TOWN COUNCIL
STAFF REPORT
Department of Finance & Administration

MEETING DATE:	February 9, 2021
PROJECT:	Discussion and Direction on Updates to Special Revenue Funds, Accommodations Tax Allocations and Fund Balance Policies
PROJECT MANAGER:	Chris Forster, MPA, CPFO, CGFM, Director of Finance & Administration

OVERVIEW:

As part of the strategic plan, the Finance department took on the initiative to evaluate Special Revenue Funds; the types that can be levied and how they may be used compared to how other similar communities are allocating Accommodations Tax (ATAX) Funds. Additionally, the Finance department assessed the Town's fund balance policy for its sufficiency and appropriateness compared to best practices and applicable risks.

Special Revenue Funds and allocations

The State of South Carolina governs what kinds of taxes and fees a local jurisdiction may approve. Currently the Town of Bluffton leverages every legally authorized revenue source in some manner. Local changes can be made to the rates at which taxes and fees may be set and the types of operational fees that may be approved.

Special revenues include State and Local Accommodations taxes and Hospitality taxes. These revenues must be used for tourism related expenditures or the promotion of tourism. The first $25 thousand plus 5% of State Accommodations revenue must be allocated to the general fund. The next 30% must be allocated to an organization promoting tourism known as the Designated Marketing Organization (DMO). For the Town of Bluffton that is the Hilton Head Island-Bluffton Chamber. The Town currently allocates the next $190,000 to the Bluffton Historical Foundation, BHF (formerly Bluffton Historical Preservation Society). The remaining amount can be granted to non-profits for tourism and cultural related events. Use of State ATAX dollars are more restrictive and can only support tourism related operations expense if not normally provided by the municipality.

Local accommodations tax can be used for Tourism related CIP, operations and maintenance, including advertising and promotional expenses. Current Town Ordinance allows an allocation up to 8% to the DMO, up to 10% for operations and maintenance and up to 1% to the reserve fund. As part of the budget ordinance the Town has traditionally allocated 51% of local ATAX to the CIP fund.

Hospitality tax must be used for tourism related CIP and expenses, drainage improvements, advertising and promotion. There are no other Town restrictions on the use of Hospitality taxes. The Town has traditionally transferred $500,000 to General Fund and a significant amount to support specific projects within the CIP.

Considerations for Discussion:

- Does the Town want to do more Town managed tourism promotion and advertising?
- Should Town consider adjusting local ATAX and HTAX allocations to designate funds for town advertising and promotion?
- Should there be adjustments to the 8% local ATAX allocation to the DMO?
- Should HBF receive a percent allocation of State ATAX like the DMO, rather than a flat dollar amount?

Fund Balance Policy

The current Town Fund Balance Policy has four main components. The Emergency Recovery Fund which is calculated as 15% of General Fund budgeted expenditures. The unassigned Fund Balance reserve which is 25% of budgeted General Fund expenditures. The Vehicle & Equipment Replacement Reserve which is capped at $1 million but is equal to 115% of designated assets depreciation cost.

The Government Finance Officers Association (GFOA), who's mission is to advance excellence in public finance, provide advisories and recommended practices on municipal financial policies and procedures. The two major best practices released by the GFOA on fund balance include the "Fund Balance Guidelines for the General Fund" and "Strategies for Establishing Capital Asset Renewal and Replacement Reserve Policies."

The GFOA recommends that a municipality maintain an unrestricted fund balance of "no less than" two months' worth (17%) of budgeted expenditures. But they qualify that with a recommendation that the adequacy of minimum unrestricted fund balance "should be based on risks unique to each municipality." All GFOA's recommendations regarding fund balance reserves seek to identify the bare minimum a municipality should maintain in unrestricted reserves and do not attempt to identify actual needs since each jurisdiction is unique. In April of 2020 GFOA released a Risk Based Reserve Assessment tool for municipalities to gauge risks and identify a minimum reserve threshold more appropriate for a jurisdiction's needs. Town Finance completed this assessment and determined the Town faced a moderate to high level of risk to retain through reserves and the assessment recommends adopting an amount of reserves significantly higher than the recommended minimum. Best practice recommends that the Town benchmark to similar communities and analyze most significant risks to make sure the Town is adequately covered compared to the unique financial costs of such risks. In addition, they recommend assessing the impact of reserves on the Town's bond rating.

The other major reserve recommended by the GFOA is the Capital Asset Renewal and Replacement Reserve. The current Town Vehicle and Equipment Reserve is limited in scope and capped at $1M. In the past ten years the Town's depreciable assets have increased 88%. They have increased 56% in just the past 5 years. The Town's CIP projects have grown significantly and large capital investments are planned to be completed over the next few years, including parks, facilities and infrastructure. Recommended practice is to maintain a reserve for all capital asset renewals and replacements. The GFOA recommends a minimum balance equal to a percentage of the Five-year average of an entity's capital budget and base annual contributions on a percentage of the annual depreciation of an entity's assets.

Considerations for Discussion:

- Adjust emergency reserves to be based on a percent of all budgeted funds rather than just General Fund.
- Consider adjusting emergency reserve to align with potential disaster recovery costs? Or commit more unassigned reserves to maintain flexibility in the use of reserves?
- Consider updating equipment reserve to a capital asset reserve?
- Define appropriate uses of excess reserves as one-time unexpected, nonrecurring costs.