

COUNTY OF JAMES CITY, VIRGINIA

Management's Discussion and Analysis

June 30, 2007

As management of James City County (the County), we offer readers of the County's financial statements this narrative overview and analysis of the financial activities of the County for the fiscal year ended June 30, 2007. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal at the front of this report and the County's financial statements, which follow this analysis.

Financial Highlights

- The County's total debt outstanding for governmental activities at June 30, 2007 was \$256,282,482. During the current year, the County issued a \$95,775,000 lease revenue bond to finance a classroom addition to Stonehouse Elementary School, the new Matoaka Elementary School, the fourth middle school and ninth elementary school. In addition, the County issued a \$21,000,000 general obligation bond to finance improvements to Warhill Sports Park, Freedom Park, Chickahominy Riverfront Park and fund greenspace and purchase of development rights.
- The County's total net assets increased by \$43.3 million over the course of this year's operations. The majority of the increase is attributed to an increase in capitalization of assets, as well as restricted cash related to debt issuance.
- The assets of the County exceeded its liabilities as of June 30, 2007 by \$359.0 million. Of this amount, \$157.6 million, or 43.9%, is the net investment in capital assets.
- Actual General Fund revenues received were 1.5%, or \$2,363,897 more than what had been budgeted and showed an 11.0% increase, or \$15,532,286 over fiscal year 2006.

Overview of the Financial Statements

The County's Comprehensive Annual Financial Report consists of three sections: introductory, financial and statistical. The financial section consists of three primary components – government-wide financial statements, fund financial statements, and notes to the basic financial statements.

Government-Wide Financial Statements

The government-wide financial statements report information about the County 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.

The two government-wide financial statements report the County's net assets and how they have changed. Net assets – the difference between the County's assets and liabilities – is one way to measure the County's financial health, or position.

- Over time, increases or decreases in the County's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the County, you need to consider additional nonfinancial factors, such as changes in the County's property tax base.

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- The government-wide financial statements of the County are divided into three categories:
 - *Governmental activities* – Most of the County's basic services are included here, such as the police, fire, parks and recreation, and general administration. Property taxes and state and federal funding finance most of these activities.
 - *Business-type activity* – Activity that is intended to recover all or a significant portion of their costs through user fee charges to external parties for goods or services are included here.
 - *Component units* – The County includes two other entities in its report – The Public Schools and the Economic Development Authority. Although legally separate, these “component units” are important because of the County's financial accountability for them.

Fund Financial Statements

The fund financial statements provide more detailed information about the County's most significant funds, not the County as a whole. Funds are accounting devices that the County 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. Other funds are established to control and manage money for particular purposes or to show that the County is properly using certain taxes and grants. The County has three kinds of funds:

- *Governmental funds* – Most of the County's basic services are included in governmental funds, which focus on (1) how cash and other financial assets can be readily converted to cash flow in and out and (2) the balances remaining 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 County's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide 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 that are intended to recover all or a significant portion of their costs through user fees are generally reported in the proprietary fund. Proprietary funds, like the government-wide statements, provide both long- and short-term financing information. The County's enterprise fund (one type of proprietary fund) is the same as its business-type activity, but provides more detail and additional information, such as cash flows.
- *Fiduciary funds* – The County is responsible for assets of various agency funds. It is responsible for ensuring that the assets reported in these funds are used for their intended purposes. All of the County's fiduciary activities are reported in a separate statement of fiduciary net assets and a statement of changes in fiduciary net assets. We exclude these activities from the County's government-wide financial statements because the County cannot use their assets to finance its operations.

Notes to the Basic Financial Statements

The notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

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Other Information

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the County's General Fund budget and progress in funding its obligation to provide pension benefits to its employees. The combining statements for nonmajor governmental funds are presented immediately following the required supplementary information on the General Fund budget and defined benefit pension plans.

Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. The County's assets exceeded liabilities by \$359,044,777 at the close of the most recent fiscal year. This represents a 13.7% increase over last year.

Condensed Summary of Net Assets

June 30, 2007

| | <u>Governmental activities</u> | <u>Business-type activity</u> | <u>Total</u> | <u>Component unit – public schools</u> |
|--|------------------------------------|-----------------------------------|---------------------------|--|
| Assets: | | | | |
| Current and other assets | \$ 183,087,733 | 36,064,572 | 219,152,305 | 18,260,366 |
| Capital assets | <u>279,976,191</u> | <u>144,278,943</u> | <u>424,255,134</u> | <u>28,460,394</u> |
| Total assets | \$ <u>463,063,924</u> | <u>180,343,515</u> | <u>643,407,439</u> | <u>46,720,760</u> |
| Liabilities: | | | | |
| Long-term liabilities | \$ 256,282,482 | 12,133,794 | 268,416,276 | 800,214 |
| Other liabilities | <u>13,742,953</u> | <u>2,203,433</u> | <u>15,946,386</u> | <u>14,088,751</u> |
| Total liabilities | \$ <u>270,025,435</u> | <u>14,337,227</u> | <u>284,362,662</u> | <u>14,888,965</u> |
| Net assets: | | | | |
| Invested in capital assets, net of related debt | \$ 25,413,961 | 132,145,149 | 157,559,110 | 28,358,026 |
| Unrestricted and restricted | <u>167,624,528</u> | <u>33,861,139</u> | <u>201,485,667</u> | <u>3,473,769</u> |
| Total net assets | \$ <u>193,038,489</u> | <u>166,006,288</u> | <u>359,044,777</u> | <u>31,831,795</u> |

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Condensed Summary of Net Assets

June 30, 2006

| | <u>Governmental activities</u> | <u>Business-type activity</u> | <u>Total</u> | <u>Component unit – public schools</u> |
|--|------------------------------------|-----------------------------------|--------------------|--|
| Assets: | | | | |
| Current and other assets | \$ 117,100,460 | 32,112,835 | 149,213,295 | 15,002,201 |
| Capital assets | 200,484,395 | 137,689,519 | 338,173,914 | 26,618,114 |
| Total assets | <u>\$ 317,584,855</u> | <u>169,802,354</u> | <u>487,387,209</u> | <u>41,620,315</u> |
| Liabilities: | | | | |
| Long-term liabilities | \$ 146,360,591 | 13,034,918 | 159,395,509 | 842,006 |
| Other liabilities | 10,476,513 | 1,781,593 | 12,258,106 | 12,649,956 |
| Total liabilities | <u>\$ 156,837,104</u> | <u>14,816,511</u> | <u>171,653,615</u> | <u>13,491,962</u> |
| Net assets: | | | | |
| Invested in capital assets, net of related debt | \$ 57,943,767 | 124,654,601 | 182,598,368 | 26,446,862 |
| Unrestricted and restricted | 102,803,984 | 30,331,242 | 133,135,226 | 1,681,491 |
| Total net assets | <u>\$ 160,747,751</u> | <u>154,985,843</u> | <u>315,733,594</u> | <u>28,128,353</u> |

The largest portion of the County's net assets at June 30, 2007 (43.9%) reflects its investment in capital assets (e.g., land, buildings, machinery and equipment), less any related debt used to acquire those assets that are still outstanding. The County uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the County's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The unrestricted portion of net assets (19.6%) may be used to meet the County's ongoing obligations to citizens and creditors. The remaining portion of net assets (36.5%) is restricted for specific purposes.

At the end of the current fiscal year, the County was able to report positive balances in all three categories of net assets, both for the primary government as a whole, as well as for its separate governmental and business-type activities.

The Public Schools' net assets increased 13.2% to \$31.8 million. Of the balance, \$3.5 million of net assets are unrestricted, but designated for specific purposes. The increase in net assets is primarily attributable to the ongoing and completed capital projects.

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Summary of Changes in Net Assets

Year ended June 30, 2007

| | <u>Governmental activities</u> | <u>Business-type activity</u> | <u>Total</u> | <u>Component unit – public schools</u> |
|---|------------------------------------|-----------------------------------|--------------------|--|
| Revenues: | | | | |
| Program revenues: | | | | |
| Charges for services | \$ 15,768,525 | 17,899,853 | 33,668,378 | 2,318,883 |
| Operating grants and contributions | 22,448,104 | — | 22,448,104 | 13,624,163 |
| Capital grants and contributions | 5,039,467 | 7,926,456 | 12,965,923 | — |
| General revenues: | | | | |
| Property taxes | 94,855,055 | — | 94,855,055 | — |
| Other taxes and permits, fees and licenses | 30,528,204 | — | 30,528,204 | — |
| Grants and contributions not restricted to specific programs | — | — | — | 93,086,380 |
| Interest and investment earnings | 7,306,357 | 1,503,939 | 8,810,296 | 281,474 |
| Miscellaneous | 5,102,599 | 1,378,725 | 6,481,324 | 29,030 |
| Total revenues | <u>181,048,311</u> | <u>28,708,973</u> | <u>209,757,284</u> | <u>109,339,930</u> |
| Expenses: | | | | |
| General government administration | 18,576,094 | — | 18,576,094 | — |
| Judicial administration | 5,053,351 | — | 5,053,351 | — |
| Public safety | 23,819,070 | — | 23,819,070 | — |
| Public works | 3,361,025 | — | 3,361,025 | — |
| Health and welfare | 6,762,204 | — | 6,762,204 | — |
| Education | 63,874,870 | — | 63,874,870 | 105,636,488 |
| Parks, recreation and cultural | 2,131,929 | — | 2,131,929 | — |
| Community development | 15,154,960 | — | 15,154,960 | — |
| Interest on long-term debt | 9,857,524 | — | 9,857,524 | — |
| Storm costs | 166,546 | — | 166,546 | — |
| Service Authority | — | 17,688,528 | 17,688,528 | — |
| Total expenses | <u>148,757,573</u> | <u>17,688,528</u> | <u>166,446,101</u> | <u>105,636,488</u> |
| Change in net assets | <u>32,290,738</u> | <u>11,020,445</u> | <u>43,311,183</u> | <u>3,703,442</u> |
| Net assets at beginning of year | <u>160,747,751</u> | <u>154,985,843</u> | <u>315,733,594</u> | <u>28,128,353</u> |
| Net assets at end of year | <u>\$ 193,038,489</u> | <u>166,006,288</u> | <u>359,044,777</u> | <u>31,831,795</u> |

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Summary of Changes in Net Assets
Year ended June 30, 2006

| | <u>Governmental activities</u> | <u>Business-type activity</u> | <u>Total</u> | <u>Component unit – public schools</u> |
|---|------------------------------------|-----------------------------------|--------------------|--|
| Revenues: | | | | |
| Program revenues: | | | | |
| Charges for services | \$ 15,335,524 | 16,805,640 | 32,141,164 | 2,284,274 |
| Operating grants and contributions | 18,790,084 | — | 18,790,084 | 11,617,249 |
| Capital grants and contributions | 785,786 | 10,077,376 | 10,863,162 | — |
| General revenues: | | | | |
| Property taxes | 86,204,347 | — | 86,204,347 | — |
| Other taxes and permits, fees and licenses | 29,243,811 | — | 29,243,811 | — |
| Grants and contributions not restricted to specific programs | — | — | — | 82,800,634 |
| Interest and investment earnings | 3,407,722 | 935,971 | 4,343,693 | 178,321 |
| Miscellaneous | 2,053,405 | 526,601 | 2,580,006 | 10,126 |
| Total revenues | <u>155,820,679</u> | <u>28,345,588</u> | <u>184,166,267</u> | <u>96,890,604</u> |
| Expenses: | | | | |
| General government administration | 5,790,007 | — | 5,790,007 | — |
| Judicial administration | 4,374,852 | — | 4,374,852 | — |
| Public safety | 13,599,920 | — | 13,599,920 | — |
| Public works | 2,674,311 | — | 2,674,311 | — |
| Health and welfare | 7,043,503 | — | 7,043,503 | — |
| Education | 77,265,247 | — | 77,265,247 | 96,930,986 |
| Parks, recreation and cultural | 8,720,218 | — | 8,720,218 | — |
| Community development | 12,662,469 | — | 12,662,469 | — |
| Interest on long-term debt | 5,962,561 | — | 5,962,561 | — |
| Nondepartmental | 5,161,844 | — | 5,161,844 | — |
| Service Authority | — | 13,205,214 | 13,205,214 | — |
| Total expenses | <u>143,254,932</u> | <u>13,205,214</u> | <u>156,460,146</u> | <u>96,930,986</u> |
| Change in net assets | 12,565,747 | 15,140,374 | 27,706,121 | (40,382) |
| Net assets at beginning of year | <u>148,182,004</u> | <u>139,845,469</u> | <u>288,027,473</u> | <u>28,168,735</u> |
| Net assets at end of year | <u>\$ 160,747,751</u> | <u>154,985,843</u> | <u>315,733,594</u> | <u>28,128,353</u> |

Governmental Activities

For the fiscal year ended June 30, 2007, revenues from governmental activities totaled \$181,048,311. Of this amount, \$55,665,052, or 30.1%, is received from sources other than local tax revenue. Real estate tax revenues, the County's largest single revenue source, totaled \$75,796,913. The County's assessed real property tax base for fiscal year 2007 was \$9,821,638,100. The County continues to experience growth in residential and commercial development. Net assets increased by \$32,290,738, or 20.1% over last year.

In fiscal year 2007, the County reported current year collections of \$14,570,346 in personal property taxes, and received reimbursement from the Commonwealth of Virginia of \$9,849,732. Under the provisions of the Personal Property Tax Relief Act (PPTRA), the state's share of local personal property tax was approximately 56% of most taxpayer's payments.

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For the fiscal year ended June 30, 2007, expenses for governmental activities totaled \$148,757,573, including payments of \$63,874,870 to Public Schools (which includes \$25.2 million for the construction of a new high school and \$16.8 for the construction of a new elementary school) and \$102,494 to the James City Economic Development Authority. Expenses increased by \$5,502,641 over fiscal year 2006. This was primarily due to transfers to schools to cover construction costs for the new schools.

Business-Type Activity

The business-type activity increased the County's net assets by \$11,020,445, accounting for 25.4% of the total growth in the County's net assets. The majority of the increase is attributed to the contribution of water and sewer systems. Expenses increased from last year by 34.0%, which is primarily due to a donation of a lift station to HRSD. This resulted in a loss on the disposal of capital assets. In addition, there was an increase in special services, which is a result of new positions being approved during the current fiscal year. Revenues increased 13.8% from last year, which was a result of an increase in the water service charges, as well as an increase in customer growth.

Component Unit – Public Schools

The Schools received \$64,467,761 from the County during fiscal year 2007. This represents 65.2% of their total intergovernmental revenue. This money supported the operating and capital activities for the Schools. Expenses increased by 9.0% over fiscal year 2006. This is primarily a result of increases in expenses for salaries, fringe benefits and pupil transportation. Revenues also increased by 12.8% over the previous fiscal year. This is primarily due to funding received from the City of Williamsburg and the County for construction costs associated with the two new schools.

Financial Analysis of the County's Funds

The County's General Fund experienced an overall increase in fund balance of \$3,150,530. A key factor to this increase was the reduced spending for personnel. The Reserve for Fiscal Liquidity totaled \$20,404,910, which was 10.2% of the total general governmental expenditures, including the County's share of the Public Schools' operating expenditures, and within the goal of 8% to 12%.

General Fund Budgetary Highlights

The overall difference between the original budget and the final amended budget for revenues increased by \$29,893, which was primarily a result of a combination of an increase in the property tax revenue as a result of a higher landbook value and a reduction in the school contribution due to the state increasing basic aid payable directly to the schools. As a result of the higher landbook value, the Board decreased the tax rate to \$0.77, but still generated an increase in tax revenue. The reduction in the school contribution was revenue neutral to the schools, but required less funding from the County. Actual General Fund revenues received were 1.5%, or \$2,363,897 more than what had been budgeted and showed a 10.9% increase, or \$15,532,286 over fiscal year 2006.

The largest increase in revenues from fiscal year 2006 to fiscal year 2007 occurred in real estate tax revenues totaling \$10,225,403. Real estate tax revenues, both current and delinquent, are the County's largest revenue source and for fiscal year 2007 totaled \$75,796,913 and was \$197,148 less than the amended budget. Personal property taxes, another large source of local tax funding, had combined collections from the state and local taxpayers of \$24,420,078. This was \$2,057,164 more than budget, and \$1,804,895, or an 8.0% increase over

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fiscal year 2006. State revenues, not including the personal property tax reimbursement, were \$267,315 less than budgeted. State revenues, not including the personal property tax reimbursement, increased \$1,918,562 in fiscal year 2007 from fiscal year 2006 levels. This increase is primarily due to state sales tax for education, which increased \$419,429 over fiscal year 2006. In addition, the communications sales and use tax is included this year from the state.

General Fund budgeted expenditures were 4.0% below the final budget, or \$5,167,884. Of this amount, \$1,999,517 is reserved in the fund balance for encumbered commitments.

Proprietary Fund

The County operates one proprietary fund, James City Service Authority (JCSA or the Authority), which provides water and sewer service to County residents. The Authority had an increase of \$11,020,445 in net assets during the fiscal year primarily due to the acceptance of contributed capital assets.

Capital Assets and Debt Administration

Capital Assets

At the end of fiscal year 2007, the County's investment in capital assets for its governmental and business-type activities totaled \$424,255,134 (net of accumulated depreciation). This investment in capital assets includes land, construction in progress, land improvements, buildings and improvements, water and sewer systems, infrastructure, equipment, and vehicles. The County does not own its roads and they are therefore not included in the capital assets. In addition, the Public Schools own all school buildings and the related debt is County debt. The value associated with the purchase and/or construction of the Public Schools' buildings is reported as capital assets in the governmental activities of the County to properly match with the associated debt, as allowed by Virginia state law. In fiscal year 2007, the net value of school buildings reflected in the governmental activities of the County equals \$105,790,411, and the associated current year's depreciation expense of \$2,115,808 is reflected in the educational expense line of the County's governmental activities in the statement of net assets.

Capital Assets, Net of Depreciation

June 30, 2007 and 2006

| | 2007 | | | 2006 Total |
|--------------------------------------|----------------------------|---------------------------|--------------------|--------------------|
| | Governmental activities | Business-type activity | Total | |
| Land | \$ — | 1,762,961 | 1,762,961 | 1,785,961 |
| Land and land rights – utility plant | — | 954,738 | 954,738 | 890,438 |
| Land and land improvements | 31,391,710 | 13,183 | 31,404,893 | 16,495,880 |
| Construction in progress | 94,166,863 | 8,913,781 | 103,080,644 | 38,136,544 |
| Water and sewer systems | — | 130,702,876 | 130,702,876 | 127,966,378 |
| Buildings and improvements | 115,153,688 | 1,222,774 | 116,376,462 | 117,862,056 |
| Improvements other than buildings | 8,074,975 | — | 8,074,975 | 6,850,825 |
| Equipment and vehicles | 25,831,499 | 708,630 | 26,540,129 | 24,957,510 |
| Infrastructure | 5,357,456 | — | 5,357,456 | 3,228,322 |
| Total | \$ 279,976,191 | 144,278,943 | 424,255,134 | 338,173,914 |

Additional information about the County's capital assets can be found in note 7 to the financial statements.

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Capital Projects Fund

The Capital Projects Fund is used by the County to account for the financing sources used to acquire and construct major capital projects for the general government. A major source of funding for the capital projects is transfers from the General Fund.

For fiscal year 2007, \$9,345,193 was transferred to the Capital Projects Fund from the General Fund. During the year, capital project expenditures of \$76,594,343 included the following:

- Transfers to schools for site improvements and construction costs for the third high school
- Transfers to schools for construction costs for the eighth elementary school
- Architectural and engineering costs associated with the Community Sports Facility
- Construction costs for the Community Building located in New Town

Long-Term Debt

At June 30, 2007 and 2006, the County had total outstanding debt of \$264,667,544 and \$155,854,494, respectively. Compensated absences and landfill postclosure care costs of \$3,748,732 and \$3,541,015 at June 30, 2007 and 2006, respectively, are not included in these amounts.

Summary of Long-Term Debt

June 30, 2007 and 2006

| | <u>2007</u> | | | <u>2006</u> <u>Total</u> |
|---|--|---|--------------------|-----------------------------|
| | <u>Governmental</u> <u>activities</u> | <u>Business-type</u> <u>activity</u> | <u>Total</u> | |
| General obligation bonds | \$ 126,590,560 | — | 126,590,560 | 106,062,319 |
| State Literary Fund loan | — | — | — | 28,950 |
| Revenue bonds | 112,780,000 | 12,133,794 | 124,913,794 | 35,604,918 |
| Capital lease – radio system | 12,350,000 | — | 12,350,000 | 13,100,000 |
| Other capital leases | 688,190 | — | 688,190 | 808,307 |
| Loan payable – Virginia Department of Transportation | 125,000 | — | 125,000 | 250,000 |
| Total | \$ <u>252,533,750</u> | <u>12,133,794</u> | <u>264,667,544</u> | <u>155,854,494</u> |

In December 2006, the County issued a \$95,775,000 lease revenue bond to finance a classroom addition to Stonehouse Elementary School, the new Matoaka Elementary School, the fourth middle school and ninth elementary school. In addition, the County issued a \$21,000,000 general obligation bond to finance improvements to Warhill Sports Park, Freedom Park, Chickahominy Riverfront Park and fund greenspace and purchase of development rights.

Additional information about the County's long-term debt can be found in note 10 to the financial statements.

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Economic Factors and Next Year's Budgets and Tax Rates

The County has a two-year budget cycle. The first year of a two-year cycle is adopted and appropriated and the second year is adopted for planning purposes. Fiscal year 2008 is the second year of the current two-year cycle. The fiscal year 2008 approved and amended budget for the General Fund is \$173,089,548.

This amended budget, adopted on April 24, 2007, reflects \$18,063,777, or an 11.8% increase over fiscal year 2007. As similar to the previous year, almost the entire area of growth is located within real estate tax revenue, which is expected to increase \$10,603,345. On September 25, 2007, the Board of Supervisors amended this budget to reflect a reduction of \$1,900,000 in General Fund expenditures due to a projected decrease in property tax revenue. Market price appreciation and the pace of new construction have slowed down and appear to be slowing even more; national and regional mortgage problems may also be contributing.

Moderate growth is expected in interest revenue while interest rates have been increasing. The County will also have an increase in rent income from the leasing of radio towers space, Legacy Hall and the Jamestown Marina.

More than 53% of the County's General Fund revenue increase is allocated to school spending. The County's contribution to the Williamsburg-James City County School Board will increase by \$9,730,524.

Contacting the County's Financial Management

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the County's finances and to demonstrate the County's accountability for the money it receives. Questions concerning this report or requests for additional information should be directed to the Department of Financial and Management Services, 101-F Mounts Bay Road, P.O. Box 8784, Williamsburg, Virginia 23187-8784.