

COMPREHENSIVE FINANCIAL ADVISORY COMMITTEE (CFAC)

CFAC Report: Fiscal Policy Reevaluation

For

FY 2022

Committee Members

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July 16, 2020

CFAC provides financial advice to the Town Council on the yearly operating and capital budgets for all town agencies, including the school department budget adopted by the School Committee. The advisory responsibilities of CFAC are found in The Administrative Code of the Town of Barnstable, Chapter 241, Section 18 and Section III, Paragraphs A-C.

INTRODUCTION

In accordance with the Town of Barnstable Charter, Part VI, Section 6-2 and Chapter 241-18 of the Administrative Code, the Comprehensive Financial Advisory Committee (CFAC) submits its review, comments, and recommendations for the proposed FY21 Operating Budget to the Town Manager and Town Council.

CFAC's advisory responsibilities do not include evaluation of fiscal policy. Fiscal policy is the responsibility of the Town Council and Town Administration. However, both Town Council President Paul Hebert and Town Manager Mark Ells approved CFAC's request to discuss and forward its comments and recommendations on the Town of Barnstable's re-evaluation of its fiscal policy for FY22.

CFAC extends its appreciation to President Paul Hebert, Manager Mark Ells, and Finance Director Mark Milne for the confidence they have in our committee's experience and familiarity with the budget process to submit comments and ideas on fiscal policy.

METHODOLOGY

CFAC Councilor Liaison Paula Schnepf informed CFAC that the Council would hold its strategic planning meeting in September 2020. She outlined the Council's expectations of CFAC's analysis and recommendations that will serve as part of the Council's resources. In this report, CFAC addresses those expectations.

The proposed strategic planning for FY22 includes a re-evaluation of a number of fiscal policies:

- Resources dedicated to capital program and operations
- Review of designation of specific revenues
- Review of allocations within General Fund operations
- Review Enterprise Fund subsidy policy
- Review indirect cost model for Enterprise Funds
- Review cost of service recovery policy
- Implement new or revised fees
- Review tax levy policy
- Review CWMP financing

Town Finance Director Mark Milne provided financial updates, background information, and the post Covid-19 budget process to assist CFAC's discussion of each of the fiscal policies designated for review.

As in its past reviews of the Town Capital Improvement Budget and the Town Operating Budget, CFAC submits this report to provide the Council and Administration with an independent assessment and recommendations. CFAC's report represents thorough discussion and input from all its members and approved for transmittal to the Town Manager and Town Council.

OVERVIEW

The serious economic effect of COVID-19 on town finances and the rapid and successful response of Town administration and Council leadership to revise revenue projections and resource allocations for FY21 produced both a revised budget that addressed immediate fiscal challenges and an opportunity to evaluate new approaches and modifications to existing fiscal policy and the processes to guide budget formation.

While the response to the economic shutdown has been timely, appropriate, and effective, it may not be the final chapter. Recovery is highly uncertain and may be subject to a sustained low level of economic activity. The Federal Reserve has predicted that the economy may take years to rebound, despite near zero interest rates and the Fed's quantitative easing bond buying and Main Street programs. In addition, the prognosis about COVID-19's resurgence remains unknown.

By re-evaluating its fiscal policy, the Town of Barnstable is taking steps to ensure that Town finances are not permanently scarred by the economy. An objective review of its economic and financial framework underscores the Town's commitment to a fiscal policy that strengthens the stability of its revenue and expenditures and its ability to respond to economic downturns.

FISCAL POLICY

Fiscal policy is directly governed by the Town Council. It is influenced by the goals and priorities established by Town Council to improve the quality of life in the Town of Barnstable. Toward that end, the Council has set a fiscal policy, which includes revenue, expenditures, and debt, to stabilize its financial framework to achieve its long-term objectives of budget sustainability, capacity to meet future needs and increase the potential for growth through investments in infrastructure and education.

The current Barnstable policy of fiscal accountability is based on sound financial management through balanced budgets, adequate reserves, stability of the tax base, and minimum government debt. The strengths of the current fiscal policy have provided sufficient revenue to fund both essential needs and expansion of programs and services. The re-evaluation of fiscal policy for FY22 seeks solutions to speed budget recovery without sacrificing support for the essential services and programs that define Barnstable's quality of life.

REVENUE

The revenue sources for the Town of Barnstable are more reliable and constant than those of other jurisdictions that depend on income and general sales taxes, which fluctuate with the economic circumstances. Property and excise taxes form the basis of Barnstable's revenue and provide 78% of the funding for the General Fund. Other sources of General Fund revenue include intergovernmental aid, fines, and penalties, fees, licenses, permits, interest, charges for services, special revenue funds, interest, Enterprise Funds, Trust Funds, and reserves.

In addition, Proposition 2 ½, which allows a statutory increase in property tax annually, guarantees an automatic increase in revenue. This revenue stability, along with new property growth, has given Barnstable the ability to fund its ongoing services and programs, expand, and/or initiate new services and programs, undertake capital improvement projects, and generate cash reserves.

This healthy and steady revenue has earned Barnstable an AAA bond rating and enabled the Town to issue bonds at very favorable interest rates.

The complex and unpredictable economy that is emerging from the unprecedented and precipitous lockdown of both citizens and economic activity presents both a challenge and an opportunity to discuss and consider changes to the conventional public revenue paradigm.

CFAC submits the following revenue suggestions for fiscal policy re-evaluation:

Designation of specific revenues

Many taxes and fees have been sources of revenue for specific departments and programs. For example, the beach revenue has traditionally been given to the Community Services Recreation; motor vehicle excise tax goes to Department of Public Works which repairs and maintains roads; and the rooms and meals tax funds the CWMP. On the other hand, CH70 funds become part of the General Fund.

The issue for consideration: should fees continue to be designated to their specific areas of service, or should fees become part of the General Fund and appropriated to specific departments and Enterprise Funds as part of the budget?

Should existing fees remain the same or increased based on increased costs to administer the services and the increase consumer price index? For example, is a small increase in transfer station fees-solid waste and recycling- appropriate to cover the increased costs of this operation? Is an increase in the Marine Enterprise Fund slip waiting fee, which currently is very low, a possibility? While fees and permits are not a major revenue source, their combined impact may increase total revenue and may decrease General Fund support of specific programs.

National reports indicate that the reopening of the economy has been uneven. It appears that tax revenue from food, beverages, and rooms will be hit hard. This will have an impact on Town revenue, but this income represents a relatively small amount overall. The increase in excise taxes and assessments could easily compensate for any shortfalls in the other amounts.

What new taxes or fees might be possible without legislative approval? For example:

- An environmental protection fee/ tax per diem at hotels/motels. Many cities have a hotel resort/day tax to pay for environmental protection and city infrastructure. These fees range from \$3.50/day in New York City to 3% /day in Miami to \$25/day in Honolulu. Boston hotels have a convention fee added to their daily room rates. This fee would help pay for CWMP or repair/maintenance of the water system.
- Tax on non-carbonated beverages, plastic bottles. This tax would raise revenue and decrease littering.

Tax levy policy

Property tax levy increases are limited by Proposition 2 ½. Through prudent budget management, Barnstable has consistently had an annual override capacity of more than \$200 million.

This capacity demonstrates Barnstable's steady ability to balance its budget without overrides. The override has seldom been used in Barnstable. The last referendum for an override was to fund Barnstable's portion of the newly constructed Regional Technical High School.

In the event that Barnstable's budget for programs and services exceeds its projected revenue, the Town may elect to use either its override or debt exclusion option. Both require voter approval through a referendum. Both the override and debt exclusion options provide mechanisms to finance CWMP, for example. The debt exclusion would allow an increased tax levy for CWMP for a specific period of time to cover the cost of the project and would not become part of the tax base. The override, on the other hand, results in a permanent increase of the levy limit of 2 1/2% each year. The key consideration in overrides and debt exclusions is its impact on property owner tax liability and the effects that an increased tax burden may have on economic development and quality of life.

Revenue to fund CWMP

Because CWMP's projected costs exceed \$1 billion over the next thirty years; Town Council faces the daunting challenge of putting together a combination of funding sources to enable this project to proceed. The existing specified funds include the hotel and meals tax and the short-term rental tax. Discussions and analysis of the viability of some other revenue sources include the Capital Trust Fund, the new stabilization fund created by the C & I 2.75% tax, property tax contributions, and assessments. The Proposition 2 1/2 override and debt exclusion are also options. In addition, the Federal Reserve Bank has recently included municipal bonds in its \$4 trillion pandemic economic assistance and may be a source worth exploring.

Revenue to fund private road maintenance

The costs of installing new sewers and possibly new drinking water pipes and utility lines along private roads raises the issue of management of the estimated 1,100 private roads in the Town of Barnstable. If a private road, meets certain criteria, its maintenance can be financed through Sewer Construction and Private Way Maintenance funds. However, as sewer infrastructure and installation progress, funds may not be sufficient. CFAC suggests that Town Council develop a new funding plan for construction and subsequent maintenance of private roads.

Capital Trust Fund

Long term projects like CWMP, wastewater management treatment, and private roads are important for health and safety in Barnstable. CFAC suggests the addition of revenue from all new growth from taxes on properties over \$1 million to the Capital Trust Fund. This will increase the capacity of the CTF to fund these projects as well as others. CFAC recommends increasing the CTF by 1-2% annually.

EXPENSES

The financial upheaval and revenue disruption caused by the pandemic required revision of the FY21 budget that freezes hiring, reduces discretionary spending, and defers capital projects. The revised budget is a remarkable achievement that reflects the experience and commitment of Town Administration and Town Council to ensure that health, safety, education, and other critical needs and programs have appropriate funding to continue operations.

Capital Improvement and Operations

Evaluation of proposed capital improvement projects through the two step process created in 2018 has streamlined the method of evaluating proposed capital improvement projects. Ranking projects in descending order from "must do" to "nice to do" has resulted in sending a list of highest-ranking projects to the Town Manager for his evaluation and approval.

CFAC reviews the CIP budget each year and has recommended that certain recurring projects be shifted from the capital budget to the operating budget. It has been the view of CFAC that capital outlays that are used to maintain current capacities or town assets should be included in the operating costs of the Town. For example, painting, replacement parts or replacement equipment repaving of parking lots, and floor repairs are recurring costs that are often included in the capital budget each year. CFAC has often recommended a deferred maintenance plan for Town properties and equipment.

CFAC suggests that Town Council discuss the issue of these recurring maintenance and replacements that are proposed as capital expenditures. Should there be a separate category of expense in the operating budget rather than repeated requests for capital outlay?

With tight budget constraints for the next few years, how much and what kind of capital expenditures would be the most prudent use of Town funds? Should more Town funds be used for the operating budget to ensure that the services and departments have the capability to meet the needs of residents? The re-evaluation of fiscal policy for FY22 should include consideration of the municipal operations and the allocation of resources. Perhaps the General Fund budget process could adopt the capital improvement process of priority ranking from “must have” in descending order to “nice to have”.

The revised FY21 budget shows clearly that proposed categories that were not “must have” were halted or deferred, and only top priority expenditures were included in the budget. Perhaps the success of this process can be helpful as Barnstable deals with its recovery strategy. Budget recovery strategy proposals include reduction of personnel costs, reduction of material, utility and contractor costs, and reduction of capital spending.

Five Year Plan addition to the Capital Plan

The FY21-25 Five Year Plan for capital projects includes \$100 million for approximately 121 sewer projects. This plan represents 40% increase over the FY20-24 Plan and reflects the Town's commitment to implementation of its Comprehensive Waste Management Plan (CWMP).

As a result of the COVID-19 economic impact, CFAC suggests that the fiscal re-evaluation process for FY22 include a review of all assumptions of the FY21 Five Year Plan to determine if any changes need to be made.

Comprehensive Wastewater Management Plan

At the request of the Town Manager, several CFAC members served as liaisons to the Water Resources Advisory Committee (WRAC) from the spring of 2016 to the summer of 2017. The thorough studies of water quality in the groundwater, ponds, rivers, failing septic systems, new flood zones, and watersheds and embayment impairments resulted in a revised CWMP plan that was submitted to MassDEP for review and approval.

CFAC's involvement with the WRAC deliberations and WRAC's finance subcommittee provided CFAC with the perspective of the scope, cost, and, most importantly, the importance of proceeding as expeditiously as possible with CWMP projects. In its review of Capital Improvement Projects during the last few years, CFAC has expressed its willingness and interest to provide input about financing of CWMP. CFAC remains available to provide input while the updated CWMP is being developed, if Town Administration and Town Council feel we can be helpful.

Progress of CWMP could be hindered by the COVID-19 economic shutdown and the uncertainty of projected 1% revenue growth from the rooms and meals taxes, which are specifically designated to fund the sewer construction.

CWMP is an enormously expensive project and should remain a top priority for funding in the budget. It is impossible to raise parking fees, greens fees, transfer station fees, ice skating fees, water rates, or the price of any other permit/sticker/stamp to significantly impact revenue growth. CFAC urges Town Council to take a hard look at all Town expenses and consider restructuring everything – including getting rid of the sacred cow of Fire Districts

Everyone agrees that Barnstable's environment affects not only the quality of life for residents but also its attraction for visitors. Updates of infrastructure and maintenance of drinking water, sewers, roads, and pristine beaches are imperative, if Barnstable hopes to maintain its level of vacationers who currently provide 40% of the Cape Cod economy.

Enterprise Funds

Enterprise Funds are intended to be financially self-supporting at the same time that they enhance the quality of life for both residents and visitors.

Temporary subsidies of some Enterprise Funds have been used occasionally, when they were needed. Based on its quality of life strategy plan, Town Council should determine the level and frequency of subsidizing specific Enterprise Funds as well as their level of indirect costs.

School Funds

The school/General Fund allocation for operations ratio has traditionally been 60/40.

CFAC recommends options that would change the present ratio:

- Ratio of Operating Budget to Schools based on enrollment: The ratio could be based on the increase or decrease in enrollment of students.
- Ratio of Operating Budget to Schools based on the size of the General Fund budget: As the percentage of Town revenue increases through tax levies and new growth, expected school expenses may not increase at the same rate. As a result, the school/ GF budget ratio would decrease accordingly. This decrease in education appropriation as a percentage of an increased operating budget has a long history across the United States. For example, when state annual budgets were in the \$4-8 billion range in the 1980's, education (K-12, community colleges, and higher education) received an average of 50% of total appropriations. In the recent past, when most state annual budgets are in the \$40-80 billion range, total education appropriations are now 30%. The FY19 MA state budget appropriated 22.9% (\$15.6 billion) to education; CT appropriated 24%, or \$18.96 billion. NH appropriated 27.9%, or \$15.34 billion. The national average was 29.9%.
- CFAC also suggests consideration of the establishment of a second school budget fund with the CH70 revenue, which currently goes into the General Fund.

Department Funds

To build a rainy day fund for department operations, CFAC suggests a 2% budget decrease in each department to be placed in a reserve fund for use during slowdowns in the economy and decreases in Town revenue.

SUMMARY

While Town Council's re-evaluation its fiscal policy focuses on FY22, CFAC recommends regular re-evaluations going forward. Two important factors influence this recommendation: NIH and CDC warnings that the virus caseload and infection rate are far from over and may have a resurgence; the Federal Reserve prediction that it may take years for the economy to recover.

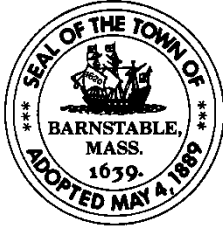
CFAC urges the Town to remain flexible and fluid as it responds to the needs of residents and businesses. Prudent use of the emergency funds and grants, like Mass Ideas, will allow the Town to adapt to new situations with innovative approaches and solutions.

Most recently, the Town has demonstrated its ability to solve problems with new solutions. One example of the Town's nimble response is the closing of one lane of Main Street in Hyannis to help businesses and restaurants to operate while social distancing advisories remain in place. Another example is the presence of a special police presence at the beaches to ensure that social distancing and crowd size are observed. These decisions and actions indicate Barnstable's adaptive responses that protect safety and health and help businesses to survive.

CFAC encourages the Town to continue its innovative approach to both fiscal policy and responses to unprecedented situations.

CFAC appreciates the opportunity to provide Town Administration and Town Council with its independent assessment of Town fiscal policy. CFAC hopes that its review of the scope of both revenue and expenses and suggested areas for consideration will be helpful when Town fiscal policy is re-evaluated for FY22. We extend our willingness to help in this process, if Town Administration and Town Council feel it would be beneficial.

As always, CFAC extends its appreciation to Mark Milne, Town Finance Director, and Nathan Empey, Finance/Budget Analyst, for providing information, insights, and assistance in this effort.



Town of Barnstable

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MEMORANDUM

To: Mark Ells, Town Manager
From: Mark Milne, Director of Finance
Date: July 13, 2020
Subject: Fiscal Year 2020 Budget Close

The following summarizes the budget performance of the Town's General Fund and Enterprise Fund operations for the fiscal year ending June 30, 2020. These numbers may change slightly when all final year end reconciliations are completed, however, no significant changes are anticipated.

Fiscal Year 2020 General Fund Revenue:

CATEGORY	BUDGET	ACTUAL	VARIANCE	% COLL
FY20 PROPERTY TAXES	\$ 127,255,503	\$ 122,572,500	\$ (4,683,003)	96.3%
PRIOR YEARS PROPERTY TAXES	-	5,095,808	5,095,808	
TOTAL PROPERTY TAXES	127,255,503	127,668,308	412,805	100.3%
TOTAL MOTOR VEHICLE EXCISE	7,131,377	8,245,044	1,113,667	115.6%
TOTAL BOAT EXCISE TAX	110,000	147,647	37,647	134.2%
HOTEL/MOTEL TAX	1,950,000	1,950,148	148	100.0%
INTERGOVERNMENTAL	16,527,258	16,750,834	223,576	101.4%
CHARGES FOR SERVICES	2,081,500	2,039,863	(41,637)	98.0%
FEES	886,200	1,012,905	126,705	114.3%
FINES & PENALTIES	1,534,000	1,803,178	269,178	117.5%
LICENSES	556,000	493,112	(62,888)	88.7%
OTHER REVENUE	1,854,678	1,981,267	126,589	106.8%
IN LIEU OF TAX	32,000	34,794	2,794	108.7%
PERMITS	1,644,400	1,847,266	202,866	112.3%
LEASES	152,000	109,449	(42,551)	72.0%
SPECIAL ASSESSMENTS	211,000	234,888	23,888	111.3%
TOTAL GENERAL FUND REVENUE	\$ 161,925,916	\$ 164,318,703	\$ 2,392,787	101.5%

The Town collected 96.3% of the FY20 tax levy within the fiscal year. This is a strong collection rate and consistent with previous years. Additionally, the town collected over \$5 million in back taxes owed.

Motor Vehicle Excise tax came in \$1.1 million higher than the estimate used to balance the FY20 budget. The total collected of \$8.2 million was the highest amount in the Town's history. This revenue category continues to grow as car sales remained strong over the past couple of years before the pandemic hit, and more emphasis has been placed on collection efforts for past due amounts.

Boat excise tax collections were 34% above the estimated amount mainly due to more timely billings and more emphasis on collection efforts.

Rooms taxes came in on target at \$1.95 million. The first two quarters performed very well while the last quarter was down due to the public health emergency.

Intergovernmental Aid (state & federal) came in \$223,000 higher than estimated as the Town received a FEMA reimbursement for storm costs incurred a couple of years ago and additional Charter School aid.

Charges for services revenue was 98% of the estimated amount. Most of this revenue category is made up of beach related revenue.

Fees were 14% above the revenue estimate as the issuance of municipal lien certificates were up and fees associated with the collection of past due taxes.

Fines and Penalty revenue was \$269,000 over the revenue estimate due to more emphasis being placed on the collection of back taxes.

License revenue came in at 89% of the estimate due to a slowdown in the renewal of liquor, entertainment and dog licenses.

The other revenue category is principally composed of investment income and renewable energy revenue. Conservative budget estimates resulted in \$126,000 of excess revenue over the estimated amount.

Permit revenue was very strong prior to the pandemic resulting in this category exceeding the budget estimate by \$203,000.

Lease revenue was down due to the closure of facilities and tenants inability to pay as a result, and conservative estimates result in actual special assessment revenue exceeding the budget by 11%.

Overall, General Fund revenue performed very well and exceeded the budget estimate by 1.5% or \$2.4 million. This will result in an increase in the Town's General Fund reserves or "Free Cash". This should not be interpreted that the pandemic has not impacted the Town's revenue. Town revenue was performing very well prior to the pandemic and economic slowdowns tend to impact the Town in subsequent years mainly through cuts in state aid, reductions in local receipts generated, and a slowdown in tax collection rates.

Fiscal Year 2020 General Fund Expenditures:

DEPARTMENT	BUDGET	ACTUAL	ENCUMBERED	BALANCE	% USED
TOWN COUNCIL	\$ 268,987	\$ 259,247	\$ 8,268	\$ 1,471	99.5%
TOWN MANAGER	769,451	716,913	26,742	25,796	96.6%
ADMINISTRATIVE SERVICES	6,322,843	5,923,228	125,850	273,765	95.7%
PLANNING AND DEVELOPMENT	2,085,304	1,885,657	85,587	114,061	94.5%
POLICE	15,447,848	14,715,763	287,722	444,364	97.1%
LICENSING	165,398	159,136	666	5,597	96.6%
INSPECTIONAL SERVICES	2,140,557	2,018,941	33,613	88,003	95.9%
PUBLIC WORKS	9,230,853	7,700,796	894,748	635,309	93.1%
SNOW & ICE	975,000	432,077	-	542,923	44.3%
MARINE & ENVIRONMENTAL AFFAIRS	1,268,947	1,076,432	69,919	122,596	90.3%
COMMUNITY SERVICES	2,569,427	2,369,009	5,742	194,676	92.4%
SCHOOL	69,802,978	67,868,492	831,295	1,103,191	98.4%
FIXED COSTS	50,467,108	48,928,104	449,232	1,089,771	97.8%
GRAND TOTAL	\$ 161,514,701	\$ 154,053,796	\$ 2,819,384	\$ 4,641,522	97.1%

The Town spent and encumbered 97% of the approved budget for Fiscal Year 2020 resulting in over \$4.6 million in appropriation returns. The closing of schools and a spending freeze contributed to these savings. A mild winter resulted in \$543,000 being returned from the snow & ice budget. A majority of the savings in the fixed costs area were attributable to health insurance expenditures. The unexpended appropriations will result in an increase in the Town's General Fund reserves or "Free Cash". This is intended to position the Town to have multiple options going in to the implementation of the Fiscal Year 2021 budget and the subsequent development of the Fiscal Year 2022 budget.

A portion of the \$1.1 million returned by the School Department may be used to prepay a portion of the FY21 out-of-district residential tuition costs.

The last certification of the Town's General Fund "Free Cash" was \$14.7 million. Of this amount, \$3.1 million was used to supplement the Fiscal Year 2020 budget and balance the Fiscal Year 2021 budget. Approximately \$7 million was generated in Fiscal Year 2020 between excess revenue generated and returned appropriations, resulting in an expected increase of \$4 million in Free Cash. This does not account for any internal borrowings that were necessary at the end of Fiscal Year 2020.

Enterprise Fund Revenue:

ENTERPRISE FUND	BUDGET	ACTUAL	VARIANCE	% COLL
AIRPORT	8,041,243	8,214,286	173,043	102.2%
GOLF	3,493,200	2,867,737	(625,463)	82.1%
SOLID WASTE	3,129,500	2,555,525	(573,975)	81.7%
SEWER	4,816,380	5,243,498	427,118	108.9%
WATER	6,565,015	6,581,448	16,433	100.3%
MARINAS	793,331	732,468	(60,863)	92.3%
SANDY NECK	957,055	847,187	(109,868)	88.5%
HYCC	1,128,102	916,139	(211,963)	81.2%
PEG	838,000	977,471	139,471	116.6%

The Airport Enterprise Fund exceeded its revenue estimate by \$173,000 due to stronger than anticipated fuel sales in May and June as well as the new ground lease at Capetown Plaza.

The golf operations generated only 82% of its revenue estimate due to the closure of the courses and their limited reopening allowed under the public health emergency.

The Solid Waste Enterprise Fund generated 82% of its revenue estimate in Fiscal Year 2020. Transfer station sticker renewals are behind last year's pace. We believe this is due to renewals having to be performed through the mail and on-line due to the pandemic. It is a timing issue and sticker renewals are anticipated to at least match those of the prior year. Through the first week of July \$215,000 of sticker renewals have been collected offsetting the negative variance noted in the above table. The negative variance is expected to be completely offset by the end of July.

The Sewer Enterprise Fund exceeded its revenue estimate by almost 9%. Much of this is attributable to an increase in septage disposal at the plant.

The Water Enterprise Fund came in on target with its revenue estimate.

The Marina Enterprise Fund achieved 92% of its revenue estimate for the year. The shortfall is a result of transient slip fees being significantly down due to the pandemic.

The Sandy Neck Enterprise Fund collected 89% of its revenue estimate for the year. Parking revenue, off-road vehicle sticker sales, and merchandise sales were all down due to the pandemic. Beach closures as a result of nesting birds also contribute to the reduction in off-road vehicles sticker sales.

The HYCC revenue shortfall was \$212,000 due to the closure of the facility.

The excess PEG Enterprise Fund revenue earned was mainly due to a new \$100,000 annual capital payment negotiated as part of the new cable license contract. This occurred after the passage of the FY20 budget.

Enterprise Fund Expenses:

ENTERPRISE FUND	BUDGET	EXPENDED	ENCUMBERED	BALANCE	% USED
AIRPORT	8,242,243	7,093,203	607,307	541,733	93.4%
GOLF	3,876,415	3,504,880	21,300	350,234	91.0%
SOLID WASTE	3,644,883	3,264,516	281,407	98,960	97.3%
SEWER	4,816,380	4,142,233	255,606	418,541	91.3%
WATER	7,685,015	6,727,410	319,285	638,320	91.7%
MARINA	832,780	754,705	3,734	74,341	91.1%
SANDY NECK	996,459	860,119	17,298	119,042	88.1%
HYCC	3,491,132	3,154,101	26,245	310,786	91.1%
PEG	877,860	714,323	80,487	83,050	90.5%

All enterprise fund operations came in under budget. The returned balances can be used to offset the revenue deficits in the Golf, Solid Waste, Marina, Sandy Neck and HYCC enterprise funds. As a result, the net deficits in these enterprise funds are as follows:

FUND	REVENUE DEFICIT	RETURNED APPROPRIATIONS	NET (DEFICIT) SURPLUS	SURPLUS BALANCE	REMAINING SURPLUS
GOLF	(625,463)	350,234	(275,229)	666,343	391,114
SOLID WASTE	(573,975)	98,960	(475,015)	2,294,760	1,819,745
MARINAS	(60,863)	74,341	13,478	861,350	874,828
SANDY NECK	(109,868)	119,042	9,173	909,529	918,702
HYCC	(211,963)	310,786	98,823	593,821	692,644

The Marina, Sandy Neck and HYCC budget savings were greater than the revenue deficits resulting in the generation of surplus. Only the Golf and Solid Waste operations experienced revenue deficits. Again, the Solid Waste Fund deficit is a timing issue as a result of sticker renewals being delayed.

General Fund Revenue Estimates for FY21:

	FY20 ACTUAL	FY21 ESTIMATE	CHANGE	
PROPERTY TAXES	\$ 127,668,308	\$ 131,026,068	\$ 3,357,760	2.63%
MOTOR VEHICLE EXCISE	8,245,044	7,000,000	(1,245,044)	-15.10%
BOAT EXCISE TAX	147,647	115,000	(32,647)	-22.11%
HOTEL/MOTEL TAX	1,950,148	1,450,000	(500,148)	-25.65%
STATE AID	16,750,834	15,625,413	(1,125,421)	-6.72%
CHARGES FOR SERVICES	2,039,863	1,845,100	(194,763)	-9.55%
FEES	1,012,905	754,200	(258,705)	-25.54%
FINES & PENALTIES	1,803,178	1,256,000	(547,178)	-30.35%
LICENSES	493,112	523,239	30,127	6.11%
OTHER REVENUE	1,981,267	1,576,500	(404,767)	-20.43%
IN LIEU OF TAX	34,794	32,000	(2,794)	-8.03%
PERMITS	1,847,266	1,190,346	(656,920)	-35.56%
LEASES	109,449	130,000	20,551	18.78%
SPECIAL ASSESSMENTS	234,888	111,000	(123,888)	-52.74%
TOTAL GENERAL FUND REVENUE	\$ 164,318,703	\$ 162,634,866	\$ (1,683,837)	-1.02%

The table above compares the actual Fiscal Year 2020 General Fund revenue with the estimates used to balance the Fiscal Year 2021 budget. This excludes transfers from reserves and other funds. General Fund revenue estimates have been conservatively projected for Fiscal Year 2021 due to the public health emergency.

It is projected that the pandemic will immediately impact revenue across the board due to the slowdown in the economy with the exception of property taxes. The pandemic does not directly impact the amount of property taxes the Town can levy; however, it may have an impact on the collection rate. It may take a longer period of time to collect property taxes levied but it won't necessarily reduce the amount. A lien can be placed on property for unpaid taxes and is in first position to be paid off in the event of sale or foreclosure.

The most vulnerable area of the General Fund revenue budget is state aid. The final passage of the State's budget may result in a lower number than presented above. Finance believes that other revenue categories have been adequately reduced to reflect the potential economic impact of the pandemic.

Enterprise Fund Revenue Estimates for FY21:

FUND	FY20 ACTUAL	FY21 ESTIMATE	CHANGE	
AIRPORT	\$ 8,214,286	\$ 6,841,627	\$ (1,372,659)	-16.7%
GOLF	\$ 2,867,737	\$ 2,825,464	\$ (42,273)	-1.5%
SOLID WASTE	\$ 2,555,525	\$ 3,081,725	\$ 526,200	20.6%
SEWER	\$ 5,243,498	\$ 4,590,439	\$ (653,059)	-12.5%
WATER	\$ 6,581,448	\$ 7,101,272	\$ 519,824	7.9%
MARINA	\$ 732,468	\$ 632,781	\$ (99,687)	-13.6%
SANDY NECK	\$ 847,187	\$ 680,455	\$ (166,732)	-19.7%
HYCC	\$ 916,139	\$ 841,800	\$ (74,339)	-8.1%
PEG	\$ 977,471	\$ 823,000	\$ (154,471)	-15.8%

Most Enterprise Fund revenue estimates are conservatively budgeted below the actual amount generated in Fiscal Year 2020 with the exception of Solid Waste and Water. It is believed that the Solid Waste sticker renewals will occur and the actual amount collected in Fiscal Year 2020 is a timing issue. The Water Enterprise Fund revenue is projected to increase as a result of a rate increase approved.

TO: Comprehensive Financial Advisory Committee
FROM: Mark Milne, Finance Director
DATE: July 20, 2020
SUBJECT: Financial Policy Review

Dear Committee Members,

I would like to discuss with the committee the following financial policy areas at our next meeting. In light of the discussions surrounding the FY 2020 budget adoption these areas need our immediate attention going into the FY 2022 budget development season as well as the policy decisions that need to be addressed surrounding the Comprehensive Water Management Plan.

Tax Levy

Section 241-51 D. (4) (c) of the Administrative Code states:

“The year-to-year increase of actual revenue from the levy of the ad valorem (property) tax shall generally not exceed 2.5% (Proposition 2 ½):

[1] Excluding taxable value gained through consolidation;

[2] Excluding the value gained through new construction; and

[3] Excluding expenditure increases funded outside the tax limit cap; and

[4] Not excluding the valuation gained or lost through revaluation or equalization programs.”

The tax levy is the predominant funding source for the Town’s operating and capital programs. Increasing the tax levy anything less than the amount allowed under the law will have an impact on the Town’s capital and operating budgets. Historically, the increase allowed under Proposition 2 ½ and new property growth of \$1 million is needed to fund the on-going costs of General Fund services.

The Town has consistently raised the tax levy since the implementation of Proposition 2 ½ by the amount allowable under the law. The estimated amount to be raised in Fiscal Year 2021 under the law is \$129,425,653. This includes a 2.5% increase in the base equal to \$3,138,431 and \$750,000 for estimated new property growth.

If the Town Council were to direct the Administration not to increase the levy by the amount under the law it would provide taxpayers some tax relief for fiscal year 2022. However, the amount not raised in fiscal 2022 gets carried forward to the subsequent year and could be levied in fiscal year 2023 or thereafter. The following example illustrates how this works:

	FY 2021	FY 2022	FY 2023	
Base levy subject to Prop 2 1/2	125,537,222	129,425,653	133,411,294	
Allowable increase	3,138,431	3,235,641	3,335,282	
Estimated new growth	750,000	750,000	750,000	
Levy limit	129,425,653	133,411,294	137,496,576	
Actual tax levy	129,425,653	129,425,653	137,496,576	6.24%
Excess taxing capacity	-	3,985,641	-	

In the example provided above, the Town could hold the tax levy level in fiscal year 2022 and increase the tax levy up to \$137,496,576 in fiscal year 2023. This would result in a tax increase of 0% in fiscal year 2022 and 6.24% in fiscal year 2023. To avoid spikes in the tax levy and to maintain a steady increase in the tax levy the Town has consistently avoided this strategy in the past.

Policy Question – Should the Town proceed with developing the fiscal year 2022 budget with the assumption that the base levy will be increased by 2.5% plus new growth?

Residential Exemption

A subset of tax levy policy is the Residential Exemption. The exemption provides tax relief to property owners who make Barnstable their primary residence with the exception of primary residences that are valued at \$1,134,500 or greater. A significant portion of primary residences benefit under this program.

The exemption does not change the amount the Town can collect in taxes. It only shifts the tax levy between taxpayers within the residential class. The benefits received by taxpayers who make Barnstable their primary residence are offset by additional taxes paid by second homeowners.

The Town Council has adopted a 20% Residential Exemption and it has been in place since the 2006 tax year. The Town Council could go as high as 35% to provide more tax relief to Barnstable residents. The Town Council could also reduce the exemption to 0% in any year.

Policy Question – Will the Town Council hold with a 20% exemption or do they want to consider changing it?

General Fund Resource Allocation – Operations vs. Capital Program

The Town uses a Stabilization Fund as allowed under MGL Chapter 40 §5B to accumulate funds to manage its General Fund capital program. This fund is commonly referred to as the Capital Trust Fund and was created in 1995. Section 241-51 D. (8) in the Administrative Code states the following:

“A Capital Trust Fund is hereby established for the purpose of financing debt service for recommended capital improvement program projects, as contained within the Town's five-year capital improvement plan.

(a) The Capital Trust fund will be funded through a general operations set-aside at a minimum of \$1,900,000 annually.

(b) The Capital Trust Fund shall not be utilized for any purpose other than that stated herein.

(c) The criteria for reviewing capital project eligibility for Capital Trust Fund borrowing include the following:

[1] The capital project shall have a financing term of 20 years or less;

[2] The capital project shall have a minimum project cost of \$250,000;

[3] The capital project is approved by the Town Council for funding through an appropriation and loan order submitted by the Town Manager.

(d) The Capital Trust Fund will have a debt service restriction on the fund, such that debt service estimates from authorized loan orders shall not exceed, at any one time, more than 80% of the amount in the fund as of the close of the fiscal year prior to the next debt service authorization, unless recommended by the Town Manager,

(e) The Capital Trust Fund shall otherwise function in accordance with related financial policies of the Town.”

The Fiscal Year 2021 budget provides \$10,692,825 of funding for the Capital Trust Fund. This is significantly more than the minimum identified in the Administrative Code due to inflation and a greater commitment to improving Town infrastructure. The current practice is to increase this by a minimum of 2.5% annually. The capital needs of the Town are significantly higher than the current level of funding provided.

Policy Question – Should the amount allocated to the capital program be increased? This would come at a cost to the operating side of the General Fund budget.

Capital Program

The Town has historically funded its General Fund and Enterprise Funds capital program within the property tax limitations of Proposition 2 ½ and user fees. The only projects funded outside the limitations have been the renovations and improvements at BHS and BIS in the 1990’s and the recent construction of the new technical high school in Harwich of which Barnstable is a member.

Policy Question – Should the Town establish criteria identifying projects that should be funded from a property tax override? Criteria could be based on a dollar threshold for larger projects, a catch-up on deferred maintenance or the construction of a new asset.

Revenue Allocation For General Fund Programs

New revenue growth within the General Fund is first directed to cover the cost increases in the Fixed Costs category of General Fund expenditures. Any residual amount is shared 60% to 40% between the School Department and Municipal operations. This excludes any revenue growth attributable to fee increases to address specific cost increases.

This policy has provided some predictability for long range planning by providing an operation protection against dramatic reductions in specific revenue sources such as Chapter 70 aid. Conversely, a significant increase in Chapter 70 aid offers the opportunity to lower the tax support for school operations providing more funding for municipal operations. It has also contributed to building a level of trust between Town and School Administration and the Town Council and School Committee.

Policy Question – Should the FY22 General Fund operating budget be developed using the same revenue allocation approach or changed?

- **The Town could use a similar approach to the capital program whereby additional spending requests would be prioritized for funding after fixed costs increases within the operating budgets are provided for, i.e. contractual labor obligations.**
- **The current “Fixed Costs” category could be allocated out to departments first to arrive at a fully allocated budget before new revenue growth is allocated.**

Fund Balance Policy

Section 241-51 D. (4) (b) [1] – [3] state the following:

[1] General Fund Undesignated Fund balance of at least 4% of total annual expenditures shall be budgeted. The Undesignated Fund balance shall be used to provide for temporary financing for unanticipated or unforeseen extraordinary needs of an emergency nature, for example, costs related to a natural disaster or calamity, or an unexpected liability created by federal or state legislation, new service needs that have been identified after the budget process, new public safety or health needs, revenue shortfalls, service enhancements, or opportunities to achieve costs savings.

[2] Funds shall be allocated from the Undesignated Fund balance only after an analysis has been prepared by the Town Manager and presented to Town Council. The analysis shall provide sufficient evidence to establish that the remaining balance is adequate to offset potential downturns in revenue sources and provide a sufficient cash balance for daily financial needs. The analysis shall address the nature of the proposed expenditure and the revenue requirement in subsequent budget years.

[3] Prior to allocating funds from the Undesignated Fund balance the Town Council shall find that an emergency or extraordinary need exists to justify the use of these funds. Funds shall be allocated each year in the budget process to replace any use of Undesignated Fund balance funds during the preceding fiscal year to maintain the balance of the Undesignated Fund balance at 4% of budgeted expenditures.

This has commonly been referred to as the “Town Council Reserve”. Based on the approved FY21 General Fund operating budget the Town Council Reserve is \$6,645,911. The last certification of the General Fund surplus (aka “Free Cash”) was \$14,688,744, or \$8,042,833 over the reserve set aside for the purposes mentioned above. Over the past 25 years the Town has never accessed the Town Council reserve fund due to the excess reserves it has maintained. The town has regularly used this excess to balance the annual operating and capital budgets and has traditionally generated sufficient reserves to replenish what it has used. The table below illustrates this.

Certification Date:	Beginning	Used For:			Ending
	Balance	Operations	Capital	Generated	Balance
July 1, 2010	\$8,411,317	(1,080,758)	-	3,416,013	\$10,746,572
July 1, 2011	\$10,746,572	(1,195,000)	(2,000,000)	4,768,613	\$12,320,185
July 1, 2012	\$12,320,185	(687,330)	-	5,639,538	\$17,272,393
July 1, 2013	\$17,272,393	(3,579,836)	(7,000,000)	4,403,107	\$11,095,664
July 1, 2014	\$11,095,664	(3,585,000)	(591,993)	6,451,368	\$13,370,039
July 1, 2015	\$13,370,039	(4,104,926)	(1,037,689)	5,721,779	\$13,949,203
July 1, 2016	\$13,949,203	(2,726,877)	(4,000,000)	5,908,772	\$13,131,098
July 1, 2017	\$13,131,098	(2,572,316)	(350,000)	5,988,373	\$16,197,155
July 1, 2018	\$16,197,155	(3,587,352)	(4,260,175)	4,293,608	\$12,643,236
July 1, 2019	\$12,643,236	(2,442,899)	(264,000)	4,752,408	\$14,688,745
Average		(\$2,556,229)	(\$1,950,386)	\$5,134,358	

Based on Fiscal Year 2020 operating results it is projected that the Town's Free Cash will be greater than the level last certified on July 1, 2019.

Policy Question – Should the Town continue using General Fund surplus as it has in the past to balance the operating and capital budgets so long as the amount used does not require the use of the Town Council's Reserve?

Enterprise Fund Subsidies

Section 241-51 D. (6) (j) states:

“Rates for offset receipts and Enterprise Funds shall be designed to generate sufficient revenues to support the full cost (direct and indirect) of operations and debt and provide debt service coverage, if applicable, and to ensure adequate and appropriate levels of working capital. Rates for the Department of Community Services Enterprise Fund shall be designed to generate revenue amounts less than required to support the full cost (direct and indirect) of operations and debt and working capital.”

Policy Question – Should the Enterprise Funds under the Department of Public Works (Sewer, Water & Solid Waste) continue to be required to cover full costs or should they be treated similar to other enterprise funds and provided a General Fund subsidy when determined appropriate?

Comprehensive Water Management Plan

The pandemic may significantly impacted the funding sources for this plan and the extent of the full effect is still unknown.

All of the Town's local meals tax and 1/3 of the local rooms tax on traditional lodging are dedicated to this program. The new Cape Cod & Islands Water Protection Fund tax of 2.75% on all lodging, including short-term rentals, has also been affected. In addition, the local rooms tax on short-term rentals has been directed to the Water Enterprise Fund to mitigate rates leaving very little available for this program.

Added to this uncertainty are several policy decisions that need to be made to implement the program. These include:

- **How will the town differentiate General Benefit Facility costs from Specific Benefit Facility costs?**
- **What assessment method will be used for allocating those costs?**
- **What limit, if any, will be set on the maximum amount for a sewer assessment? Will it be a dollar cap or a percentage cap?**
- **What interest rate will be charged on sewer assessments?**
- **Will amortization period will be used sewer assessments?**
- **When will a property abutter be required to hookup?**
- **Will bond amortization be authorized beyond 20 years?**
- **Will the General Fund contribute to the program? If so; how much and what mechanism will be used?**
- **Will a Systems Development Charge be included?**
- **Should the town pursue special legislation to create a revolving loan program? What would be the amortization period and loan rate?**
- **Should the town administer a sewer connection program?**

The Town has created a tool to illustrate various financial scenarios and to gauge the impact of assumptions used to fund the program.

Community Preservation Fund

This fund is supported by an annual property tax surcharge of 3% on real estate which generates approximately \$3.9 million in tax revenue. It provides funding for historic preservation, community housing and open space and recreation land. The repayment of the bonds issued under the former Landbank program are paid for out of this fund and will substantially be retired at the end of Fiscal Year 2023. This will create an opportunity for this program to significantly expand its charge.

Other communities in this position have reduced the surtax amount and redirected to other areas of the budget in order to address higher priorities with a neutral impact to the taxpayers. The Town Council could adopt a similar strategy if they felt there was a higher priority than the 3 areas addressed by this program.

Policy Question – Should the Town consider redirecting a portion of the CPA surtax to another priority?

Municipal Purpose Stabilization Funds

The Town may also take advantage of a unique funding source available under M.G.L c. 59, § 21C(g). A special purpose stabilization fund helps a community to:

- Think long term. A program like the CWMP requires ongoing evaluation of the assets, management of a repair/replace schedule, and calculations of long-term projected costs,
- Manage debt. A plan to accumulate cash over time and pay outright for a moderate-range capital expenditures helps preserve debt capacity for major, higher-dollar purchases or projects. An approach that balances debt with pay-as-you-go practices and protects against unforeseen costs and is viewed in a positive light by credit rating agencies,
- Build resident confidence in government. Special purpose stabilization funds directly address resident concerns and provide assurance that money appropriated for a particular purpose will be used for that purpose and not be diverted.

The creation of a special purpose stabilization fund requires a two-thirds vote of the Town Council, and this vote must clearly define the purpose of the fund being established. As with a general stabilization fund, the Town Council may appropriate into a special stabilization fund by majority vote and may appropriate out of one by two-thirds vote.

There are three options for building up the balance in special purpose stabilization fund.

1. A traditional appropriation, presented either as a budget line item or in a separate article and sourced from within the levy or from other general fund revenues, such as a transfer of funds from another account.
2. Any fee, charge or other receipt may be dedicated to a stabilization fund, except locally assessed taxes, excises and property tax surcharges, or revenues reserved by law for a particular purpose, such as betterments that are dedicated to pay debt services. The Town Council recently created a Stabilization Funds dedicating taxes on short-term rentals and revenue to be received on the host agreement with Vineyard Wind.
3. The third funding option is a unique type of Proposition 2½ override. Like a general override, additional tax revenue can be raised year after year without a communitywide ballot question beyond the year of inception. For this kind of override, however, the addition to the levy limit can be discontinued in a future year. In each succeeding year after a community has approved a

stabilization fund override, the Town Council can continue the additional tax earmarked for the fund or may lower it, defer it, or resume a prior deferral solely through an annual two-thirds “appropriation” vote. The additional tax that can be appropriated for any year is limited to 102.5 percent of the amount when it was last appropriated.

For example, in FY2021, residents approve a \$100,000 override for a special purpose stabilization fund and Town Council appropriates that amount. In FY2022, \$102,500 (1.025 x \$100,000) is available for "appropriation" and that entire amount is "appropriated." For FY2023, \$105,062 is available (1.025 x \$102,500), but only \$80,000 is "appropriated." The amount available in FY2024 now becomes \$82,000 (1.025 x \$80,000), but the Town Council choose to make no appropriation. The amount available in FY2025 is \$82,000 (1.025 x last appropriation made, which was \$80,000 in FY2023).

Building up stabilization balances through an override unquestionably involves an increase to the tax levy but, as important, the creation of a special purpose stabilization fund provide a means for the Town to respond to resident concerns about a lack of long-term planning. If considered thoughtfully and implemented prudently, these funds offer strategic mechanisms to help plan for future costs.

Policy Question – Should the Town consider creating a Stabilization fund through additional property taxing authority?