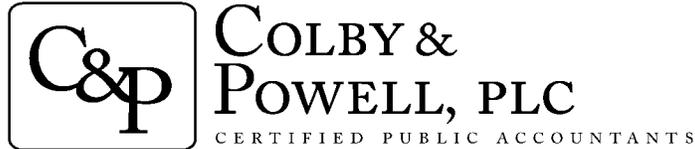


TOWN OF PATAGONIA, ARIZONA

Annual Financial Statements
and Independent Auditors' Reports
June 30, 2017

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INDEPENDENT AUDITORS' REPORT

To the Town Council
Town of Patagonia, Arizona

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Town of Patagonia, Arizona, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Town's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Town of Patagonia, Arizona, as of June 30, 2017, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 through 10, Budgetary Comparison Schedules on pages 51 through 54, Schedule of the Town's Proportionate Share of the Net Pension Liability – Cost-Sharing Pension Plans on page 55, Schedule of Changes in the Town's Net Pension Liability (Asset) and Related Ratios – Agent Pension Plans on page 56, Schedule of Town Pension Contributions on page 57, and Schedule of Agent OPEB Plans' Funding Progress on page 59, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated February 28, 2018, on our consideration of the Town of Patagonia, Arizona's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance

with *Government Auditing Standards* in considering the Town of Patagonia, Arizona's internal control over financial reporting and compliance.

Other Reporting Required by Arizona Revised Statutes

In connection with our audit, nothing came to our attention that caused us to believe that the Town failed to use highway user revenue fund monies received by the Town pursuant to Arizona Revised Statutes Title 28, Chapter 18, Article 2 and any other dedicated state transportation revenues received by the Town solely for the authorized transportation purposes, insofar as they relate to accounting matters. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Town's noncompliance with the use of highway user revenue fund monies and other dedicated state transportation revenues, insofar as they relate to accounting matters.

A handwritten signature in cursive script that reads "Colby + Powell".

February 28, 2018

TOWN OF PATAGONIA, ARIZONA
Management's Discussion and Analysis
June 30, 2017

Describe the Basic Financial Statements

This discussion and analysis of the Town of Patagonia's financial performance reviews the Town's activities for the fiscal year ended June 30, 2017. The Town has two major parts to its financial statements. One part is the government-wide statements combining all operations carried out by the Town. The second part is the fund statements, again in two parts. One part is the governmental funds, which represents the normal governmental activities of administration, public safety, etc. The other part consists of the proprietary funds representing the Town's water, sewer and solid waste utilities. These funds operate and are accounted for much like a business.

Impacts, Fiscal Year 2017

- Governmental revenues for the year continued to increase as the overall economy has improved.
- Proprietary revenues increased over the two previous years but still fall below FY 2009
- Total revenues exceeded 2011 through 2016 but still did not reach the FY 2009 level, remaining well below totals from earlier years and below the levels needed to provide for needed maintenance and upgrade of major equipment and infrastructure.

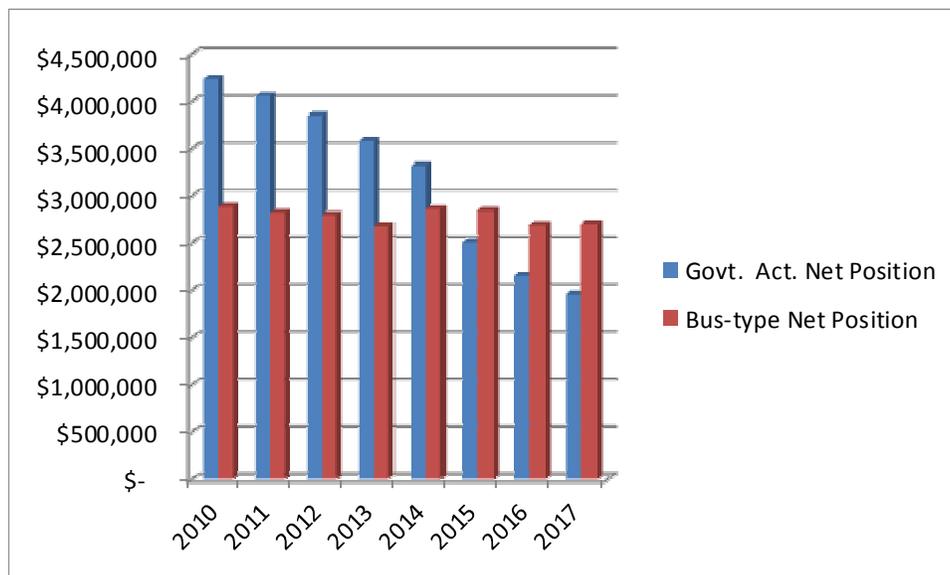
| Condensed Statement of Net Position | | |
|---|-------------------------|--------------------------|
| | Governmental Activities | Business-type Activities |
| Assets | | |
| Cash and cash equivalents | \$ 584,499 | \$ 171,271 |
| Other assets | 76,533 | 82,760 |
| Capital assets, net of depreciation | 2,232,777 | 3,673,094 |
| Total Assets | 2,893,809 | 3,927,125 |
| Deferred outflows of resources | | |
| | 242,680 | 52,458 |
| Liabilities | | |
| Current liabilities | 155,775 | 96,357 |
| Long-term liabilities, net of current portion | 946,213 | 1,145,865 |
| Total Liabilities | 1,101,988 | 1,242,222 |
| Deferred inflows of resources | | |
| | 78,938 | 32,278 |
| Net Position | | |
| Net investment in capital assets | 2,232,777 | 2,966,506 |
| Restricted | 89,248 | 53,714 |
| Unrestricted | (366,462) | (315,137) |
| Total Net Position | \$ 1,955,563 | \$ 2,705,083 |

TOWN OF PATAGONIA, ARIZONA
Management's Discussion and Analysis
June 30, 2017

Net Position FY 2010 to FY 2017

| | Govt. Act. Net Position | Bus-type Net Position | Total Net Position |
|------|----------------------------|--------------------------|--------------------|
| 2010 | \$ 4,247,159 | \$ 2,886,575 | \$ 7,133,734 |
| 2011 | 4,066,251 | 2,825,865 | 6,892,116 |
| 2012 | 3,857,857 | 2,801,031 | 6,658,888 |
| 2013 | 3,592,822 | 2,684,837 | 6,277,659 |
| 2014 | 3,321,239 | 2,862,317 | 6,183,556 |
| 2015 | 2,505,205 | 2,844,593 | 5,349,798 |
| 2016 | 2,161,826 | 2,695,724 | 4,857,550 |
| 2017 | 1,955,563 | 2,705,083 | 4,660,646 |

Net Position continued to decrease as reserves were used to maintain essential services even as revenues traditionally received from the State were diverted to other purposes.

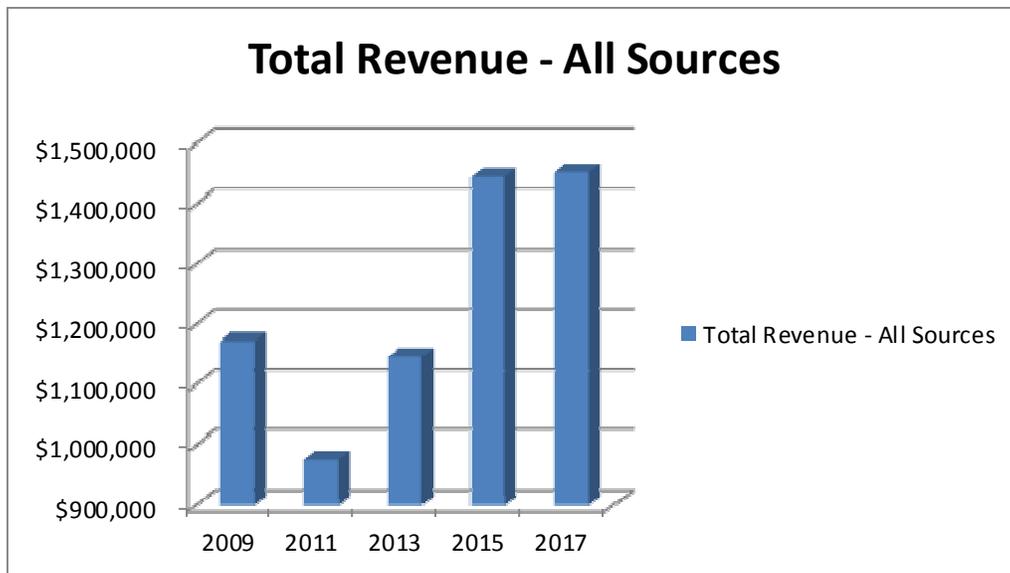


TOWN OF PATAGONIA, ARIZONA
Management's Discussion and Analysis
June 30, 2017

Comparison of Revenues by Year

| | 2009 | 2011 | 2013 | 2015 | 2017 |
|------------------------------------|---------------------|-------------------|---------------------|---------------------|---------------------|
| Governmental Fund Revenues | | | | | |
| Local sales taxes | \$ 190,942 | \$ 158,776 | \$ 197,540 | \$ 244,484 | \$ 263,558 |
| Intergovernmental net of grants | 444,157 | 351,807 | 379,302 | 523,026 | 471,590 |
| Charges for services | 27,883 | 28,645 | 27,669 | 25,406 | 33,340 |
| Franchise fees | 28,155 | 23,569 | 14,310 | 13,217 | 14,145 |
| Other revenue | 7,325 | 17,871 | 7,245 | 25,043 | 30,788 |
| Fines and forfeitures | 52,177 | 14,059 | 83,394 | 131,562 | 80,950 |
| Licenses and permits | 16,189 | 13,867 | 32,174 | 18,923 | 13,105 |
| Investment income | 334 | 2,652 | 6,097 | 2,025 | 2,742 |
| Total | \$ 767,162 | \$ 611,246 | \$ 747,731 | \$ 983,686 | \$ 910,218 |
| Proprietary Fund Revenues | | | | | |
| Water | \$ 116,077 | \$ 93,952 | \$ 110,090 | \$ 140,109 | \$ 181,780 |
| Sewer | 161,379 | 147,873 | 154,699 | 146,027 | 182,495 |
| Solid waste | 126,743 | 121,220 | 133,629 | 174,652 | 177,251 |
| Total | \$ 404,199 | \$ 363,045 | \$ 398,418 | \$ 460,788 | \$ 541,526 |
| Total Revenue - All Sources | \$ 1,171,361 | \$ 974,291 | \$ 1,146,149 | \$ 1,444,474 | \$ 1,451,744 |

The revenue picture is varied looking at the comparisons shown above. State revenues showed a modest increase, but are still far short of previous levels. Sales taxes continued their increase. Fines and forfeitures were at a higher level but have now dropped again due to state restrictions on citations for expired Mexican registrations which were briefly a major source of revenue. A rate increase for water and sewer fees returned that proprietary fund to a positive level.



TOWN OF PATAGONIA, ARIZONA
Management's Discussion and Analysis
June 30, 2017

Annual Expenditures by Function

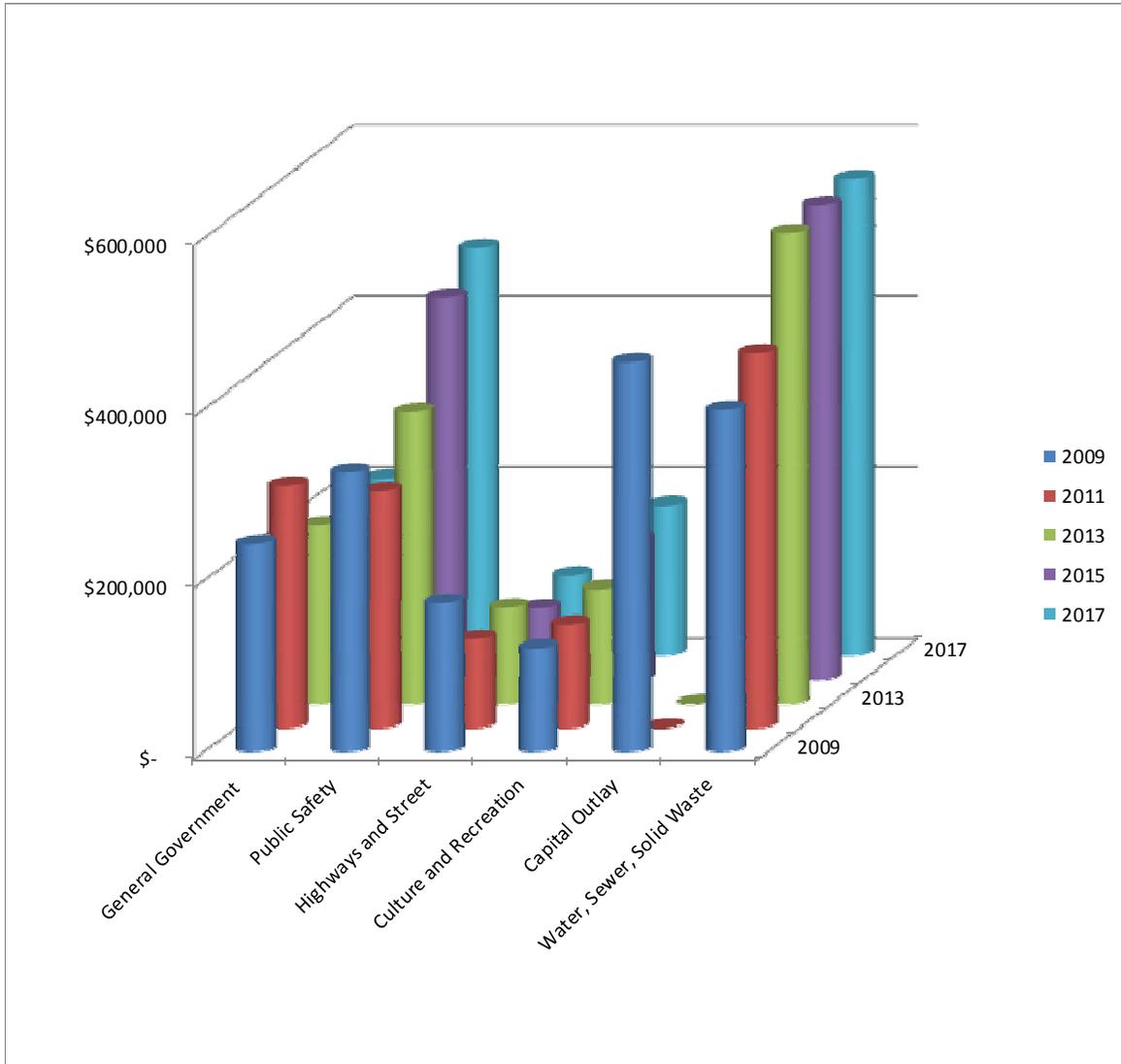
Annual expenditures have varied by function, with general government slightly down while public safety is up, culture and recreation is up reflecting some grants received for work in the park by the tree and park committee and the proprietary funds are up reflecting major charges to the Water Fund for emergency repairs.

The following chart and graph shows a comparison of annual expenditures by major account.

| | 2009 | 2011 | 2013 | 2015 | 2017 |
|-------------------------------------|------------|------------|------------|------------|------------|
| Government Fund Expenditures | | | | | |
| General Government | \$ 243,422 | \$ 283,055 | \$ 207,793 | \$ 205,444 | \$ 205,897 |
| Public Safety | 325,983 | 276,892 | 340,288 | 445,773 | 474,807 |
| Highways and Street | 174,169 | 103,645 | 112,101 | 82,989 | 93,073 |
| Culture and Recreation | 121,214 | 120,892 | 133,730 | 163,532 | 174,730 |
| Capital Outlay | 455,142 | - | - | 151,651 | 161,063 |
| Proprietary Fund Expenses | | | | | |
| Water, Sewer, Solid Waste | \$ 399,530 | \$ 437,675 | \$ 549,571 | \$ 554,299 | \$ 555,799 |

TOWN OF PATAGONIA, ARIZONA
Management's Discussion and Analysis
June 30, 2017

Comparative Expenditures by Function



Analysis of Overall Financial Position and Results of Operations

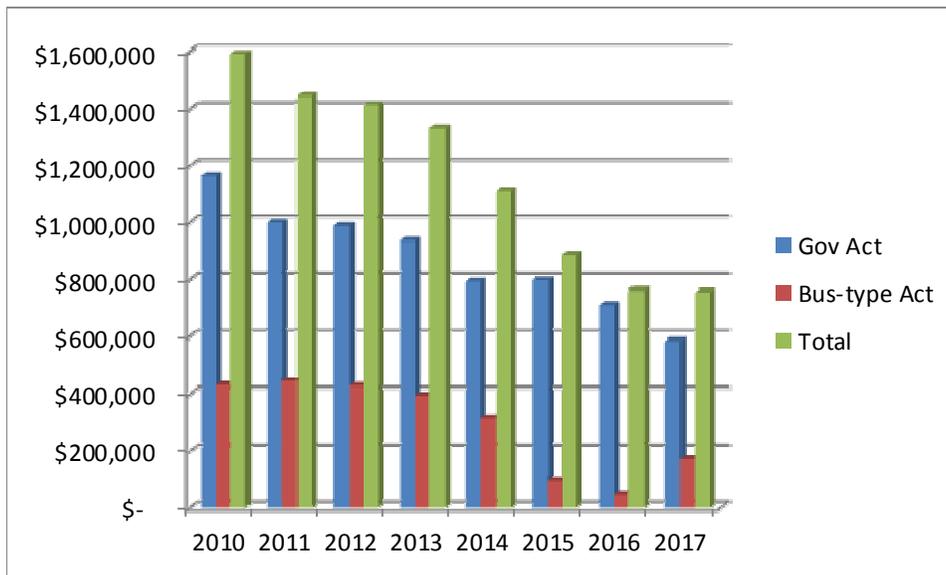
Discussion of Significant Transactions and Changes in Funds

- After a downward trend stretching back to 2007, the Town's overall position continued modestly upwards. It reflects increases in sales tax revenue and water and sewer rate increases.
- Aging equipment and infrastructure continued to cause significant charges in the maintenance category as items that should have been replaced were patched together again and again.
- Fines for expired Mexican registrations were ruled uncollectible by the AZ Supreme Court.

TOWN OF PATAGONIA, ARIZONA
Management's Discussion and Analysis
June 30, 2014

Cash and Equivalents

| | Gov Act | Bus-type Act | Total |
|------|--------------|--------------|--------------|
| 2010 | \$ 1,163,126 | \$ 428,369 | \$ 1,591,495 |
| 2011 | 999,035 | 443,046 | 1,442,081 |
| 2012 | 987,611 | 425,980 | 1,413,591 |
| 2013 | 934,659 | 394,383 | 1,329,042 |
| 2014 | 793,562 | 312,860 | 1,106,422 |
| 2015 | 797,333 | 90,870 | 888,203 |
| 2016 | 712,204 | 49,120 | 761,324 |
| 2017 | 584,499 | 171,271 | 755,770 |



Patagonia continues to enjoy a relatively healthy financial position with reserves in both the Governmental Activities and the Business-type Activities at a level adequate to offset short-term revenue variations such as those caused by the continuing global financial crisis, however, expenditures for the highway system resulted in a slight reduction in the overall cash position.

TOWN OF PATAGONIA, ARIZONA
Management's Discussion and Analysis
June 30, 2017

Revenues - Budget vs. Actual

| General Fund Revenues | Budget | Actual | Variation |
|-----------------------|------------|------------|-----------|
| Local sales taxes | \$ 245,000 | \$ 263,558 | \$ 18,558 |
| Intergovernmental | 539,857 | 366,405 | (173,452) |
| Charges for services | 33,708 | 33,340 | (368) |
| Franchise fees | 13,250 | 14,145 | 895 |
| Other revenue | 114,700 | 30,788 | (83,912) |
| Fines and forfeitures | 143,500 | 80,950 | (62,550) |
| Licenses and permits | 27,500 | 13,105 | (14,395) |
| Investment income | 1,000 | 2,506 | 1,506 |
| Total | 1,118,515 | 804,797 | (313,718) |

The variations in intergovernmental and other revenue were a result of the Town not receiving some grants that had been hoped for and a contingency that was also not realized.

Expenditures - Budget vs. Actual

| General Fund Expenditures | Budget | Actual | Variation |
|---------------------------|------------|------------|-----------|
| General government | \$ 288,157 | \$ 205,897 | \$ 82,260 |
| Public safety | 627,294 | 474,807 | 152,487 |
| Culture and recreation | 174,730 | 174,730 | - |
| Capital outlay | 27,974 | 27,974 | - |
| Total | 1,118,155 | 883,408 | 234,747 |

Description Long-term Debt Activity during FY 2017

There was no significant long-term debt activity other than regular annual principal and interest payments.

Description of Currently Known Facts, Decisions and Conditions Expected to have a Significant Effect on next year and beyond.

Governor Ducey continues to promise to restore local revenues but so far has failed to do so.

Contacting the Town of Patagonia's Financial Management:

This report is designed to provide our citizens, taxpayers, customers and investors and creditors with a general overview of the Town's finances and to demonstrate the Town's accountability for the money it receives. If you have questions about this report or need additional financial information contact the Town offices at 310 McKeown Avenue, Patagonia, AZ 85624, or by calling 520-394-2229. Budget information is also available at the Town website www.townofpatagonia.com.

TOWN OF PATAGONIA, ARIZONA
Statement of Net Position
June 30, 2017

| | Primary Government | | |
|--|----------------------------|-----------------------------|---------------------|
| | Governmental Activities | Business-type Activities | Total |
| ASSETS | | | |
| Cash and cash equivalents | \$ 584,499 | \$ 94,109 | \$ 678,608 |
| Cash and cash equivalents, restricted | - | 77,162 | 77,162 |
| Accounts receivable | - | 55,455 | 55,455 |
| Taxes receivable | 2,119 | - | 2,119 |
| Due from other governments | 37,308 | 8,752 | 46,060 |
| Prepaid expenses | 37,106 | 18,553 | 55,659 |
| Capital assets, not being depreciated | 355,867 | 150,540 | 506,407 |
| Capital assets, being depreciated, net | 1,876,910 | 3,522,554 | 5,399,464 |
| Total assets | <u>2,893,809</u> | <u>3,927,125</u> | <u>6,820,934</u> |
| DEFERRED OUTFLOWS OF RESOURCES | | | |
| Deferred outflows related to pensions | 242,680 | 52,458 | 295,138 |
| LIABILITIES | | | |
| Accounts payable | 108,545 | 22,513 | 131,058 |
| PSPRS Parker liability | 13,000 | - | 13,000 |
| Refundable deposits | - | 23,448 | 23,448 |
| Compensated absences | | | |
| Due within 1 year | 34,230 | 12,959 | 47,189 |
| Noncurrent liabilities | | | |
| Due within 1 year | - | 37,437 | 37,437 |
| Due in more than 1 year | 946,213 | 1,145,865 | 2,092,078 |
| Total liabilities | <u>1,101,988</u> | <u>1,242,222</u> | <u>2,344,210</u> |
| DEFERRED INFLOWS OF RESOURCES | | | |
| Deferred inflows related to pensions | 78,938 | 32,278 | 111,216 |
| NET POSITION | | | |
| Net investment in capital assets | 2,232,777 | 2,966,506 | 5,199,283 |
| Restricted for: | | | |
| Court enhancement | 86,054 | - | 86,054 |
| Library | 3,194 | - | 3,194 |
| Debt service | - | 26,857 | 26,857 |
| Repairs and replacements | - | 26,857 | 26,857 |
| Unrestricted (deficit) | (366,462) | (315,137) | (681,599) |
| Total net position | <u>\$ 1,955,563</u> | <u>\$ 2,705,083</u> | <u>\$ 4,660,646</u> |

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Statement of Activities
Year Ended June 30, 2017

| Functions / Programs | Expenses | Program Revenue | | | Net (Expense) Revenue and Changes in Net Position | | |
|---------------------------------------|---------------------|----------------------|------------------------------------|----------------------------------|---|---|------------------|
| | | Charges for Services | Operating Grants and Contributions | Capital Grants and Contributions | Governmental Activities | Primary Government Business-type Activities | Total |
| Primary government: | | | | | | | |
| Governmental activities | | | | | | | |
| General government | \$ 246,290 | \$ 43,840 | \$ 12,213 | \$ - | \$ (190,237) | \$ - | \$ (190,237) |
| Public safety | 462,890 | 80,950 | - | 2,094 | (379,846) | - | (379,846) |
| Highways and streets | 204,608 | - | 105,185 | - | (99,423) | - | (99,423) |
| Culture and recreation | 202,693 | 2,605 | 33,277 | - | (166,811) | - | (166,811) |
| Total governmental activities | 1,116,481 | 127,395 | 150,675 | 2,094 | (836,317) | - | (836,317) |
| Business-type activities | | | | | | | |
| Water/wastewater | 409,238 | 364,275 | - | 21,876 | - | (23,087) | (23,087) |
| Solid waste | 146,561 | 177,251 | - | - | - | 30,690 | 30,690 |
| Total business-type activities | 555,799 | 541,526 | - | 21,876 | - | 7,603 | 7,603 |
| Total primary government | \$ 1,672,280 | \$ 668,921 | \$ 150,675 | \$ 23,970 | (836,317) | 7,603 | (828,714) |
| General revenue: | | | | | | | |
| Taxes: | | | | | | | |
| Town sales tax | | | | | 263,558 | - | 263,558 |
| Franchise fees | | | | | 14,145 | - | 14,145 |
| State revenue sharing | | | | | 183,514 | - | 183,514 |
| State sales tax | | | | | 81,367 | - | 81,367 |
| Auto lieu tax | | | | | 71,806 | - | 71,806 |
| Miscellaneous | | | | | 12,922 | - | 12,922 |
| Investment income | | | | | 2,742 | 1,756 | 4,498 |
| Total general revenue | | | | | 630,054 | 1,756 | 631,810 |
| Change in net position | | | | | (206,263) | 9,359 | (196,904) |
| Net position, beginning of year | | | | | 2,161,826 | 2,695,724 | 4,857,550 |
| Net position, end of year | | | | | \$ 1,955,563 | \$ 2,705,083 | \$ 4,660,646 |

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Balance Sheet
Governmental Funds
June 30, 2017

| | General Fund | HURF Fund | Grants Fund | Total Governmental Funds |
|---|-------------------|------------------|-----------------|--------------------------------|
| Assets | | | | |
| Cash and cash equivalents | \$ 581,305 | \$ - | \$ 3,194 | \$ 584,499 |
| Taxes receivable | 2,119 | - | - | 2,119 |
| Due from other governments | 27,539 | 9,769 | - | 37,308 |
| Prepaid expenses | 18,553 | 18,553 | - | 37,106 |
| Due from other funds | 87,040 | - | - | 87,040 |
| Total assets | \$ 716,556 | \$ 28,322 | \$ 3,194 | \$ 748,072 |
| Liabilities | | | | |
| Accounts payable | \$ 17,468 | \$ 91,077 | \$ - | \$ 108,545 |
| Due to other funds | - | 87,040 | - | 87,040 |
| Total liabilities | 17,468 | 178,117 | - | 195,585 |
| Fund balances | | | | |
| Nonspendable | 18,553 | 18,553 | - | 37,106 |
| Restricted for: | | | | |
| Court enhancement | 86,054 | - | - | 86,054 |
| Library | - | - | 3,194 | 3,194 |
| Unassigned | 594,481 | (168,348) | - | 426,133 |
| Total fund balance | 699,088 | (149,795) | 3,194 | 552,487 |
| Total liabilities and fund balance | \$ 716,556 | \$ 28,322 | \$ 3,194 | \$ 748,072 |

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Reconciliation of the Balance Sheet to the Statement of Net Position
Governmental Funds
June 30, 2017

| | |
|--|----------------------------|
| Fund balances-total governmental funds | \$ 552,487 |
| Amounts reported for governmental activities in the Statement of Net Position are different because: | |
| Capital assets used in governmental activities are not financial resources and, therefore, are not reported in | 2,232,777 |
| Long-term liabilities, such as net pension liabilities and bonds payable, are not due and payable in the current period and, therefore, are not reported as a liability in | (993,443) |
| Deferred outflows and inflows of resources related to pensions and deferred charges or credits on debt refundings are applicable to future reporting periods and, therefore, are not reported in the funds. | <u>163,742</u> |
| Net position of governmental activities | <u><u>\$ 1,955,563</u></u> |

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Statement of Revenue, Expenditures, and Changes in Fund Balance
Governmental Funds
Year Ended June 30, 2017

| | General Fund | HURF Fund | Grants Fund | Total Governmental Funds |
|---------------------------------|-------------------|---------------------|-----------------|--------------------------------|
| Revenues | | | | |
| Intergovernmental | \$ 366,405 | \$ 105,185 | \$ - | \$ 471,590 |
| Taxes | 263,558 | - | - | 263,558 |
| Fines and forfeitures | 80,950 | - | - | 80,950 |
| Charges for services | 33,340 | - | - | 33,340 |
| Other revenue | 30,788 | - | - | 30,788 |
| Franchise fees | 14,145 | - | - | 14,145 |
| Licenses and permits | 13,105 | - | - | 13,105 |
| Investment income | 2,506 | 236 | - | 2,742 |
| Total revenues | 804,797 | 105,421 | - | 910,218 |
| Expenditures | | | | |
| Current | | | | |
| General government | 205,897 | - | - | 205,897 |
| Public safety | 474,807 | - | - | 474,807 |
| Highways and streets | - | 93,073 | - | 93,073 |
| Culture and recreation | 174,730 | - | - | 174,730 |
| Capital outlay | 27,974 | 133,089 | - | 161,063 |
| Total expenditures | 883,408 | 226,162 | - | 1,109,570 |
| Net change in fund balances | (78,611) | (120,741) | - | (199,352) |
| Fund balance, beginning of year | 777,699 | (29,054) | 3,194 | 751,839 |
| Fund balance, end of year | <u>\$ 699,088</u> | <u>\$ (149,795)</u> | <u>\$ 3,194</u> | <u>\$ 552,487</u> |

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Reconciliation of the Statement of Revenue, Expenditures,
and Changes in Fund Balances to the Statement of Activities
Governmental Funds
Year Ended June 30, 2017

Net change in fund balances-total governmental funds \$ (199,352)

Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental funds report capital outlays as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

| | | |
|----------------------|------------------|----------|
| Capital outlay | 161,063 | |
| Depreciation expense | <u>(211,358)</u> | (50,295) |

Town pension contributions are reported as expenditures in the governmental funds when made. However, they are reported as deferred outflows of resources in the statement of net position because the reported net pension liability is measured a year before the Town's report date. Pension expense, which is the change in the net pension liability adjusted for changes in deferred outflows and inflows of resources related to pensions, is reported in the

| | | |
|----------------------------|-----------------|--------|
| Town pension contributions | 95,945 | |
| Pension expense | <u>(39,688)</u> | 56,257 |

Under the modified accrual basis of accounting used in the governmental funds, expenditures are not recognized for transactions that are not normally paid with expendable available resources. In the Statement of Activities, however, which is presented on the accrual basis of accounting, expenses are reported regardless of when the financial resources are available.

| | | |
|--|------------|-----------------|
| PSPRS Parker liability | (13,000) | |
| Decrease in compensated absences payable | <u>127</u> | <u>(12,873)</u> |

Change in net position of governmental activities \$ (206,263)

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Statement of Net Position
Proprietary Funds
June 30, 2017

| | Business-type Activities--Enterprise Funds | | |
|--|--|------------------------|---------------------|
| | Water/ Wastewater Fund | Solid Waste Fund | Total |
| Assets | | | |
| Current assets | | | |
| Cash and cash equivalents | \$ 14,328 | \$ 79,781 | \$ 94,109 |
| Cash and cash equivalents, restricted | 68,917 | 8,245 | 77,162 |
| Accounts receivable-net | 36,879 | 18,576 | 55,455 |
| Due from other governments | 8,752 | - | 8,752 |
| Prepaid expenses | 18,553 | - | 18,553 |
| Total current assets | <u>147,429</u> | <u>106,602</u> | <u>254,031</u> |
| Noncurrent assets | | | |
| Capital assets, net of accumulated depreciation, where applicable: | | | |
| Land | 30,540 | 120,000 | 150,540 |
| Utilities systems | 2,841,167 | 496,105 | 3,337,272 |
| Equipment | 74,558 | 110,724 | 185,282 |
| Capital assets, net | <u>2,946,265</u> | <u>726,829</u> | <u>3,673,094</u> |
| Total assets | <u>3,093,694</u> | <u>833,431</u> | <u>3,927,125</u> |
| Deferred outflows of resources | | | |
| Deferred outflows related to pensions | <u>39,536</u> | <u>12,922</u> | <u>52,458</u> |
| Liabilities | | | |
| Current liabilities | | | |
| Accounts payable | 19,323 | 3,190 | 22,513 |
| Refundable deposits | 15,203 | 8,245 | 23,448 |
| Compensated absences | 8,558 | 4,401 | 12,959 |
| Notes payable, current | 18,394 | 19,043 | 37,437 |
| Total current liabilities | <u>61,478</u> | <u>34,879</u> | <u>96,357</u> |
| Noncurrent liabilities | | | |
| Note payable | 518,644 | 150,507 | 669,151 |
| Estimated liability for landfill closure | - | 281,780 | 281,780 |
| Net pension liability | 146,917 | 48,017 | 194,934 |
| Total noncurrent liabilities | <u>665,561</u> | <u>480,304</u> | <u>1,145,865</u> |
| Total liabilities | <u>727,039</u> | <u>515,183</u> | <u>1,242,222</u> |
| Deferred inflows of resources | | | |
| Deferred inflows related to pensions | <u>24,327</u> | <u>7,951</u> | <u>32,278</u> |
| Net position | | | |
| Net investment in capital assets | 2,409,227 | 557,279 | 2,966,506 |
| Restricted for: | | | |
| Debt service | 26,857 | - | 26,857 |
| Repairs and replacements | 26,857 | - | 26,857 |
| Unrestricted (deficit) | <u>(81,077)</u> | <u>(234,060)</u> | <u>(315,137)</u> |
| Total net position | <u>\$ 2,381,864</u> | <u>\$ 323,219</u> | <u>\$ 2,705,083</u> |

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Statement of Revenue, Expenses, and Changes in Fund Net Position
Proprietary Funds
Year Ended June 30, 2017

| | Business-type Activities--Enterprise Funds | | |
|---|--|------------------------|---------------------|
| | Water/ Wastewater Fund | Solid Waste Fund | Total |
| Operating revenue | | | |
| Water (net of bad debts of \$288) | \$ 181,780 | \$ - | \$ 181,780 |
| Sewer (net of bad debts of \$378) | 182,495 | - | 182,495 |
| Sanitation (net of bad debts of \$352) | - | 177,251 | 177,251 |
| Total operating revenue | <u>364,275</u> | <u>177,251</u> | <u>541,526</u> |
| Operating expenses | | | |
| Personnel | 141,505 | 53,716 | 195,221 |
| Depreciation | 116,106 | 42,656 | 158,762 |
| Supplies | 42,717 | 11,466 | 54,183 |
| Contract services | 25,028 | 21,101 | 46,129 |
| Utilities | 36,894 | 2,329 | 39,223 |
| Insurance | 15,895 | 5,900 | 21,795 |
| Repairs and maintenance | 11,803 | 1,688 | 13,491 |
| Other | 1,031 | - | 1,031 |
| Travel and training | 365 | - | 365 |
| Landfill closure expense | - | 300 | 300 |
| Total operating expenses | <u>391,344</u> | <u>139,156</u> | <u>530,500</u> |
| Operating income (loss) | <u>(27,069)</u> | <u>38,095</u> | <u>11,026</u> |
| Nonoperating revenue (expenses) | | | |
| Investment income | 1,679 | 77 | 1,756 |
| Interest expense | (17,894) | (7,405) | (25,299) |
| Total nonoperating revenue (expenses) | <u>(16,215)</u> | <u>(7,328)</u> | <u>(23,543)</u> |
| Income (loss) before capital grant contribution | (43,284) | 30,767 | (12,517) |
| Capital grant contribution | <u>21,876</u> | <u>-</u> | <u>21,876</u> |
| Increase (decrease) in net position | (21,408) | 30,767 | 9,359 |
| Total net position, beginning of year | <u>2,403,272</u> | <u>292,452</u> | <u>2,695,724</u> |
| Total net position, end of year | <u>\$ 2,381,864</u> | <u>\$ 323,219</u> | <u>\$ 2,705,083</u> |

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Statement of Cash Flows
Proprietary Funds
Year Ended June 30, 2017

| | Business-type Activities--Enterprise Funds | | |
|---|--|------------------------|-------------------|
| | Water/ Wastewater Fund | Solid Waste Fund | Total |
| Cash Flows from Operating Activities | | | |
| Receipts from customers | \$ 356,326 | \$ 175,593 | \$ 531,919 |
| Payments to suppliers | (135,245) | (41,332) | (176,577) |
| Payments to employees | (141,210) | (52,710) | (193,920) |
| Net cash provided (used) by operating activities | <u>79,871</u> | <u>81,551</u> | <u>161,422</u> |
| Cash Flows from Non-capital Financing Activities | | | |
| Advances (to) from other funds | (26,302) | 24,284 | (2,018) |
| Cash Flows from Capital and Related Financing Activities | | | |
| Contributions from capital grants | 13,124 | - | 13,124 |
| Interest payments on notes payable | (17,894) | (7,405) | (25,299) |
| Principal payments on notes payable | (17,787) | (18,276) | (36,063) |
| Purchase of capital assets | (17,628) | - | (17,628) |
| Net cash provided (used) by capital and related financing activities | <u>(40,185)</u> | <u>(25,681)</u> | <u>(65,866)</u> |
| Cash Flows from Investing Activities | | | |
| Interest received | 1,679 | 77 | 1,756 |
| Net increase (decrease) in cash and cash equivalents | 15,063 | 80,231 | 95,294 |
| Cash and cash equivalents, beginning of year | 68,182 | 7,795 | 75,977 |
| CASH AND CASH EQUIVALENTS, END OF YEAR | <u>\$ 83,245</u> | <u>\$ 88,026</u> | <u>\$ 171,271</u> |
| Cash and cash equivalents | \$ 14,328 | \$ 79,781 | \$ 94,109 |
| Cash, restricted | 68,917 | 8,245 | 77,162 |
| CASH AND CASH EQUIVALENTS, END OF YEAR | <u>\$ 83,245</u> | <u>\$ 88,026</u> | <u>\$ 171,271</u> |

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Statement of Cash Flows
Proprietary Funds
Year Ended June 30, 2017
(Continued)

| | <u>Business-type Activities--Enterprise Funds</u> | | |
|---|---|---------------------------------|-------------------|
| | <u>Water/ Wastewater Fund</u> | <u>Solid Waste Fund</u> | <u>Total</u> |
| Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities: | | | |
| Operating income (loss) | \$ (27,069) | \$ 38,095 | \$ 11,026 |
| Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities: | | | |
| Depreciation | 116,106 | 42,656 | 158,762 |
| Bad debt | 666 | 352 | 1,018 |
| Pension expense | 9,785 | 3,198 | 12,983 |
| Employer pension contributions | (9,479) | (3,097) | (12,576) |
| (Increase) decrease in: | | | |
| Accounts receivable | (9,350) | (2,460) | (11,810) |
| Prepaid expenses | 586 | - | 586 |
| Increase (decrease) in: | | | |
| Accounts payable | (2,404) | 1,351 | (1,053) |
| Refundable deposits | 735 | 450 | 1,185 |
| Compensated absences | 295 | 1,006 | 1,301 |
| Estimated liability for landfill closure | - | - | - |
| Total adjustments | <u>106,940</u> | <u>43,456</u> | <u>150,396</u> |
| NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES | <u>\$ 79,871</u> | <u>\$ 81,551</u> | <u>\$ 161,422</u> |

NON-CASH INVESTING AND FINANCING ACTIVITIES - The Town had purchased \$8,642 of capital assets on account in the Water/Wastewater Fund.

The accompanying notes are an integral part of these financial statements.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements of the Town of Patagonia, Arizona have been prepared in conformity with U.S. generally accepted accounting principles applicable to governmental units adopted by the Governmental Accounting Standards Board (GASB). A summary of the Town's more significant accounting policies follows.

A. Reporting Entity

The Town is a general purpose local government that is governed by a separately elected Town Council. The accompanying financial statements present the activities of the Town (the primary government) and its component units.

Component units are legally separate entities for which the Town is considered to be financially accountable. Blended component units, although legally separate entities, are, in substance, part of the Town's operations. Therefore, data from these units is combined with data of the primary government. Discretely presented component units, on the other hand, are reported in a separate column in the combined financial statements to emphasize they are legally separate from the Town. The blended component unit discussed below has a June 30 year-end. The Town has no discretely presented component units.

The Town of Patagonia Municipal Property Corporation is a nonprofit corporation incorporated under the laws of the State of Arizona. The principal objective of the Corporation is to assist the Town of Patagonia, Arizona, in acquiring, constructing, financing, operating, improving or modifying public facilities for the benefit of all Town of Patagonia, Arizona, residents. The Corporation's board of directors consists of three members appointed by the Patagonia Town Council.

B. Basis of Presentation

The basic financial statements include both government-wide statements and fund financial statements. The government-wide statements focus on the Town as a whole, while the fund financial statements focus on major funds. Each presentation provides valuable information that can be analyzed and compared between years and between governments to enhance the usefulness of the information.

Government-wide statements—provide information about the primary government (the Town). The statements include a statement of net position and a statement of activities. These statements report the financial activities of the overall government. They also distinguish between the governmental and business-type activities of the Town. Governmental activities generally are financed through taxes and intergovernmental revenues. Business-type activities are financed in whole or in part by fees charged to external parties.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

A statement of activities presents a comparison between direct expenses and program revenues for each function of the Town's governmental activities and segment of its business-type activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. The Town does not allocate indirect expenses to programs or functions. Program revenues include:

- charges to customers or applicants for goods, services, or privileges provided,
- operating grants and contributions, and
- capital grants and contributions.

Revenues that are not classified as program revenues, including internally dedicated resources and all taxes, are reported as general revenues.

Generally, the effect of interfund activity has been eliminated from the government-wide financial statements to minimize the double counting of internal activities. However, charges for interfund services provided and used are not eliminated if the prices approximate their external exchange values.

Fund financial statements—provide information about the Town's funds. Separate statements are presented for governmental and proprietary fund categories. The emphasis of fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as nonmajor funds.

Proprietary fund revenues and expenses are classified as either operating or nonoperating. Operating revenues and expenses generally result from transactions associated with the fund's principal activity. Accordingly, revenues, such as user charges and insurance premiums, in which each party receives and gives up essentially equal values are operating revenues. Other revenues, such as subsidies, result from transactions in which the parties do not exchange equal values and are considered nonoperating revenues along with investment earnings and revenues ancillary activities generate. Operating expenses include the cost of services, administrative expenses, and depreciation on capital assets. Other expenses, such as interest expense, are considered nonoperating expenses.

The Town reports the following major governmental funds:

The ***General Fund*** is the Town's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The ***HURF Fund*** accounts for specific revenue received from the State of Arizona Highway User Revenue Fund, which is legally restricted to expenditures for authorized transportation purposes.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

The ***Grants Fund*** accounts for specific revenue received that is legally restricted to expenditures for specified purposes.

The Town reports the following major enterprise funds:

The ***Water/Wastewater*** and ***Solid Waste Funds*** account for operations that are financed and operated in a manner similar to private business enterprises, in which the intent of the Town Council is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or for which the Town Council has decided that periodic determination of revenue earned, expenses incurred, or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

C. Basis of Accounting

The government-wide, proprietary fund, and fiduciary fund financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Property taxes are recognized as revenue in the year for which they are levied. Grants and donations are recognized as revenue as soon as all eligibility requirements the provider imposed have been met.

Under the terms of grant agreements, the Town funds certain programs by a combination of grants and general revenues. Therefore, when program expenses are incurred, there are both restricted and unrestricted resources available to finance the program. The Town applies grant resources to such programs before using general revenues.

Governmental funds in the fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when they become both measurable and available. The Town considers all revenues reported in the governmental funds to be available if the revenues are collected within 60 days after year-end. The Town's major revenue sources that are susceptible to accrual are property taxes, special assessments, intergovernmental, charges for services, and investment earnings. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, compensated absences, landfill closure and postclosure care costs, and pollution remediation obligations, which are recognized as expenditures to the extent they are due and payable. General capital asset acquisitions are reported as expenditures in governmental funds. Issuances of general long-term debt and acquisitions under capital lease agreements are reported as other financing sources.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

D. Cash and Investments

For the statement of cash flows, the Town's cash and cash equivalents are considered to be cash on hand, demand deposits, investments in the State Treasurer's local government investment pool, and only those highly liquid investments with a maturity of three months or less when purchased.

E. Allowance for Uncollectible Accounts

Allowances for uncollectible accounts receivable in the Water/Wastewater Fund and the Solid Waste Fund are estimated by the Town. The amounts recorded as uncollectible in the Water/Wastewater and Solid Waste Funds at June 30, 2017 totaled \$13,000 and \$6,700, respectively.

F. Investment Income

Investment income is composed of interest, dividends, and net changes in the fair value of applicable investments.

G. Compensated Absences

Compensated absences consist of vacation leave earned by employees based on services already rendered.

Employees may accumulate up to 240 hours of vacation hours depending on their years of service. Upon termination of employment, all unused vacation benefits are paid to employees. Accordingly, vacation benefits are accrued as a liability in the financial statements.

Employees may accumulate up to 360 hours of sick leave hours but any sick hours in excess of the maximum amount that are unused at year-end are forfeited. Because sick leave benefits do not vest with employees, a liability for sick leave benefits is not accrued in the financial statements.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

H. Capital Assets

Capital assets are reported at actual cost (or estimated historical cost if historical records are not available). Donated assets are reported at acquisition value.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods, and estimated useful lives of capital assets are as follows:

| | <u>Capitalization Threshold</u> | <u>Depreciation Method</u> | <u>Estimated Useful Life (years)</u> |
|-------------------------|-------------------------------------|--------------------------------|--|
| Land | \$ 5,000 | N/A | N/A |
| Buildings | 5,000 | Straight-line | 40 |
| Parks | 5,000 | Straight-line | 40 |
| Streets | 5,000 | Straight-line | 20-30 |
| Sewer collection system | 5,000 | Straight-line | 10-40 |
| Furniture and fixtures | 5,000 | Straight-line | 5-10 |
| Equipment | 5,000 | Straight-line | 5-10 |

I. Deferred Outflows/Inflows of Resources

The statement of net position and balance sheet include separate sections for deferred outflows of resources and deferred inflows of resources. Deferred outflows of resources represent a consumption of net position that applies to future periods that will be recognized as an expense or expenditure in future periods. Deferred inflows of resources represent an acquisition of net position or fund balance that applies to future periods and will be recognized as a revenue in future periods.

J. Fund Balance Reporting

The governmental funds' fund balances are reported separately within classifications based on a hierarchy of the constraints placed on those resources' use. The classifications are based on the relative strength of the constraints that control how the specific amounts can be spent. The classifications are nonspendable, restricted, and unrestricted, which includes committed, assigned, and unassigned fund balance classifications.

The nonspendable fund balance classification includes amounts that cannot be spent because they are either not in spendable form, such as inventories, or are legally or contractually required to be maintained intact. Restricted fund balances are those that have externally imposed restrictions on

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

their usage by creditors (such as through debt covenants), grantors, contributors, or laws and regulations.

The unrestricted fund balance category is composed of committed, assigned, and unassigned resources. Committed fund balances are self-imposed limitations that the Town Council has approved, which is the highest level of decision-making authority within the Town. Only the Town Council can remove or change the constraints placed on committed fund balances.

Assigned fund balances are resources constrained by the Town's intent to be used for specific purposes, but that are neither restricted nor committed. The Town Council has authorized the Town manager to assign resources for a specific purpose.

The unassigned fund balance is the residual classification for the General Fund and includes all spendable amounts not reported in the other classifications. Also, deficits in fund balances of the other governmental funds are reported as unassigned.

When an expenditure is incurred that can be paid from either restricted or unrestricted fund balances, it is the Town's policy to use (the Town will use) restricted fund balance first. It is the Town's policy to use (the Town will use) committed amounts first when disbursing unrestricted fund balances, followed by assigned amounts, and lastly unassigned amounts.

K. Impact of Recently Issued Accounting Principles

In June 2015, the GASB issued Statement 73, *Accounting and Financial Reporting for Pensions and Related Assets that are not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. The objective of this Statement is to improve the usefulness of information about pensions included in the general purpose external financial reports of state and local governments for making decisions and assessing accountability. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all postemployment benefits with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. The Town implemented this standard during this fiscal period.

In June 2015, the GASB issued Statement 75, *Accounting and Financial Reporting for Postemployment Benefits other than Pensions*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for all postemployment benefits (pensions and OPEB) with regard to providing decision-useful

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

information, supporting assessments of accountability and interperiod equity, and creating additional transparency. This Statement is effective for fiscal years beginning after June 15, 2017. Upon implementation, it is anticipated that this Statement will cause a restatement of beginning net position of the Governmental Activities, Business-type Activities, and the proprietary funds.

In December 2015, the GASB issued Statement 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*. The objective of this Statement is to address a practice issue regarding the scope and applicability of Statement No. 68, Accounting and Financial Reporting for Pensions. This issue is associated with pensions provided through certain multiple-employer defined benefit pension plans and to state or local governmental employers whose employees are provided with such pensions. The Town implemented this standard during this fiscal period.

In March 2016, the GASB issued Statement 82, *Pension Issues—an amendment of GASB Statements No. 67, No. 68, and No. 73*. The objective of this Statement is to address certain issues that have been raised with respect to Statements No. 67, *Financial Reporting for Pension Plans*, No. 68, *Accounting and Financial Reporting for Pensions*, and No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Specifically, this Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The requirements of this Statement are effective for reporting periods beginning after June 15, 2017, except for the requirements of this Statement for the selection of assumptions in a circumstance in which an employer's pension liability is measured as of a date other than the employer's most recent fiscal year-end. In that circumstance, the requirements for the selection of assumptions are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017.

In March 2017, the GASB issued Statement 85, *Omnibus 2017*. The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). The requirements of this Statement are effective for reporting periods beginning after June 15, 2017.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

In June 2017, the GASB issued Statement 87, *Leases*. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. The requirements of this Statement are effective for reporting periods beginning after December 15, 2019.

L. Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the pension plans' fiduciary net position and additions to/deductions from the plans' fiduciary net position have been determined on the same basis as they are reported by the plans. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

NOTE 2 – DEPOSITS AND INVESTMENTS

Arizona Revised Statutes (A.R.S.) authorize the Town to invest public monies in the State Treasurer's investment pool; obligations issued or guaranteed by the United States or any of the senior debt of its agencies, sponsored agencies, corporations, sponsored corporations, or instrumentalities; specified state and local government bonds, notes, and other evidences of indebtedness; interest-earning investments such as savings accounts, certificates of deposit, and repurchase agreements in eligible depositories; specified commercial paper issued by corporations organized and doing business in the United States; specified bonds, debentures, notes, and other evidences of indebtedness that are denominated in United States dollars; and certain open-end and closed-end mutual funds, including exchange traded funds. In addition, the Town Treasurer may invest trust funds in certain fixed income securities of corporations doing business in the United States or District of Columbia.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 2 – DEPOSITS AND INVESTMENTS – Continued

Credit risk

Statutes have the following requirements for credit risk:

1. Commercial paper must be of prime quality and be rated within the top two ratings by a nationally recognized rating agency.
2. Bonds, debentures, notes, and other evidences of indebtedness that are denominated in United States dollars must be rated “A” or better at the time of purchase by at least two nationally recognized rating agencies.
3. Fixed income securities must carry one of the two highest ratings by Moody’s investor’s service and Standard and Poor’s rating service. If only one of the above-mentioned services rates the security, it must carry the highest rating of that service.

Custodial credit risk

Statutes require collateral for deposits at 102 percent of all deposits federal depository insurance does not cover.

Concentration of credit risk

Statutes do not include any requirements for concentration of credit risk.

Interest rate risk

Statutes require that public monies invested in securities and deposits have a maximum maturity of 5 years. The maximum maturity for investments in repurchase agreements is 180 days.

Foreign currency risk

Statutes do not allow foreign investments unless the investment is denominated in United States dollars.

The Town’s investment policy states that the Town will conform with Arizona Revised Statutes. The Town does not have a formal investment policy with respect to custodial credit risk, concentration of credit risk, or foreign currency risk.

Deposits—At June 30, 2017, the carrying amount of the Town’s total cash in bank was \$48,069, and the bank balance was \$69,052. The entire bank balance was covered by federal depository insurance or similar insurance.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 2 – DEPOSITS AND INVESTMENTS – Continued

Investments—The Town reported the following investments with the State Treasurer:

| <u>Investment</u> | <u>Rating Organization</u> | <u>Credit Rating</u> | <u>Reported Amount</u> | <u>Fair Value</u> |
|-----------------------|--------------------------------|--------------------------|----------------------------|-----------------------|
| Arizona LGIP Pool 5 | S&P | AAA | \$ 553,225 | \$ 553,225 |
| Arizona LGIP Pool 7 | N/A | Unrated | 91,312 | 91,312 |
| Arizona LGIP Pool 500 | N/A | Unrated | 36,007 | 36,007 |
| | | | <u>\$ 680,544</u> | <u>\$ 680,544</u> |

Investments in the State Treasurer’s investment pools are valued at the pool’s share price multiplied by the number of shares the Town held. The fair value of a participant’s position in the pools approximates the value of that participant’s pool shares. The State Board of Investment provides oversight for the State Treasurer’s investment pools.

A reconciliation of cash, deposits, and investments to amounts shown on the statements of net position follows:

| | |
|--|-------------------|
| Deposits | |
| Cash on hand | \$ 300 |
| Cash held by trustee | 26,857 |
| Cash in bank | 48,069 |
| Investments | |
| State Treasurer's Investment Pool | <u>680,544</u> |
| Total deposits and investments | 755,770 |
| Cash and cash equivalents - restricted | <u>(77,162)</u> |
| Total cash and cash equivalents | <u>\$ 678,608</u> |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 3 – DUE FROM OTHER GOVERNMENTS

Amounts due from other governments in the governmental funds at June 30, 2017 included \$6,898 in state-shared revenue from sales taxes, \$12,379 in town sales taxes collected by the State of Arizona, \$2,937 in county-shared revenue from auto lieu taxes, \$5,325 in county library grants, and \$9,769 in state-shared revenue from highway user revenue fund (HURF) taxes.

NOTE 4 – CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2017, was as follows:

| | Balance July 1, 2016 | Increases | Decreases | Balance June 30, 2017 |
|--|-------------------------|--------------|-----------|--------------------------|
| Governmental activities: | | | | |
| Capital assets not being depreciated: | | | | |
| Land | \$ 355,867 | \$ - | \$ - | \$ 355,867 |
| Capital assets being depreciated: | | | | |
| Equipment | 644,792 | 22,936 | - | 667,728 |
| Buildings | 1,824,136 | 5,039 | - | 1,829,175 |
| Parks | 241,427 | - | - | 241,427 |
| Streets | 3,516,832 | 133,088 | - | 3,649,920 |
| Total | 6,227,187 | 161,063 | - | 6,388,250 |
| Less accumulated depreciation for: | | | | |
| Equipment | (445,342) | (34,177) | - | (479,519) |
| Buildings | (948,104) | (59,112) | - | (1,007,216) |
| Parks | (220,855) | (8,325) | - | (229,180) |
| Streets | (2,685,681) | (109,744) | - | (2,795,425) |
| Total | \$ (4,299,982) | \$ (211,358) | \$ - | (4,511,340) |
| Total capital assets being depreciated, net | 1,927,205 | (50,295) | - | 1,876,910 |
| Governmental activities capital assets, net | \$ 2,283,072 | \$ (50,295) | \$ - | \$ 2,232,777 |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 4 – CAPITAL ASSETS – Continued

| | Balance <u>July 1, 2016</u> | <u>Increases</u> | <u>Decreases</u> | Balance <u>June 30, 2017</u> |
|--|--------------------------------|---------------------|------------------|---------------------------------|
| Business-type activities: | | | | |
| Capital assets not being depreciated: | | | | |
| Land | \$ 150,540 | \$ - | \$ - | \$ 150,540 |
| Capital assets being depreciated: | | | | |
| Land improvements | 738,732 | - | - | 738,732 |
| Buildings | 1,737,224 | - | - | 1,737,224 |
| Utility systems | 2,326,456 | 8,642 | - | 2,335,098 |
| Machinery and equipment | 681,540 | - | - | 681,540 |
| Total | <u>5,483,952</u> | <u>8,642</u> | <u>-</u> | <u>5,492,594</u> |
| Less accumulated depreciation for: | | | | |
| Land improvements | (218,002) | (24,625) | - | (242,627) |
| Buildings | (539,085) | (43,431) | - | (582,516) |
| Utility systems | (587,451) | (61,187) | - | (648,638) |
| Machinery and equipment | (466,740) | (29,519) | - | (496,259) |
| Total | <u>\$ (1,811,278)</u> | <u>\$ (158,762)</u> | <u>\$ -</u> | <u>(1,970,040)</u> |
| Total capital assets being depreciated, net | <u>3,672,674</u> | <u>(150,120)</u> | <u>-</u> | <u>3,522,554</u> |
| Business-type activities capital assets, net | <u>\$ 3,823,214</u> | <u>\$ (150,120)</u> | <u>\$ -</u> | <u>\$ 3,673,094</u> |

Depreciation expense was charged to functions as follows:

| | |
|---|-------------------|
| Governmental activities: | |
| General government | \$ 39,812 |
| Public safety | 32,460 |
| Highways and streets | 111,461 |
| Culture and recreation | 27,625 |
| Total governmental activities depreciation expense | <u>\$ 211,358</u> |
| Business-type activities: | |
| Water/Wastewater | \$ 116,106 |
| Solid Waste | 42,656 |
| Total business-type activities depreciation expense | <u>\$ 158,762</u> |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 5 – LONG-TERM LIABILITIES

The following schedule details the Town’s long-term liability and obligation activity for the year ended June 30, 2017.

| | Balance July 1, 2016 | Additions | Reductions | Balance June 30, 2017 | Due within 1 year |
|---|-------------------------|------------------|------------------|--------------------------|----------------------|
| Governmental activities: | | | | | |
| Compensated absences payable | \$ 34,357 | \$ - | \$ 127 | \$ 34,230 | \$ 34,230 |
| Net pension liability | 980,506 | - | 34,293 | 946,213 | - |
| Governmental activities long-term liabilities | <u>\$ 1,014,863</u> | <u>\$ -</u> | <u>\$ 34,420</u> | <u>\$ 980,443</u> | <u>\$ 34,230</u> |
| Business-type activities | | | | | |
| Compensated absences payable | \$ 11,658 | \$ 1,301 | \$ - | \$ 12,959 | \$ 12,959 |
| Net pension liability | 164,664 | 30,270 | - | 194,934 | - |
| Landfill closure costs | 281,780 | - | - | 281,780 | - |
| Notes payable | 742,651 | - | 36,063 | 706,588 | 37,437 |
| Business-type activities long-term liabilities | <u>\$ 1,200,753</u> | <u>\$ 31,571</u> | <u>\$ 36,063</u> | <u>\$ 1,196,261</u> | <u>\$ 50,396</u> |

The following schedule details debt service requirements to maturity for the Town’s notes payable at June 30, 2017.

| Year Ending June 30 | <u>Business-type activities</u> | |
|---------------------------|---------------------------------|-------------------|
| | <u>Notes Payable</u> | |
| | <u>Principal</u> | <u>Interest</u> |
| 2018 | \$ 37,437 | \$ 23,924 |
| 2019 | 38,864 | 22,497 |
| 2020 | 40,347 | 21,015 |
| 2021 | 41,886 | 19,475 |
| 2022 | 43,485 | 17,876 |
| 2023-2027 | 115,110 | 70,822 |
| 2028-2032 | 49,716 | 59,424 |
| 2033-2037 | 58,475 | 50,665 |
| 2038-2042 | 68,778 | 40,362 |
| 2043-2047 | 80,896 | 28,244 |
| 2048-2052 | 95,149 | 13,991 |
| 2053-2057 | 36,445 | 1,074 |
| Total | <u>\$ 706,588</u> | <u>\$ 369,369</u> |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 5 – LONG-TERM LIABILITIES – Continued

Notes payable consisted of the following:

| <u>Description</u> | <u>Original Amount</u> | <u>Maturity Ranges</u> | <u>Interest Rates</u> | <u>Outstanding Principal</u> |
|---|----------------------------|----------------------------|---------------------------|----------------------------------|
| <u>Business-type Activities</u> | | | | |
| Note payable - Water Infrastructure Finance Authority of Arizona | \$ 375,000 | 2002-2021 | 3.420% | \$ 69,373 |
| Note payable - United States Department of Agriculture | 400,000 | 2009-2025 | 4.125% | 169,550 |
| Note payable - United States Department of Agriculture | <u>481,000</u> | 2015-2054 | 3.250% | <u>467,665</u> |
| | <u>\$ 1,256,000</u> | | | <u>\$ 706,588</u> |

NOTE 6 – RISK MANAGEMENT

The Town is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Town carries commercial insurance for all such risks of loss, including workers' compensation and employees' health and accident insurance. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

NOTE 7 – PSPRS PARKER LIABILITY

In 2011, legislators passed Senate Bill 1609, which contained several provisions meant to shore up the plans administered by PSPRS. One of those provisions was a gradual increase in member contribution rates from 7% to 11% in the elected officials' plan (EORP) and from 7.65% to 11.65% in the public safety plan (PSPRS). In August 2011, those provisions were challenged via two separate, but parallel, lawsuits—Hall for EORP and Parker for PSPRS. In November 2016, the Supreme Court upheld the lower court decision in Hall that ruled those increased member contribution rates were unconstitutional. These two lawsuits have been adjudicated separately where the Parker case was stayed (put on hold) pending the final outcome of Hall. Nevertheless, the facts and circumstances are essentially the same where both parties to Parker agreed, at the time of stay, to appropriately apply the remedies of Hall when finalized.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 7 – PSPRS PARKER LIABILITY – Continued

PSPRS members who became members of the system prior to July 20, 2011 and who paid employee contributions that exceeded 7.65% are eligible to receive a refund of those excess contributions unless they terminated and already received a refund. PSPRS has prepared a list of affected members for each employer, along with the amount of excess contributions that must be returned to them. The Town has estimated that the total amount of refunds due to employees (including applicable interest) will be \$13,000.

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS

The Town contributes to the pension plans described below. The plans are component units of the State of Arizona.

At June 30, 2017, the Town reported the following aggregate amounts related to pensions for all plans to which it contributes:

| Statement of Net Position and Statement of Activities | <u>Governmental Activities</u> | <u>Business-type Activities</u> | <u>Total</u> |
|--|------------------------------------|-------------------------------------|--------------|
| Net pension liabilities | \$ 946,213 | \$ 194,934 | \$ 1,141,147 |
| Deferred outflows of resources | 242,680 | 52,458 | 295,138 |
| Deferred inflows of resources | 78,938 | 32,278 | 111,216 |
| Pension expense | 39,688 | 12,983 | 52,671 |

The Town reported \$95,945 of pension expenditures in the governmental funds related to all pension plans to which it contributes.

A. Arizona State Retirement System

Plan Description – Town employees not covered by the other pension plans described below participate in the Arizona State Retirement System (ASRS). The ASRS administers a cost-sharing multiple-employer defined benefit pension plan, a cost-sharing multiple-employer defined benefit health insurance premium benefit (OPEB) plan, and a cost-sharing multiple-employer defined benefit long-term disability (OPEB) plan. The Arizona State Retirement System Board governs the ASRS according to the provisions of A.R.S. Title 38, Chapter 5, Articles 2 and 2.1. The ASRS issues a publicly available financial report that includes its financial statements and required supplementary information. The report is available on its website at www.azasrs.gov.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

Benefits Provided – The ASRS provides retirement, health insurance premium supplement, long-term disability, and survivor benefits. State statute establishes benefits terms. Retirement benefits are calculated on the basis of age, average monthly compensation, and service credit as follows:

| ASRS | Retirement | |
|--|--|--|
| | Initial membership date: | |
| | Before July 1, 2011 | On or after July 1, 2011 |
| Years of service and age required to receive benefit | Sum of years and age equals 80 10 years age 62 5 years age 50* any years age 65 | 30 years age 55 25 years age 60 10 years age 62 5 years age 50* any years age 65 |
| Final average salary is based on | Highest 36 months of last 120 months | Highest 60 months of last 120 months |
| Benefit percent per year of service | 2.1% to 2.3% | 2.1% to 2.3% |

*With actuarially reduced benefits.

Retirement benefits for members who joined the ASRS prior to September 13, 2013, are subject to automatic cost-of-living adjustments based on excess investment earning. Members with a membership date on or after September 13, 2013, are not eligible for cost-of-living adjustments. Survivor benefits are payable upon a member’s death. For retired members, the retirement benefit option chosen determines the survivor benefit. For all other members, the beneficiary is entitled to the member’s account balance that includes the member’s contributions and employer’s contributions, plus interest earned.

Contributions – In accordance with state statutes, annual actuarial valuations determine active member and employer contribution requirements. The combined active member and employer contribution rates are expected to finance the costs of benefits employees earn during the year, with an additional amount to finance any unfunded accrued liability. For the year ended June 30, 2017, statute required active ASRS members to contribute at the actuarially determined rate of 11.48 percent (11.34 percent for retirement and 0.14 percent for long-term disability) of the members’ annual covered payroll, and statute required the Town to contribute at the actuarially determined rate of 11.48 percent (10.78 percent for retirement, 0.56 percent for health insurance premium benefit, and 0.14 percent for long-term disability) of the active members’ annual covered payroll. The Town’s contributions to the pension plan for the year ended June 30, 2017,

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

were \$32,954. The Town’s OPEB contributions for the current and two preceding years, all of which were equal to the required contributions, were as follows:

| ASRS | Health Benefit Supplement Fund | Long-term Disability Fund |
|---------------------|---|--------------------------------------|
| Year ended June 30, | | |
| 2017 | \$ 1,712 | \$ 428 |
| 2016 | 1,481 | 355 |
| 2015 | 1,536 | 312 |

During fiscal year 2017, the Town paid for ASRS pension and OPEB contributions as follows: 54.56 percent from the General Fund, 8.05 percent from the HURF/LTAF Fund, 28.18 percent from the Water/Wastewater Fund, and 9.21 percent from the Solid Waste Fund.

Pension Liability – At June 30, 2017, the Town reported a liability of \$521,354 for its proportionate share of the ASRS’ net pension liability. The net pension liability was measured as of June 30, 2016. The total pension liability used to calculate the net pension liability was determined using update procedures to roll forward the total pension liability from an actuarial valuation as of June 30, 2015, to the measurement date of June 30, 2016. The total pension liability as of June 30, 2016, reflects a change in actuarial assumption for a decrease in loads for future potential permanent benefit increases.

The Town’s proportion of the net pension liability was based on the Town’s actual contributions to the plan relative to the total of all participating employers’ contributions for the year ended June 30, 2016. The Town’s proportion measured as of June 30, 2016, was .003230 percent, which was an increase of .0004 percent from its proportion measured as of June 30, 2015.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

Pension Expense and Deferred Outflows/Inflows of Resources – For the year ended June 30, 2017, the Town recognized pension expense for ASRS of \$34,723. At June 30, 2017, the Town reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

| ASRS | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|---|--|
| | <u> </u> | <u> </u> |
| Differences between expected and actual experience | \$ 3,168 | \$ 35,865 |
| Changes of assumptions or other inputs | - | 27,584 |
| Net difference between projected and actual earnings on pension plan investments | 56,497 | - |
| Changes in proportion and differences between Town contributions and proportionate share of contributions | 47,681 | 22,880 |
| Town contributions subsequent to the | <u>32,954</u> | <u>-</u> |
| Total | <u>\$ 140,300</u> | <u>\$ 86,329</u> |

The \$32,954 reported as deferred outflows of resources related to ASRS pensions resulting from Town contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2018. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to ASRS pensions will be recognized in pension expense as follows:

| | | |
|---------------------|----|----------|
| Year ended June 30, | | |
| 2018 | \$ | (20,781) |
| 2019 | | (1,206) |
| 2020 | | 27,163 |
| 2021 | | 15,842 |
| 2022 | | - |
| Thereafter | | - |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

Actuarial Assumptions – The significant actuarial assumptions used to measure the total pension liability are as follows:

ASRS

| | |
|-----------------------------|-------------------|
| Actuarial valuation date | June 30, 2015 |
| Actuarial roll forward date | June 30, 2016 |
| Actuarial cost method | Entry age normal |
| Investment rate of return | 8% |
| Projected salary increases | 3 - 6.75% |
| Inflation | 3% |
| Permanent benefit increase | Included |
| Mortality rates | 1994 GAM Scale BB |

Actuarial assumptions used in the June 30, 2015, valuation were based on the results of an actuarial experience study for the 5-year period ended June 30, 2012.

The long-term expected rate of return on ASRS pension plan investments was determined to be 8.75 percent using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

ASRS

| <u>Asset Class</u> | <u>Target Allocation</u> | <u>Long-term Arithmetic Expected Real Rate of Return</u> |
|--------------------|--------------------------|--|
| Equity | 58% | 6.73% |
| Fixed income | 25% | 3.70% |
| Real estate | 10% | 4.25% |
| Multi-asset class | 5% | 3.41% |
| Commodities | 2% | 3.84% |
| Total | <u>100%</u> | |

Discount Rate – The discount rate used to measure the ASRS total pension liability was 8 percent, which is less than the long-term expected rate of return of 8.75 percent. The projection of cash flows used to determine the discount rate assumed that contributions from participating employers will be made based on the actuarially determined rates based on the ASRS Board’s funding policy, which establishes the contractually required rate under Arizona statute. Based on those assumptions, the pension plan’s fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Town’s Proportionate Share of the ASRS Net Pension Liability to Changes in the Discount Rate – The following table presents the Town’s proportionate share of the net pension liability calculated using the discount rate of 8 percent, as well as what the Town’s proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (7 percent) or 1 percentage point higher (9 percent) than the current rate:

| ASRS | 1 % Decrease (7 %) | Current Discount Rate (8 %) | 1 % Increase (9 %) |
|---|-----------------------|--------------------------------|-----------------------|
| Town's proportionate share of the net pension liability | \$ 664,767 | \$ 521,354 | \$ 406,369 |

Pension Plan Fiduciary Net Position – Detailed information about the pension plan’s fiduciary net position is available in the separately issued ASRS financial report.

B. Public Safety Personnel Retirement System

Plan Descriptions – Town police and fire employees participate in the Public Safety Personnel Retirement System (PSPRS). The PSPRS administers an agent multiple-employer defined benefit pension plan and an agent multiple-employer defined benefit health insurance premium benefit (OPEB) plan (agent plans). A seven-member board known as the Board of Trustees and the participating local boards govern the PSPRS according to the provisions of A.R.S. Title 38, Chapter 5, Article 4.

The PSPRS issues publicly available financial report that includes financial statements and required supplementary information. The report is available on the PSPRS website at www.psprs.com.

Benefits Provided – The PSPRS provide retirement, health insurance premium supplement, disability, and survivor benefits. State statute establishes benefits terms.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

Retirement, disability, and survivor benefits are calculated on the basis of age, average monthly compensation, and service credit as follows:

PSPRS

| | <u>Initial membership date:</u> | |
|--|--|--|
| | Before January 1, 2012 | On or after January 1, 2012 |
| Retirement and Disability | | |
| Years of service and age required to receive benefit | 20 years, any age 15 years, age 62 | 25 years, age 52.5 |
| Final average salary is based on | Highest 36 months of last 20 years | Highest 60 months of last 20 years |
| Benefit percent | | |
| Normal Retirement | 50% less 2.0% for each year of credited service less than 20 years OR plus 2.0% to 2.5% for each year of credited services over 20 years, not to exceed 80% | 2.5% per year of credited service, not to exceed 80% |
| Accidental Disability Retirement | 50% or normal retirement, whichever is greater | |
| Catastrophic Disability Retirement | 90% for the first 60 months then reduced to either 62.5% or normal retirement, whichever is greater | |
| Ordinary Disability Retirement | Normal retirement calculated with actual years of credited service or 20 years of credited service, whichever is greater, multiplied by years of credited service (not to exceed 20 years) divided by 20 | |
| Survivor Benefit | | |
| Retired Members | 80% to 100% of retired member's pension benefit | |
| Active Members | 80% to 100% of accidental disability retirement benefit or 100% of average monthly compensation if death was result of injuries received on the job | |

Retirement and survivor benefits are subject to automatic cost-of-living adjustments based on excess investment earning. In addition, the Legislature may enact permanent one-time benefit increases after a Joint Legislative Budget Committee analysis of the increase's effects on the plan. PSPRS also provides temporary disability benefits of 50 percent of the member's compensation for up to 12 months.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

Employees Covered by Benefit Terms – At June 30, 2017, the following employees were covered by the agent pension plans’ benefit terms:

| | PSPRS Police |
|--|---------------------|
| Inactive employees or beneficiaries currently receiving benefits | 2 |
| Inactive employees entitled to but not yet receiving benefits | 3 |
| Active employees | 2 |
| Total | 7 |

Contributions and Annual OPEB Cost – State statutes establish the pension contribution requirements for active PSPRS employees. In accordance with state statutes, annual actuarial valuations determine employer contribution requirements for PSPRS pension and health insurance premium benefits. The combined active member and employer contribution rates are expected to finance the costs of benefits employees earn during the year, with an additional amount to finance any unfunded accrued liability. Contributions rates for the year ended June 30, 2017, are indicated below. Rates are a percentage of active members’ annual covered payroll.

| | PSPRS Police |
|----------------------------------|---------------------|
| Active Members - Pension | 11.65% |
| Town | |
| Pension | 53.13% |
| Health insurance premium benefit | 0.00% |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

For the agent plans, the Town’s contributions to the pension plan and annual OPEB cost and contributions for the health insurance premium benefit for the year ended June 30, 2017, were:

PSPRS

| Pension | <u>PSPRS Police</u> |
|---|----------------------------|
| Contributions Made | \$ 74,886 |
| | |
| Health Insurance Premium Benefit | |
| Annual OPEB cost | - |
| Contributions made | - |

During fiscal year 2017, the Town paid for 100 percent of PSPRS pension and OPEB contributions from the General Fund.

Net Pension Liability (Asset) – At June 30, 2017, the Town reported the following net pension liability:

| | <u>Net Pension Liability (Asset)</u> |
|--------------|---|
| PSPRS Police | \$ 619,793 |

The net pension liability (asset) was measured as of June 30, 2016, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date.

The total pension liabilities as of June 30, 2016, reflect the following changes of benefit terms and actuarial assumptions.

- In May 2016 voters approved Proposition 124 that authorized certain statutory adjustments to PSPRS’ automatic cost-of-living adjustments. The statutory adjustments changed the basis for cost-of-living adjustments from excess investment earnings to the change in the consumer price index, limited to a maximum annual increase of 2 percent.
- Laws 2016, Chapter 2, changed the benefit formula and contribution requirements for members hired on or after July 1, 2017.
- The investment rate of return actuarial assumption was decreased from 7.85 percent to 7.50 percent for PSPRS plans.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

The net pension liabilities measured as of June 30, 2017, will reflect changes of actuarial assumptions based on the results of an actuarial experience study for the 5-year period ended June 30, 2016. The change in the Town’s net pension liabilities as a result of these changes is not known.

Pension Actuarial Assumptions – The significant actuarial assumptions used to measure the total pension liability are as follows:

PSPRS

| | |
|----------------------------|---|
| Actuarial valuation date | June 30, 2016 |
| Actuarial cost method | Entry age normal |
| Discount rate | 7.50% |
| Projected salary increases | 4.0%-8.0% |
| Inflation | 4.0% |
| Permanent benefit increase | Included |
| Mortality rates | RP-2000 mortality table (adjusted by 105% for both males and females) |

Actuarial assumptions used in the June 30, 2016, valuation were based on the results of an actuarial experience study for the 5-year period ended June 30, 2011.

The long-term expected rate of return on PSPRS pension plan investments was determined to be 7.50 percent using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expenses and inflation) are developed for each major asset class. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

| <u>Asset Class</u> | <u>Target Allocation</u> | <u>Long-term Expected Arithmetic Real Rate of Return</u> |
|------------------------|--------------------------|--|
| Short term investments | 2% | 0.75% |
| Absolute return | 5% | 4.11% |
| Risk parity | 4% | 5.13% |
| Fixed Income | 7% | 2.92% |
| Real assets | 8% | 4.77% |
| GTAA | 10% | 4.38% |
| Private Equity | 11% | 9.50% |
| Real estate | 10% | 4.48% |
| Credit opportunities | 13% | 7.08% |
| Non-U.S. equity | 14% | 8.25% |
| U.S. equity | 16% | 6.23% |
| Total | <u>100%</u> | |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

Pension Discount Rates – At June 30, 2016, the discount rate used to measure the PSPRS total pension liabilities was 7.50 percent, which was a decrease of 0.35 from the discount rate used as of June 30, 2015. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rate and that employer contributions will be made at rates equal to the difference between the actuarially determined contribution rate and the member rate. Based on those assumptions, the pension plans’ fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Changes in the Net Pension Liability (Asset)

| | Increase (Decrease) | | |
|--|--|--|--|
| | Total Pension Liability (Asset) (a) | Plan Fiduciary Net Position (b) | Net Pension Liability (Asset) (a) - (b) |
| Balances at June 30, 2016 | \$ 1,288,244 | \$ 583,471 | \$ 704,773 |
| Changes for the year | | | |
| Service Cost | 32,762 | - | 32,762 |
| Interest on the total pension liability | 99,645 | - | 99,645 |
| Changes of benefit terms | (137,660) | - | (137,660) |
| Differences between expected and actual experience in the measurement of the pension liability | (43,689) | - | (43,689) |
| Changes of assumptions or other inputs | 53,993 | - | 53,993 |
| Contributions-employer | - | 71,823 | (71,823) |
| Contributions-employee | - | 15,649 | (15,649) |
| Net investment income | - | 3,452 | (3,452) |
| Benefit payments, including refunds of employee | (70,533) | (70,533) | - |
| Administrative expense | - | (898) | 898 |
| Other changes | - | 5 | (5) |
| Net changes | (65,482) | 19,498 | (84,980) |
| Balances at June 30, 2017 | \$ 1,222,762 | \$ 602,969 | \$ 619,793 |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

Sensitivity of the Town’s Net Pension Liability to Changes in the Discount Rate – The following table presents the Town’s net pension liabilities (assets) calculated using the discount rate of 7.50 percent, as well as what the Town’s net pension liability (asset) would be if it were calculated using a discount rate that is 1 percentage point lower (6.50 percent) or 1 percentage point higher (8.50 percent) than the current rate:

| | <u>1% Decrease (6.50%)</u> | <u>Current Discount Rate (7.50%)</u> | <u>1% Increase (8.50%)</u> |
|-----------------------|----------------------------|--|----------------------------|
| PSPRS Police | | | |
| Rate | 6.50% | 7.50% | 8.50% |
| Net pension liability | \$ 769,458 | \$ 619,793 | \$ 497,423 |

Pension Plan Fiduciary Net Position – Detailed information about the pension plans’ fiduciary net position is available in the separately issued PSPRS financial reports.

Pension Expense – For the year ended June 30, 2017, the Town recognized the following pension expense:

| | <u>Pension Expense</u> |
|--------------|------------------------|
| PSPRS Police | \$ 17,948 |

Pension Deferred Outflows/Inflows of Resources – At June 30, 2017, the Town reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

| | <u>Deferred Outflows of Resources</u> | <u>Deferred Inflows of Resources</u> |
|--|---|--|
| Differences between expected and actual experience | \$ 12,281 | \$ 24,887 |
| Changes of assumptions or other inputs | 30,756 | - |
| Net difference between projected and actual earnings on pension plan investments | 36,915 | - |
| Town contributions subsequent to the measurement date | 74,886 | - |
| Total | <u>\$ 154,838</u> | <u>\$ 24,887</u> |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

The amounts reported as deferred outflows of resources related to pensions resulting from Town contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2018. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

| Year ended June 30, | PSPRS Police |
|---------------------|---------------------|
| 2018 | \$ 24,223 |
| 2019 | 8,942 |
| 2020 | 13,304 |
| 2021 | 8,596 |
| 2022 | - |
| Thereafter | - |

Agent Plan OPEB Actuarial Assumptions – The health insurance premium benefit contribution requirements for the year ended June 30, 2017, were established by the June 30, 2015, actuarial valuations, and those actuarial valuations were based on the following actuarial methods and assumptions.

Actuarial valuations involve estimates of the reported amounts' value and assumptions about the probability of events in the future. Amounts determined regarding the plans' funded status and the annual required contributions are subject to continual revision as actual results are compared to past expectations and new estimates are made. The required schedule of funding progress for the health insurance premium benefit presented as required supplementary information provides multiyear trend information that shows whether the actuarial value of the plans' assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

Projections of benefits are based on (1) the plans as understood by the Town and plans’ members and include the types of benefits in force at the valuation date, and (2) the pattern of sharing benefit costs between the Town and plans’ members to that point. Actuarial calculations reflect a long-term perspective and employ methods and assumptions that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets. The actuarial methods and assumptions used to establish the fiscal year 2017 contribution requirements are as follows:

PSPRS - OPEB Contribution Requirements

| | |
|-------------------------------|--|
| Actuarial valuation date | June 30, 2015 |
| Actuarial cost method | Entry age normal |
| Amortization method | Level percent closed for unfunded actuarial accrued liability, open for excess |
| Remaining amortization period | 21 years for unfunded actuarial accrued liability, 20 years for excess |
| Asset valuation method | 7-year smoothed market value; 80%/120% market corridor |
| Actuarial assumptions: | |
| Investment rate of return | 7.85% |
| Projected salary increases | 4.0%-8.0% |
| Wage growth | 4.0% |

Agent Plan OPEB Trend Information – Annual OPEB cost information for the health insurance premium benefit for the current and two preceding years:

| Year ended June 30, | Annual OPEB Cost | Percentage of Annual Cost Contributed | Net OPEB Obligation |
|---------------------|------------------|---------------------------------------|---------------------|
| PSPRS Police | | | |
| 2017 | \$ - | 100% | \$ - |
| 2016 | - | 100% | - |
| 2015 | 590 | 100% | - |

Agent Plan OPEB Funded Status – The health insurance premium benefit plans’ funded status as of the most recent valuation date, June 30, 2016, along with the actuarial assumptions and methods used in those valuations follow.

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 8 – PENSIONS AND OTHER POSTEMPLOYMENT BENEFITS – Continued

| | | <u>PSPRS Police</u> |
|--|----|----------------------------|
| Actuarial value of assets (a) | \$ | 34,126 |
| Actuarial accrued liability (b) | \$ | 4,617 |
| Unfunded actuarial accrued liability (funding excess) (b) - (a) | \$ | (29,509) |
| Funded ratio (a)/(b) | | 739.14% |
| Annual covered payroll (c) | \$ | 140,949 |
| Unfunded actuarial accrued liability (funding excess) as a percentage of covered payroll | | 0.00% |

The actuarial methods and assumptions for the most recent valuation date are as follows:

PSPRS - OPEB Funded Status

| | |
|-------------------------------|--|
| Actuarial valuation date | June 30, 2016 |
| Actuarial cost method | Entry age normal |
| Amortization method | Level percent closed for unfunded actuarial accrued liability, open for excess |
| Remaining amortization period | 20 years for unfunded actuarial accrued liability, 20 years for excess |
| Asset valuation method | 7-year smoothed market value; 80%/120% market corridor |
| Actuarial assumptions: | |
| Investment rate of return | 7.50% |
| Projected salary increases | 4%-8% |
| Wage growth | 4% |

TOWN OF PATAGONIA, ARIZONA
Notes to Financial Statements
June 30, 2017

NOTE 9 – CLOSURE AND POSTCLOSURE COSTS

State and federal laws and regulations require the Town to place a final cover on its landfill when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. Although closure and postclosure care costs will not be paid until near or after the date that the landfill stops accepting waste, the Town reports a portion of these closure and postclosure care costs as an operating expense in each period based on landfill capacity used as of each balance sheet date. The \$281,780 reported as landfill closure and post closure care liability at June 30, 2017, represents the cumulative amount reported to date based on the use of 40 percent of the estimated capacity of the landfill. The Town will recognize the remaining estimated cost of closure and postclosure care of \$422,670 as the remaining estimated capacity is filled. These amounts are based on what it would cost to perform all closure and postclosure care in fiscal year 2016-2017. The Town expects to close the landfill in the year 2050, and the actual cost may be higher due to inflation, changes in technology, and changes in regulations.

The Town of Patagonia, Arizona is required to file certain information relating to the landfill closure, postclosure, and monitoring with the State of Arizona Department of Environmental Quality (ADEQ). The required information was filed with the State subsequent to June 30, 2017.

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Budgetary Comparison Schedule
General Fund
Year Ended June 30, 2017

| | Budgeted Amounts | | Actual Amounts | Variance with Final Budget |
|---|-------------------|-------------------|-------------------|-------------------------------|
| | Original | Final | | |
| Revenues | | | | |
| Intergovernmental | \$ 539,857 | \$ 539,857 | \$ 366,405 | \$ (173,452) |
| Taxes | 245,000 | 245,000 | 263,558 | 18,558 |
| Fines and forfeitures | 143,500 | 143,500 | 80,950 | (62,550) |
| Charges for services | 33,708 | 33,708 | 33,340 | (368) |
| Other revenue | 114,700 | 114,700 | 30,788 | (83,912) |
| Franchise fees | 13,250 | 13,250 | 14,145 | 895 |
| Licenses and permits | 27,500 | 27,500 | 13,105 | (14,395) |
| Investment income | 1,000 | 1,000 | 2,506 | 1,506 |
| Total revenues | <u>1,118,515</u> | <u>1,118,515</u> | <u>804,797</u> | <u>(313,718)</u> |
| Expenditures | | | | |
| Current | | | | |
| General government | 288,157 | 288,157 | 205,897 | 82,260 |
| Public safety | 627,294 | 627,294 | 474,807 | 152,487 |
| Culture and recreation | 174,730 | 174,730 | 174,730 | - |
| Capital outlay | 27,974 | 27,974 | 27,974 | - |
| Total expenditures | <u>1,118,155</u> | <u>1,118,155</u> | <u>883,408</u> | <u>234,747</u> |
| Excess (deficiency) of revenue over (under) expenditures | <u>360</u> | <u>360</u> | <u>(78,611)</u> | <u>(78,971)</u> |
| Other financing sources (uses) | | | | |
| Transfers | <u>(9,500)</u> | <u>(9,500)</u> | <u>-</u> | <u>9,500</u> |
| Net change in fund balances | (9,140) | (9,140) | (78,611) | (69,471) |
| Fund balance, beginning of year | <u>777,699</u> | <u>777,699</u> | <u>777,699</u> | <u>-</u> |
| Fund balance, end of year | <u>\$ 768,559</u> | <u>\$ 768,559</u> | <u>\$ 699,088</u> | <u>\$ (69,471)</u> |

See accompanying notes to budgetary comparison schedule.

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Budgetary Comparison Schedule
HURF Fund
Year Ended June 30, 2017

| | Budgeted Amounts | | Actual Amounts | Variance with Final Budget |
|---|-------------------|-------------------|---------------------|-------------------------------|
| | Original | Final | | |
| Revenues | | | | |
| Intergovernmental | \$ 131,966 | \$ 131,966 | \$ 105,185 | \$ (26,781) |
| Investment income | - | - | 236 | 236 |
| Total revenues | <u>131,966</u> | <u>131,966</u> | <u>105,421</u> | <u>(26,545)</u> |
| Expenditures | | | | |
| Current | | | | |
| Highways and streets | 58,112 | 58,112 | 93,073 | (34,961) |
| Capital outlay | 63,335 | 63,335 | 133,089 | (69,754) |
| Total expenditures | <u>121,447</u> | <u>121,447</u> | <u>226,162</u> | <u>(104,715)</u> |
| Excess (deficiency) of revenue over (under) expenditures | <u>10,519</u> | <u>10,519</u> | <u>(120,741)</u> | <u>(131,260)</u> |
| Other financing sources (uses) | | | | |
| Transfers | 9,500 | 9,500 | - | (9,500) |
| Net change in fund balances | 20,019 | 20,019 | (120,741) | (140,760) |
| Fund balance, beginning of year | <u>(29,054)</u> | <u>(29,054)</u> | <u>(29,054)</u> | <u>-</u> |
| Fund balance, end of year | <u>\$ (9,035)</u> | <u>\$ (9,035)</u> | <u>\$ (149,795)</u> | <u>\$ (140,760)</u> |

See accompanying notes to budgetary comparison schedule.

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Budgetary Comparison Schedule
Grants Fund
Year Ended June 30, 2017

| | Budgeted Amounts | | Actual Amounts | Variance with Final Budget |
|---|------------------|-----------------|-------------------|-------------------------------|
| | Original | Final | | |
| Revenues | | | | |
| Intergovernmental | \$ - | \$ - | \$ - | \$ - |
| Taxes | - | - | - | - |
| Fines and forfeitures | - | - | - | - |
| Charges for services | - | - | - | - |
| Other revenue | - | - | - | - |
| Licenses and permits | - | - | - | - |
| Franchise fees | - | - | - | - |
| Investment income | - | - | - | - |
| Total revenues | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> |
| Expenditures | | | | |
| Current | | | | |
| General government | - | - | - | - |
| Public safety | - | - | - | - |
| Highways and streets | - | - | - | - |
| Culture and recreation | - | - | - | - |
| Capital outlay | - | - | - | - |
| Total expenditures | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> |
| Excess (deficiency) of revenue over (under) expenditures | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> |
| Other financing sources (uses) | | | | |
| Transfers | - | - | - | - |
| Sale of capital assets | - | - | - | - |
| Total other financing sources (uses) | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> |
| Net change in fund balances | - | - | - | - |
| Fund balance, beginning of year | <u>3,194</u> | <u>3,194</u> | <u>3,194</u> | <u>-</u> |
| Fund balance, end of year | <u>\$ 3,194</u> | <u>\$ 3,194</u> | <u>\$ 3,194</u> | <u>\$ -</u> |

See accompanying notes to budgetary comparison schedule.

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Notes to Budgetary Comparison Schedules
June 30, 2017

NOTE 1 – BUDGETING AND BUDGETARY CONTROL

Arizona Revised Statutes (A.R.S.) require the Town to prepare and adopt a balanced budget annually for each governmental fund. The Town Council must approve such operating budgets on or before the third Monday in July to allow sufficient time for the legal announcements and hearings required for the adoption of the property tax levy on the third Monday in August. A.R.S. prohibits expenditures or liabilities in excess of the amounts budgeted.

Expenditures may not legally exceed appropriations at the department level. In certain instances, transfers of appropriations between departments or from the contingency account to a department may be made upon the Town Councils' approval.

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Schedule of the Town's Proportionate
Share of the Net Pension Liability
Cost-Sharing Pension Plans
June 30, 2017

Arizona State Retirement System

| | Reporting Fiscal Year | | | |
|---|------------------------------|---------------|---------------|----------------|
| | (Measurement Date) | | | |
| | 2017 | 2016 | 2015 | 2014 |
| | (2016) | (2015) | (2014) | through |
| | | | | 2007 |
| Town's proportion of the net pension liability | 0.003230% | 0.002830% | 0.003194% | Information |
| Town's proportionate share of the net pension liability | \$ 521,354 | \$ 440,397 | \$ 472,585 | not available |
| Town's covered-employee payroll | \$ 302,433 | \$ 260,413 | \$ 287,907 | |
| Town's proportionate share of the net pension liability as a percentage of its covered-employee payroll | 172.39% | 169.11% | 164.15% | |
| Plan fiduciary net position as a percentage of the total pension liability | 67.06% | 68.35% | 69.49% | |

See accompanying notes to pension plan schedules.

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Schedule of Changes in the Town's
Net Pension Liability (Asset) and Related Ratios
Agent Pension Plans
June 30, 2017

PSPRS

| | Reporting Fiscal Year (Measurement Date) | | | 2014 through 2007 |
|---|---|------------------------------|------------------------------|--|
| | 2017 (2016) | 2016 (2015) | 2015 (2014) | |
| Total pension liability | | | | Information not available |
| Service cost | \$ 32,762 | \$ 23,998 | \$ 12,222 | |
| Interest on the total pension liability | 99,645 | 89,395 | 65,583 | |
| Changes of benefit terms | (137,660) | - | 51,744 | |
| Differences between expected and actual experience in the measurement of the pension liability | (43,689) | 83,333 | 5,598 | |
| Changes of assumptions or other inputs | 53,993 | - | 232,088 | |
| Benefit payments, including refunds of employee contributions | (70,533) | (70,533) | (69,041) | |
| Net change in total pension liability | (65,482) | 126,193 | 298,194 | |
| Total pension liability - beginning | 1,288,244 | 1,162,051 | 863,857 | |
| Total pension liability - ending (a) | <u>\$ 1,222,762</u> | <u>\$ 1,288,244</u> | <u>\$ 1,162,051</u> | |
| Plan fiduciary net position | | | | |
| Contributions - employer | \$ 71,823 | \$ 53,850 | \$ 22,396 | |
| Contributions - employee | 15,649 | 13,518 | 10,293 | |
| Net investment income | 3,452 | 20,805 | 70,331 | |
| Benefit payments, including refunds of employee contributions | (70,533) | (70,533) | (69,041) | |
| Administrative expense | (898) | (889) | - | |
| Other changes | 5 | (523) | (23,125) | |
| Net change in plan fiduciary net position | 19,498 | 16,228 | 10,854 | |
| Plan fiduciary net position - beginning | 583,471 | 567,243 | 556,389 | |
| Plan fiduciary net position - ending (b) | <u>\$ 602,969</u> | <u>\$ 583,471</u> | <u>\$ 567,243</u> | |
| Town's net pension liability (asset) - ending (a) - (b) | <u>\$ 619,793</u> | <u>\$ 704,773</u> | <u>\$ 594,808</u> | |
| Plan fiduciary net position as a percentage of the total pension liability | 49.31% | 45.29% | 48.81% | |
| Covered-employee payroll | \$ 134,324 | \$ 122,331 | \$ 101,139 | |
| Town's net pension liability (asset) as a percentage of covered-employee payroll | 461.42% | 576.12% | 588.11% | |

See accompanying notes to pension plan schedules.

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Schedule of Town Pension Contributions
June 30, 2017

Arizona State Retirement System

| | Reporting Fiscal Year | | | | 2013 through 2007 |
|--|------------------------------|-----------------|-----------------|-----------------|----------------------------------|
| | 2017 | 2016 | 2015 | 2014 | |
| Statutorily required contribution | \$ 32,954 | \$ 32,814 | \$ 28,359 | \$ 30,806 | Information not available |
| Town's contributions in relation to the statutorily required contribution | <u>(32,954)</u> | <u>(32,814)</u> | <u>(28,359)</u> | <u>(30,806)</u> | |
| Town's contribution deficiency (excess) | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | |
| Town's covered-employee payroll | \$ 305,700 | \$ 302,433 | \$ 260,413 | \$ 287,907 | |
| Town's contributions as a percentage of covered- employee payroll | 10.78% | 10.85% | 10.89% | 10.70% | |

PSPRS

| | Reporting Fiscal Year | | | | 2013 through 2007 |
|--|------------------------------|-----------------|-----------------|-----------------|----------------------------------|
| | 2017 | 2016 | 2015 | 2014 | |
| Actuarially determined contribution | \$ 74,886 | \$ 71,823 | \$ 53,850 | \$ 22,396 | Information not available |
| Town's contributions in relation to the actuarially determined contribution | <u>(74,886)</u> | <u>(71,823)</u> | <u>(53,850)</u> | <u>(22,396)</u> | |
| Town's contribution deficiency (excess) | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | |
| Town's covered-employee payroll | \$ 140,949 | \$ 134,324 | \$ 122,331 | \$ 101,139 | |
| Town's contributions as a percentage of covered- employee payroll | 53.13% | 53.47% | 44.02% | 22.14% | |

See accompanying notes to pension plan schedules.

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Notes to Pension Plan Schedules
June 30, 2017

NOTE 1 – ACTUARIALLY DETERMINED CONTRIBUTION RATES

Actuarial determined contribution rates for PSPRS are calculated as of June 30 two years prior to the end of the fiscal year in which contributions are made. The actuarial methods and assumptions used to establish the contribution requirements are as follows:

| | |
|--|---|
| Actuarial cost method | Entry age normal |
| Amortization method | Level percent closed for unfunded actuarial accrued liability, open for excess |
| Remaining amortization period as of the 2015 actuarial | 21 years for unfunded actuarial accrued liability, 20 years for excess |
| Asset valuation method | 7-year smoothed market value; 80%/120% market corridor |
| Actuarial assumptions: | |
| Investment rate of return | In 2013 actuarial valuation, the investment rate of return was decreased from 8.0% to 7.85% |
| Projected salary increases | In 2014 actuarial valuation, projected salary increases were decreased from 4.5% - 8.5% to 4.0% - 8.0%. In 2013 actuarial valuation, projected salary increases were decreased from 5.0% - 9.0% to 4.5% - 8.5%. |
| Wage growth | In 2014 actuarial valuation, wage growth was decreased from 4.5% to 4.0%. In 2013 actuarial valuation, wage growth was decreased from 5.0% to 4.5% |
| Retirement age | Experience-based table of rates that is specific to the type of eligibility condition. Last updated for the 2012 valuation pursuant to an experience study of the period July 1, 2006 - June 30, 2011. |
| Mortality | RP-2000 mortality table (adjusted by 105% for both males and females) |

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Schedule of Agent OPEB Plans' Funding Progress
June 30, 2017

Health Insurance Premium Benefit - PSPRS

| Actuarial Valuation Date | Actuarial Value of Plan Assets (a) | Actuarial Accrued Liability (b) | Funding Liability (Excess) (b-a) | Funded Ratio (a/b) | Annual Covered Payroll (c) | Unfunded Liability as Percentage of Covered Payroll ((b-a)/c) |
|--------------------------------|--|--|---|--------------------------|-------------------------------------|--|
| 06/30/17 | \$ 34,126 | \$ 4,617 | \$ (29,509) | 739.1 % | \$ 140,949 | 0.00 % |
| 06/30/16 | 31,978 | 4,020 | (27,958) | 795.5 | 134,324 | 0.00 |
| 06/30/15 | 29,977 | 2,910 | (27,067) | 1030.1 | 122,331 | 0.00 |

See accompanying notes to schedule of agent OPEB plans' funding progress.

TOWN OF PATAGONIA, ARIZONA
Required Supplementary Information
Notes to Schedule of Agent OPEB Plans' Funding Progress
June 30, 2017

NOTE 1 – FACTORS THAT AFFECT THE IDENTIFICATION OF TRENDS

Beginning in fiscal year 2014, PSPRS established separate funds for pension benefits and health insurance premium benefits. Previously, the plan recorded both pension and health insurance premium contributions in the same Pension Fund. During fiscal year 2014, the plan transferred prior-year health insurance premium benefit contributions that exceeded benefit payments from the plan's Pension Fund to the new Health Insurance Fund.



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**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING AND ON COMPLIANCE AND
OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

To the Town Council
Town of Patagonia, Arizona

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, and each major fund of the Town of Patagonia, Arizona, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Town of Patagonia, Arizona's, basic financial statements, and have issued our report thereon dated February 28, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Town of Patagonia, Arizona's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Town of Patagonia, Arizona's internal control. Accordingly, we do not express an opinion on the effectiveness of the Town of Patagonia, Arizona's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying

schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses. We consider all of the deficiencies described in the accompanying schedule of findings and questioned costs to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Town of Patagonia, Arizona's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that is required to be reported under *Government Auditing Standards*.

Town of Patagonia, Arizona's Response to Findings

The Town of Patagonia, Arizona's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The Town of Patagonia, Arizona's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Colby + Powell

February 28, 2018

TOWN OF PATAGONIA, ARIZONA
Schedule of Findings and Responses
June 30, 2017

Financial Statement Findings

Item: 2017-001

Subject: General ledger maintenance and reconciliation.

Criteria/Specific Requirements: To help ensure that internal and external financial reports are accurate, timely, and in accordance with generally accepted accounting principles, general ledger accounts should be reconciled on a monthly basis and supporting schedules should be prepared and reconciled with these general ledger accounts.

Condition: At the time of the audit, the Town had incorrect balances in many of its asset and liability accounts. Significant audit adjustments were necessary in order to present the financial statements in accordance with generally accepted accounting principles. These entries were proposed, accepted, and recorded by the Town in the financial statements.

Cause/Effect: Due to employee oversight, the need of proper training, and lack of management's review of performance, internal control procedures such as reconciliations of various general ledger accounts were not performed.

Recommendation: The Town's Finance Department should evaluate and implement closing procedures that establish clear deadlines for recording transactions and reconciling accounts to the general ledger and subsidiary ledgers. The Finance Department should also evaluate procedures to ensure that all accounts are reconciled and supported by documentation.

Response: Management agrees with this finding and will evaluate and implement closing procedures that will establish clear timelines and deadlines for recording transactions and reconciliations to the general ledger and sub ledgers.