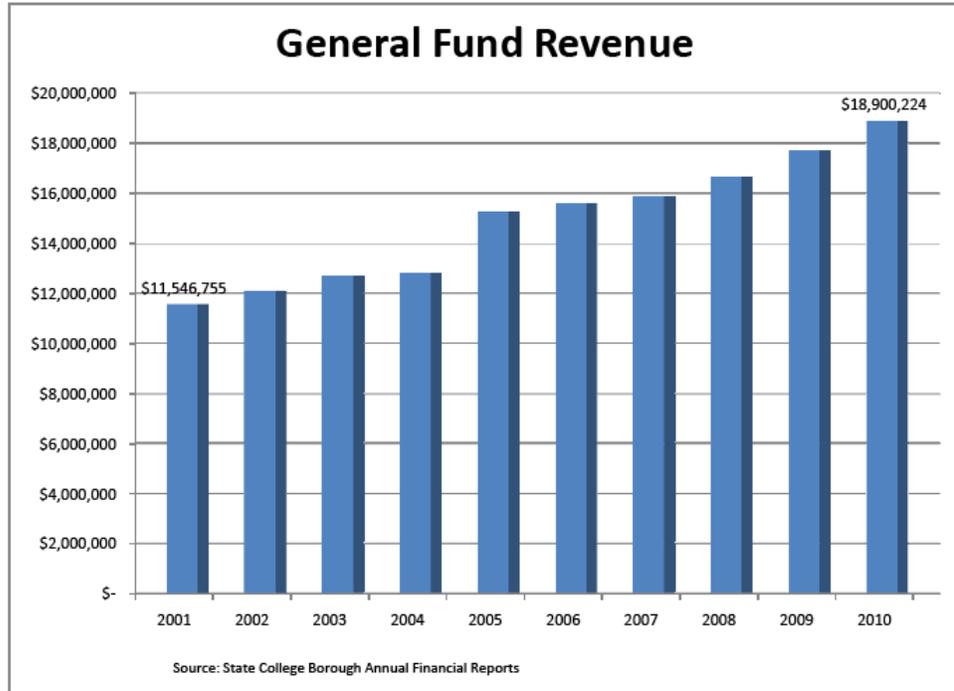


Source: U S Department of Commerce Census Bureau

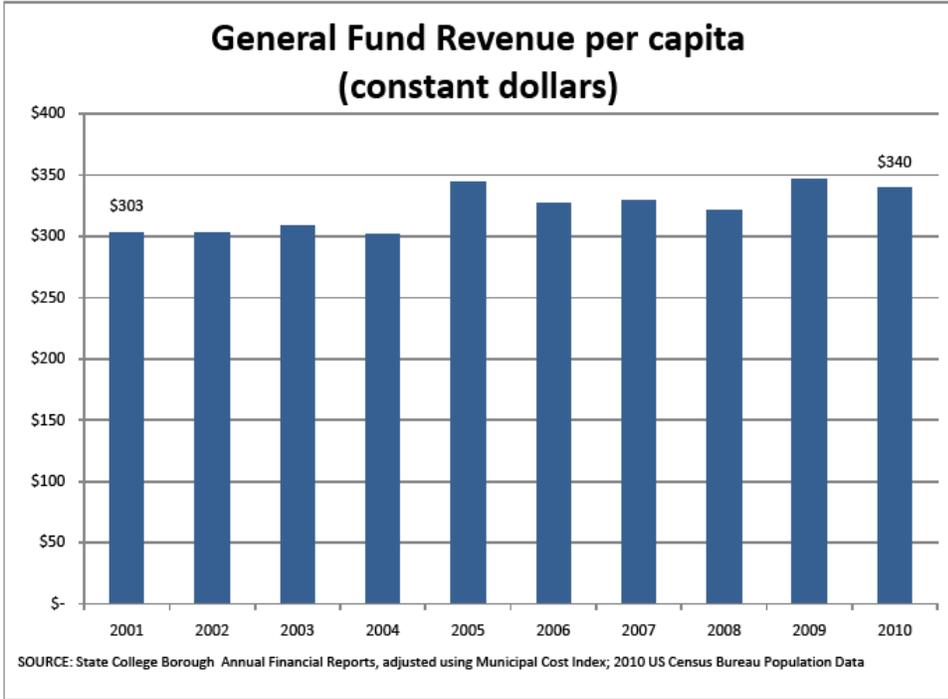
Revenues

General Fund Revenues

Overall, the Borough's General Fund revenues increased almost \$7.4 million or 63.7% during the period. This increase in revenue is largely due to increases in the real estate tax millage and the transition from the \$5 occupational privilege tax to the \$47 local services tax.



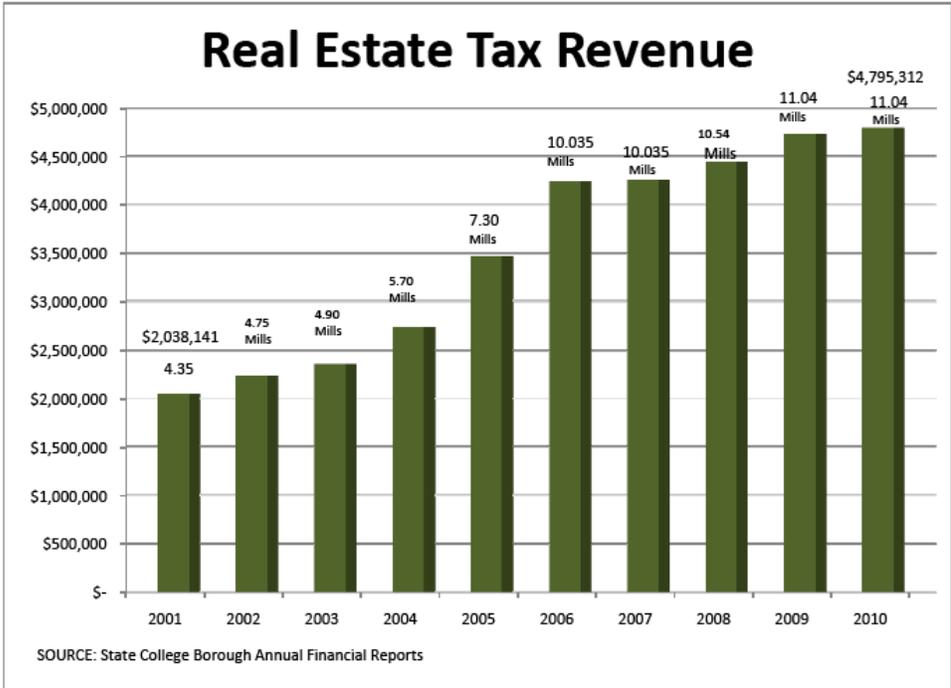
When adjusted to compensate for inflation, however, the increase in General Fund revenues is actually quite modest, rising just \$2.7 million or 23.8% over ten years.

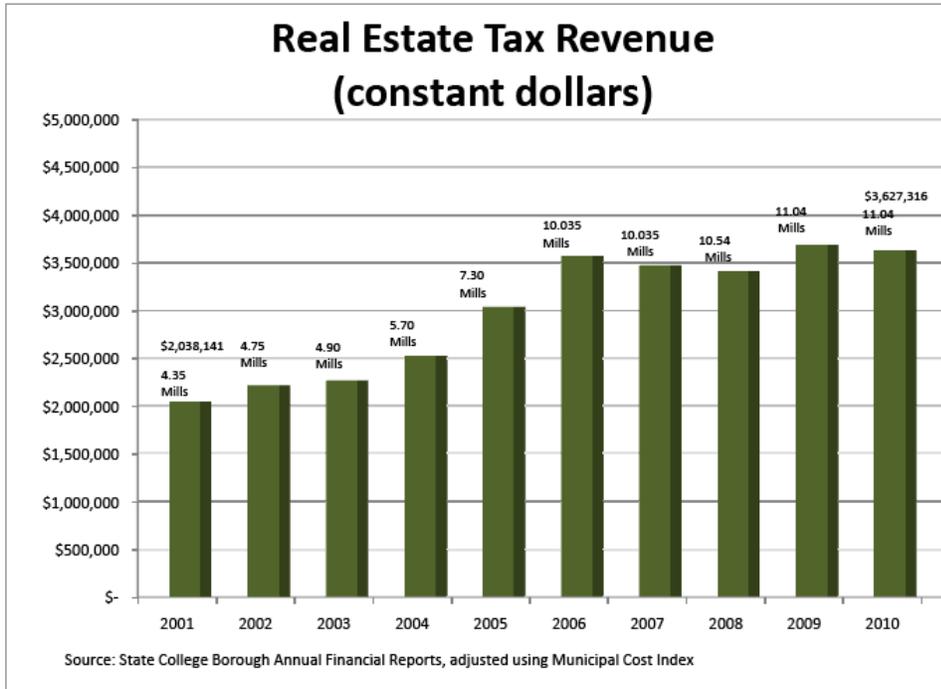


Expressed on an inflation-adjusted per capita basis, General Fund revenues rose from \$303 to \$340 per person for the period. It's interesting to note that General Fund revenues expressed as constant dollars declined from 2003 to 2004 and again from 2005 through 2008, indicating that the increases in revenue did not keep pace with the rate of inflation during those times.

Real Estate Tax Revenue

The growth in the Borough's real estate tax revenue is principally due to increases in the millage rate, which are referenced on the graph.



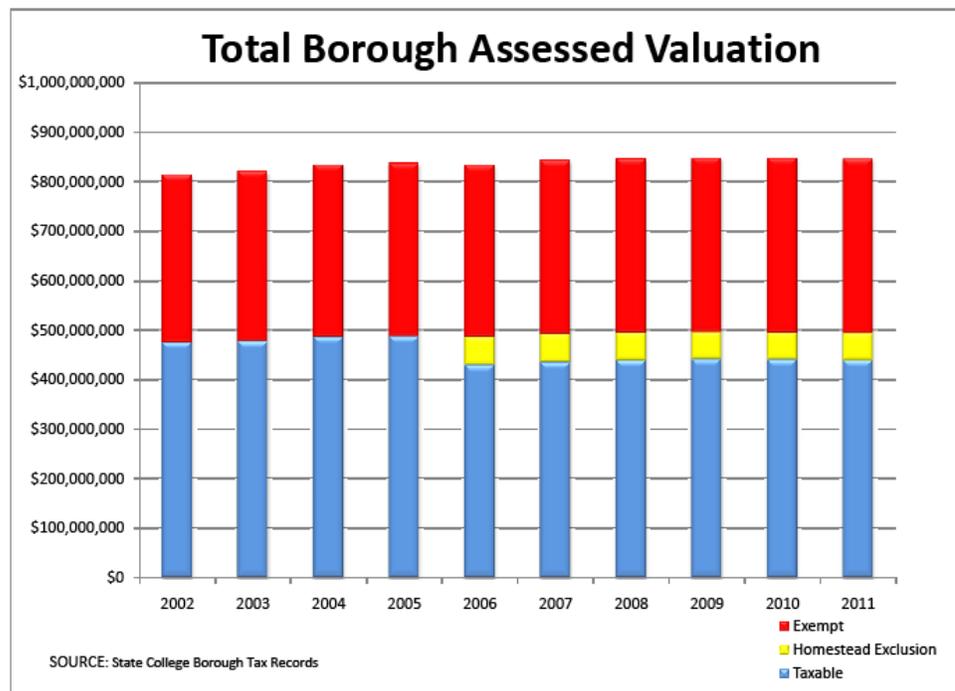


Adjusting the real estate tax revenue for inflation provides a more accurate picture of our revenue growth. In years where there was no millage increase (2006-2007 and 2009-2010), real estate tax revenue effectively declined. A decline also occurred in 2008 even though there was a rate increase of .505 mills, indicating the

amount of that increase did not offset the impact of inflation.

Assessed Valuation

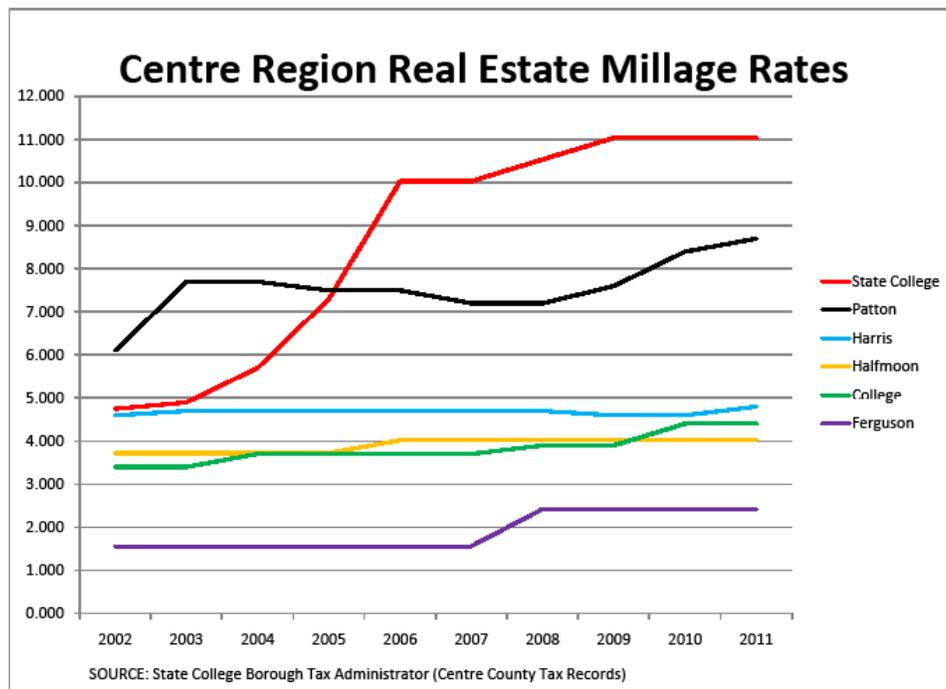
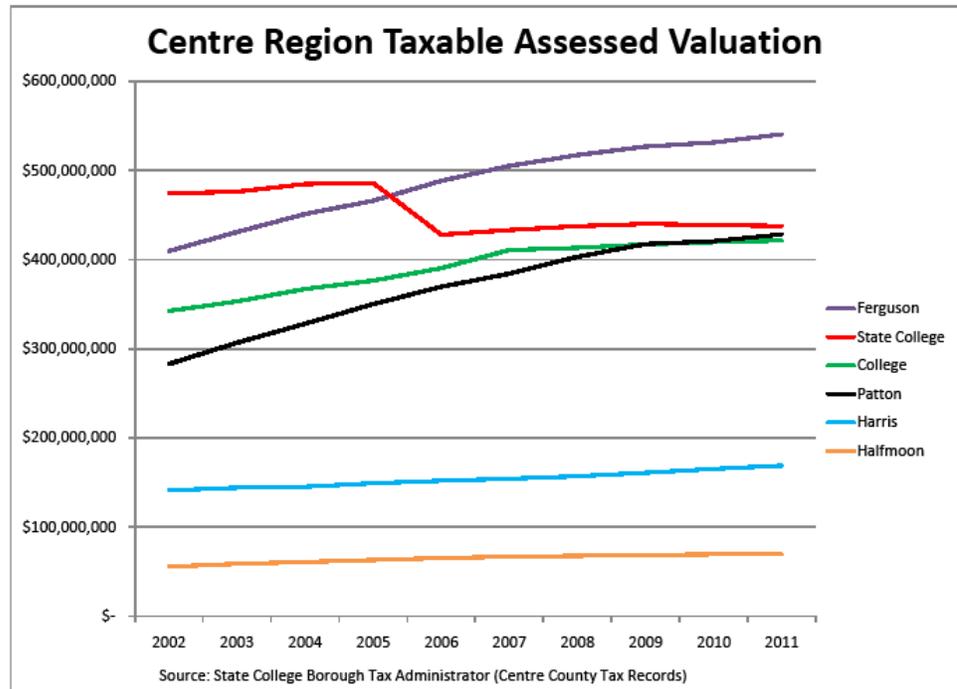
The Borough's taxable real estate assessed valuation has remained relatively stagnant during the period, growing by an average of only 0.4% a year. Increases in valuation from new construction have largely been offset by reductions resulting from commercial assessment appeals, and



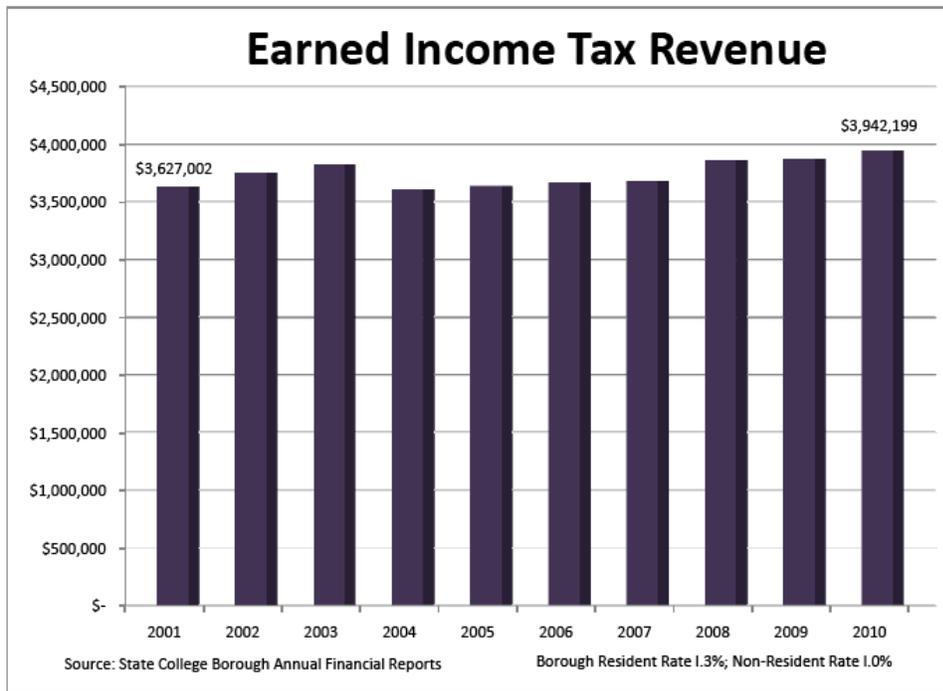
taxable valuation has actually declined since 2009. As shown in the graph, tax exempt realty continues to comprise a significant portion (44.6%) of the Borough's total assessed valuation. The impact of homestead exclusion forgiveness, granted to the owners of qualified residential properties beginning in 2006, is also illustrated. Because the Borough is almost fully developed, significant future increases in taxable valuation will come about primarily through redevelopment.

Our situation is in rather stark contrast to our neighbors in the Centre Region, who have enjoyed

moderate but steady growth in their taxable valuation, and thus their real estate tax revenue, primarily due to new development. Comparisons of the Borough's taxable assessed valuation and real estate millage with those of the municipalities in the Centre Region are offered to illustrate our plight.



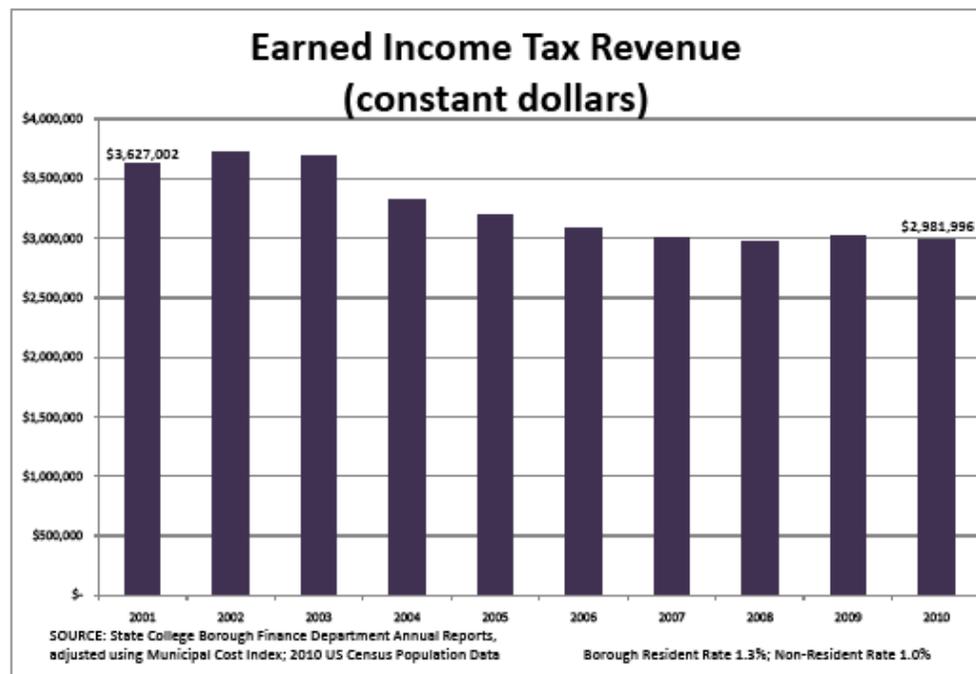
Earned Income Tax Revenue



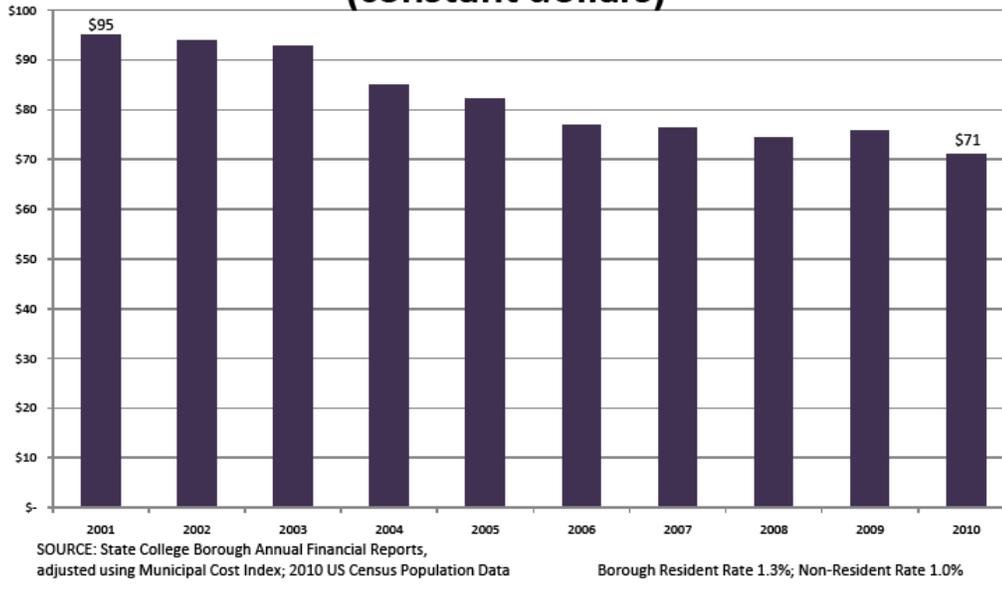
Earned income tax revenue has increased \$315,197 or 8.7% during the period, an average growth of less than one percent annually. The tax rate has remained unchanged. As the Borough's Ad Hoc Tax Study Committee pointed out in their 2005 report, a significant portion of our population has little or no earned income which is subject to the tax, a

situation which hasn't improved. An amendment to the state enabling legislation, further limiting income subject to local taxation, resulted in the decline in revenue evident from 2004-2007.

When an adjustment for inflation is made, the Borough's earned income tax revenue has actually declined about 18% over the last ten years.



Earned Income Tax Revenue per capita (constant dollars)

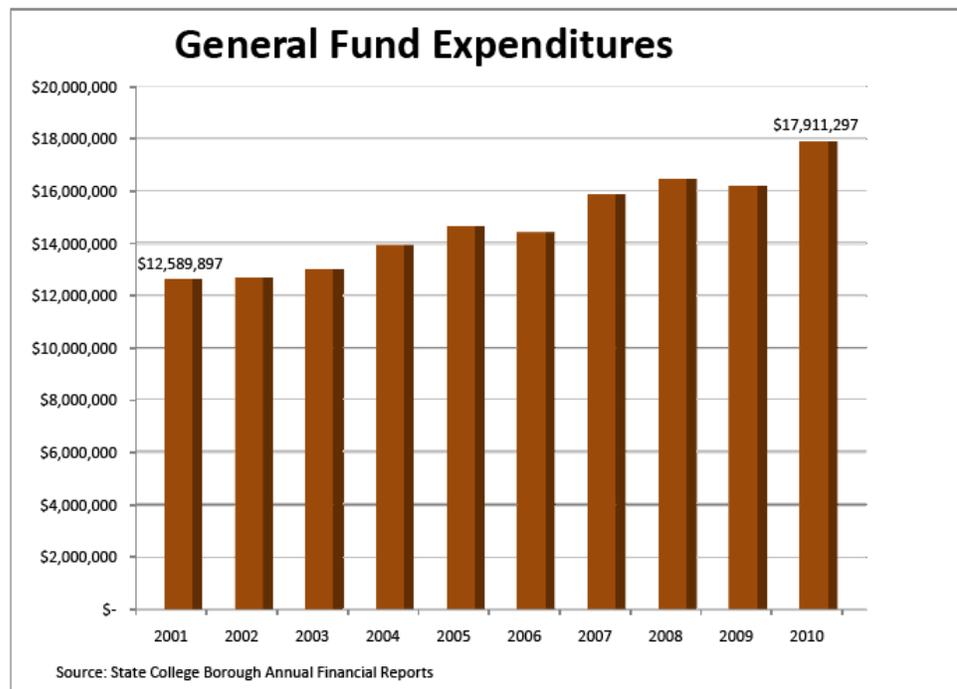


Similarly, earned income tax revenue per capita declined from \$95 to \$71 during the period, when adjusted for inflation.

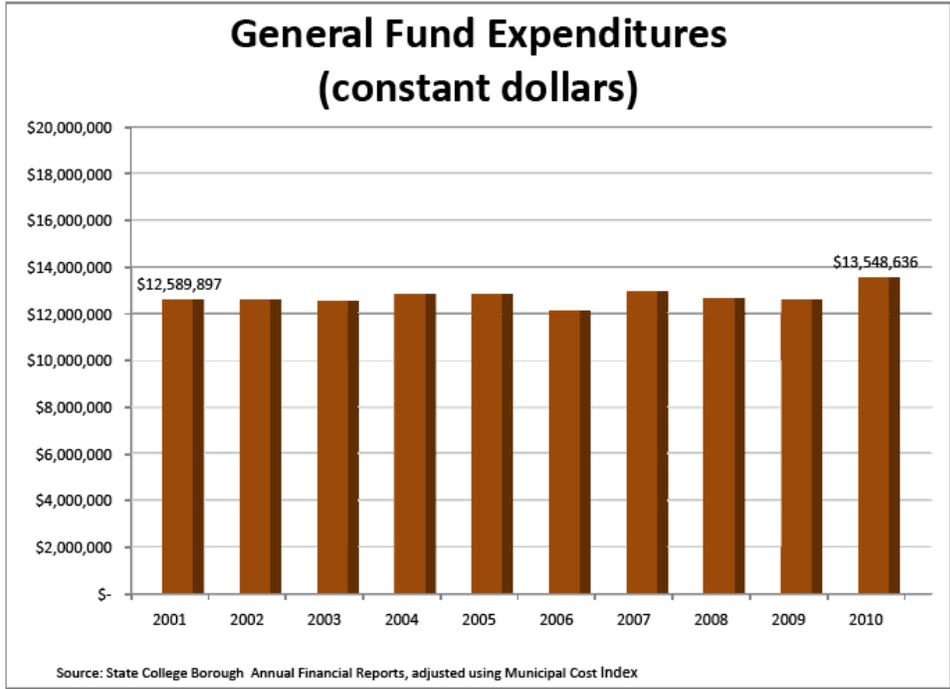
Expenditures

General Fund Expenditures

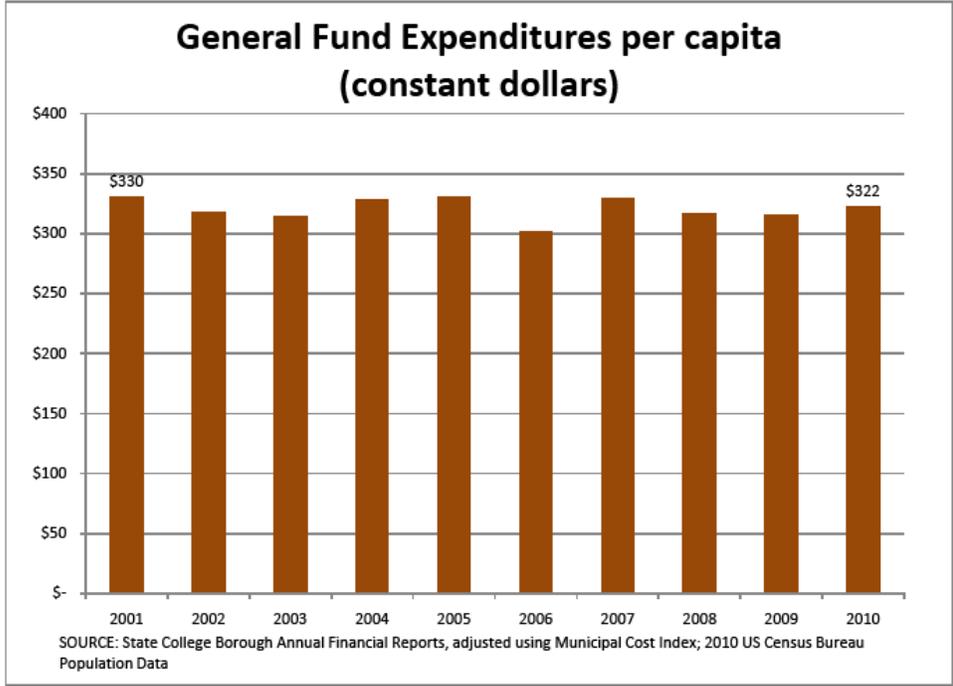
Overall, expenditures in the Borough's General Fund increased \$5.3 million, or 42.3%, during the period. These increases reflect increased costs of operations and additional debt service for capital projects. It should also be noted that one-time transfers of fund balance earmarked for several major



capital projects accounted for approximately \$2.3 million of the increase in expenditures. These transfers included \$1.2 million to fund the new Municipal Building in 2001; \$471,200 for the Borough's share of the COG office building in 2002; and \$607,000 for the new Schlow Library facility in 2004.



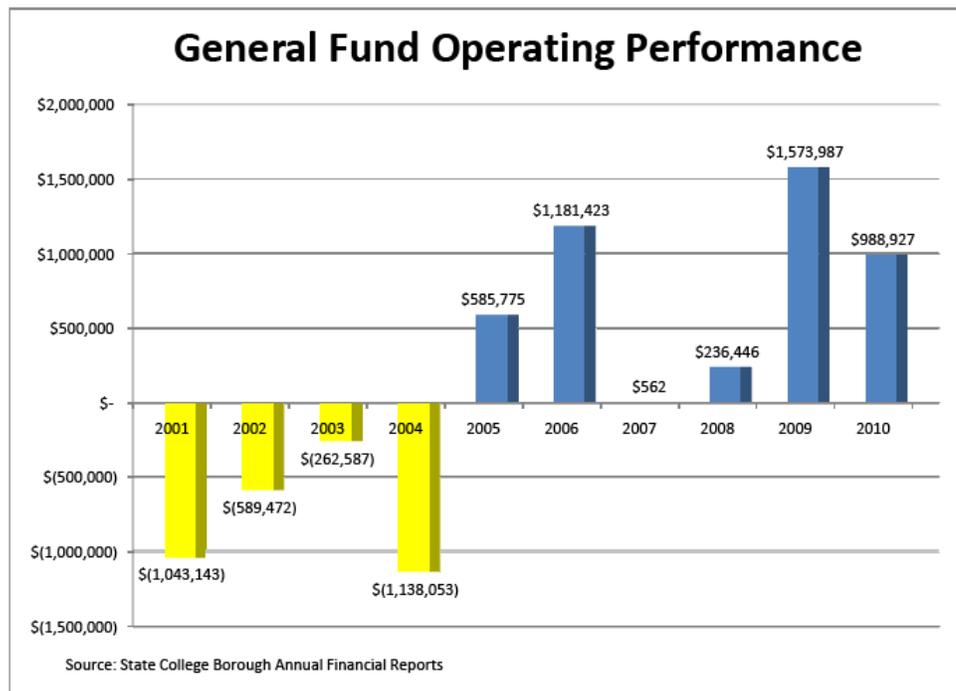
When adjusted to compensate for inflation, General Fund expenditures increased just \$959 thousand or 7.6% for the period. On an inflation-adjusted per capita basis, they declined slightly from \$330 to \$322 per person over ten years.



Operating Position

General Fund Operating Performance

During the period, there were four years (2001-2004) in which the Borough's General Fund expenditures exceeded its revenues. However, it must be remembered that the expenditures for three of those four years included the one-time transfers of fund balance which had been earmarked for the major capital projects mentioned previously. If those transfers were excluded, General Fund revenues would have exceeded expenditures in 2001, and the difference between revenues and expenditures would have been \$471,200 less in 2002 and \$607,000 less in 2004. It should also be noted that the General Fund received \$200,000 in revenue from the Fraser Centre land transfer agreement in 2008. Improvement in the General Fund's operating performance since 2009 has resulted from increases in revenues and decreases in operating and debt service costs.

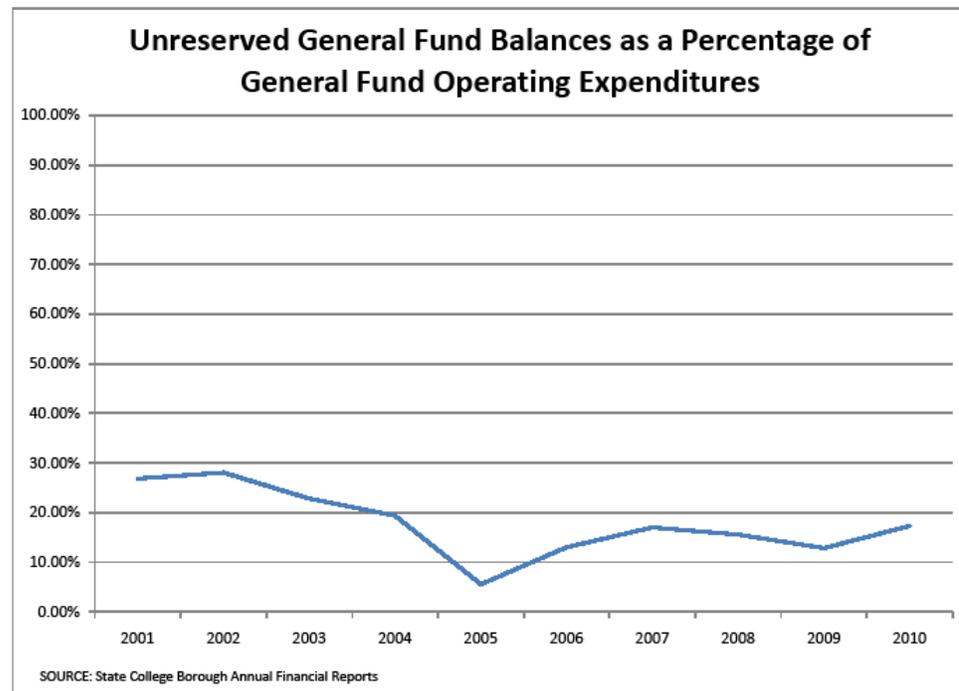


Unreserved General Fund Balance

The credit rating agencies consider the maintenance of a prudent amount of unreserved fund balance to be an indicator of a financially healthy and well-managed government. Traditionally, the Borough has maintained an unreserved fund balance in the range of ten to fifteen percent of budgeted expenditures. This level of fund balance sustains Borough operations during the first several months of

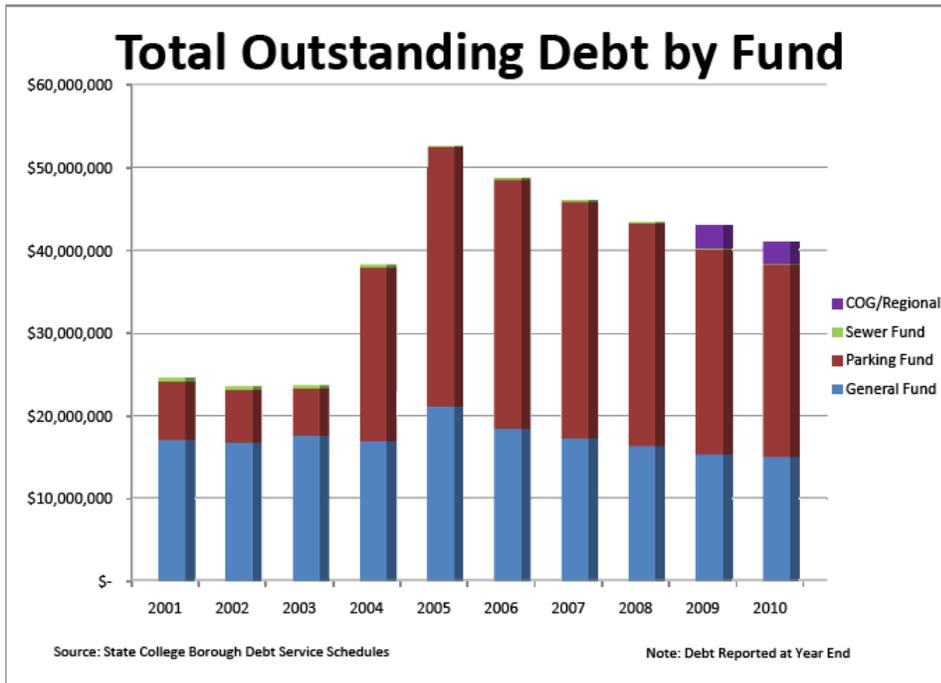
the new fiscal year and eliminates the need to temporarily borrow funds in anticipation of the receipt of taxes and other revenue. It would also help the Borough weather a temporary economic downturn or respond to a disaster or other unforeseen event. Because of financial commitments to the Municipal Building, COG

office building, and Schlow Library projects, the Borough's unreserved fund balance was permitted to grow prior to 2001, with a portion of those monies being earmarked by Council to reduce the amount of debt which the Borough needed to assume in order to fund those major capital projects. From 2001 through 2004, the earmarked funds were transferred from the fund balance to pay for those projects. During 2005, Council adopted a policy calling for the unreserved fund balance to be maintained at a minimum level equal to 12% of General Fund expenditures and that target has been achieved.



Debt Structure

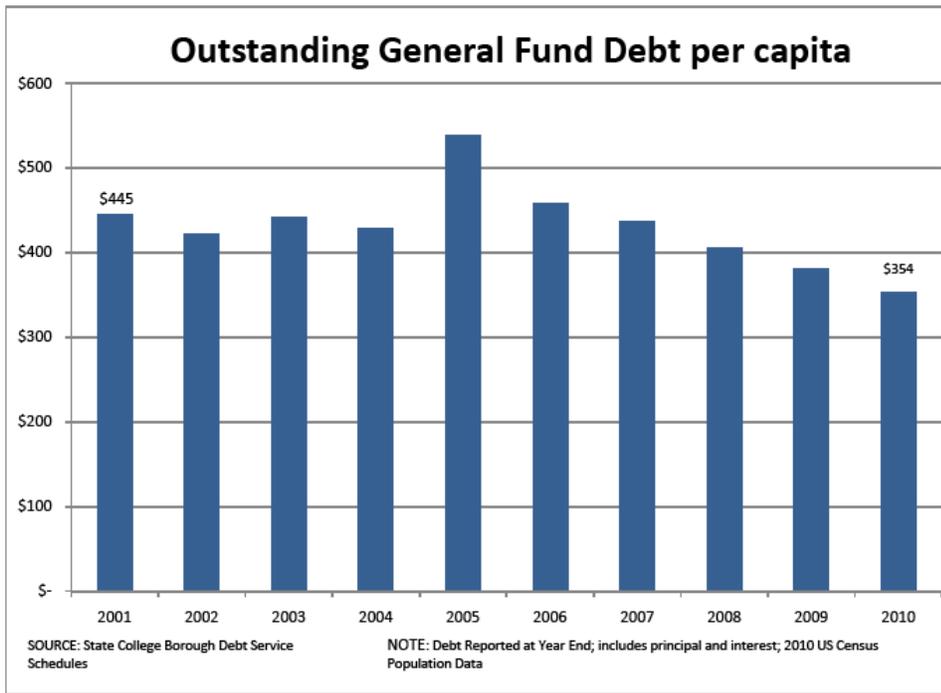
Total Outstanding Debt by Fund



As shown on the graph, most of the Borough's outstanding debt is allocated to the General and Parking Funds. The Borough refinanced most of its debt in 2009 to take advantage of historically low market interest rates. There are presently two general obligation bond issues outstanding, along with a Pennsylvania

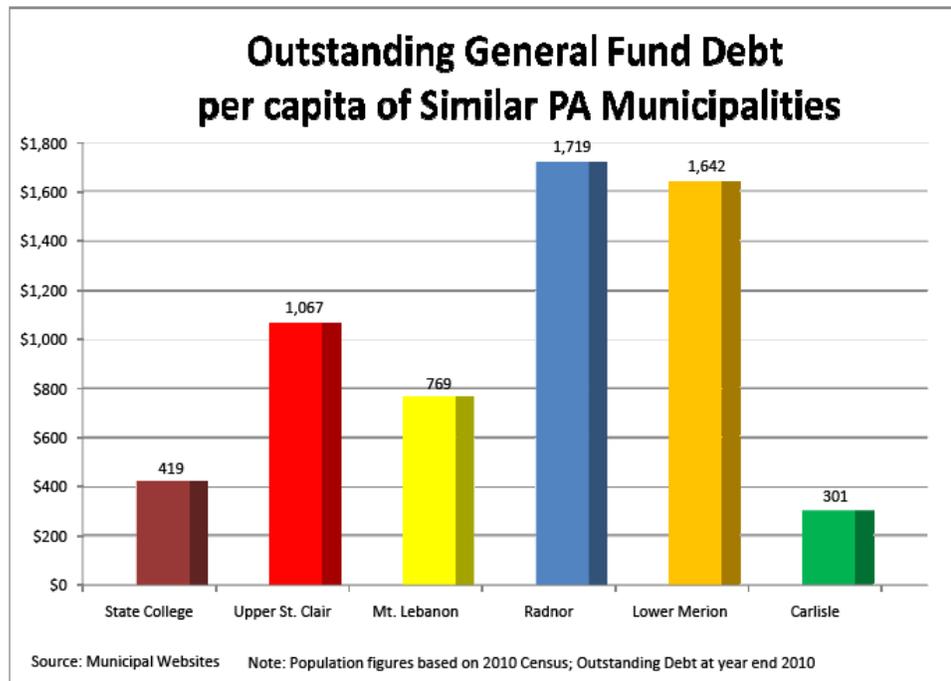
Infrastructure Bank Loan, for which the future debt service (principal and interest) payments total approximately \$41 million. In addition, the Borough is responsible for its portion of the Centre Regional Recreation Authority's debt service for the regional swimming pool improvement projects, which totals approximately \$2.8 million. The debt service payments are allocated to the General, Parking, and Sanitary Sewer Funds according to each fund's share of the total debt. The General Fund debt is repaid using tax revenues, while the Parking and Sanitary Sewer Fund debt is considered to be "self liquidating" because it is repaid through user fees.

Outstanding General Fund Debt Per Capita



Because General Fund debt is repaid from tax revenues, the credit rating agencies consider outstanding General Fund debt per capita when evaluating a government's financial condition.

The Borough's outstanding General Fund debt per capita declined from \$445 to \$419 per person during the period, which is a manageable amount and compares very favorably with a sampling of five similar communities in Pennsylvania, whose average was \$1,099 in 2010. In conjunction with the 2009 debt



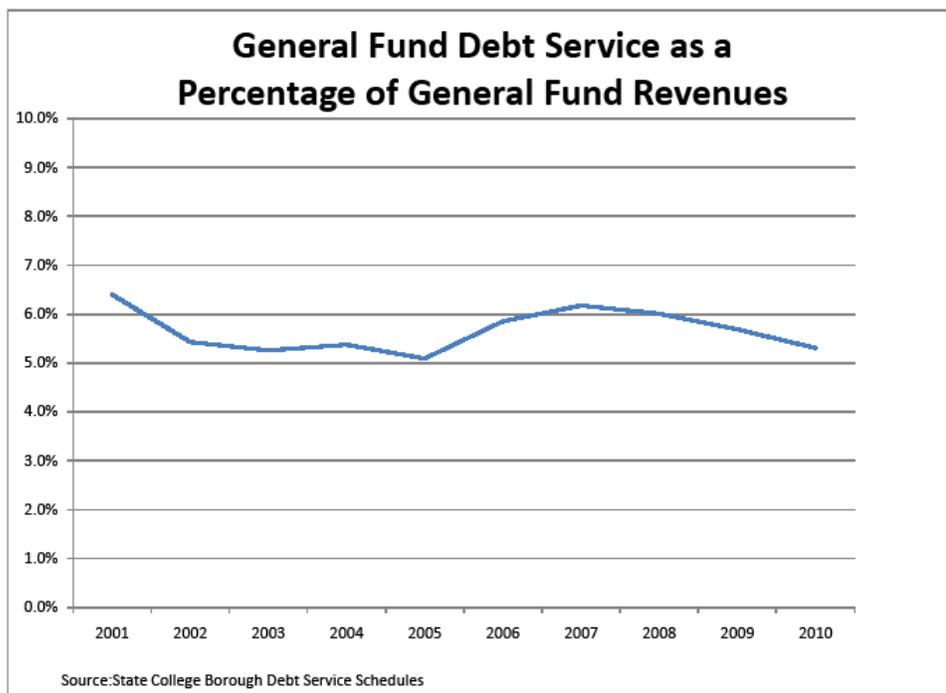
refinancing, the Borough achieved the coveted AA rating from Standard & Poor's, which represents an upgrade of the Aa3 rating previously assigned to the Borough by Moody's Investors Service. This high rating is considered a firm indication of the Borough's overall financial health and strong management practices.

General Fund Debt Service as a Percentage of General Fund Revenues

The credit rating agencies also consider the relationship of General Fund debt service to General Fund revenues to be an important indicator of the financial health of a government, since the General Fund is primarily supported by tax revenues.

Guidelines set forth by the GFOA recommend that a government's annual General

Fund debt service not exceed 12% of its annual General Fund revenues. In 2008, Council adopted a debt policy limiting the Borough's General Fund debt service to no more than 10% of its General Fund revenues. The Borough's ratio has remained significantly under this level during the period.



Summary

Review and analysis of the trends presented in this report will enhance our understanding of the factors which impact the Borough's financial condition. It will also assist us in planning for the future by helping to identify current or potential financial problems, providing insight as to their cause, and allowing us time to develop a plan of action to address those problems.

Observations and Conclusions

The Executive Summary prefacing this report presents the fifteen FTMS indicators and assigns a rating of favorable, unfavorable, neutral or alert based upon staff's review of their impact on the Borough's financial condition. Twelve of the fifteen indicators have been assigned a rating of favorable or neutral, an indication of the Borough's sound fiscal health. Two of the indicators, both related to earned income tax revenue adjusted for inflation, have been assigned an unfavorable rating. These ratings reflect the fact that the effects of inflation have offset the modest growth in earned income revenue during the period, and underscore the importance of efforts to attract more wage earners to locate in the Borough. One indicator, assessed valuation,

has been assigned an alert rating, meaning the trend should be studied in greater detail and appropriate action considered. Growth in the Borough's assessed valuation has been minimal during the period and as noted previously, taxable valuation actually declined in 2010 and 2011. While many of the reasons for the lack of growth are beyond the Borough's control, this situation underscores the importance of promoting redevelopment in the Borough. The Fraser Centre project is an example of mixed-use redevelopment which will enhance the Borough's tax base.

Acknowledgements

The preparers wish to thank Borough Manager Tom Fontaine and Assistant Manager Roger Dunlap for their guidance, suggestions, and support during this project. Special thanks are due to Tax Administrator Linda Welker and Planning Director Carl Hess for their assistance with the gathering of data for several of the indicators.

Prepared and submitted by:

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