

INTRODUCTORY SECTION

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- Organizational Chart



McMinnville



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November 22, 2006

Mayor Edward J. Gormley
City Councilors
Citizens of the City of McMinnville

City management is pleased to submit the City of McMinnville's *Comprehensive Annual Financial Report* for the fiscal year ended June 30, 2006. The *Comprehensive Annual Financial Report (CAFR)* presents the financial position of the City of McMinnville (City) as of June 30, 2006 and the results of City operations and proprietary fund cash flows for the year then ended. The City's financial statements and schedules were prepared following generally accepted accounting principles (GAAP) and were audited by Talbot, Korvola & Warwick LLP in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*. Talbot, Korvola & Warwick LLP concluded the basic financial statements are free of material misstatement and issued an unqualified opinion presented in the second section of this report. Financial accuracy, completeness, and fairness of presentations in the *CAFR* are the responsibility of City of McMinnville's management. City management asserts the *CAFR* is complete and reliable in all material respects.

Comprehensive Annual Financial Report: The *CAFR* contains the following four sections:

Introductory Section: This letter of transmittal, Government Financial Officers Association Certificate of Achievement for period ended June 30, 2005, list of elected officials, and the City's organizational chart comprise the introductory section.

Financial Section: Talbot, Korvola & Warwick LLP's independent auditor's report, management's discussion and analysis (MD&A), government-wide financial statements for the City as a whole and the component unit, fund financial statements, notes to the financial statements, supplemental combining and individual fund statements and schedules, and supplemental information comprise the financial section. The MD&A is intended to provide a narrative introduction, overview, and analysis to accompany the basic financial statements. This letter of transmittal is designed to complement the MD&A and should be read together with it. The MD&A is found on pages 19–32.

Statistical Section: This section provides financial statements users with additional, primarily historical, information to assist the user in better understanding the financial statements. The section includes information on financial trends, revenue capacity, debt capacity, demographic and economic data, and operating information. The statistical section has been reformatted according to *Governmental Accounting Standards Board (GASB) Statement #44, Economic Condition Reporting: The Statistical Section*. The statistical section is found on pages 141–178.

Reports of Independent Certified Public Accountants: Following these three sections are reports of the City's independent certified public accountants, Talbot, Korvola & Warwick LLP, which are required by State of Oregon statutes and *Government Auditing Standards*.

Reporting Entity:

City: The City is a municipal government incorporated as a town in 1876 and as a city in 1882, and now operates under a council-manager form of government. The elected officials are a mayor and six city council members. All seven positions are elected for staggered four-year terms. The City provides a full range of services --- City administration, finance, and information services; police protection and investigation; municipal court; fire protection and inspection; wastewater treatment and system construction and maintenance; street construction and maintenance; engineering services; planning services; building inspection services; library; parks and recreation including aquatic center, community center, Kids-on-the-Block After-School Program, recreational sports, and senior center; park system; emergency ambulance; and a municipal airport.

Department: In addition to the City's primary services, over which the elected officials exercise financial control, the City has one discretely presented component unit, the McMinnville Water and Light Department (Department) that is governed by a City Council appointed Water and Light Commission. The Department provides water and electrical services to City residents. Besides the component unit financial statements, additional information on the Department is located in the notes to the financial statements, note I. A. 2., page 67.

Factors Affecting Financial Condition:

Employers: The City of McMinnville is located in the agriculturally rich Willamette Valley 40 miles southwest of Portland and 25 miles northwest of Salem at an elevation of 157 feet. The area has a mild climate averaging 70 degrees from June to September and 40 degrees from November to February. The average rainfall is 42 inches with the growing season approximately 175 days. The City of McMinnville's economy is widely diversified and continues to grow at a moderate pace. The primary industries include commercial aviation, steel rebar production, medical services, insurance products and services, manufactured home and recreational vehicle production, plastics fabrication, tourism, and food production. As the county seat of Yamhill County and the home of Linfield College, McMinnville is the economic hub for a growing county. Agriculture plays a major role in the county, as does McMinnville's commercial sector. The City's diverse economy is based primarily on companies of smaller than 50 employees, although several larger companies are also based in McMinnville. The City's largest employers are listed in the Statistical Section on pages 170-171.

Employment: Employment in McMinnville in 2004¹ was concentrated in the retail/wholesale trade, transportation and utilities sectors, 17 percent; followed by private education and health services employment, 15 percent; in large part due to Linfield College. Manufacturing employment also represented a large percentage of total employment, 14 percent, a slightly larger percentage than that found statewide; government employment, 14 percent, was slightly lower than the state average. The remaining employment was divided amongst a number of categories. According to the Oregon Employment Department's 2004 data, most of the employment in McMinnville is in industries with above-average levels of payroll per employee. McMinnville's average payroll per employee is \$29,721. During the past decade, most of the largest industries in McMinnville showed increases in employment, with health services, 664 new employees; local government, 496; and construction, 320, leading the way. It is interesting to note that during this same period of time, over half of the employment growth was from industries with a payroll per employee above the average for McMinnville as a whole.

¹ Source: Oregon Department of Employment, compilation of 2005 employment data not yet available.

Recent economic forecasts for McMinnville suggest that the area will continue to grow at a slightly faster rate than Yamhill County and the northern Willamette Valley Region, as it has over the last several decades. These same forecasts estimate that McMinnville's employment, which currently totals approximately 15,000, will continue to grow at an average annual growth rate of 2.06 percent over the course of the next twenty years.

Population Growth: Connected to the growth of the employment base, over the last ten years, McMinnville has experienced one of the fastest population growth rates in Oregon, 32.1 percent. Both new employers and residents are attracted to McMinnville because of its "livability" and its close proximity to the Portland metropolitan area; Salem, the state's capital; the Cascade mountain range; and the Oregon coast. Other factors contributing to the livability besides the location and economic base are the vitality of McMinnville's downtown, Linfield College, excellence of medical services, and excellence of City services. During the same 10-year period, the state of Oregon has grown 16.0 percent, less than half the rate of growth of McMinnville, while Yamhill County population has grown by 18.3 percent. Since 1985, the city's population has doubled while the State of Oregon's population has increased by 27.6 percent. Although the official estimated population for McMinnville shows a 0.6 percent increase, anecdotal data indicates a much higher population growth. For example, the City's Building Division issued 196 permits for new residential construction, a 2.5 percent increase; the Department opened 249 new residential electrical service accounts, a 2.2 percent increase, and McMinnville School District experienced a 4.5 percent increase in student enrollment.

Population Estimates

<u>Year</u>	<u>McMinnville</u>		<u>Yamhill County</u>		<u>State of Oregon</u>	
	<u>Population</u>	<u>Percent Change</u>	<u>Population</u>	<u>Percent Change</u>	<u>Population</u>	<u>Percent Change</u>
1996	22,800	3.3%	77,500	3.9%	3,181,000	1.6%
2002	28,200	6.4	87,500	1.2	3,504,700	1.0
2003	28,890	2.4	88,150	0.7	3,541,500	1.1
2004	29,200	1.1	89,200	1.2	3,582,600	1.2
2005	30,020	2.8	90,310	1.2	3,628,700	1.3
2006	30,215	0.6	91,675	1.5	3,690,160	1.7

Source: US Census Bureau, Portland State University Population Research Center certified yearly rounded estimates

Using forecasts published by the Oregon Office of Economic Analysis, McMinnville's population is expected to increase over the next twenty years at an average annual increase of 2.4 percent. At this rate, McMinnville's year 2025 population is expected to reach 46,195; an increase of some 15,980 residents from its 2006 estimated population total.

Residential, Commercial, and Industrial Development: McMinnville's residential, institutional, and commercial sectors continue to see steady growth, as evidenced by the activity experienced this past year and in preceding years. In the past year alone, the following significant new developments occurred: 1) the ground breaking for an estimated \$11 million expansion of the Willamette Valley Medical Center, and completion of a new oncology center, at a cost of some \$5 million; 2) Oregon Mutual Insurance's construction of a new 60,000 square foot office building within downtown McMinnville, valued at more than \$7 million; 3) initial construction of a new Comfort Inn hotel on Highway 18, at a cost of nearly \$4 million; 4) additions totaling approximately \$2.5 million to the Nazarene Church in northwest McMinnville; 5) the opening of two new furniture stores: Lewis Furniture, on Lafayette Avenue, valued at \$1 million, and Furniture Outlet, on Cumulus Avenue, valued at \$2 million; 6) interior remodel of the Evergreen Aviation Air Museum to accommodate the display of antique and historic guns and artillery; 7) construction of additional mini-storage units on land adjacent to Riverside Drive; 8) demolition of the former Stan's Market and construction in its place of a new office building, valued at nearly \$400,000; 9) an approximately \$750,000 addition to the existing Wilco Farmers Coop; 10) expansion of the Oregon

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Hotel's popular rooftop bar; 11) construction of a new office building complex at the corner of Hill Road and West Second Street; 12) extensive exterior façade renovation work to the McMinnville Plaza shopping center located in northeast McMinnville; and 13) redevelopment of a several acre parcel on Highway 99W to allow for the construction of a new commercial retail and office complex.

In addition to these commercial improvements, permits were issued for several other projects that are expected to get underway within the next few months. These include a new building for the McMinnville Community Media, the local access channel, offices and studios on the Linfield College campus, valued at more than \$500,000; and interior renovation of the Oregon Mutual Insurance Regional building to accommodate the relocation of the City of McMinnville's Community Development Departments. Projects expected to get underway also include the construction of a new \$7.2 million Public Safety Building to house the City's Police Department and Yamhill Communications Agency (YCOM), the county's emergency dispatch center; and \$24,000,000 construction estimate of another building on the Evergreen Aviation Museum campus that will mirror in design and size the existing air museum, which is slated to become a space museum. In November 2006, McMinnville School District passed a \$66 million general obligation bond which will construct a new elementary school at the corner of Booth Bend Road and South Davis Street, expand McMinnville High School, and construct additional classrooms and renovate several other existing schools in the district.

In addition, in the past two years alone, the City has granted approval for the development of 19 residential subdivisions that, when completed, will add 789 lots to help meet the area's demand for housing. For purposes of comparison, the 2000 US Census Bureau estimates that there existed a total of 9,834 housing units within McMinnville.

As evidence of the level of residential building activity experienced in McMinnville in the past year, Building Division records show that there were 348 permits issued for residential construction in 2006. This compares to 363 and 377 permits for the years of 2005 and 2004, respectively. In addition, the level of commercial and industrial construction was 173 permits for 2006, as compared to 155 in 2005 and 177 in 2004.

In October of 2003, the McMinnville City Council adopted the *McMinnville Growth Management and Urbanization Plan* that will ensure adequate lands for economic growth, housing, recreation, and infrastructure for the next twenty years.

Property Values: Real market value growth is another factor in measuring the economic health of a community. As illustrated below, the real market value for McMinnville has grown by a healthy 120.7 percent over the last ten years. Also illustrated is the effect of a tax limitation measure enacted in 1996 that split maximum assessed value for taxation valuation purposes from real market values. This tax limitation measure rolled back assessed values for taxing purposes two years, and limited future growth to three percent except for new construction and major improvements made to existing structures. Over this same ten-year period, maximum assessed values increased by 56.4 percent. The property values table below also illustrates that McMinnville is located in a growing economic region, as the growth of Yamhill County's real market value has grown by 118.0 percent in the last ten years.

Cascade Steel Rolling Mills (CSRM), the City's largest taxpayer, appealed their maximum assessed valuation, which is valued by special State of Oregon industrial assessors for fiscal years 2002 and 2003. With the economic problems of the steel industry in the United States, the Oregon Tax Court lowered CSRM's assessed valuation by approximately \$35 and \$44 million, for those years respectively. With the recent high demand for steel in the Pacific Rim, and particularly in China, CSRM's operating position looks bright. With the improving steel industry climate, it is extremely unlikely CSRM's valuation will again significantly decrease. Even with the significantly lower CSRM valuation, in 2002 and 2003, the City's maximum assessed valuation rose 5.0 percent during that

two-year period. This rise in assessed valuation is a testament to the overall economic health and diversity of McMinnville.

Property Values --- Maximum Assessed Value and Real Market Value
 (\$s in thousands)

<u>Fiscal Year End</u>	<u>McMinnville</u>				<u>Yamhill County</u>	
	<u>Maximum Assessed Value</u>	<u>Percent Change</u>	<u>Real Market Value</u>	<u>Percent Change</u>	<u>Real Market Value</u>	<u>Percent Change</u>
1996	\$ 1,003,698	17.2%	\$ 1,003,698	17.2%	\$ 3,311,385	15.1%
2002	1,275,635	1.2	1,610,697	2.4	5,327,822	2.3
2003	1,323,091	3.7	1,716,334	6.5	5,616,522	5.4
2004	1,381,286	4.4	1,760,704	2.6	5,814,566	3.5
2005	1,473,341	6.7	2,020,287	14.7	6,587,913	13.3
2006	1,570,074	6.6	2,215,610	9.7	7,218,305	9.6

Source: Yamhill County Assessor's Office

Property Tax Rates: The 1996 property tax limitation measure converted the prior property tax system, which for McMinnville was a combination system of dollar property tax base which could rise by 6 percent per year and rate based millage levies for fire and parks services, to an entirely rate based property tax system. The new property tax system, finalized with the passage of Measure 50, allows the maximum assessed valuation of established residences and businesses to rise by only 3 percent per year. New construction is valued at estimated real market value discounted by the percentage differential between the City's total maximum assessed value and the City's total real market value.

Since the 2000-2001 fiscal year, the City of McMinnville has levied the entire \$5.02 permanent property tax rate for operations, which was established by the 1996 tax limitation measure. Also illustrated below is McMinnville citizens' support of a new 20-year parks improvement general obligation bond, first levied in fiscal year 2001-2002.

Property Tax Rates
 (per thousand of assessed valuation)

<u>Fiscal Year Ended</u>	<u>City of McMinnville - Only</u>			<u>McMinnville Tax Code #40</u>
	<u>Operating Levy</u>	<u>Debt Service Levy</u>	<u>Total Property Tax Levy</u>	<u>Consolidated Property Tax Rate</u>
1996	\$ 4.16	\$ 0.81	\$ 4.97	\$ 20.71
2002	5.02	1.30	6.32	17.12
2003	5.02	1.27	6.29	17.30
2004	5.02	1.25	6.27	17.50
2005	5.02	0.96	5.98	15.93
2006	5.02	0.90	5.92	16.31

Source: Yamhill County Assessor's Office

City of McMinnville Government: The 2005-2006 fiscal year continued to be a challenging one for most of Oregon's local governments and the City of McMinnville was not exempt from those challenges. As mentioned above, the City has levied the maximum operating property tax rate of \$5.02 for the last six years. Given the pressures of increased operating costs, most notably police and fire union salary and cost-of-living adjustments, medical insurance funding, and the Oregon Public Employee Retirement System contribution rate, the City has been able to maintain fund balances due to the continued increases in the City's maximum assessed valuation and the City Council decision to maintain spending at levels where additional revenue sources would not be needed, at least over the short-term.

2005-2006 – Year in Review – Major Accomplishments and Issues:

Governance and Fiscal Policy: The City's operating Budget for fiscal 2005-2006 was again essentially a "hold the line" budget. The City's portion of the property tax rate fell from \$5.98 in 2004-2005 to \$5.92 due to the increase of the maximum assessed valuation. Although City Council was considering a November 2006 local option levy to increase operating revenues, they instead decided to place a \$13,120,000 bond measure on the May 2006 ballot which will fund a much needed public safety building and multi-purpose Municipal Courtroom/City Council Chambers, and public meeting space building. Funds were budgeted to successfully acquire an office building from Oregon Mutual Insurance Company. The building will serve as a new Community Development Center to house the City's Building, Engineering, and Planning Departments. A major success story was completing the City Council's community outreach program, "Community Choices." Community attitude surveys, seven neighborhood meetings, service club presentations, direct mailings to residents all served to both obtain information on citizens' values, attitudes, and service priorities and to provide information to the public on City services. The feedback received was used by the staff and City Council to help establish City Council Goals and Objectives for 2006, including adjustments to fiscal policy that affected spending levels and priorities in the preparation of the 2006-2007 budget – e.g. significant increases in spending for public safety services were adopted.

Public Safety: In May of 2006, McMinnville voters overwhelmingly approved the issuance of general obligation bonds to finance the construction of a new public safety building and multipurpose Municipal Court/Council Chambers building. A citizen advisory committee is working with City staff and an architecture firm to finalize the plans, and construction is scheduled to begin in the spring of 2007 on the public safety building. A new Chief of Police, Ron Noble, began work in May 2006. As an outgrowth of the Community Choices discussions, the 2006-2007 Budget, developed and adopted in spring of 2006, increased resources dedicated to public safety by the adding of three new police officers and three new paramedic/firefighters. Funds were also budgeted to begin a motorcycle unit in the Police Department. The 2005-2006 Budget included funds to purchase a new ambulance, which will be delivered in January 2007.

Parks: Construction was completed in the fall of 2005 on a major section of the Westside Pedestrian/Bicycle Path along a Bonneville Power Administration easement, between West Second Street and Wallace Road. One additional parks maintenance worker position was funded in 2005-2006 to help with park maintenance given the new Discovery Meadows Park which opened in the spring of 2005. In the fall of 2005, the new Park Watch Program began with the help of interested citizens located near the community parks.

2006-2007 – Future Issues and Initiatives:

Governance and Fiscal Policy: Community outreach efforts continue, primarily in the form of additional neighborhood meetings being held at local schools in the fall of 2007. A written City of McMinnville Annual Report is scheduled for distribution to citizens in the winter of 2007. Monitoring of the City's tax-supported operating funds will be important to ensure the continued funding of operating services, particularly given the higher level of public safety services added July 1, 2006.

Public Safety: Final design of the new public safety building to house the Police Department and YCOM, the county's emergency communications center, is now underway. Construction on the new public safety building is scheduled to begin in spring of 2007. The Municipal Court/City Council Chambers building is in the preliminary design stage and is scheduled to be constructed in 2008.

Public Works & Community Development: The City's *Master Transportation Plan* is currently in the process of being reviewed and updated. A citizen advisory committee is working with City staff and a transportation engineer. The findings of this work will undoubtedly include recommendations for significant transportation capital improvements. Finding funding sources for these improvements will be a significant challenge. Remodel work on the new Community Development

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Center is expected to begin in December of 2006 and be completed early in 2007. Upon completion the staffs from Planning, Engineering, and Building Departments will relocate from City Hall to the new building. This move not only provides new space for Community Development but also frees up City Hall for more effective housing of Finance and Municipal Court staff.

Wastewater Services: Work continues on updating the Sanitary Sewer Collection System Master Plan, the Water Reclamation Facility Master Plan, and the Wet Weather Overflow Management Plan. These documents will serve as the basis for the next significant capital improvements to the sanitary sewer and storm water systems. After the updates are completed, City Council will hear the reports and ultimately work toward financing the recommended improvements.

Airport: A feasibility study will be completed in 2007 to determine the future of facilities for the McMinnville Municipal Airport's fixed base operator. Engineering for an approximate \$5,000,000 capital improvement project at the airport, being funded in cooperation with the Federal Aviation Administration and Evergreen International Aviation, will take place in 2007.

Planning and Economic Development: The Department of Land Conservation and Development has issued an official approval of the City's proposed Urban Growth Management Plan, although the appeal deadline has not passed as of this writing. Once approved, work will need to begin on implementing ordinances and more plan detail. A draft sign ordinance has been prepared and early in 2007 will be reviewed by the Planning Commission and City Council. City staff will continue to work with the McMinnville Economic Development Partnership and their recently hired Executive Director. This new position, filled in the summer of 2006, is funded in partnership with McMinnville Chamber of Commerce, McMinnville Industrial Promotions, McMinnville Water & Light Department, Yamhill County, and the City of McMinnville.

Debt Service:

The details to the City's long-term debt issuances can be found in note III. F. on pages 85-92.

Cash and Investment Management:

Cash Management: Day-to-day City cash needs are managed using four bank accounts: a general operations account, a linked payroll account, a municipal court bail account, and an escrow account. The four bank accounts utilize a sweep system, which invests overnight surplus float in bank repurchase agreements, note III. A., pages 76-78.

Investment Management: The City's general operations account balance, which exceeds current operating needs, is invested following the City's investment policy and Oregon Revised Statutes. The City's investment policy's first priority is preservation of capital; second priority is liquidity; and third priority is rate of return. The management of the City's investment portfolio is kept relatively simple due to its comparative small size and due to staffing limitations. During this fiscal year, all surplus capital was invested in the State of Oregon Local Government Investment Pool, notes I. E. 1. and III. A., pages 72 and 76-78, respectively.

Risk Management:

The City is covered for comprehensive liability, property, auto liability and physical damage, employers' liability, and workers' compensation insurance through City County Insurance Services (CIS). CIS is a public entity risk pool, established in 1981, by the League of Oregon Cities and the Association of Oregon Counties. CIS provides a full range of insurance coverages and loss control services to a significant number of Oregon cities and counties. More comprehensive insurance information is found in the notes to the financial statements, note IV. A. pages 93-94.

Certificate of Achievement:

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of McMinnville for its *Comprehensive Annual Financial Report (CAFR)* for the fiscal year ended June 30, 2005. The City has received this recognition for seventeen consecutive years. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized *CAFR* and must satisfy both generally accepted accounting principles and applicable legal requirements. This award is the highest form of recognition for excellence in state and local government financial reporting.

A Certificate of Achievement is valid for a period of one year only. We believe our current *CAFR* continues to meet these standards and will be submitted to GFOA to determine eligibility for another certificate.

Acknowledgements:

The preparation of the *Comprehensive Annual Financial Report (CAFR)* is the final step in completing a successful year for the City's Finance Department. We would like to thank the City's two full-time and two part-time accountants for their day-to-day dedication providing the City with professional accounting services and accurate accounting records which are the critical basis for successful financial statement preparation in the City's *CAFR*.

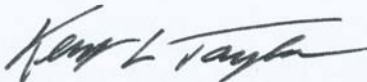
This fourth year of the City implementation of the *GASB Statement #34* reporting model established by the Governmental Accounting Standards Board (GASB) went smoothly. The revised reporting and capitalization procedures established in the first year of implementation continued to work effectively. The continued help from the City's Engineering Department is greatly appreciated and critical to accurate infrastructure reporting.

We would like to give special recognition to the dedication of Laurie S. LeCours, CPA, as the City's financial statement preparation project leader. During this fiscal year, Ms. LeCours lead the implementation of *GASB Statement #44, Economic Condition Reporting: The Statistical Section*. The revamped and much improved statistic section is a testament to her dedication in bringing new governmental accounting guidance into the City's *CAFR*.

Furthermore, we would like to acknowledge the efforts of all City department personnel who during the year conscientiously follow internal controls; and during *CAFR* preparation, provide additional information that make the report more meaningful than merely a presentation of financial statements.

Special appreciation should also go to the City of McMinnville Mayor and City Councilors for their interest and support in conducting the financial operations of the City in a responsible and progressive manner.

Respectfully submitted,



Kent L. Taylor
City Manager



Carole M. Benedict, CPA
Finance Director

