



EL DORADO

THE FINE ART OF LIVING WELL

May 1, 2019

Honorable City Commission and Citizens of El Dorado:

The City of El Dorado, Kansas finished the year ended December 31, 2018 with an aggregate net position of \$38,118,541 compared to an aggregate net position of \$38,399,410 at year ended December 31, 2017. This information is meaningless unless we consider its purpose. The ultimate goal of the City's financial statements is to determine whether the City is financially healthy.

The City's financial health was not in the best condition when I arrived in March 2016 to begin my appointment as city manager of El Dorado. Several funds were experiencing depleting reserves as these funds were spending more than was coming in from revenue sources. The City was not making the tough decisions necessary to resolve the underlying structural trend. Further complicating matters, the City had been facilitating this spending habit over a few years.

As I mentioned in prior letters, financial health for a municipality is defined as a local government's ability to deliver the public services its residents expect, with the resources its citizens provide, both now and in the future. Despite the financial situation the City found itself in, I confidently report that the actions taken by the City during the last two years have made great strides to return the City's finances to a more resilient condition without greatly undermining the public services the community has come to rely on.

When I first approached this challenge, I informed the City Commission that solutions would be forthcoming although the ultimate resolution of the situation would still take several years. My letter will confirm that the City continues to make a valiant effort to repair its financial health even though there is still some work needing to be done before victory may be declared. To be sure, the journey to financial health is never truly complete and will require the utmost attention and discipline to ensure that the City remains resilient well into the future.

Once again, I am grateful for the hard work the City Commission and staff have done to develop and implement the 2018 budget. The financial statements contained with this letter will provide you the financial information you need to better understand the City's financial condition. I hope the information will enlighten you.

MAJOR FACTORS AFFECTING THE FINANCIAL STATEMENTS

Record Sales Tax Collections. The City of El Dorado received a record amount of sales tax from its one-cent (1.0%) sales tax on retail sales. In 2018, the City brought in \$2,692,452 in sales tax receipts, which represents a 9.4% increase from 2017. The City has breached the \$2.6 million mark in sales tax receipts only twice in its history. The only other time this phenomena occurred was 2015 when the City received \$2,610,528.

Rising Assessed Valuations. The assessed valuation for the City of El Dorado increased \$5.3 million, or 6.2%, bringing the total assessed valuation for the community to \$91,979,212. As a

result of the increased valuation, the City's mill levy, which is presently set at 53.013 mills, annually generates about \$4.8 million in ad valorem property taxes. Of this amount, the City received about \$4.4 million, meaning about 10% of taxes assessed to property owners was delinquent. The estimated actual value of real and personal property in El Dorado is \$597.6 million.

El Dorado will see increasing assessed valuations in the coming years due to heightened private development as well as the expiration of several tax abatements. LakePoint El Dorado, LLC, a retirement community, will add about \$2.8 million to the assessed valuation in 2021, and BG Products, Inc. will add another \$24.7 million beginning in 2022. These two projects will collectively contribute nearly \$370,000 in property taxes per year to the City of El Dorado once the tax abatements sunset.

Transient Guest Tax Receipts. The City collected \$195,007 in transient guest taxes for overnight stays in 2018. Transient guest tax receipts were up 19.3% compared to the prior year, primarily as a result of HollyFrontier's turn-around, which is an extensive capital investment program that requires several weeks and well over 1,000 contractors. The City sees a bump in transient guest taxes and sales taxes during turn-around as contractors stay in hotels, shop at the grocery stores, and eat out in restaurants during their brief time in El Dorado. HollyFrontier schedules a turn-around every five years or so. The City plans to use the surplus in transient guest tax receipts to develop a community branding and marketing program.

Forgiveness of Internal Debt. The City Commission "forgave" \$2.43 million of internal debt issued to finance the City's portion of BG Products Veterans Sports Complex. In 2012, the City partnered with Butler Community College and Unified School District No. 490 to construct the stadium with the City's participation in the project about \$3 million. The City's funds initially came from the Lake Debt Fund, and were to be repaid over twenty years at 4% interest.

The City identified the use of the Lake Debt Funds as a way to finance its portion of the project's construction while earning a modest rate of return on funds reserved for future lake debt payments. In 2018, the City Commission discussed a plan to pre-pay a portion of outstanding Lake Debt with \$8.3 million held in cash. The decision to pre-pay Lake Debt and change strategy, made the need to repay the internal loan irrelevant.

The City Commission thought it more advantageous to use these funds in more productive ways that directly benefit citizens such as service delivery enhancements. The City Commission formally approved the forgiveness of the internal debt issued to finance the construction of BG Stadium in 2018.

The participating funds will have additional dollars available to allocate annually to mission-critical functions as follows: Water Fund (\$65,000); Sewer Fund (\$65,000); Industrial Mill Levy Fund (\$40,000); Tourism Fund (\$40,000); and Refuse Fund (\$20,000). In addition, the remaining \$2.43 million of internal debt will be removed from the City's balance sheet as an outstanding obligation.

Wind Turbine Lawsuit. In 2018, the City spent \$220,213 on legal expenses related to the wind turbine project. The City will continue to make an annual debt service payment of \$80,157 until 2033; 2) funds of \$494,890 spent primarily on maintenance and repair; and 3) legal expenses related to the lawsuit of \$472,440. It goes without saying that the lawsuit has had a considerable impact on the City's Sewer Fund, causing this fund's cash reserve to be significantly depleted over the years.

Underfunded Public Pensions. The City of El Dorado participates in the Kansas Public Employees Retirement System (KPERS) for its post-employment retirement benefits. Employees of the City are required to participate in KPERS, and the City is required to contribute to KPERS on employees' behalf. Recent changes to state law require the City to publish in its financial statements the current and future liability associated with the unfunded portion of KPERS attributed to the City. The City's unfunded pension liability as December 31, 2018 totaled \$7,367,251 compared to \$7,741,878 from a year ago. The pension liability may be subdivided as follows: KPERS at \$3,289,622, Kansas Police & Fire (KP&F) at \$3,874,582, and the Library's participation in KPERS at \$203,047.

Renewal of One-Cent Sales Tax. In November 2018, the citizens of El Dorado renewed the City's one-cent sales tax on retail sales for another five years. The sales tax has averaged about \$2.54 million per year over each of the last five years including 2018. The City's sales tax is annually distributed as follows: \$1.65 million for property tax reduction; \$600,000 for street maintenance; and \$50,000 for economic development.

Funds received in excess of the \$2.3 million is allocated as excess sales tax funds for special projects at the recommendation of the Excess Sales Tax Committee. The only major change in the recent ballot initiative increased the amount allocated to economic development to \$100,000 per year. The one-cent sales tax will become effective on October 1, 2019, and be up for renewal again in 2023.

Strengthening Utility Revenues. In 2017, the City increased its readiness-to-serve fees for both water and sewer utilities as a measure to help both funds establish a more stable financial position.

The Water Fund will continue to add to its cash position and add \$247,276 to its carry-over balance, making the year-end cash balance for the fund at \$1,089,471. The City's cash reserve policy for the Water Fund requires a cash balance between 15% and 25% of operating expenditures equal to the average the prior three years, or a minimum of \$594,744. The Water Fund exceeds the minimum requirement by \$494,727. The primary reason for the high reserve balance in the Water Fund is due to the fact that the City is preparing to make a substantial payment on outstanding debt obligations on debt issued for the construction of El Dorado Lake. The City is also preparing to pay for several water infrastructure projects with cash in lieu of taking these projects to bond.

The Sewer Fund will also add \$193,397 to its cash balance, making the year-end cash balance for the fund \$351,873. As a result of its strengthening position, the Sewer Fund now meets the City's minimum reserve policy by \$7,565. The City's cash reserve policy for the Sewer Fund requires a cash balance between 15% and 25% of operating expenditures equal to the average the prior three years. The City projected the year-ending balance for the Sewer Fund at about \$200,000 during the preparation of the 2018 budget, so the City underestimated the carry-over balance by nearly \$150,000.

Refuse/Recycling Fee. The City increased its Refuse/Recycling fee in April 2018. The fee was increased from \$14.75 to \$15.75 for residential customers. The increase generated about \$60,000 in new revenue for the refuse/recycling operations, and was implemented to offset significant increases in hauling charges associated with recycling materials.

The City's cash reserve policy for the Refuse Fund requires a cash balance between 15% and 25% of operating expenditures equal to the average the prior three years, or a minimum of \$217,418. The Refuse Fund's year-ending cash balance of \$492,004 exceeds the minimum requirement by \$274,586. The Refuse Fund maintains a seemingly high cash balance because of setting aside cash balance to allow for planned capital purchases in future years.

Recruitment Challenges. Recruitment is perhaps the most critical challenge to the City's current level of service, and 2018 was no exception. During the year, the Police Department, Public Works Department, and Public Utilities Department experienced challenges in filling vacant positions. It goes without saying that people are the City's most important asset because in a service-oriented government, people provide services directly to citizens.

Some of these challenges were likely caused, at least in part, by external factors outside of the City's control. The riots and unrest in Ferguson, Missouri and other communities changed the national landscape for law enforcement. What was once considered a noble trade seemed to lose credibility with the general public throughout the nation. As a result, interest in serving as a police officer seemed to wane as young people considered different options for a career. The City's application pool for new police officers went from being in the hundreds to barely reaching twenty.

Other departments, like Public Works and Public Utilities, are having a more difficult time finding qualified candidates who want to work. These positions require a certain type of individual who enjoys working outdoors in an environment similar to construction. The City's wages may not be as competitive as the private sector, which pushes laborers to jobs beyond the public sector.

In departments that have experienced a tougher recruiting environment, the City has taken a more proactive approach and has tried many different and innovative ways of reaching out to prospective employees. Job fairs, Facebook advertisements, and face-to-face recruiting are just some of the ways departments are working to recruit the next generation of employees. The City is also reviewing its pay plan to determine if adjustments are necessary to compete with the private sector.

As we prepare the financial statements for 2018, it is always wise to look back on the year's budget to determine if what we said we were going to do was actually done. The following analysis provides readers with a brief reconciliation of actions promised with actions completed. It is only through such review can we begin to understand where we fell short from a budgetary and financial standpoint.

Structural deficits remain one of the challenges faced by the City. The City Commission and staff continue to closely monitor the City's financial position to determine if any additional adjustments are needed to address the structural deficits previously maintained in several major funds. The City has taken aggressive steps to address the structural concerns, and many funds are strengthening.

The General Fund closed the year with a budget surplus of \$414,348, making the total cash balance for the fund at year-end \$1,566,233. The Tourism Fund closed the year with a budget deficit of \$158,954, making the total cash balance for the fund at year-end \$197,060. The City has intentionally spent down fund balance from the Tourism Fund in an effort to complete a few projects to promote the community.

In Enterprise Funds, the Water Fund closed the year with a budget surplus of \$695,235, making the total cash balance for the fund at year-end \$1,089,472. The Sewer Fund closed the year with a budget surplus of \$193,397, making the total cash balance for the fund at year-end \$351,873. The Refuse Fund closed the year with a budget surplus of \$215,240, making the total cash balance for the fund at year-end \$492,004.

Each of these funds were carefully monitored and revenues were added to strengthen the funds and continue the City's progress to restore financial sustainability. To be sure, there is still some work that needs done to ensure that the City's funds do not spend more than they generate in revenue each year. Careful management of expenses has, for the most part, allowed the City to end the year with positive cash carry-over balances.

Readiness-to-serve fees were not increased for either the Water or Sewer Funds during 2018. These fees were previously increased in 2017, and were a significant contributor to the plan to strengthen these critical enterprise funds. Due to the improving condition for both of these funds, the City did not approve utility rate increases for either Water or Sewer Utilities during the year.

The City continues to evaluate opportunities to sell additional water as a means to generate revenue for its Water Fund. In addition, water revenue may also be allocated to other uses if sufficient revenue is generated to cover all operational expenses, debt service, and fully fund the Water Fund's cash balance requirements. The City has started to discuss opportunities for selling water to industrial users that may locate in El Dorado's West Industrial Park. Such users have the benefit of increasing water volume sales, while also increasing the City's tax base that will generate increasing amounts of ad valorem property taxes.

The City is required to provide language in its transmittal letter, included with its Comprehensive Annual Financial Report ("CAFR") that explains the policies and controls designed to ensure the City's stewardship of public assets. I will briefly discuss these items in this next section of the letter.

The Comprehensive Annual Financial Report of the City of El Dorado, Kansas, for the year ended December 31, 2018, has been prepared for the review of the governing body, citizens, and other interested in the financial condition of the City. Responsibility for both the accuracy of the presented data and the completeness and fairness of the presentation, including all disclosures, rests with the City. Staff believes the data as presented is accurate in all material respects and that it is presented in a manner designed to fairly represent the financial position and results of operations of the City measured by the financial activity of its various funds. Disclosures necessary to enable the reader to gain the maximum understanding of the City's financial activity have been included.

The management of the City 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 warrant that adequate accounting data is compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. 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 a control should not exceed the benefits likely to be derived; and 2) the valuation of costs and benefits requires estimates and judgments by management.

All internal control evaluations occur within the above framework. Management believes that the City's internal accounting controls adequately safeguard assets and provide reasonable assurance of proper recording of financial transactions.

Generally accepted accounting principles, also known by the abbreviation GAAP, 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 (also referred to as MD&A). This Letter of Transmittal is designed to complement the MD&A section, and should be read in conjunction with it. The MD&A section of the report may be found immediately following the report of the independent auditors.

Independent Audit

State statutes require an annual audit of the books of accounts, financial records and transactions of all departments of the City be performed by independent certified public accountants. Berberich Trahan & Co., P.A., conducted an independent audit of the City's financial statements, and their opinion has been included with the financial statements. Interested persons are encouraged to refer to their opinion in reviewing the City's financial statements.

Relevant Financial Policies

The City of El Dorado's "General Financial and Budgetary Policies," adopted by Resolution No. 2849, have been included with the Comprehensive Annual Financial Report for your information. I would recommend readers who are interested in reviewing these policies refer to the table of contents to determine where the policies are located in this document. These financial policies provide the framework with which the City is working to resolve the financial challenges discussed earlier, and will provide readers with a better understanding of how the City will manage its finances moving forward. There were no changes to these policies during the year.

Needless to say, the City continuously reviews its practices to determine where opportunities exist to improve. As a result of an internal audit, management has identified several areas where an improved process and enhanced discipline will help us better serve citizens. Please bear in mind that I am not hinting at a refined bureaucratization of existing processes, although some definition and accountability may be warranted to ensure that all facets of the organization uniformly comply with policies and practices that will serve to strengthen the City's financial condition.

ECONOMIC CONDITION AND OUTLOOK

Private Sector Investment:

The City of El Dorado continues to maintain a positive investment environment in the private sector with several major project contributing significant capital investment to the community. BG Products, Inc. committed to a \$24.2 million expansion of its warehouse and distribution center in El Dorado. The project commenced construction in 2018, and is expected to create fifteen jobs when completed. Union Tank Car also had a \$7.0 million expansion that created one hundred new jobs for the local economy.

White Eagle Credit Union commenced construction on a new branch valued at \$1.33 million. Taco John's built a franchise valued at \$650,000 and South Central Kansas Mental Health expanded its footprint with a \$300,000 expansion. Susan B. Allen Memorial Hospital developed a \$200,000 Urgent Care facility to serve the community's health service needs.

In addition to these private sector investments, the City of El Dorado and El Dorado Inc. partnered on the preparation of the West Industrial Park Master Plan to begin planning public

infrastructure investments needed to serve El Dorado's anticipated industrial park expansion to the west of the Kansas Turnpike (I-35). The \$90,000 Master Plan will allow the City to better understand the cost of developing additional industrial land to accommodate its goal of selling water from El Dorado Lake for water-intensive, industrial uses.

In 2018, the City experienced private development activity that contributed \$26.65 million in valuation. Four building permits were issued for new commercial development with an aggregate valuation of \$1.875 million, compared to six new commercial developments in 2017 with a valuation of \$26.5 million. In 2018, the City issued twenty-seven building permits for commercial additions, remodels, and repairs with a valuation of \$21.5 million. Comparatively, the City issued twenty-six building permits for similar activity with a valuation of \$8.4 million in 2017.

The City issued ten residential building permits for new construction with a valuation of \$1.86 million. The City issued twenty building permits for new residential construction in 2017 with a valuation of \$3.8 million. In 2018, 104 building permits were issued for residential additions, remodels, and repairs, with a valuation of \$1.2 million. In 2017, sixty building permits were issued for the same activity with a valuation of \$0.60 million.

As previously mentioned in this letter, the City of El Dorado received the largest amount of retailers' sales tax in the history of the City's one-cent sales tax. The City brought in \$2.64 million from retail sales occurring within the corporate limits of El Dorado. The total receipts also include compensation use tax proceeds, which are paid by individuals or businesses purchasing items outside El Dorado but that are delivered to El Dorado. The record-setting sales tax year provides the best indicator for the health of the economy.

An important consideration in this year's collections was the fact that HollyFrontier Refinery had a major "turn around" event whereby a significant capital investment is done every few years to ensure that the refinery is well-maintained to meet the needs of the company. Thousands of contractors come to El Dorado during the several weeks of turn-around. The contractors stay in hotels, eat in local restaurants, and produce many retail sales during their stay. The community's adage during these times should be "come to El Dorado for turn-around and leave with only a few pennies in your pocket." Even if in jest, turn-around contractors spend a lot while in El Dorado and contributed much to the local economy.

In 2018, one of El Dorado's census tracts was designated as an Opportunity Zone under the Tax Cuts and Jobs Act of 2017. The designation provides special tax benefits on capital gains taxes for investors who invest in projects located within the Opportunity Zone geographical area. Such benefits include deferment of capital gains taxes for a number of years and possible forgiveness of certain capital gains meeting program requirements. At the time of this writing, the City knows of one Opportunity Zone Fund that has organized to take advantage of the program. Other investors may elect to use the program with investments in the El Dorado Opportunity Zone, although the full impact of the program will not be fully realized for several years.

To assist the development of moderate income housing, the City applied for and received a \$190,000 Moderate Income Housing grant from the Kansas Housing Resources Corporation. The program will provide first-time homebuyer down payment assistance and financial assistance to developers building new residential properties meeting moderate income requirements. In 2018, three single-family homes and eight rental units were built through the program. Eight more rental units are anticipated for construction with the remainder of the KHRC funds.

The City also hosted several prominent events that contributed to the local economy. BG Products Veterans Stadium hosted the Kansas Shrine Bowl, Drums Across Kansas, and an AAU regional track meet. The economic impact of these three events is estimated at \$1.4 million in direct and indirect benefits as well as \$18,740 in local sales taxes and hotel guest taxes. The Dam Music Festival, hosted at El Dorado Lake, provided a unique music experience to the El Dorado community and surrounding region.

Public Sector Investment:

In 2018, the City invested more than \$2.0 million in various public infrastructure projects. Major projects include:

- Country Club Road Extension (\$578,711)
- Police Storage Building and Park Shop Acquisition (\$235,537)
- 6th Avenue Sidewalks (\$145,114)
- Downtown Alley Repairs (\$132,548)
- McCollum Road Pedestrian Path (\$104,690)
- Airport Parking Lot and Road Mill and Overlay (\$75,727)
- Griffith Street Paving (\$30,475)

The City also acquired and/or replaced various vehicles and equipment in its fleet, to include:

- Backhoe (\$88,009);
- Three HVAC Units (\$21,595)
- Two Mowers (\$16,776)
- Administration Car (\$8,990);
- Mini-Excavator (Capital Lease - \$7,150)
- Skid Steer (Capital Lease - \$6,350)

SUBSEQUENT EVENTS TO THE FINANCIAL STATEMENTS

The City also makes note of the following events that will affect the 2019 financial statements.

Prairie Trails Golf Course. The City began a process to sell Prairie Trails Golf Course to GreatLIFE Golf and Fitness, LLC at an agreed upon price of \$550,000, following receipt of a proposal from the company to acquire the City's golf assets. The transaction will not be completed until 2019. The City anticipates one-time revenue of \$550,000 from the sale, as well as a slight increase in annual water sales and taxable retail sales. The property will also become taxable real estate and will begin to pay property taxes in 2020. In addition, the City will reduce its overall annual expenses by approximately \$200,000, following the completion of the sale to GreatLIFE.

Issuance of Bonds. In 2019, the City issued General Obligation Bonds, Series 2019A with a principal amount of \$2,825,000 to permanently finance temporary notes that were due in June 2019. The temporary notes were used to finance various public infrastructure projects.

Wind Turbine Lawsuit. The City settled a lawsuit concerning a wind turbine installed in 2011 intended to provide a source of renewable energy to the Water Reclamation Facility. The Sewer Fund will receive funds from the settlement, which will be used to offset the cost of decommissioning and demolishing the wind turbine.

Lake Debt Pre-payment. At the time of this writing, the City Commission has approved the pre-payment of \$8.3 million of outstanding obligations associated with debt issued by the federal government for the construction of El Dorado Lake by the U.S. Army Corps of Engineers (USACE). The City of El Dorado purchased the water rights from the USACE, and has been making annual payments of about \$440,000 on what is referred to as Stages 2 and 3.

After saving funds over the years, the City Commission has elected to pre-pay the debt on Stages 2 and 3 at a “savings” of about \$5.9 million in interest expenses over the remaining life of the obligation. Once the transaction is complete, the City of El Dorado will own 49% of the water available in El Dorado Lake for the general water supply needs of the community and surrounding region.

Recognition

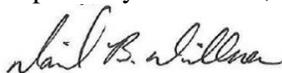
It goes without saying that a municipal government cannot operate and provide public services without a dedicated workforce. The financial statements merely articulate the numbers associated with the provision of such public services; the employees of the City work each day towards the task of serving the public in a myriad of different ways that ultimately make El Dorado a great place to live, work, and play. On behalf of the City, I am extremely appreciative of their hard work and effort in making El Dorado a great community. Department Directors and supervisors are also commended for their efforts in managing the daily activities of the municipal government.

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 El Dorado, Kansas for its comprehensive annual financial report for the fiscal year ended December 31, 2017. This was the fortieth consecutive year that the municipal government has achieved this prestigious award.

In order to be awarded a Certificate of Achievement, a municipal government must publish an easily readable and efficiently organized comprehensive annual financial report. The report must satisfy both generally accepted accounting principles and applicable legal requirements. It should also communicate the City’s financial condition in a manner that allows the public to understand such condition and affirm the City’s spending meets prudent standards and public expectations.

The Certificate of Achievement is valid for one year period only. The City believes that the comprehensive annual financial report for year-ending December 31, 2018 continues to meet the Certificate of Achievement Program’s requirements and will submit it to the GFOA for consideration for another certificate.

Respectfully Submitted,



David B. Dillner
City Manager



Tammy Schaffer
Finance Director