

TO: City Council

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CC: John Connet, City Manager  
Brian Pahle, Assistant City Manager  
Department Heads

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SUBJECT: Mid-Year Budget Report, FY23

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DATE: January 30, 2023

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FROM: Adam Murr, Budget Manager  
Jenny Floyd, Budget & Mgmt. Analyst

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The following report provides information on the City of Hendersonville's fiscal year 2022-2023 (FY23) budget and the respective analysis for revenues and expenditures at mid-year, January 2023. The report will summarize high-level observations, provide an overview of recommended adjustments, and provide an amendment for accounts requiring Council approval.

The report is broken down by a governmental and enterprise section and reports on the City's seven (7) major operating funds: General, Main St. MSD, 7<sup>th</sup> Ave. MSD, Water & Sewer, Parking, Stormwater, and Environmental Services. This report will be submitted to City Council at the February 8<sup>th</sup>, 2023, meeting.

#### **Governmental Funds**

The three governmental funds covered in this report include the General Fund, Main St. MSD Fund, and 7<sup>th</sup> Avenue MSD Fund. The General Fund revised budget as of 01/03/2023 totals \$24,308,483 including a budgeted fund balance appropriation of \$1,959,090. The Main Street MSD Fund revised budget totals \$675,218 including a budgeted fund balance appropriation of \$115,933. The 7<sup>th</sup> Avenue MSD Fund revised budget totals \$185,863 including a budgeted fund balance appropriation of \$86,225. Major highlights of these fund's mid-year performance and recommended adjustments are presented in the following sections.

#### **Ad Valorem Tax (Revenues)**

For the tax year 2022, the City continued an interlocal agreement with Henderson County to consolidate tax collection under the County. The County provides this service for a fee of 0.5% of the total collections. At mid-year, collections for the tax year 2021 (FY22) General Fund ad valorem taxes total approximately 48.40% (\$5.2m) of the total levy. Comparably, in 2022 (FY23) at mid-year, collections totaled 56.29%. We continue to anticipate total collections on the year of \$10,668,868, based on forecasting and property tax distribution expectations. The Main Street MSD fund property tax actuals total 38.11% of budget, to date. 7<sup>th</sup> Avenue MSD fund property tax actuals total 40.27% of the revised budget, to date.

Prior year collections have exceeded initial budget estimates in the General Fund and 7<sup>th</sup> Avenue MSD Fund. Our mid-year amendment includes adjustments considering the increased collection amounts.

#### Unrestricted Intergovernmental Taxes (Revenues)

Sales tax collections for FY23 have trended above initial budget estimates. We have received sales tax revenue from the State for four (4) of our twelve (12) collection cycles in FY23. Sales tax actuals total \$1,977,574 at mid-year – this reflects a \$339,256 collection over our adopted budget. The proposed mid-year amendments include adjustments for higher than budgeted sales tax collections (+\$287,000); however, we remain intentionally conservative with our adjustments. Erring on the side of conservative sales tax revenue adjustments is a best-practice budgetary strategy to provide the City flexibility in case there are future sales tax collection periods that do not meet or exceed budgetary targets. We speculate, due to the Fed's inflationary policy in late 2022 and early 2023, that consumer spending may slow as we progress further into FY23. Conservative consumer spending, coupled with the Fed's goal to increase the unemployment rate could result in a short-term contraction in sales tax revenue.

#### Debt Proceeds (Revenues)

The City commonly finances vehicles and other equipment purchases through debt proceeds (loans). The City is aware of capital items that will not be received prior to the end of the fiscal year (pothole patching machine, and police vehicles). These delays in delivery are due to long lead times from manufacturers. Due to the delay, there is a recommended \$567,700 decrease in debt proceeds within the General Fund, and a decrease to the capital expenditure accounts. Our mid-year amendments move the debt proceeds and corresponding expenditure budget to a capital project ordinance (CPO, #00023) to move forward with the purchase of equipment past June 30, 2023.

#### Other (Revenues)

Powell Bill distributions are a large, restricted source of revenue in the General Fund. According to North Carolina General Statute (NCGS) 136-41.3(a), funds must be used primarily for street resurfacing within corporate limits, with some allowance to maintain bridges, drains, curbs, and other necessary public transportation amenities. At mid-year FY23, there is no proposed adjustment to Powell Bill distribution revenues. The State has provided \$459,283, with the City collecting approximately \$3,600 in interest at mid-year. Our adopted Powell Bill Allocation budget is \$467,859.

Additional significant revenue amendments include a \$31,300 increase to Payment In Lieu of Sidewalk revenues, a \$53,000 increase to Market Adjustment revenues, a \$15,900 increase to Refund revenues, a \$27,150 increase to Insurance Proceed revenues, and a \$50,650 increase to Sale of Capital Asset revenues.

#### Summary (Revenues)

Overall, the proposed amendments result in a net decrease of \$105,037 in the General Fund. Our mid-year amendment does not include any adjustments to fund balance appropriations in the General Fund. The Main Street MSD Fund amendment increases revenues \$6,470, including a \$5,000 increase to special event revenues and no change to fund balance appropriated. Increased Main Street MSD revenues are being used to balance an unanticipated increase in overtime budget usage. – there is no change to the fund balance appropriation at mid-year. 7<sup>th</sup> Avenue MSD Fund revenues will increase \$2,023 with the proposed mid-year amendment. No changes to 7<sup>th</sup> Avenue's fund balance appropriated are recommended. The increase for 7<sup>th</sup> Avenue will also be used to adjust salaries and benefits accounts related to higher than anticipated overtime budget usage.

Salaries & Benefits (Expenditures)

City Council implemented a 75<sup>th</sup> percentile pay and classification structure upon budget adoption for FY23. Included in the mid-year budget amendment recommendations are increases for Fire, Police, and Public Works Department salaries and benefits (\$269,770). The largest portion of our adjustment is for an adjustment to the Police Department's salaries and wages – regular account, which covers Officers earning higher grade standings within the department due to qualifications, following pay and classification implementation. For example, an Officer previously classified as a Grade 14/Officer I may have been moved to Grade 17/Officer IV following pay and classification adoption, which includes a budgetary impact.

Other Equipment, Supplies, & Services (Expenditures)

There is a long list of smaller proposed amendments to regular operating accounts to fix budget issues that have arisen in the first half of the fiscal year. These are typical amendments for repairs and other supplies. Of note, there are recommended increases to Liability & Property Insurance accounts throughout the General Fund, which total \$35,516. Other operating increases cover needed increases to fuel, contracted services, repair and maintenance, and training budgets.

Contingencies (Expenditures)

Finally, the General Fund's contingency account had an adopted budget of \$50,000. At mid-year, this budget amount has decreased to \$4,359 to cover various overages across all departments within the General Fund. At this time, it is recommended we increase the contingency budget by \$45,000 to \$49,359 to provide the City Manager's office financial flexibility to cover unforeseen challenges and opportunities through the remainder of the fiscal year.

The total recommended change in total budget for the governmental funds is presented, as follows.

<b>Fund</b>	<b>\$ Change (Net)</b>
General Fund (010)	Decrease \$60,037
Main Street MSD Fund (020)	Increase \$6,470
7 <sup>th</sup> Avenue MSD (021)	Increase \$2,023

The amendment detailing these changes is included with the agenda item.

## **Enterprise Funds**

The four enterprise funds covered in this report include the Water and Sewer Fund, Parking Fund, Stormwater Fund, and Environmental Services Fund. The Water and Sewer Fund revised budget as of 01/03/2023 totals \$22,882,286 including a budgeted fund balance appropriation of \$757,039. The Parking Fund revised budget totals \$1,488,666, including a \$682,603 fund balance appropriation. The Stormwater Fund revised budget totals \$1,490,476 including a budgeted fund balance appropriation of \$192,186. The Environmental Services Fund revised budget totals \$1,631,401 including a budgeted fund balance appropriation of \$108,301. Major highlights of these fund's mid-year performance and recommended adjustments is presented in the following sections.

### *User Charges (Revenues)*

User charges for the sale of utility services are the largest income source for the enterprise funds. Operating under a business-like structure, the City charges customers directly based on the amount of a service or resource consumed. The City has deliberated with rate experts and consultants to recommend rates to the City Council. Adherence to recommendations for the current fiscal year (FY21-22) and forward is an important consideration as we continually prioritize capital projects, analyze the health and longevity of our utility systems, and meet financial covenants set through our revenue bond (parity bond) and other borrowings.

As of 01/03/2023, the water sales account has collected \$6,299,002 (42.42%) of budgeted user charge revenue. This collection amount reflects approximately 20 cycles of revenue collection out of 48 total cycles. 28 major collection cycles remain this fiscal year. Compared to prior fiscal years at the same collection period, water sales revenues are higher. This increased actual water sale revenue trend can be attributed to a few factors including finance department efforts to improve utility bill collections and increased economic growth in greater Henderson County (with utility connections increasing over time). The sewer charges account has collected \$2,695,305 (43.47%) of budgeted revenues. The Parking Fund has not yet collected \$121,586 (22.82%) of budgeted monthly parking revenues, plus parking meter revenues. The Stormwater Fund has collected \$384,217 (33.21%) of budgeted stormwater fee revenue. The Environmental Services Fund has collected \$602,493 (39.62%) of budgeted user charge revenue (for both residential and commercial waste collection).

At a high level, staff recommends a \$210,000 increase to water sales revenues, and a \$125,000 increase to sewer charge revenues in the Water and Sewer Fund. It is recommended commercial waste disposal fees in the Environmental Services Fund increase by \$38,700. Other major revenue sources have no recommended change.

### *Tap Fees (Revenues)*

In addition to user charges, the Water and Sewer Fund tracks revenues collected from the connection of customers to our infrastructure. The tap fee revenue source is a good indicator of the local economy, providing insight to the rate of development in the City and Henderson County. Thus far, in FY23, we have collected \$177,773 (46.48%) of our \$382,500 budgeted water and sewer tap revenues. Based on current collections, staff recommend no change to budgeted revenues for water and sewer tap fees.

### *Other (Revenues)*

Various other minor revenue sources are accounted for in the enterprise funds. Some other sources of revenue include disconnect/reconnect fees, customer participation charges, investment earnings, sale of assets, and miscellaneous income. At mid-year, staff recommends Council approve the following adjustments to other revenues: \$400 increase to miscellaneous sales revenues, \$38,200 increase to

water and sewer inspection fees revenues, \$500 increase to disconnection fees, a \$15,300 increase to utility billing service charges, a \$21,000 increase to sewer surcharges, and a \$500 increase to interest income.

*Salary & Benefits (Expenditures)*

There are several needed increases to salaries lines, including adjustments for worker's comp. insurance claims, salaries & wages – regular, uniforms, and overtime budgets within the Water and Sewer Fund.

*Inventory (Expenditures)*

The largest, and most notable increases to the Water and Sewer Fund budget at mid-year are for inventory related items for \$287,000. For accounting purposes, we have created two (2) offsetting expenditure accounts to assist with the management of inventory – these accounts do not impact the day-to-day operations of our water and sewer teams. The newly created "Inventory Purchases" and "Contra Inventory Purchases" accounts are budgeted at + / - \$622,000.

*Other Equipment, Supplies, & Services (Expenditures)*

Other operating expenditure amendments include increases for fuel, training, repair and maintenance of vehicles and equipment, and non-capital equipment expenditures. Fuel budgets will also receive increased budget via the proposed amendment to cover for higher than anticipated usage and prices which have increased significantly since budget preparation and adoption last Spring and Summer. In the Environmental Services Fund, a \$253,013 fund balance appropriation is recommended to purchase a waste truck using loan proceeds collected in FY22, which were added to fund balance in FY23.

*Contingencies, Transfers, and Others (Expenditures)*

Contingencies in the Water and Sewer Fund have decreased from \$100,000 to \$79,351 at mid-year. There are no recommended adjustments to contingencies with our mid-year amendments, funds will be used for unforeseen opportunities and to supplant operating needs as we approach the end of FY23. There are no contingencies changes recommended for the Stormwater Fund or Environmental Services Fund.

The total recommended adjustment in total budget for the enterprise funds is presented, as follows.

<b>Fund</b>	<b>\$ Change (Net)</b>
Water & Sewer Fund (060)	Increase \$410,900
Parking Fund (064)	No change
Stormwater Fund (067)	Increase \$6,080
Environmental Services Fund (068)	Increase \$295,013

The amendment detailing these changes is included with the agenda item.