

Management's Discussion and Analysis

As management of the City of Highland Park (City), we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the twelve months ended December 31, 2008. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal, which can be found in the Introductory Section of this report.

Financial Highlights

- The assets of the City exceeded its liabilities at December 31, 2008 by \$165.2 million (net assets).
- The government's total net assets increased by \$3,670,405 during the twelve months ended December 31, 2008. Business-type activities resulted in an \$18,859 increase, while net assets of governmental activities increased by \$3,651,546. The increase in governmental activities is primarily due to appreciation in the fair market value of investments held in the General Fund.
- As of December 31, 2008, the City's governmental funds reported combined ending fund balances of \$48.2 million, an increase of \$4.6 million in comparison with the prior fiscal period. This increase is due to a \$5.48 million appreciation in the fair market value of investments as noted above. Of the total fund balance, \$14.9 million is available for spending in the General Fund at the government's discretion (*unreserved, undesignated fund balance*).
- At the end of the current fiscal period, unreserved and undesignated fund balance of the general fund was \$14,910,292, or 41% of total general fund annual expenditures, exceeding the City's policy to maintain a minimum balance of 25-33%.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements.

Government-wide financial statements. The *government-wide financial statements* are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on all of the City's assets and liabilities, with the difference between the two reported as *net assets*. The *statement of activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through

user fees and charges (*business-type activities*). The governmental activities of the City include general government, public safety, public works, economic and physical development, transit, commissions and interest costs. The business-type activities of the City include a parking system, water utility, and operations of the Highland Park Country Club.

The government-wide financial statements include not only the City itself (known as the *primary government*), but also a legally separate library for which the City is financially accountable. Financial information for this *component unit* is reported separately from the financial information presented for the primary government.

The government-wide financial statements can be found on pages 3 - 5 of this report.

Fund financial statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental funds. *Governmental funds* are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The City maintains nine individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the general fund, street and bridge fund, debt service fund, and capital projects fund, all of which are considered to be major funds. Data for the other governmental funds are combined into a single, aggregated presentation labeled *nonmajor governmental funds*. Individual fund data for each of these nonmajor governmental funds is provided in the *combining statements and schedules* provided on pages 77 - 82 in this report.

The City adopts an annual appropriated budget for its governmental funds, with the exception of the Foreign Fire Insurance Tax Fund. Budgetary comparisons have been provided to demonstrate compliance with the budget.

The basic governmental fund financial statements can be found on pages 6 - 11 of this report.

Proprietary funds. The City maintains two different types of proprietary funds. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The City uses enterprise funds to account for its parking, water, and country club operations. *Internal service funds* are an accounting device

used to accumulate and allocate costs internally among the City's various functions. The City uses internal service funds to account for its equipment maintenance and replacement, as well as certain insurance activities. Because both of these services predominantly benefit governmental rather than business-type functions, they have been included within *governmental activities* in the government-wide financial statements.

Proprietary funds provide the same type of information as the government-wide financial statements, but in more detail. The proprietary fund financial statements provide separate information for the parking, water, and country club operations, all of which are considered to be major funds of the City. Conversely, both internal service funds are combined into a single, aggregated presentation in the proprietary fund financial statements. Individual fund data for the internal service funds is provided in the form of *combining and individual fund statements and schedules* on pages 86 - 90 in this report.

The basic proprietary fund financial statements can be found on pages 12 - 17 of this report.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are *not* available to support the City's programs. The accounting used for fiduciary funds is much like that used for proprietary funds.

The basic fiduciary fund financial statements can be found on pages 18 - 19 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 20 - 57 of this report.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information*. Budgetary comparisons for the general fund and street and bridge fund are provided, as well as information concerning the City's progress in funding its obligation to provide pension benefits and other post employment benefits to its employees. Required supplementary information can be found on pages 58 - 69 of this report.

The combining statements and schedules are presented immediately following the required supplementary information. Combining and individual fund statements and schedules can be found on pages 70 - 94 of this report.

Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City, assets exceeded liabilities by \$165.2 million at the close of the most recent fiscal year.

By far the largest portion of the City's net assets (76.6%) is its investment in capital assets – land, buildings, machinery, and equipment – less any related debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; thus, these assets are not available for future spending. Although the City's investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the City's net assets (4.3%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of *unrestricted net assets* (19.1% of total) may be used to meet the government's ongoing obligations to citizens and creditors.

**City of Highland Park's Net Assets
December 31, 2008**

	Governmental Activities		Business-Type Activities		Total	
	12/31/2008	12/31/2007	12/31/2008	12/31/2007	12/31/2008	12/31/2007
Current and Other Assets	\$69,292,648	\$63,675,530	13,178,009	12,741,929	82,470,657	76,417,459
Capital Assets	121,129,933	124,490,798	35,960,037	36,658,750	157,089,970	161,149,548
Total Assets	190,422,581	188,166,328	49,138,046	49,400,679	239,560,627	237,567,007
Long-Term Liabilities Outstanding	45,458,896	47,615,718	13,461,882	13,944,403	58,920,778	61,560,121
Other Liabilities	14,538,321	13,776,792	870,857	669,828	15,409,178	14,446,620
Total Liabilities	59,997,217	61,392,510	14,332,739	14,614,231	74,329,956	76,006,741
Net Assets:						
Capital Assets, net of Debt	96,490,406	96,339,097	30,126,135	29,931,296	126,616,541	126,270,393
Restricted	7,107,210	9,225,744	0	0	7,107,210	9,225,744
Unrestricted	26,827,748	21,208,977	4,679,172	4,855,152	31,506,920	26,064,129
Total Net Assets	130,425,364	126,773,818	34,805,307	34,786,448	165,230,671	161,560,266

The City reports positive balances in all three categories of net assets, both for the government as a whole, as well as for its separate governmental and business-type activities. The City has adopted a philosophy of funding capital improvements to a large extent on a pay-as-you-go basis, and retires debt obligations quickly, resulting in the positive net asset calculations.

Within the governmental activities, the City increased "Current and Other Assets" and "Unrestricted Net Assets", primarily as a result of the appreciation in fair market value of investments and increased cash balances. "Capital Assets" decreased primarily as a result of depreciation.

A breakdown of the change in net assets follows:

Water Utility	\$426,561
Parking System	(74,398)
Country Club	(333,304)
Governmental Activities	<u>3,651,543</u>
Change in Net Assets	<u>\$3,670,402</u>

Reductions in Net Assets of the Parking and Country Club funds are discussed in more detail on page MD&A-7.

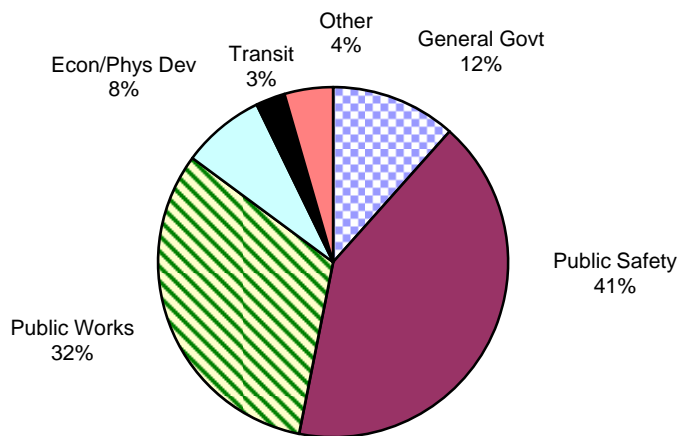
City of Highland Park's Changes in Net Assets

	Governmental Activities		Business-Type Activities		Total	
	12/31/2008	12/31/2007	12/31/2008	12/31/2007	12/31/2008	12/31/2007
Program Revenues						
Charges for Services	\$9,489,286	\$6,799,111	10,773,041	8,597,308	20,262,327	15,396,419
Operating Grants	796,375	652,180	0	0	796,375	652,180
Capital Grants	780,469	408,052	289,084	297,608	1,069,553	705,660
General Revenues						
Property Taxes	10,628,574	9,952,745	0	0	10,628,574	9,952,745
Sales Taxes	12,451,204	9,397,328	0	0	12,451,204	9,397,328
Other Taxes	11,959,642	8,011,821	0	0	11,959,642	8,011,821
Other	6,470,264	2,609,554	393,686	127,500	6,863,950	2,737,054
TOTAL REVENUES	52,575,814	37,830,791	11,455,811	9,022,416	64,031,625	46,853,207
Expenses						
General Government	5,682,530	3,291,348	0	0	5,682,530	3,291,348
Public Safety	20,358,646	13,931,034	0	0	20,358,646	13,931,034
Public Works	15,695,341	9,309,655	0	0	15,695,341	9,309,655
Economic/Physical Dev	3,765,001	2,929,461	0	0	3,765,001	2,929,461
Transit	1,325,557	967,852	0	0	1,325,557	967,852
Commissions	432,611	354,650	0	0	432,611	354,650
Interest	1,764,585	1,161,404	0	0	1,764,585	1,161,404
Parking	0	0	1,160,791	568,121	1,160,791	568,121
Water	0	0	6,993,813	4,387,664	6,993,813	4,387,664
Country Club	0	0	3,182,348	2,414,382	3,182,348	2,414,382
TOTAL EXPENSES	49,024,271	31,945,404	11,336,952	7,370,167	60,361,223	39,315,571
Increase in Net Assets before Transfers, Special Items and Contributions						
Contributions	3,551,543	5,885,387	118,859	1,652,249	3,670,402	7,537,636
Special Items	0	1,306,489	0	0	0	1,306,489
Contributions	0	0	0	409,327	0	409,327
Prior Period Adjustment	0	42,620	0	0	0	42,620
Transfers	100,000	100,000	(100,000)	(100,000)	0	0
Increase in Net Assets	3,651,543	7,334,496	18,859	1,961,576	3,670,402	9,296,072

- Variances exist in nearly all categories due to an 8-month fiscal period reported as of December 31, 2007, compared to a 12-month fiscal year reported as of December 31, 2008. This is due to a change in the City's fiscal year effective January 1, 2008.
- Property tax revenue increased by \$675,829 (6.8%) over the prior year, due to a small increase in the annual levy and the first year of collections for Special Service Area #16. Although the City is a home-rule municipality and not subject to property tax limitations, the property tax levy has increased by an average of only 2.3% per year over the past ten years.

- Sales tax revenue for calendar year 2008, compared to calendar year 2007, decreased by \$665,125 (7.72%), reflective of national economic conditions. Comparison of other taxes for the eight month period ending December 31, 2007, compared to the same eight month period in 2008, reveal increases in local use tax (4.61%), utility tax on natural gas (33.58%), and cable television franchise fees (19.59%). However, declines were reported in income taxes (35.18%), personal property replacement tax (3.13%), hotel taxes (16.67%), and real estate transfer taxes (50.63%).
- The increase in other revenues is attributable in large part to an unrealized gain of \$5,475,734 to reflect General Fund investments at fair value.
- Expenses totaled \$39.3 million for the eight months ended December 31, 2007, which represents 65% of expenses for the 12-month calendar fiscal year 2008.

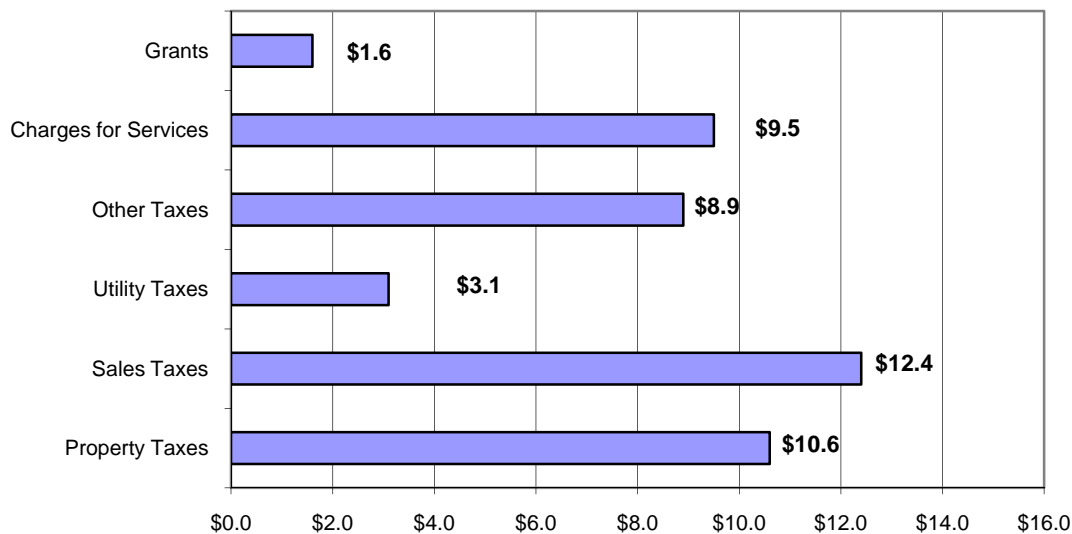
Expenses and Program Revenues – Governmental Activities



Public Safety expenses (police and fire) account for the greatest percent of governmental activities with 41%, followed by public works, general government, and economic/physical development.

Revenues by Source – Governmental Activities

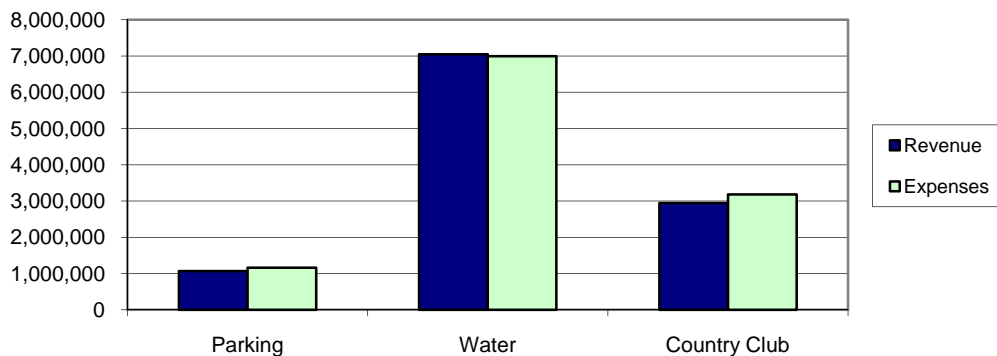
Amounts in Millions



Sales taxes account for the greatest proportion of funding for governmental activities on an annualized basis, followed by property taxes and charges for services. Growth in expenses has been closely monitored for nine consecutive years, with operating departments mandated to contain non-personnel related operating costs. However, the City has continued an aggressive capital improvement plan, investing \$3.8 million annually in street, sewer and ravine improvements from governmental revenues.

Business-Type Activities

Business-type activities increased the City’s net assets by \$18,859. As noted previously, business-type activities are intended to be self sufficient – charges for services should be sufficient to cover all costs associated with the operation. The following graph shows a comparison of revenues and expenses of each business-type activity:



- Net assets of the parking fund decreased by \$74,398 in the current fiscal year, the majority of which is due to depreciation.
- The water utility fund net assets increased by \$426,561, which includes a \$289,084 contribution associated with the Cliff Road water main.
- Net assets of the country club fund decreased by \$333,304, the majority of which is due to decreased golf and banquet revenues.
- Revenue of business-type activities is almost exclusively charges for services. During the current fiscal period, non-operating revenues/expenses totaled (\$203,047).

Financial Analysis of the City’s Funds

As noted earlier, the City utilizes fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental funds. The focus of the City’s *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the City’s financing requirements. In particular, *unreserved fund balance* serves as a useful measure of a government’s net resources available for spending at the end of the fiscal year.

As of December 31, 2008, the City’s governmental funds reported combined ending fund balances of \$48.2 million, an increase of \$4.6 million in comparison with the prior fiscal year. As noted previously, a large portion of this increase is the result of an unrealized gain of \$5,475,734 included in investment income of the General Fund associated with the reporting of investments at fair market value. Of the total fund balance, \$14.9 million constitutes *unreserved*,

undesignated fund balance in the General Fund, which is available for spending at the government's discretion. *Reserved fund balance* totaling \$29.4 million is not available for discretionary spending because it has already been committed for a variety of purposes, including police and fire pension obligations, payment of debt service, long-term loans receivable, public facilities, street improvements, and public safety expenditures (E-911 Fund). The City also reports a *designated fund balance* of \$3.6 million in the General Fund to meet future obligations for other post-employment benefits. Please refer to page 7 for a detailed description and amounts of reserved fund balance.

The general fund is the primary operating fund of the City. At the end of the current fiscal period, unreserved and undesignated fund balance of the general fund was \$14.9 million. As a measure of the general fund's liquidity, it is useful to compare unreserved fund balance to total fund expenditures. Unreserved, undesignated fund balance represents 43% of total general fund expenditures for the 2008 fiscal year. The unreserved, undesignated fund balance of the general fund increased by \$223,604 during the current fiscal period.

The street and bridge fund has a total fund balance of \$361,101. For the current fiscal year, fund balance decreased by \$786,921, which was due primarily to unanticipated snow and ice control expenditures requiring mid-year budget amendments to address an unusually severe winter.

The debt service fund has a total fund balance of \$904,425, all of which is reserved for the payment of debt service. During the current fiscal year, the fund posted a \$79,863 increase in fund balance.

The capital projects fund has a fund balance of \$4.6 million at December 31, 2008. During the current fiscal year, the fund posted a \$568,126 decrease in fund balance due primarily to current year expenditures funded by prior year bond proceeds.

Nonmajor governmental funds combined for a total fund balance of \$1.55 million at year end.

Proprietary funds. The City's proprietary fund statements provide the same type of information found in the government-wide financial statements, but in more detail.

Net assets of the parking system totaled \$5.2 million at December 31, 2008. Net assets of the water utility fund amounted to \$19.3 million. Net assets of the country club operation amounted to \$10.4 million. The total growth in net assets for all proprietary funds was \$18,859. Factors concerning the finances of these funds have been addressed in the discussion of the City's business-type activities.

General Fund Budgetary Highlights

The General Fund budget was amended during the fiscal period to transfer appropriations between operating departments and to provide for unanticipated expenditures. Actual revenues exceeded the budget by \$4.4 million, with positive variances reported in investment income and other revenues which offset shortfalls in sales tax, utility tax, real estate transfer tax and permits. Total general fund expenditures were 90% of budget, resulting in a budgetary savings of nearly \$3.6 million. The increase in fund balance of \$6.6 million compared favorably to the budget projection that fund balance would decrease by \$453,134. The increase in fund balance is due primarily to appreciation in the fair value of investments of \$5.5 million and forfeited guaranteed deposits of \$1.1 million.

Capital Asset and Debt Administration

Capital assets. The City's investment in capital assets for its governmental and business type activities as of December 31, 2008, amounts to \$126.6 million, net of accumulated depreciation and outstanding related debt. This investment in capital assets includes land, buildings, other improvements, machinery and equipment, streets, bridges, sanitary and storm sewers, and water production and distribution systems.

Major capital asset events during the current fiscal year included the following:

- Water system improvements totaling \$1.2 million, consisting primarily of the Patton Road and Waukegan Avenue water main improvement projects, but also including the Cliff Road water main dedication.
- Infrastructure improvements totaled \$976,020, including improvements at Linden Avenue, Old Deerfield Road, and Ravine #10 Check Dam Installation.
- Land assets increased due to the Purchase of property at 1870 Green Bay Road.

City of Highland Park's Capital Assets (net of depreciation)

	Governmental activities		Business-type activities		Total	
	12/31/2008	12/31/2007	12/31/2008	12/31/2007	12/31/2008	12/31/2007
Land	\$8,923,202	\$8,744,366	\$4,981,323	\$4,981,323	\$13,904,525	\$13,725,689
Buildings and improvements	52,132,889	53,614,192	15,409,267	16,180,092	67,542,156	69,794,284
Machinery and equipment	4,760,052	4,962,968	1,158,842	1,378,430	5,918,894	6,341,398
Infrastructure	55,313,790	57,169,276	14,310,302	14,118,905	69,624,092	71,288,181
Construction in progress	-	-	100,303	-	100,303	-
Total	\$121,129,933	\$124,490,802	\$35,960,037	\$36,658,750	\$157,089,970	\$161,149,552

Additional information on the City's capital assets can be found in note 5 on pages 33 - 34 of this report.

Long-term debt. At the end of the current fiscal period, the City had total general obligation bonded debt outstanding of \$53,761,914. Of this amount, \$40,506,914 comprises debt to be paid by the debt service fund from general governmental revenues. The remainder of the City's debt will be paid from revenue of business-type activities.

City of Highland Park's Outstanding Debt General Obligation Bonds

	Governmental activities		Business-type activities		Total	
	12/31/2008	12/31/2007	12/31/2008	12/31/2007	12/31/2008	12/31/2007
Total	\$40,506,914	\$43,466,444	\$13,255,000	\$14,060,000	\$53,761,914	\$57,526,444

The City's total bonded debt decreased by \$3.76 million during the current fiscal period. The City's general obligation bonds maintain a "Aaa" rating from Moody's Investors Service.

Under the 1970 Illinois Constitution, there is no legal debt limit for home rule municipalities except as set by the General Assembly. If the City were subject to such a limitation, outstanding indebtedness could not exceed 8.625% of equalized assessed valuation. Currently, the City's direct bonded debt of \$53.76 million represents 1.93% of the City's equalized assessed valuation.

Additional information on the City's long-term debt can be found in the Notes to Financial Statements note 7 of this report.

Economic Factors and Next Year's Budgets and Rates

The City has a long-standing heritage as one of the prestigious communities along Chicagoland's "north shore" of Lake Michigan. The long term economic outlook remains strong as the City's stable property tax base increased by 3.9% this year. With 92% of the tax base consisting of residential property, property tax revenue is exceedingly stable. If the current economic trends in the housing and retail markets continue the City anticipates little increase in the assessed value and decreased sales tax, building permit and real estate transfer tax revenues. With sales tax being the primary revenue source for general fund operations, the City is monitoring this revenue closely. Other economic factors impacting the City's budget are as follows:

- The unemployment rate for the City is currently 4.4%, which compares favorably to the 6.7% rate for Lake County and 6.5% rate for the State of Illinois.
- The total value of building permits in the City for fiscal year 2008 was \$126.7 million, a decrease of \$22.4 million from 2007, indicative of the current housing market. In calendar year 2008 the total number of building permits issued declined by 16% compared to 2007.
- The per capita income of the City's labor force was \$55,331 according to the latest census, which placed the City among the nation's wealthiest communities with populations of 25,000 or more.

Due to the City's conversion to a calendar fiscal year effective January 1, 2008, a 20-month budget was adopted in April 2007, which encompasses the May 2007 - December 2007 shortened fiscal period as well as the calendar fiscal year 2008. Therefore, the 2008 budget was adopted prior to the decline in the national economy. The City has monitored sales tax, building permit and real estate transfer tax revenue on a monthly basis, as these three revenue sources have declined in the last twelve months. This practice allows the City to continually assess the need for reduced expenditures to offset revenue shortfalls.

Employee benefit expenditures continue to increase due to mandated pension costs and health and dental insurance. City operating departments were required to maintain a 0.00% increase in non-personnel costs for the current budget period.

The 2009 budget projects a \$1,446,413 decrease in unreserved fund balance of the general fund due to reductions in sales tax, building permit and real estate transfer tax revenues.

Requests for Information

This financial report is designed to provide a general overview of the City's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information may be addressed to the Office of the Finance Director, City of Highland Park, 1707 St. Johns Avenue, Highland Park, Illinois 60035.