## Management's Discussion And Analysis

The management discussion and analysis section of the City of Redmond's Comprehensive Annual Financial Report provides an overview of the City's financial activities for the year ending December 31, 2012, and for the City's financial position at December 31, 2012. This information should be read in conjunction with the preceding letter of transmittal and the financial statements and notes to the financial statements that follow. Particular attention should be paid to the discussion regarding the City's implementation of GASB's Statement 54 which occurred in 2011.

## Financial Highlights

- Net position, the amount by which total assets exceed total liabilities, equaled \$685,376,330 at the end of 2012. The City's net position increased by \$25,014,930 or 3.78% in 2012. Governmental activities had a increase of \$8,566,168 or 2.43% from 2011. The increase is predominantly due to an increase in grant revenue of \$2,945,253 or 90.00% with transportation projects showing the largest increase. There was also increase in charges for services of \$3,667,168 or 10.70% primarily in economic environment. Business-Type activities had an increase of \$16,448,762 or 5.33% from 2011 which is largely attributed to increased grant revenues of \$3,640,914 or 52.00%.
- Of the remaining net position, \$32,127,404 and \$51,425,779 are restricted and unrestricted, respectively, for Governmental Activities. A major component of the legally restricted portion is for capital projects, which account for \$12,005,233 or 33.82% of total restricted net position citywide compared to \$18,565,237 or 56.29% in 2011. Business-type activities show \$3,366,947 and \$57,802,105 restricted and unrestricted respectively. The restricted portion is related to the bond reserve fund and the rate stabilization fund.
- Governmental fund balances at year-end were \$76,118,254 a decrease of \$1,595,678 from the prior year. The City experienced a decrease in cash and investments of \$5,725,141 and also had an increase in total liabilities of \$657,790. The City saw an increase of \$871,588, \$11,471,854 and \$947,543 in unassigned, assigned and restricted fund balances respectively in the General Fund. Other legally restricted or committed by City policy fund balances are \$6,596,111, \$310,856 and \$9,867,809 for special revenue, debt service, and capital improvement projects (CIP) fund purposes, respectively.

# **Budget Adjustments**

The difference between the original budget and final budget for the general fund for the biennium 2011-2012 totaled an increase of \$3,838,509 in revenues and \$13,288,312 in expenditures which accounts for a budgetary decrease of \$9,499,803 of total net position of the City. The result is to reduce the anticipated excess of revenues over expenditures from \$12,705,625 to \$3,255,822. These adjustments included an increase in the biennial budgets for transportation and parks maintenance and capital projects, as well as economic development. The adjustments occurred as part of the city's transition to comply with GASB Statement 54 as described in full detail in the notes to the financial statements in the 2011 Comprehensive Annual Financial Report.

## Overview of the Financial Statements

The City's basic financial statements are presented in three parts: 1) government-wide financial statements; 2) fund financial statements; and 3) notes to the financial statements. Other supplementary information in addition to the basic financial statements is also contained in this report. This section of the management's discussion and analysis is intended to introduce and explain the basic financial statements.

#### Government-wide financial statements

The government-wide financial statements are designed to give the reader a picture of the financial condition and activities of the City as a whole. This broad overview is similar to the financial reporting of private sector businesses. The government-wide financial statements have separate columns for governmental activities and business-type activities. Governmental activities of the City include general government (finance, executive and human resources), security (police and fire), physical environment, economic environment, transportation, mental/physical health, and culture and recreation. The City's business-type activities are limited to water/wastewater and stormwater utilities. Governmental activities are primarily supported by taxes, charges for services, and grants. Business-type activities are primarily self-supporting through user fees and charges.

The Statement of Net Position presents information on all of the City of Redmond's assets and liabilities, highlighting the difference between the two as net position. This statement is similar to the balance sheet of a private sector business. Over time, increases or decreases in net position may be one indicator of improvement or deterioration in the City's overall financial health.

The Statement of Activities presents information designed to show how the City's net position changed during the year. This statement distinguishes revenue generated by specific functions from revenue provided by taxes and other sources not related to a specific function. The revenue generated by the specific functions (charges for services, grants, and contributions) is compared to the expenses for those functions to show the degree to which each function supports itself or relies on taxes and other general funding sources for support. All activity on this statement is reported on the accrual basis of accounting, requiring that revenues are reported when they are earned and expenses are reported when they are incurred, regardless of when cash is received or disbursed. Items such as (but not limited to) uncollected taxes, unpaid vendor invoices for goods or services received during the year, and earned but unused vacation leave are included in the statement of activities as revenue and expenses even though no cash has changed hands.

## **Fund Financial Statements**

The annual financial report includes fund financial statements in addition to the government-wide financial statements. While the government-wide statements present the City's finances based on the type of activity, general government versus business-type, the fund financial statements are presented by fund type such as the general fund, special revenue funds, and proprietary funds. A fund is a fiscal and accounting entity with a self-balancing set of accounts used to account for specific activities or meet certain objectives. Funds are often set up in accordance with special regulations, restrictions or limitations. The City of Redmond, like other state and local governments, uses fund accounting to ensure and show compliance with finance-related legal requirements. The City's funds are divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental funds are used to account for essentially the same functions as are reported as governmental activities in the government-wide financial statements. These reports use a different "basis of accounting" than that used in government-wide financial statements. The governmental fund statements focus on near-term revenues/financial resources and expenditures while the government-wide financial statements include both near-term and long-term revenues/financial resources and expenses. The information in the governmental fund statements can be used to evaluate the City's near-term financing requirements and immediate fiscal health. Comparing the governmental fund statements with the government-wide statements can help the reader better understand the long-term impact of the City's current year financing decisions. To assist in this comparison, reconciliations between the governmental fund statements and the government-wide financial statements are included with the governmental fund Balance Sheet and the governmental fund Statement of Revenues, Expenditures, and Changes in Fund Balances.

The City of Redmond maintains thirteen individual governmental funds. The City's two major governmental funds – the general fund and the capital improvements program fund – are presented separately in the governmental fund Balance Sheet and the governmental fund Statement of Revenues, Expenditures, and Changes in Fund Balances. The remaining governmental funds are combined in this statement into a single column labeled other governmental funds. Individual fund data for each of the other governmental funds can be found in combining statements later in this report.

The City maintains budgetary control over its operating funds through the adoption of a biennial budget. Budgets are adopted at the fund level for all funds in accordance with state law. All budgetary comparison schedules are included following the other governmental funds' combining statements in this report.

Proprietary funds are used by governments to account for their business-type activities. Business-type activities provide specific goods or services to a group of customers that are paid for by fees charged to those customers. There is a direct relationship between the fees paid and the services received.

The City of Redmond has two types of proprietary funds, enterprise funds and internal service funds. Enterprise funds are used to account for goods and services provided to citizens and the community. Internal service funds are used to account for goods and services provided internally to various City departments. The same basis of accounting is used for proprietary funds in both the government-wide statements and the individual fund statements.

Enterprise funds of the City are used to report the same functions presented as business-type activities in the government-wide statements with the fund statements providing more detail than is reported in the government-wide statements. The enterprise fund statements provide separate information for the City's water/wastewater utility, an Urban Planned Development (UPD) water/wastewater utility outside the City limits, and the City's stormwater utility.

Internal service funds are an accounting device used to accumulate and allocate costs internally among the City's various functions. The City uses internal service funds to account for its fleet of vehicles, insurance premiums and claims, medical self-insurance, workmen's compensation self-insurance program, information technology, and one blended component unit, Redmond Community Properties. Internal service funds benefit both governmental and business-type activities and are allocated accordingly in the government-wide statement of activities. Internal service fund assets and liabilities are predominantly governmental and have been included in the governmental activities column of the government-wide statement of net position.

Fiduciary funds account for assets held by the City in a trustee capacity or as an agent for individuals, private organizations, other governments, or other funds. Fiduciary funds are not included in the government-wide financial statements because their assets are not available to support the City of Redmond's activities.

The City has two types of fiduciary funds, a pension fund and agency funds. The accounting for the pension fund is on the accrual basis. Agency funds are custodial in nature and do not include revenues and expenses as they do not measure the results of operations.

## Notes to the financial statements

The notes to the financial statements provide additional information that is important for a full understanding of the data in the government-wide and fund financial statements. The notes are located immediately following the basic financial statements.

#### Other information

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the City's progress in funding its obligation to provide pension benefits to certain retired firefighters and lifetime medical benefits to uniformed personnel hired before October 1, 1977. Required supplementary information may be found immediately following the notes to the financial statements.

The combining statements for other governmental funds, internal service funds, and agency-type fiduciary funds are presented immediately following the required supplementary information.

# Government-wide Financial Analysis

## Statement of Net Position

The Statement of Net Position can serve as a useful indicator of the City's financial position. The City of Redmond's net position at December 31, 2011 and 2012 total \$660,698,559 and \$685,376,330 respectively. Following is a condensed version of the government-wide Statement of Net Position for 2012 compared to 2011.

## City of Redmond's Net Position (in thousands)

		Governmental Activities				Business	-Type A	ctivities			Total	
	_	2012	_	2011	_	2012	_	2011	-	2012		2011
Current and other assets	\$	103,227	\$	103,523	\$	64,094	\$	55,375	\$	167,321	\$	158,898
Capital assets, net of accumulated depreciation		349,212		341,265		273,626		266,467		622,838		607,732
Total assets	\$	452,439	\$	444,788	\$	337,720	\$	321,842	\$	790,159	\$	766,630
Long-term liabilities Other liabilities	\$	79,343 12,906	\$	80,490 12,430	\$	10,133 2,400	\$	10,853 2,159	\$	89,476 15,306	\$	91,343 14,589
Total liabilities	\$	92,249	\$	92,920	\$	12,533	\$ _	13,012	\$	104,782	\$	105,932
Net Position Invested in capital												
assets, net of related debt	\$	276,636	\$	266,802	\$	264,018	\$	256,195	\$	540,654	\$	522,997
Restricted		32,127		47,237		3,367		2,220		35,494		49,457
Unrestricted	_	51,426	_	37,829	_	57,802	_	50,415	_	109,228		88,244
Total net position	\$_	360,189	\$	351,868	\$ _	325,187	\$ _	308,830	\$	685,376	\$	660,698

# Changes in net position

The changes in net position table illustrates the increases or decreases in net position of the City resulting from its operating activities. Following is a condensed version of the City's changes in net position. The table shows the revenues, expenses, and related changes in net position in tabular form for the governmental activities separate from the business-type activities for 2011 and 2012.

# City of Redmond's Changes in Net Position (in thousands)

	Governmental Activities					Business-Type Activities						Total				
		2012			2011		2012			2011			2012			2011
Revenues:																
Program revenues																
Charges for services	\$	37,950		\$	34,283		\$ 47,405		\$	44,981		\$	85,355		\$	79,264
Operating grants and contributions		4,571			760		1,194			599			5,765			1,359
Capital grants and contributions		1,648			2,513		9,449			6,403			11,097			8,916
General revenues		00.044			04.070								00.044			04.070
Property taxes		22,611			21,978	-	-			-			22,611			21,978
Sales taxes		20,722			24,895		-			-			20,722			24,895
Other taxes		20,222			19,338		-			-			20,222			19,338
Investment interest		632			937		(8)			48			624			985
Miscellaneous		1,165			2,152	_	176			143			1,341			2,295
Total revenues	\$	109,521		\$	106,856		\$ 58,216		\$	52,174		\$	167,737		\$	159,030
Expenses:																
General government	\$	18,888		\$	24,253		\$		\$	-		\$	18,888		\$	24,253
Security		37,630			28,751					-			37,630			28,751
Physical environment		6,013			5,976					-			6,013			5,976
Economic environment		5,603			6,218					-			5,603			6,218
Transportation		15,748			14,818					-			15,748			14,818
Mental/physical health		-			890					-			-			890
Culture and recreation		13,762			15,191					-			13,762			15,191
Interest on long term debt		3,310			3,506					-			3,310			3,506
Water/Wastewater		-			-		28,397			27,519			28,397			27,519
Novelty Hill Water/Wastewater		-			-		6,121			5,752			6,121			5,752
Stormwater		-			-		7,249			7,061			7,249			7,061
Total expenses	\$	100,955		\$	99,603		\$ 41,767		\$	40,332		\$	142,722		\$	139,935
Increase/(Decrease) in net position		8,566			7,253		16,449			11,842			25,015			19,095
Net position - beginning		351,869			344,616		308,830			296,989			660,699			641,604
Prior Period Adjustment*		(245)			-		(92)			-			(337)			-
Net position - ending	\$	360,190		\$	351,869		\$ 325,187		\$	308,830		\$	685,377		\$	660,699

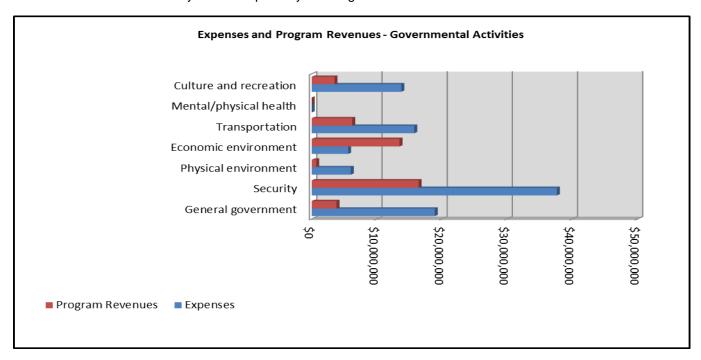
<sup>\*</sup>Due to the implementation of GASB 65. See note 19 for further details.

Governmental activities experienced an increase in total net position of \$8,566,168. Governmental activities accounts for 52.55% of the City's net position in 2012.

Key elements of the 2012 increase are as follows:

- Total assets from Governmental activities increased by \$7,650,543.
  - Cash and investments reflect a decrease of \$3,552,093 from 2011 to 2012 (a change of 3.88%) while investment in capital assets increased by \$7,945,978. This is consistent with the City's plans for investments in infrastructure and technology.
  - There was also an increase in due from other governments related to grant billings processed for the last quarter of 2012.
- Total liabilities from Governmental activities decreased by \$670,670 (0.72%).
  - Long-term debt decreased by \$1,480,834 as a result of principal payments on debt previously held by the City. See Note 13 to the financial statements for more information.
  - Due from other governements, unearned revenue and customer deposits increased by \$526,072, \$76,553, \$1,021,690 respectively.
- The total revenue increased between 2011 and 2012 by \$2,665,258. This increase largely related to taxes received in 2012 but consisted of several components.
  - Increases were primarily in operating grants and contributions as well as charges for services.
  - Sales taxes in 2011 included a one-time payment of sales taxes of approximately \$4.7 million which resulted from an audit conducted by the Washington State Department of Revenue. As a result the 2012 sales tax is more consistent with economic trends.
- Total expenses showed an increase from 2011 to 2012 of \$1,351,738.
  - This increase amounts to an average of 1.36% and is consistent with typical cost increases in operations. It is important to note that some activities in the city experienced larger increases than others. For example security of persons and property incurred a 30.89% increase which is due to the completion of construction of a new fire station which is an expense on the governmental statements. This is a one-time increase and not due to regular operations.

The graph that follows compares program revenues to program expenses from the Statement of Activities and illustrates the revenues by source separately for the governmental activities for 2012.

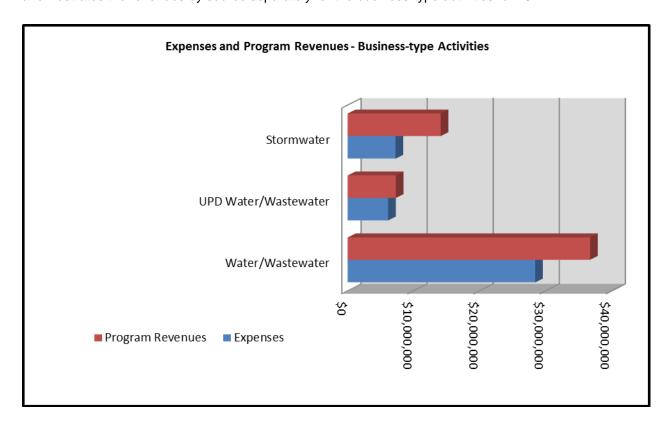


Business-type activities of the City's utilities increased the City of Redmond's net position by \$16,448,762 (5.33%). Business-type activities accounts for 47.45% of the City's net position.

Key elements of this increase are as follows:

- The investments in capital assets increased \$7,158,911 or 2.82% between 2011 and 2012.
- The Water/Wastewater utility showed operating income of \$1,291,080 in 2012 (compared to \$457,835 in 2011) while the UPD Water/Wastewater utilities showed an operating income of \$478,300. When non-operating income and capital contributions are included, the change in net position is \$8,084,723 for the Water/Wastewater utility and \$1,302,379 for the UPD Water/Wastewater utility.
- The City has begun work on significant stormwater projects that will place a central line that will include filtration that will discharge to a pond. This project is tied to the acquisition of a rail corridor which was finalized in 2010. Construction on this project commenced in 2012. The total operating revenue for 2012 was \$11,117,216 with operating expenses of 7,249,420 for a net operating income of \$3,867,796.

The graph that follows compares program revenues to program expenses from the Statement of Activities and illustrates the revenues by source separately for the business-type activities for 2012.



## City of Redmond's Capital Assets (net of depreciation)

The City continued its commitment to investment in capital assets in 2012 as reflected in the following table. The increase from 2011 to 2012 was \$15,104,888 or 2.49% from 2011.

Governmental activities increased \$7,945,978 (2.33%) partially made up of:

 Acquisition of land for parks and investments in buildings and related improvements (such as the new fire station completed in 2012)

Business-Type Activities reflected an increase of \$7,158,910 (2.69%) partially made up of:

• Improvements to utility infrastructure both completed by the city as well as provided by private development and then dedicated to the city for future maintenance and upkeep.

		Governme	ntal	Activities	_	Busine Acti	<b>J</b> 1		Total		
	-	2012	-	2011		2012	 2011	_	2012		2011
Land	\$	99,358,356	\$	85,065,414	\$	12,608,494	\$ 12,453,045	\$	111,966,850	\$	97,518,459
Buildings/ Bldg. Improvements		59,188,486		53,339,082		31,760,000	32,502,952		90,948,486		85,842,034
Improvements other than buildings		19,293,264		19,308,280		220,580,255	209,225,171		239,873,519		228,533,451
Machinery and equipment Construction		11,976,074		12,491,423		98,264	173,627		12,074,338		12,665,050
in progress		5,798,531		16,951,480		8,579,078	12,112,386		14,377,609		29,063,866
Infrastructure		153,200,724		153,765,346		-	-		153,200,724		153,765,346
Art	_	396,154		344,583		-	 -		396,154		344,583
Total	\$	349,211,589	\$	341,265,608	\$	273,626,091	\$ 266,467,181	\$	622,837,680	\$	607,732,789

Additional information on the City of Redmond's capital assets can be found in note 8 of this report.