A Good News/Bad News Financial Outlook

By Susan Siegel

(Note: The following was written before the Town Board voted on November 14th to make some changes to the supervisor's 2015 Tentative Budget.)

The good news is that for 2015, there may be only modest increases in most of the separate tax rates that, when combined, represent a taxpayer's total town tax bill. The bad news is that in order to keep the tax rate increases as low as possible, the town has put itself in a financial bind that will likely have serious financial consequences for taxpayers in future years. It's a classic case of what happens when the financial can is kicked down the road: short term benefits will create long term pain. What we don't know – yet – is when that pain will hit and how hard it will hit.

Part I of a two-part series, explores how the town's increasing reliance on fund balance over the past three years has enabled the town to reduce some tax rates and limit the increase in other tax rates.

Part II explores how the increasing reliance on fund balance has had a negative effect on the town's tax levy limit and what this means for future budgets and tax rates.

Part I

The goal of all town officials is to keep taxes as low as possible while maintaining the existing level of services, and hopefully expanding services. In order to achieve that goal, officials have four basic tools in their financial toolbox.

1. **Reduce expenses, aka appropriations**

While the town is always looking for ways to operate more efficiently and at a lower cost, with approximately 78% of the town's budget allocated for staff and staff related expenses, any major reduction of expenses would likely require cutbacks in services and/or layoffs of town employees, both of which are politically not palatable.

2. **Find ways to increase non-tax revenue such as fees, fines, sales tax, mortgage tax, etc.**

Realistically, there are limits to how much additional non-tax revenue can be generated because the town doesn't control the big ticket non-tax revenue sources such as sales tax and mortgage tax. Some fees, such as building permit fees, are dependent on a good economy. There are also limits on increasing town imposed fees. For example, increasing the cost of pool passes could be counterproductive because it could lead to fewer residents buying passes.

3. **Increase the tax base (aka the town's total assessed value), especially the commercial tax base.**

This is the most talked about option — but it can take years to be realized, and, like the sales tax and mortgage tax, is something the town has limited control over. For example, it's been six years since Costco announced its intention to come to Yorktown, but we're still waiting for the first shovel in the ground, and most of the delay can be attributed to Costco, not the town. There are other commercial projects that have been approved by the Planning Board, some dating back several years, but which have yet to be built.

4. **Use the town's rainy day funds, aka, the fund balance, aka the town's reserves, to supplement the revenue side of the budget.**

Since by law town budgets must be balanced (revenue must equal expenses), when non-tax revenue is less than expenses, the difference has to be made up either by taxes or using the fund balance. As highlighted in the example below, every dollar of fund balance used to as a revenue means one dollar less that has to be raised in taxes.

The following three tax rate scenarios for the "Town" tax, the tax that includes the General, Highway and Library Funds, *the only funds that include all taxpayers*, illustrate how using different amounts of fund balance affects the tax rate. The first scenario, in rounded numbers, is from the supervisor's 2015 Tentative Budget. The second and third scenarios that rely on less fund balance are hypothetical with approximate tax rates.

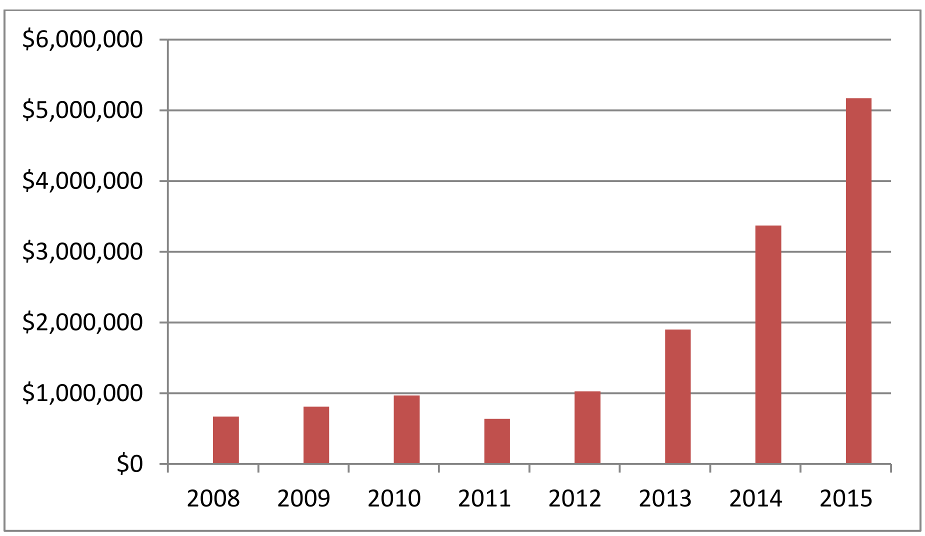
	Expenses	Non-tax revenue	Revenue shortfall	Fund balance	Tax Levy	Tax Rate/ $1,000 assessed value	Taxes/$10,000 assessment	$ Tax increase	% Tax rate increase
1	$34,700,000	$14,200,000	20,500,000	1,600,00	$18,800,000	$148.78	$1,488		0.87%
2	$34,700,000	$14,200,000	20,500,000	1,000,00	$19,400,000	$153.27	$1,530	$42.00	3.90%
3	$34,700,000	$14,200,000	20,500,000	$500,000	$19,900,000	$157.22	$1,570	$82.00	6.60%

Beginning in 2013, in order reduce some taxes and limit the tax rate increase for other taxes, the town relied on an infusion of an ever increasing amount of revenue from its rainy day funds.

In the five years between 2008-2012, the town took a combined total of $4.1 million from the fund balances of its 27 separate funds (budgets), or an average of $823,000 each year.

That changed dramatically with the 2013 budget that relied on $1.9 million of fund balance. In 2014, the town used $3.7 million of fund balance. And the supervisor's Tentative 2015 Budget projects using $5.2 million of fund balance.

Historic Use of Fund Balances (All Funds) 2008 - 2015



From a financial perspective, there's nothing fundamentally wrong with the town using the fund balance to tide the town over during difficult times. As homeowners, we've often had to resort to our savings during hard times. The problem , however, for our personal budgets, as well as the town's, is what happens when we've become addicted to using our reserves to pay for ongoing expenses, especially expenses increase at a faster rate than our incomes. What happens when the reserves are exhausted or so little is left that there's no safety cushion in the event of an emergency or when we want to undertake a special project?

There are significant differences between the town's 27 separate budget funds and their respective fund balances. In the water and sewer funds, for example, that are financed almost exclusively from taxpayer dollars, the reserves increase when tax revenue exceeds expenses. But in the General Fund, the fund that represents 77% of the

“Town” tax, the reserve accumulates because non-tax revenues, such as the sales tax and mortgage tax come in higher than anticipated. (Hurricane Sandy actually added $500,000 to the reserve, over and above reimbursing the town for its clean-up costs.) To a lesser extent, the General Fund reserves can also grow when the town doesn’t spend what was budgeted for a given expense. For example, the budget may include the salary and benefits expense for a vacant position that never gets filled. The General Fund reserve doesn’t grow because too much money was taken from taxpayers. Unlike the water and sewer funds, the General Fund reserve doesn’t represent “unused taxpayer money.”

Reducing taxes isn’t the only possible use of fund balance. Reserves or rainy day funds are can also be used to:

- cover unanticipated emergency expenses, such as storm clean-up costs that are not reimbursed by the federal government
- cover needed expenses that were not anticipated when the budget was passed, such as needed repairs to a building’s heating system
- cover an unexpected increase in costs, such as for snow plowing or higher fuel oil costs due to a cold winter
- pay cash for needed major expenditures such as trucks and capital projects in order to avoid having to borrow and pay 3%-4% interest over 20+ years. (The Junior Lake pool was paid for with cash; the Shrub Oak Pool was bonded.)

The size of the fund balance also affects the town’s bond rating if and when we do have to borrow. The larger the fund balance, the higher the bond rating and the lower the interest rate we would have to pay.

In the end, when discussing whether to use or save a fund’s reserves, what needs to be remembered is that budgets are financial as well as political documents. Ideally, they should balance the political goal of elected officials who want to keep taxes as low as possible with the town’s long term fiscal health and the need to replace the town’s aging infrastructure. Continuous deficit budgets that offer short term benefits and long term pain are clearly out of balance.