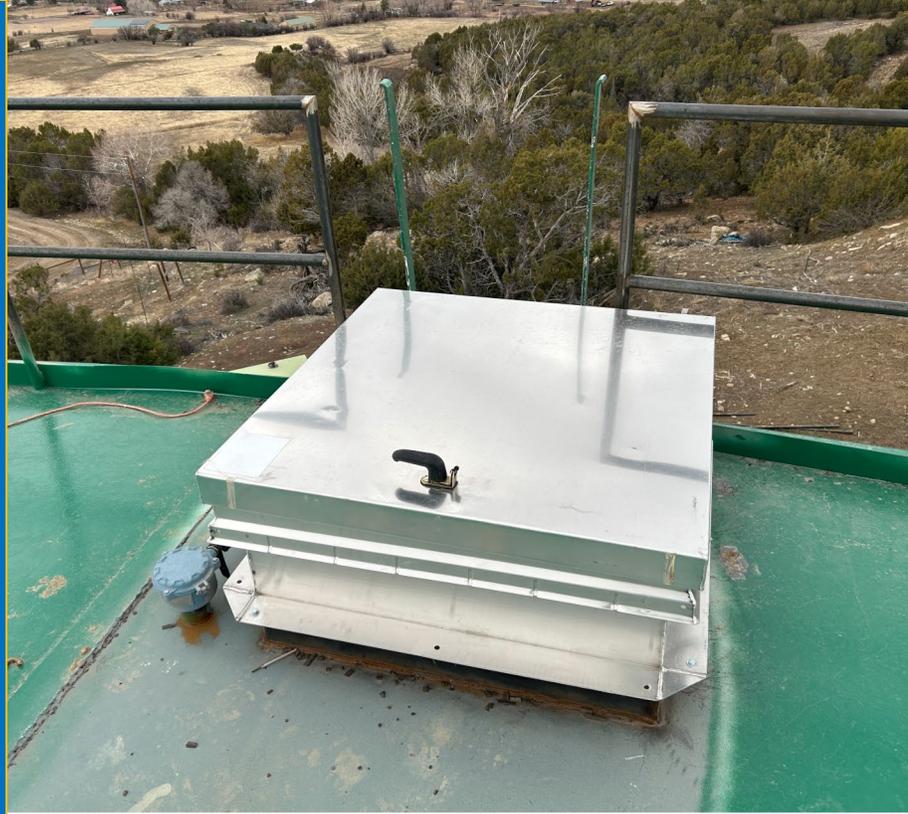




**1st Quarter
2026
Town Administrator's
Report**



**Paonia's Financial
Condition**

**Grants,
Reimbursements,
Capital Project
Accounting &
Water Operations**

**5th & Grand
Realignment; 2MG
Tank Relining
Project Updates**

Paonia’s Financial Condition, Internal Controls, and Audit Status

Clean Audits, Strong Internal Controls, and National Recognition for Budgeting

The Town continues to operate under fund-based legal budgetary control in accordance with Colorado Revised Statutes and the Town’s adopted financial policies. On 9/17/2024, the Town adopted its first ever financial policies for purchasing and codified them in Paonia Municipal Code §4-6-10 through §4-6-90 including the adoption of an official Purchasing Manual.

Annual budgets are adopted by fund, with legal appropriations established independently for the General Fund, Special Revenue Funds, Capital Funds, and Enterprise Funds. A balanced budget is defined as planned expenditures not exceeding available resources within each individual fund, where available resources consist of current year revenues and legally available beginning fund balances. This process is similar to a business that expects revenue to come in based on forecasting and agreements in place for grants and other forms of revenue (accounts receivable), booking revenue into a checkbook as it comes in, and also using previous years surplus revenue (profit in business terms), known as fund balance, to balance the budget.

Throughout the fiscal year, staff performs routine budget to actual monitoring at the fund and departmental level. Variances are reviewed for timing, project phasing, and revenue realization, and corrective action is taken as needed through public budget amendments. Encumbrance accounting is used to ensure that contractual commitments are recognized and tracked against available appropriations, strengthening expenditure control and reducing the risk of over obligation.

At the end of FY-2025, the Town passed Resolution 30-2025, amending the annual budget. The reason that the Town updated the budget was to reduce the amount of revenue that was received, not because of shoddy accounting, but because projects didn’t move as fast as anticipated and expenses weren’t incurred that required drawdowns from State Revolving Fund (low-interest) loans or from reimbursable state and federal grants. The Budget Amendment reduced revenue and expenditures, to align with the reality that projects didn’t incur costs as quickly as planned. Following this process improves transparency.

The Town’s FY-2024 Annual Comprehensive Financial Report (the Audit) received an unmodified audit opinion from the Town’s independent auditors. This opinion confirms that the Town’s financial statements fairly represent, in all material respects, the Town’s financial position, results of operations, and cash flows in accordance with generally accepted accounting principles (GAAP), and with all required Government Accounting Standards Board (GASB) requirements. During the audit presentation provided in calendar year 2025, the auditors also reviewed and affirmed the Town’s budget amendment practices, particularly as they relate to multiyear capital and grant funded projects.

Internal controls over cash handling, disbursements, payroll, and financial reporting continue to be evaluated and refined as part of normal operations. No material weaknesses were identified by the auditors, and management continues to implement best practices appropriate for a small but complex municipal organization with multiple enterprise utilities.

Don’t just take the Town’s word for it, instead you can find all of the Town’s financial information on the Town’s website: www.townofpaonia.colorado.gov.

Budgets: www.townofpaonia.colorado.gov/departments/paonia-budget-financial-information

Audits: <https://townofpaonia.colorado.gov/government/budget-financial-information/town-of-paonia-audits>

Monthly Budget to Actuals: (Started in 2025)
<https://townofpaonia.colorado.gov/departments/budget-financial-information/budget-to-actuals>



GOVERNMENT FINANCE OFFICERS ASSOCIATION

*Distinguished
Budget Presentation
Award*

PRESENTED TO

**Town of Paonia
Colorado**

For the Fiscal Year Beginning
January 01, 2025

Christopher P. Morill
Executive Director

Grants, Reimbursements, Capital Project Accounting, and Water Utility Operations

12 Grants Totaling Approximately \$6.5MM, How Paonia Budgets for Capital Projects, and Water Utility Operations and System Reliability

The Town actively manages a portfolio of twelve state and federal grants supporting transportation, water, wastewater, and planning initiatives. All grant revenues included in the budget are supported by executed grant award letters or agreements. The Town does not budget speculative grant revenue. This means that every grant listed in revenue items in either the General Fund or a Capital Outlay Fund has an active grant agreement and award letter. Simply put, the Town doesn't budget for grants that we *might* get, rather they're available for the Town to receive after meeting the disbursement conditions of the grant agreement.

For governmental funds, grant accounting follows the modified accrual basis. Expenditures are incurred first for eligible project costs, reimbursement requests are submitted in accordance with grant agreements, and revenue is recognized only when reimbursement is received or is both measurable and available. This approach ensures that revenues reflected in the financial statements correspond to actual, compliant expenditures.

When grant funded projects extend beyond a single fiscal year, staff brings forward budget amendments to reduce both budgeted revenues and expenditures for the uncompleted portion of the project. This practice prevents the artificial inflation of budget totals and aligns appropriations with realistic project timelines. This approach was specifically recommended by the Town's independent auditors during the FY-2024 Audit (as reported in 2025) and is reflected in the FY-2025 Budget Amendment adopted by the Board. The Town is actively improving its reporting processes through guidance from the Independent Auditors.

Capital projects are tracked by fund and by project, allowing staff to monitor remaining appropriations, grant reimbursement status, and cash flow impacts. This project level tracking supports compliance with grant requirements, Buy America and other federal provisions where applicable, and long-range capital planning.

Water Utility Operations and System Reliability

Paonia's municipal water supply is derived from a series of mountain spring complexes located on Mount Lamborn and surrounding drainages. Following the 2019 system failure that resulted in a 23-day service interruption, the Town adopted a moratorium on new water taps until it could better understand system performance, address infrastructure deficiencies, and confirm long term reliability.

The Hydrogeological Investigation completed in October 2025 significantly advanced that understanding. The study determined that existing spring sources likely provide more physical water than is currently being captured, particularly during peak snowmelt and runoff periods. The primary constraints identified were not source depletion, but infrastructure limitations, bypass of high flows at collection structures, and measurable losses between spring sources and the Upper Water Treatment Plant.

To Review the redacted version of the Hydrogeological Study, click here: www.townofpaonia.colorado.gov/capital-improvement-projects

Specifically, the investigation documented that existing spring collection boxes routinely bypass excess runoff due to limited pipeline capacity and the absence of optimized raw water capture infrastructure. It also identified discrepancies between measured spring discharge and plant inflows,

indicating transit losses, operational inefficiencies, or measurement limitations that require correction. In practical terms, available water is not fully reaching the treatment facility.

Current priority actions therefore focus on installation and refinement of raw water metering at key spring collection points, improved quantification of conveyance losses, evaluation of collection structure upgrades, and targeted infrastructure improvements designed to increase effective capture and delivery of existing supply. These steps are intended to establish a defensible firm yield based on measured performance rather than assumption.

Raw Water Storage

With respect to raw water storage, staff continues to evaluate strategies appropriate to Paonia’s system configuration. The hydrogeological investigation does not identify construction of a traditional surface reservoir as a prerequisite to system reliability or to lifting the tap moratorium. Instead, the study supports first optimizing capture, conveyance, and data collection to determine the magnitude and timing of recoverable supply. Storage options under consideration therefore include right sized raw water storage at or near the treatment plant, operational equalization strategies, and other alternatives that align with measured demand, regulatory requirements, and cost benefit analysis.

The water tap moratorium remains in place as a structured risk management tool while these improvements and analyses are completed. Any recommendation to lift or modify the moratorium will be based on demonstrated system reliability, verified firm yield derived from measured data, and consistency with the adopted Capital Improvement Plan. The objective is to ensure that future growth decisions are grounded in engineering evidence and operational readiness rather than speculative infrastructure expansion.

Planning, Housing Policy, and Code Implementation

Work continues to implement the Paonia Comprehensive Plan and the Housing Needs Assessment and Housing Action Plan adopted by the Board in 2025 and 2023 respectively. Staff is coordinating land use planning with infrastructure capacity, particularly water and wastewater utilities, to ensure that regulatory updates support both housing availability and long-term system sustainability.

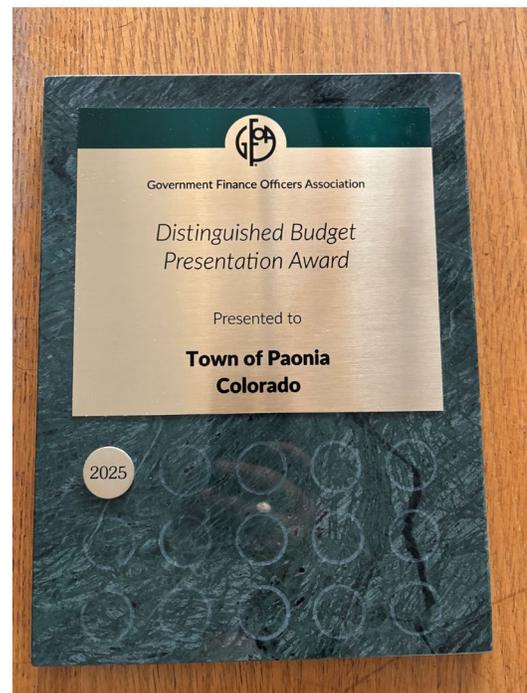
Priority implementation items include clarification of accessory dwelling unit standards, including water tap requirements and fee structures, and development of enforceable short term rental regulations consistent with the Housing Action Plan. These efforts are intended to balance housing needs, neighborhood character, and infrastructure capacity while providing clear and predictable rules for property owners.

Staff will continue to bring forward policy recommendations, code amendments, and implementation updates for Board consideration as this work progresses.

Outlook and Forward Planning

The Town remains focused on strengthening financial resilience, improving utility system performance, and advancing adopted community plans through disciplined implementation. Ongoing priorities include maintaining adequate fund balances, managing grant funded capital investments responsibly, improving infrastructure data and monitoring, and ensuring transparency in public reporting.

Quarterly reporting will continue to provide the Board and the public with updates on financial condition, major capital projects, grant activity, and implementation progress tied to adopted plans.





5th and Grand Realignment Update

Awaiting FHWA Central Office Review in D.C. Since 12/19/2025

Work may be delayed until 2027

Executive Summary

The 5th Street and Grand Avenue Realignment Project has reached full project readiness from a local and state perspective. Design is complete, right of way has been acquired, and state funding sources through the Revitalizing Main Streets (RMS) and Safe Routes to School (SRTS) programs have been secured.

The project is currently delayed at the federal level pending execution of the BUILD Grant Agreement by the Federal Highway Administration (FHWA) central office. While the Town finalized and transmitted the draft agreement in November 2025, and the FHWA local office transmitted the agreement to their central office on December 19, 2025, the agreement remains under federal review with no timeline for execution.

As a result, the project may be bid in 2026, but construction may not begin until 2027 depending on federal action.

Project Overview and Current Status

The project consists of a full reconstruction and realignment of the 5th Street and Grand Avenue intersection, including pedestrian safety improvements, roadway reconstruction, stormwater and utility upgrades, and ADA compliant infrastructure. The project is a critical safety and infrastructure investment aligned with the Town’s Comprehensive Plan goals related to mobility, downtown vitality, and safe routes to school.

All engineering, design, and preconstruction activities have been completed. The Town has advanced the project to a fully construction ready status, including completion of geotechnical analysis, utility coordination, and final plans and specifications. All required right of way has been successfully acquired, and necessary certifications have been completed in coordination with CDOT and FHWA processes.

Funding

The total project funding, inclusive of all sources and previously incurred costs, is **\$3,360,279.88**.

Funding Breakdown

Federal Funding

- BUILD Grant (FHWA): **\$1,884,901.00**

State Funding (CDOT Programs)

- Revitalizing Main Streets (RMS) and Safe Routes to School (SRTS): **\$1,241,721.00**

Local Match and Previously Incurred Costs (Town of Paonia)

- Required Local Match (RMS): **\$30,182.00**
- Previously Incurred Design and Engineering Costs: **\$203,475.88**

Total by Category

- Total Federal Funding: **\$1,884,901.00**
- Total State Funding: **\$1,241,721.00**
- Total Town Contribution: **\$233,657.88**
- Total Project Cost: **\$3,360,279.88**

Federal Grant Agreement Status

The BUILD Grant Agreement is currently under review by FHWA headquarters. The review process has progressed through:

- Program Office review
- Budget review (HACG 30)
- Pending review by Office of Chief Counsel, Office of the Secretary, and Office of Cooperative Agreements and Non-State Grants Awards



As of February 2026, FHWA has indicated that no updates are available and the agreement remains under review at headquarters.

The Town has:

- Completed all required documentation
- Responded to all federal comments
- Finalized and transmitted the draft agreement in November 2025
- Ensured compliance with all grant requirements in a timely manner

There are no outstanding actions required from the Town at this time.

Schedule Update

The previously anticipated construction schedule has been impacted by federal delays.

Updated Status:

- Design: Complete
- Right of Way: Complete
- State Funding: Secured
- Federal Agreement: Pending execution
- Bid Advertisement: Pending Federal Notice to Proceed

Revised Outlook:

- Advertisement for construction: Dependent on FHWA execution
- Bid timing: Potentially late 2026
- Construction start: Likely 2027 if federal approval is not received in time

While the original schedule anticipated a 2026 construction season, the inability to obligate federal funds prevents the Town from advertising the project under federal requirements.

Key Issue and Implications

The project is currently at a **federal administrative standstill**. Despite full local and state readiness, the Town cannot:

- Advertise the project for construction
- Obligate federal funds
- Execute construction contracts utilizing BUILD funding

This delay is not related to project readiness, compliance, or performance by the Town. Rather, it is the result of extended federal review timelines, including impacts from federal level disruptions and processing delays.

Cost Escalation Risk

Delays increase exposure to construction cost inflation, which has already been reflected in updated project estimates. The Town anticipated this as a worst-case scenario and built in inflation and cost escalation into the FHWA grant agreement to maintain the Town’s required local match of \$30,182.00.

Seasonal Construction Constraints

Missing the 2026 construction window would push the project into the 2027 construction season, extending community disruption and delaying safety improvements.

Grant Coordination Complexity

The project requires coordination between multiple funding sources. Continued delay increases administrative complexity and risk of misalignment between funding timelines.

Next Steps

Staff will continue direct coordination with FHWA and CDOT to monitor the status of the grant agreement and request timeline updates where available. The Town has completed all required actions and remains fully prepared to execute the agreement immediately upon federal approval, ensuring no delay on the local side once authorization is received.

At the same time, staff will maintain procurement readiness by finalizing bid documents and preparing all materials necessary to advertise the project as soon as federal authorization is granted. This ensures the Town can move efficiently into construction and minimize any additional delays tied to administrative processes.

Staff will also evaluate contingency scenarios based on the timing of FHWA action, including the feasibility of late season 2026 bidding with deferred construction or a full transition to the 2027 construction season. Throughout this process, staff will continue to provide clear communication to the Board and the public, emphasizing project readiness, the federal source of delay, and any necessary adjustments to the project timeline.

5th & Grand Realignment Project Funding Overview

Total Project Cost: **\$3,360,279.88**
Project is fully funded through federal, state, and local sources.

Funding Source	Amount	Percent
Federal (BUILD)	\$1,884,901	56.1%
State (RMS + SRTS)	\$1,241,721	37.0%
Town Match (RMS)	\$30,182.00	0.9%
Town Incurred (Design/Engineering)	\$203,475.88	6.0%
Total	\$3,360,279.88	100%

Key Message: The Town's total contribution of \$233,657.88 (6.9%) includes both required match and previously incurred design costs, leveraging over 93% of project funding from state and federal sources.

2MG Finished Water Tank Relining Project

Work is progressing with crews remobilized on site

The entire project remains under original estimated budget although factors could increase costs

Summary of Work

Work on the 2MG Tank Relining Project has resumed following winter conditions and remobilization of the contractor. Current efforts are focused on structural steel rehabilitation, surface preparation, and continued interior and exterior coating work. The contractor is actively completing weld repairs, addressing deficiencies identified during abrasive blasting, and advancing remaining structural components including rafters, clips, and associated connections. These activities are necessary to ensure the integrity of the tank prior to final coating application and are typical of rehabilitation projects where additional deficiencies are revealed once existing coatings are removed.

As part of this phase of work, several field conditions have been identified that require modification to the original scope. These include relocation of the roof access hatch to meet safety and access requirements, repair of roof pinholes and pitting uncovered during blasting, and the potential need for additional rafter bolt replacement beyond the quantities originally anticipated. These items are under active coordination between the contractor, engineer, and staff, and will likely result in additional change orders as final quantities and costs are confirmed.

Previously approved change orders include standby and delay costs associated with late availability of the temporary water storage system, as well as access road improvements necessary to support construction access to the tank site. These adjustments reflect the realities of sequencing a project of this complexity while maintaining uninterrupted water service to the community. The project continues to progress, but remains in a phase where final quantities and conditions are still being confirmed, which is the primary driver of potential cost variability moving forward.

Financial Status & Budget Analysis

The Engineer's Preliminary Opinion of Construction Cost for the project was **\$2,181,300**, with a total project cost including engineering and inspection estimated at **\$2,301,300**.

Costs to Date by Major Component

MPC (Tank Rehabilitation Construction) The original construction contract was **\$916,250**, with approved change orders totaling approximately **\$59,895**, resulting in a current contract value of **\$976,146**.

Payments to date total **\$638,997.80**, leaving **\$337,148.20** remaining under the current contract.

KLM Engineering (Construction Inspection) The inspection services contract was originally **\$97,860**, with an approved change order of **\$32,935** for additional inspection time, resulting in a revised not to exceed amount of **\$130,795**.

Payments to date total **\$87,981**, leaving **\$42,814** remaining.

Viaflex (Temporary Water Storage System) The temporary tank system, necessary to maintain water service during construction, has incurred **\$320,248** in costs to date.

This exceeds the engineer's preliminary estimate of **\$300,000**, and costs will continue to accrue until the permanent tank is returned to service.

Sitework and Access (Earthwork and Subcontracted Work) Sitework and related construction support activities total approximately **\$373,703.28** to date.

An additional **\$15,000** has been added through Change Order No. 2 for access road improvements, bringing total site-related costs to approximately **\$388,703.28**.

Total Financial Position

- **Total Costs Incurred to Date:** approximately **\$1,420,930**
- **Remaining Obligated Under Existing Contracts:** approximately **\$379,962**
- **Projected Total Based on Current Known Commitments:** approximately **\$1,800,892**

Budget Comparison and Risk Assessment

At this stage, the project remains **within the Engineer's estimated construction budget of \$2,181,300**, with an approximate remaining margin of **\$380,000** based on current commitments.

However, that margin is actively narrowing due to several factors inherent to the current phase of work:

The project has entered the most variable portion of construction, where unknown conditions are being identified during blasting and structural exposure. This has already resulted in additional scope items and will likely continue to do so as work progresses.

The temporary water system has exceeded initial estimates and continues to generate ongoing costs, directly impacting the overall project budget.

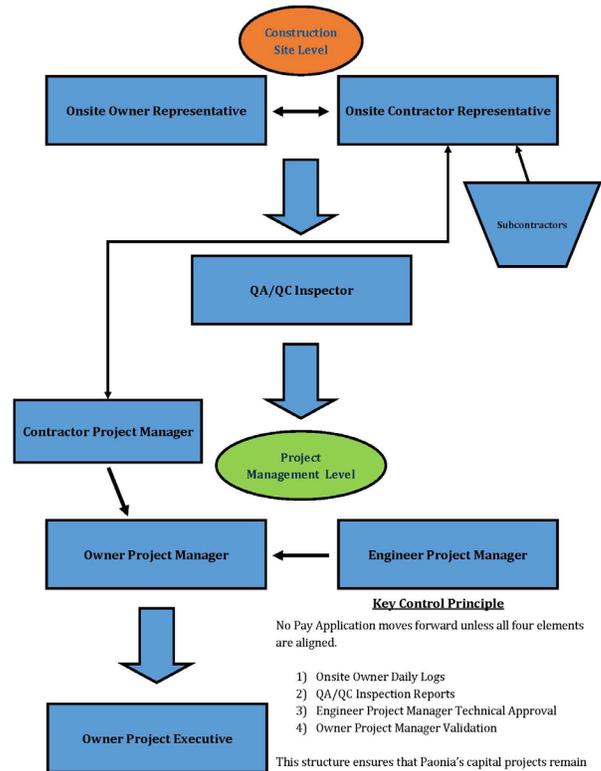
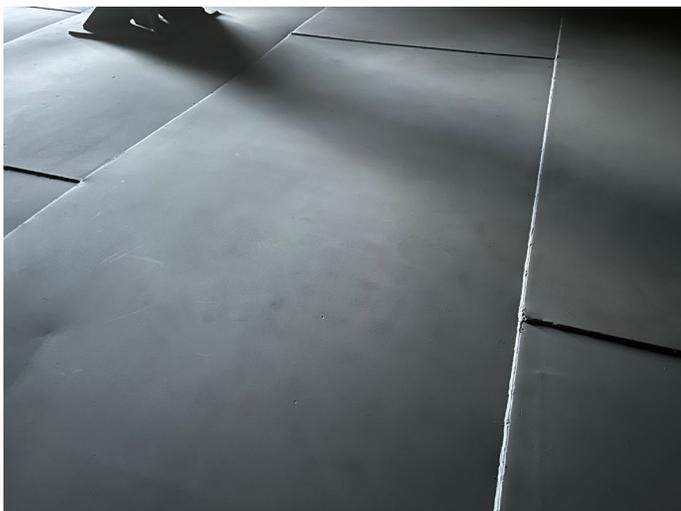
Pending change orders related to structural repairs, roof modifications, and material quantities have not yet been fully priced, but are expected to increase the total construction cost.

Conclusion on Budget Position

Based on current trends, the project is tracking within the overall construction budget, but is expected to move closer to the engineer's estimated cost as remaining work is completed and change orders are finalized. At this time, there is no indication that the project will exceed the total budget; however, the remaining contingency should be considered actively at risk and managed accordingly.

Next Steps

Staff will continue to work directly with the engineer and contractor to finalize pending change orders, monitor remaining contract balances, and track total project costs against the established budget. Additional updates will be provided as costs are formalized and as the project advances toward completion and return of the tank to service.



This structure ensures that Paonia's capital projects remain fully compliant and defensible under audit conditions and resilient against contractor disputes.



1st Quarter Department Head Meeting Updates

The Department Head meetings conducted throughout the first quarter of 2026 reflect a continued emphasis on operational stability, organizational alignment, and the implementation of systems that support long-term municipal performance. Across the January 27th, February 10th, and February 24th meetings, staff demonstrated consistent progress in formalizing internal processes, improving interdepartmental coordination, and advancing key administrative initiatives. Foundational efforts included refinement of the Capital Improvement Plan, updates to hiring and personnel procedures, and the continued transition toward centralized systems such as Laserfiche and improved IT infrastructure. These efforts are indicative of a broader organizational focus on accountability, documentation, and sustainability in service delivery.

Operationally, the Town has made measurable progress in strengthening core service areas, including utilities, public works, and public safety. Discussions throughout the quarter reflect active management of staffing levels, onboarding of new personnel, and alignment of resources to meet service demands. Utility operations continue to evolve through enhancements to billing processes, meter management, and system oversight, while public works operations have focused on service delivery adjustments such as yard waste collection and infrastructure coordination. In parallel, the organization has advanced technology improvements, including new phone systems, device replacements, and network upgrades, all of which support more efficient and reliable municipal operations.

The meetings also highlight a proactive approach to governance, compliance, and community facing services. Key initiatives include preparation for the 2026 municipal election, continued development of facility management frameworks, and updates to building permit and code enforcement processes. Community related efforts, such as the trash can standardization rollout and coordination for upcoming events, are being approached with an emphasis on clear communication and structured implementation, including a scheduled pre-event meeting for the Arbol Farmers Market. Collectively, the 1st quarter meetings demonstrate a disciplined and forward-looking administrative approach, balancing immediate operational needs with the establishment of systems and policies that will support the Town's long-term effectiveness and public service mission.

Ellen Hansen Smith Center

A significant focus during the quarter has been the evaluation and transition planning for the Ellen Hansen Smith Center. Discussions identified the need to formalize governance, operational control, and financial transparency associated with the facility. Staff has taken steps to re-

establish clear Town oversight, including securing access control through re keying, limiting distribution of keys, and ensuring that use of the facility aligns with established municipal authority. In addition, the building is currently undergoing assessment and improvement efforts to address safety and code compliance items, including life safety systems, accessibility requirements, and necessary mechanical and structural repairs.

Moving forward, staff is developing a formal operational and legal framework for the Ellen Hansen Smith Center to ensure that its use is consistent with Town policies, public accountability standards, and long-term community benefit. This includes establishing clear agreements for facility use, defining rental or programming structures, and aligning the center with broader parks and recreation and community services goals. These efforts are intended to transition the facility into a transparent, well-managed public asset that supports community programming while protecting the Town's financial and legal interests.

