REVERSION STUDY PRESENTATION

Monday, November 18, 2013 7 pm

Why Is Reversion Being Considered?

- The cost to provide services for the citizens of Martinsville continues to increase, while revenue does not. Balancing the budget requires use of fund balance, increasing rates and fees, or significant reductions in service (or combinations of all 3).
- Continued use of fund balance to balance the annual budget is unsustainable.
- Reversion allows the possibility of consolidation of certain like services (schools and constitutional functions) with those currently provided by Henry County.

What is the “Reversion Study”?

The “Reversion Study”(or studies) in this particular case consists collectively of 3 separate and independent studies developed for the purpose of providing Martinsville City Council with information necessary to evaluate and consider the possibility of change in status for Martinsville from City to Town. Should reversion not be considered, the long range financial forecast will be a tool used to help guide future budget decisions.

What Specific Elements Are Included?

- A feasibility study for the consolidation of Martinsville City and Henry County School Divisions
- An evaluation of the prospective financial impact of the City of Martinsville's transition to town status
- Financial forecast for the period FY2014 to FY2019 for the City of Martinsville

Study Team

- Carter Glass IV, Attorney, Troutman Sanders LLP, Richmond, VA
- Steven Jacobs, Robinson Farmer Cox Associates, Richmond, VA
- S. John Davis & Associates, Ltd, an affiliate of Education Programs and Services, LLC, Norfolk, VA

SCHOOL CONSOLIDATION STUDY

A Study Update to Explore the Feasibility for Consolidation of Martinsville City and Henry County School Divisions

Background

- The study is an update of the study completed in 2004 by Education Programs and Services LLC (contracted by the MHC Chamber of Commerce in 2002 for this purpose). S. John Davis & Associates, an affiliate of Education Programs and Services LLC was contacted in September, 2012 for the purpose of updating the 2004 study.

The Study Consists Of 5 Phases

- **Phase I** provides a current and historical assessment of the input of resources and a critique of the educational outputs as measured by several performance indicators for both school divisions
- **Phase II** is a review of the system used by the Commonwealth of Virginia to finance public elementary and secondary education as well as an assessment of local fiscal effort

The Study Consists Of 5 Phases

- **Phase III** is a review of potential personnel costs related to a consolidated system
- **Phase IV** is an assessment of capital facilities and current school buildings
- **Phase V** consists of comments regarding observations, findings, and a summary of information in Phases I – IV; and discussion of the financial implications of 6 possible consolidation scenarios

Consolidated System Financial Benefits

- The study identifies financial benefits related to a consolidated school system coming from two main areas – personnel and application of the Local Composite Index (LCI). The LCI determines a school division's ability to pay education costs fundamental to the State's Standards of Quality, which in turn determines the level of State aid for local education.

Consolidated System Financial Benefits Related to Personnel

- Cost savings resulting from a reduction of 11.5 administrative positions
- Financial impact of merging 2 different pay scales – there is an approximate 4% difference between City and County School pay scales (City is approximately 4% lower).

Consolidated System Financial Benefits Related to Local Composite Index

- The City of Martinsville has a lower LCI than Henry County.
- Under the State's Consolidation Incentive Program Legislation, the lower index may be used (established by the BOE) to determine state aid of a consolidated system for a period from 5 to 15 years after consolidation.

Financial Impact – Combination 1/6

- Combination 1 – City School Division teachers placed on HC School Division salary scale - ($431,527); Consolidated Incentive Program - Additional State Aid by full use of Martinsville LCI - $1,230,197; Reduction of Administrative Positions - $1,035,000, for total savings of **$1,833,670**

Financial Impact – Combination 2/6

- Combination 2 - City School Division teachers placed on HC School Division salary scale - ($431,527); Consolidated Incentive Program - Additional State Aid by use of a median LCI - $612,686; Reduction of Administrative Positions - $1,035,000, for total savings of **$1,216,159**

Financial Impact – Combination 3/6

- Combination 3 – City and County School Division teachers placed on a median salary scale - $466,466; Consolidated Incentive Program - Additional State Aid by full use of Martinsville LCI - $1,230,197; Reduction of Administrative Positions - $1,035,000, for total savings of **$2,731,663**

Financial Impact – Combination 4/6

- Combination 4 - – City and County School Division teachers placed on a median salary scale - $466,466; Consolidated Incentive Program - Additional State Aid by use of a median LCI - $612,686; Reduction of Administrative Positions - $1,035,000, for total savings of **$2,064,152**

Financial Impact – Combination 5/6

- <u>Combination 5</u> – Current HC School teachers placed on City School Division pay scale - $1,501,335; Consolidated Incentive Program - Additional State Aid by full use of Martinsville LCI - $1,230,197; Reduction of Administrative Positions - $1,035,000, for total savings of **$3,766,532**

Financial Impact – Combination 6/6

- Combination 6 - Current HC School teachers placed on City School Division pay scale - $1,501,335; Consolidated Incentive Program - Additional State Aid by use of a median LCI - $612,686; Reduction of Administrative Positions - $1,035,000, for total savings of **$3,149,021**

Financial Impact – Conclusions

- Combinations of costs/cost savings that generate the largest amounts are likely to be the most controversial.
- Potential additional costs savings could come from integrating transportation services, operation and maintenance, school nutrition, fiscal affairs, and others.

AN EVALUATION OF THE PROSPECTIVE FINANCIAL IMPACT OF THE CITY OF MARTINSVILLE'S TRANSITION TO TOWN STATUS

Overview

- The evaluation is developed assuming an evenly applied proportional reduction to all City/Town tax rates sufficient for the Town to "break even", or balance revenues with expenditures.
- In comparison to the City of Martinsville, the Town of Martinsville would experience a substantial reduction in operational expenses of approximately $28 million.

Overview

- To generate revenues to balance with operational expenses, Town property tax rates could be proportionately reduced by over 90% compared to current City levels, resulting in a reduction of approximately $28 million in revenues from property taxes and other local, state, and federal funds. Even when including County property taxes paid by Town residents, the aggregate property tax burden for Town residents would decrease by about 42%.

Overview

- The County of Henry would experience an increase in revenues of approximately $26 million and an increase in expenditures of approximately $27.3 million. If that operating loss were funded entirely from real estate taxes, an increase of approximately 3.2 cents would be required.

Summary - Revenues

- Generally, the amounts of “City revenues” no longer associated with a Town offered service have been recognized on a dollar for dollar basis as new revenues of the County

Summary - Revenues

- Revenue assumptions – City receipts from the State for Constitutional Offices are continued on a dollar-for-dollar basis as County revenue
- Net gain in State school aid of $1.2 million from the Davis School Study is included
- The Town would generate approximately $28 million in revenue less than the City
- The County is expected to experience a revenue increase of approximately $26 million

Summary – Expenditures

- As with the revenue analysis, as a general matter the amounts of City expenditures no longer performed by the Town but performed by the County have been recognized on a dollar for dollar basis as new expenses of the County.

Summary - Expenditures

- Staff and related expenses for all Constitutional offices, save one, are expected to transfer to the County. Two positions from the office of the COR whose transfer is not supported by State Compensation Board analysis are anticipated to be retained within the structure of the Town's finance operations.

Summary - Expenditures

- Opportunities for School-related savings of approximately $600,000 noted by the Davis School Study are recognized.
- The Town of Martinsville would expend approximately $28 million less than the City of Martinsville
- The County of Henry is expected to expend approximately $27.3 million more after the transition

Other Notes

- Calculations from the study show that assessing tax rates at approximately 7.4% of the City's current rate for each class of taxable property will yield revenues sufficient, with other expected revenues, to "balance" and "break even" with prospective expenditures.
- No estimates have been made with respect to the cost, if any, for transfer or use of general capital facilities such as the jail or courthouse that might be needed by the County

Other Notes

- No estimates have been made regarding additional office space that might be needed by the County for employees, in particular Constitutional employees.
- Also possible - there could be efficiencies and cost savings in the provision of County services to Town residents by elimination of certain positions or other expenditures.

Concluding Summary

- In a transition from City to Town status, Constitutional functions and City Schools becomes a function of the County
- The Town of Martinsville would realize a decrease in both revenue and expenses of approximately $28 million
- The County of Henry is expected to experience a revenue increase of approximately $26 million, and expenditures of approximately $27.3 million

Concluding Summary

- For a “break even” budget with revenues balancing expenditures, Town residents could see an approximate 42% reduction in property taxes. Similarly, if the tax rate were left as is, the Town would realize a substantial increase in revenue that could be used for a variety of Town projects, programs, and infrastructure improvements.

Concluding Summary

- Other current City services such as Police, Fire, Utilities, Public Works, Finance, General Administration, etc. remain since these services will continue to remain as a function of the Town.
- The Town can annex, whereas the City cannot.

Financial Forecast for the Period FY2014 to FY2019

Introduction

- Study includes a forecast of City financial operations
- Detail and summary financial information on the City's contemplated capital program
- An analysis of the impact of the prospective capital program upon the forecasted financial operations

Forecasts – General

- Should be noted the forecasts are for planning purposes and are not to be regarded as accountant's opinions of the present or future financial position of the City. The forecasts are based upon trends, and their validity depends upon the outcomes of future events. Modification will become necessary as City growth and development progresses, or if there are changes in market or other economic conditions.

Forecast For 3 Possible Options

- Maintain status quo, tax rate remains revenue neutral, does not include capital or new debt, and fully depletes fund balance (Table 5)
- Maintains status quo but does not deplete fund balance – maintains 10% cash balance margin, does not include capital (Table 6)
- Includes capital funding and maintains 10% cash balance margin (Table 7)

Capital Program

- Projects of a fixed nature and having a long service life. Includes, but not limited to public buildings, utilities, large equipment, major replacement or reconstruction projects.
- Currently programming consists of arranging the projects in a time series schedule of anticipated implementation. Schedule is reviewed in light of 3 major considerations:

Capital, continued

- 3 major considerations are:

- The City's Comprehensive Plan and City's Goals & Initiatives
- Considerations of the public health, safety, and general welfare of the City's citizens, and
- The City's fiscal capabilities

Capital, continued

- The schedule is reviewed annually and subject to modification – projects may be added, deleted, or rescheduled.
- The total capital program during the planning period (FY14 through FY18) contemplates capital expenditures totaling $15.4 million. FY14 contemplated $3.55 million in capital expenditures.

Forecast of Financial Operations

- FY2014 budget was used as the base year. The forecast was prepared by applying prospective annual rates of change to the detailed sources of City revenue and objects of expenditure.
- Neither addition of new sources of revenue nor discontinuance of current sources of revenue are anticipated.

Forecast of Financial Operations

- Neither addition of new programs, services, or staff nor discontinuance of existing programs, services, or staff are anticipated.
- There are no unanticipated non-recurring costs.
- New capital projects and any new debt service are not included nor is existing debt service beyond the budget year.

Forecast of Financial Operations

- 5 years (2008 to 2012) of data for forecast factors (Table 2) were used.
- Revenues are anticipated to remain approximately constant at $71.3 million for the forecast period, FY2014 through FY2019.
- Expenditures are forecasted to grow from $75.5 million (FY14) to $78.2 million (forecasted FY19).

Forecast of Financial Operations

- The initial use of fund balance of approximately $4.1 million by all funds causes an initial imbalance between revenues and expenditures exacerbated by forecasted expenditures exceeding revenues in each year of the forecast period.
- Computations of prospective real property tax revenue reflecting normal growth and growth attributable to reassessment and market conditions are included.

Forecast of Financial Operations

- The real property tax rates represent an equalized tax rate (adjusted with each reassessment to be revenue neutral).
- Incorporates existing debt service
- A beginning fund balance of approximately $17 million is used; includes funds reserved for future capital and debt service, but does not include impact of the prospective capital program.
- Recognizes expected declines in State and Federal funding and the local revenue base.

Forecast of Financial Operations

- Given the related parameters, revenue, and expense projections, the $17 million fund balance is forecast to be depleted by sometime in FY2017.
- This forecast is based upon past trends and their validity depends upon the outcome of future events, and the forecast is not to be regarded as the accountant's opinions of the present or future financial position of the City.
- Summary is highlighted in Table 5

Forecasted Impact – Operations and Capital Program

- Maintains cash balance to meet operational and minimum cash requirements (10%)
- Financial Forecast for the period FY2014 through FY2019 – to continue to fund operations exclusive of funding the capital program, the real estate tax would need to increase incrementally from the current \$1.06/\$100 of assessed value, to \$2.03/\$100 in FY2019.
- Summary is highlighted in Table 6

Forecasted Impact – Operations and Capital Program

- Factors that could influence the rate change includes controlling and reducing City expenditure patterns and/or programs.
- Enhancing revenues attributable to City growth and development
- Rate and fee increases for services rendered
- Other tax rate adjustments.

Forecasted Impact – Operations and Capital Program

- Using the same analysis and including costs related to funding the City's Capital Improvement Program, the real estate tax would need to increase incrementally from the current $1.06/$100 of assessed value, to $2.11/$100 in FY2016, and remain above $2/$100 through FY2019.
- Summary is highlighted in Table 7

Conclusions

- During contemplation of the budget and capital expenditures, it is recommended that revenue, expenditures, and fund balance levels be carefully monitored. The City's financial condition is being negatively impacted by reliance on fund balance, negatively trending market conditions, and decreases from State and Federal funding sources.

Conclusions

- "The prudence of City Council's timely decision to undertake this financial planning exercise has been borne out. It would appear the City is at a juncture where careful fiscal deliberation can preserve its current fiscal position and mitigate anticipated trends. The validity of the assumptions underlying these forecasts must be carefully monitored."