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June 13, 2016

Dear Mayor Hemminger and Members of the Chapel Hill Town Council:

In accordance with the Local Government Budget and Fiscal Control Act, I hereby submit the adopted annual budget for the Town of Chapel Hill for Fiscal Year 2016-17.

Budget in Brief

The FY2016-17 Adopted Budget is balanced without an increase in taxes. The aggregate increase for all funds is 1.08% and the increase in the General Fund is 2.17%. We are projecting a moderate increase in overall revenues that includes increases in some economy driven revenues such as sales tax and decreases in others such as planning permits.

Technically the economy has been in a recovery for the past few years, but unfortunately the benefits of that recovery are not being felt in all sectors of the economy. In fact, there is growing sentiment among some economists that we will be moving from a weak recovery into another recession. Regardless of where the economy moves in future, the lessons of the economic crisis of 2008 still resonate. Financial resiliency, the ability to withstand financially stressful events, is the new standard for local governments. This includes building basic financial safeguards such as a strong reserves (fund balance), diversification of revenues, manageable debt levels and conservative budgeting practices. In addition, financial resiliency requires, among other things, transparency, flexibility and collaboration. These are strategies that we try to employ as we build the financial plans for FY17 and beyond.

The adopted budget makes major investments in strategies to achieve Council Goals including the following:

- **Affordable Housing** – The FY17 Budget continues to reflect the Town's commitment to affordable housing. Operational funding for housing initiatives, roughly equivalent to a penny on the tax rate, was first budgeted in FY15 and is being continued for FY17. An additional \$28,147 is being added to the performance agreement with the Housing and Land Trust based on the funding formula adopted by Council. Also included in this year's public housing program

budget is \$50,000 for development of a Public Housing Master Plan. We envision the Plan to include an assessment of the condition of all of the Town's thirteen public housing communities as well as strategies to create new housing and preserve our existing inventory; identify new ways to manage our public housing program; and recommend a funding plan to implement the strategies.

- **Human Service Agency Funding** – The Town's allocation for performance agreements with Human Service agencies has been the same for the past four years. The FY17 budget includes an increase of \$74,400 in funding to the Human Services Advisory Board and \$25,000 to the Visitor's Bureau.
- **Adverse Weather Response** – One of the most challenging situations for any local government to manage is adverse weather. Storms are unpredictable at any time of year and coordinating a response that emphasizes public safety while also addressing continuity of services and recovery can strain even the most comprehensive and well thought-out plan. For this reason, we treat every storm event as an opportunity to receive feedback, reassess our performance and adjust our plans. Winter Storm Jonas was our most recent opportunity to respond to an adverse weather event and while the overall performance of our team was consistent with our high standards, the nature and duration of the storm revealed gaps in our response plan. Changes we are making based on this experience include improving communications with the public, adjusting staffing deployment in preparation for a storm event and strategic use of contracted services. The FY17 Adopted Budget includes an additional \$30,000 for contracted services related to storm events.
- **Capital Investment Plan** – The successful bond referendum of 2015 has paved the way for funding many high priority capital projects. With the stated goal of managing capital expenditures within the existing capacity of the Debt Management Fund, the Town will begin issuing significant amounts of new debt in FY17. Careful coordinated project and financial planning allows the Town to invest these borrowed funds in infrastructure improvements and repay the bonds without increasing taxes. Over the next four years, issuance of about \$50 million of debt is planned, beginning with approximately \$22 million in FY17. Debt planned for FY17 includes funding for greenways, public safety facilities and streets and sidewalks.
- **Transit Sustainability** – In cooperation with its funding Partners, UNC and Carrboro, the Town has shifted its funding model for fleet replacement to reflect the loss of Federal funding. Using a combination of fund balance, grants and debt financing, Chapel Hill Transit has begun the process of "catching-up" with bus replacements. The FY17 Transit budget includes \$967,000 for financing bus replacements. By borrowing funds and spreading the cost of new buses over their useful life, we can begin the process of bringing the average fleet age within industry standards, thereby reducing breakdowns and maintenance costs. The recent Council approval of a Bus Purchase Agreement and a Bus Financing Agreement has paved the way for a major purchase of new buses to be delivered in

FY17. The 1.9% reduction in the FY17 Transit Operating budget is due to the unexpected receipt of \$934,000 in State grants and the adjustment of cost estimates based on current year actual numbers. As we plan for financial sustainability for public transit service in the future, however, we anticipate increases in required local funding.

- **Stormwater** – The Bond referendum approved in November 2015 included authority to issue \$5.9 million for stormwater improvement projects. After the completion of sub-watershed studies, that will assist in prioritization of stormwater improvements, the bonds will be issued over the next 7 years to fund the highest priority projects. As discussed in last year’s budget, a series of graduated rate increases over several years will be needed to address Stormwater Master Plan projects, including projects that will be funded through the authorized stormwater referendum bonds. The stormwater fee is unchanged for FY17.
- **Public Safety** - Planning for a multi-agency complex that could include Police, Fire, Parks & Recreation Administration and other Town Offices is currently in progress. The proceeds of the sale of 523 East Franklin are being used for the design costs of the new facility. The balance of the project costs will be funded through a combination of GO bonds and an installment financing. This project will also include costs related to the ultimate disposition of the current Police Headquarters Building. The site is a former coal ash dump and analysis to determine the required remediation and clean-up is currently ongoing.
- **Bicycle and Pedestrian Safety** –One recurring theme in the 2020 conversations and in Council Goals is the need to make the City “walkable” and friendly to cyclists. In addition to the near-term initiatives spearheaded by the Bicycle/Pedestrian Safety Team, creating a safer multi-modal transportation infrastructure is a key component of our strategy to make the Town a safer place to travel for everyone. The successful 2015 Bond Referendum includes \$7.8 million for bike and pedestrian safety projects, \$2.0 million for sidewalks and \$5.0 million for trails & greenways. This funding is the first installment of a long-term investment in better infrastructure that supports alternatives to motor vehicle travel and attracts future economic development.
- **Employee Compensation** – Maintaining competitive and stable compensation is a critical factor in recruiting and retaining excellent employees who provide the high quality services recognized routinely by the community in the community survey. For FY2016-17 we are splitting the employee salary adjustment, with a 2% increase in July and another 1.5% increase in January. We initiated this split in the current fiscal year to reduce the annual cost and also set the stage for implementation of pay for performance, as recommended by the Employee Compensation Task Force. While we continue to work on the pay for performance plan, we will keep this split in anticipation of its implementation.

- **Employee Wellness** – Since its inception in 2011, the Employee Wellness Program has helped reduce the rate of increase in the cost of employee medical insurance. For FY17 a spike in health insurance costs of 15.5% is contrary to the recent trend of stable rates. While this sharp break in a favorable trend is jarring, it is not indicative of the impact of the wellness program. Since the Town’s costs are based on experience, we can be negatively affected by a small number of high dollar value claims. Overall there is no indication that, as a group, employees are becoming less healthy; rather we have had several unfortunate high value claims in the same coverage period. We believe this is more of a statistical anomaly than a trend; however, we are carefully monitoring healthcare usage and the health insurance market so that we can be prepared if other cost control strategies become necessary.
- **Retiree Healthcare** – The Town’s liability for paying future retiree healthcare benefits, earned by employees hired before 2010, continues to play a role in the Town’s financial well-being. Beginning in 2017-18 the Town will be required to report this liability, which was last calculated as \$64 million by the Town’s actuarial consultant, on the face of our balance sheet. The Town has taken several positive steps in managing its liability, including setting aside a relatively small amount to pre-fund the liability. This has been accomplished most recently by setting aside a portion of available fund balance. We feel it is time to normalize our pre-funding contributions and for 2016-17 the Adopted Budget includes pre-funding contributions from the General, Transit, Parking and Stormwater Funds.

Budget by the Numbers

The following table compares the FY2015-16 Adopted Budget with the FY2016-17 Adopted Budget for all Town funds.

BUDGET SUMMARY – ALL FUNDS

Fund	FY16 Adopted	FY17 Adopted	Incr./Decr.	Incr./Decr. %
General Fund	\$ 61,701,000	\$ 63,039,000	\$ 1,338,000	2.17%
Transit Funds	21,773,354	21,449,037	(324,317)	-1.49%
Stormwater	2,363,388	2,366,284	2,896	0.12%
Parking Funds	2,701,200	2,694,007	(7,193)	-0.27%
Housing	2,091,821	2,442,116	350,295	16.75%
Debt Service	7,602,782	7,528,782	(74,000)	-0.97%
Capital Projects	853,856	898,434	44,578	5.22%
Other Funds	5,026,445	4,820,461	(205,984)	-4.10%
Total	\$ 104,113,846	\$ 105,238,121	\$ 1,124,275	1.08%
<i>Note: Includes intrafund transfers</i>				

- **General Fund** – A 15.5% increase in the cost of healthcare insurance and a 2% + 1.5% split salary adjustment account for the bulk of the 2.17% increase. The budgeting of a conservative amount of lapsed salaries, recognizing the fact that the Town will have vacant positions throughout the next budget year, helps to reduce the increase. Increases in sales taxes and utility sales taxes provide sufficient revenue to balance the General Fund Budget without the need for a tax increase.
- **Transit Fund** – The reduction in the Transit Fund Budget is due to reductions in cost estimates based on FY16 actual numbers. In addition the unexpected receipt of \$934,000 in State grant funds in FY16 helped reduce costs in FY17. The Transit budget also includes \$967,000 for debt payments on the purchase of new buses that will begin in FY17. With nearly half of the bus fleet at or past replacement age, funding replacement buses is a top priority and key recommendation of the Transit Sustainability Study.
- **Stormwater Fund** – Overall the Stormwater budget remains at approximately the same level as FY16. Increases in personnel costs are offset by reductions in operating and capital outlay costs. The FY17 adopted Stormwater budget is balanced with about \$158,000 of appropriated fund balance. No increase in the stormwater fee is included in the adopted budget for FY17, however additional rate increases totaling about \$5 per ERU will be needed to pay for planned capital projects in the next 5-7 years.
- **Parking Funds** – On-street Parking operations are expected to generate \$23,534 in revenues above the amount required to support operations. The additional revenue will be transferred to Off-street parking. The combined Off-street and On-street budgets are balanced with the use of \$27,431 of fund balance.
- **Housing** – The 16.8% increase in the FY17 adopted Housing Fund Budget is due to an increase in capital expenditures for roof replacements and funding for a Housing Master Plan. An appropriation of available fund balance will be used to fund these projects.
- **Debt Service** – The overstatement of expected FY16 property tax revenues makes the debt fund appear to decrease slightly in FY17. When compared to FY16 estimates the property tax revenue will actually be going up slightly reflecting a little less than 1% growth in the tax base. The excess of revenues over expenses in FY17 results in an addition to fund balance of about \$473,000. This addition to fund balance creates capacity for future debt.
- **Capital Projects** - This budget represents the “pay-go” portion of the Town’s Capital Funding Plan. While the adopted amount falls short of the \$1 million annual pay-go target, planned debt issuance will fund several high priority projects that might otherwise be funded through pay-go.
- **Other Funds** – The aggregate reduction in these funds, that include internal service and grant funds, is due in part to reductions in one-time expenditures.

The estimated General Fund revenues for FY17 reflect an increase in revenue sources that are driven by economic activity such as sales taxes and utility sales taxes. The following table shows the expected changes to major revenue categories in the General Fund:

GENERAL FUND REVENUES

Fund	FY16 Adopted	FY17 Adopted	Incr./Decr.	Incr./Decr. %
Property Taxes	\$ 29,970,000	\$ 29,535,000	\$ (435,000)	-1.45%
Sales Taxes	12,059,494	12,790,797	731,303	6.06%
Other Taxes	1,114,000	1,224,000	110,000	9.87%
State Shared Revenues	6,649,590	8,079,590	1,430,000	21.51%
Charges for Services	4,666,537	4,602,428	(64,109)	-1.37%
Licenses & Permits	3,213,451	2,917,986	(295,465)	-9.19%
Grants	782,114	780,614	(1,500)	-0.19%
Other Revenues	540,450	402,035	(138,415)	-25.61%
Appropriated Fund Balance	2,705,364	2,706,550	1,186	0.04%
Total	\$ 104,113,846	\$ 63,039,000	\$ 1,338,000	-39.45%

- **Property Taxes** – The decrease in property taxes budgeted for FY17 (comparing FY16 Budget with FY17 Budget) reflects an error in calculating the FY16 tax levy which overstated the FY16 property tax budget estimate. The FY17 Adopted Budget represents an increase over the expected FY16 revenues of a little less than 1%. This is consistent with the rate of property tax revenue growth for the past two years.
- **Sales Taxes** – Sales taxes continue to show strong growth. Based on year-to-date results, we are anticipating the growth rate will continue at about 6% into FY17.
- **Other Taxes** – The hotel occupancy tax is the main component of this category. They have shown steady growth in the past few years. Receipts for FY16 have exceeded budget by a significant margin. Due to concerns about the impact of HB2 on the North Carolina tourism industry we are not budgeting any growth over the FY16 expected receipts.
- **State Shared Revenues** – The increase in this category recognizes the growth in Utility Sales Taxes which have exceeded the current year’s budget estimate by more than 40%. The reason for this increase is the change in the distribution formula passed as part of tax reform legislation that went into effect FY15. The legislation applied the general sales tax rate to the sale of electricity, replacing the franchise tax.
- **Charges for Services** – The decrease in this category is due, in part, to a decrease in projected Planning fee revenues (Ephesus Fordham form code permits). Police, Public Works, Parks & Recreation and Library all expect a slight increase in revenues from charges for services in FY17.
- **Licenses and Permits** – The decrease in this category is due to a significant decline in Fire and Building permit revenue. This is offset somewhat by an expected increase in Planning special use and development compliance permits.
- **Grants & Other Revenues** – Revenues in these categories are expected to remain about the same as current year revenue for this category.
- **Appropriated Fund Balance** – The amount of fund balance used to balance the budget reflects, in large part, the available unspent funding from the previous fiscal year. The amount budgeted for FY17 represents about 4.3% of the FY17 Adopted

Budget revenues and is slightly higher than the amount of fund balance appropriated in the adopted budget for FY16.

The Adopted FY2016-17 budget maintains the existing tax rates. Since the last revaluation in FY10 the Town’s tax rate has increased 3 cents or 6.1%. That is less than 1% per year and less than the rate of inflation. The last increase in property tax rates was the addition of 1 penny for the Debt Management Fund in FY15 to kick-start the Town’s capital improvement program. In FY14 the Transit and General Fund rates were each increased by 1 penny to pay for increases in operating costs. The property tax rates since the last revaluation are shown in the following table:

Property Tax Rates

	FY09-10	FY10-11	FY11-12	FY12-13	FY13-14	FY14-15	FY15-16	FY16-17
General Fund	36.0	36.0	37.8	37.8	38.8	38.8	38.8	38.8
Debt Service	9.3	9.3	7.5	7.5	7.5	8.5	8.5	8.5
Transit	4.1	4.1	4.1	4.1	5.1	5.1	5.1	5.1
Total	49.4	49.4	49.4	49.4	51.4	52.4	52.4	52.4

Note: Tax rate is expressed as cents per \$100 of assessed valuation

Revaluation 2017 – In 2017 the County will conduct a revaluation of all real property in Orange County. The revaluation will update all property to its current market value. The new values will be reflected in the Town’s FY18 Budget. The Town is required by statute to declare a revenue neutral rate which is a tax rate that generates the same revenue as the prior year after adjusting for growth. The Council may decide to adopt a tax rate that is higher or lower than the tax neutral rate.

Council Goals






The starting point for building the Town’s annual operating budget is the development of Council Goals. At the 2016 Council Planning Retreat, we continued our discussion of Council Goals and specific budget challenges that we face for FY2016-17 and beyond. Based on our discussion, we refined and added to the goals that were developed during the 2014 Council Planning Retreat. Council Goals for FY16-18 and the initiatives that are planned to further those goals are attached.

Council Goals, along with status updates can be found on the Town’s website. These goals are intended to bridge the long-term vision of Chapel Hill 2020 process and the annual budget, helping to ensure that our incremental short-term decisions ultimately take us to the destination that we envisioned as a community.

We continue to live in a time of economic uncertainty and ongoing debate about the vision for the future and the refinement of that vision. Our unlimited ideas, new projects

and initiatives are balanced by limited resources. The process of policy choice is difficult. As we struggle to meet high expectations with limited resources we are constantly challenged to prioritize new strategic initiatives while maintaining core services at the high level expected in Chapel Hill. In FY17 we will be working on creating stronger connections between Council Goals and the measures we use to gauge our progress.

Council Goals:

☒		Create a Place for Everyone	☒		Develop Good Places, New Spaces
☒		Support Community Prosperity	☒		Nurture Our Community
☒		Facilitate Getting Around	☒		Grow Town and Gown Collaboration

Budget Challenges

Asset Management

The sale of Town owned properties is an important potential source of funding for major capital projects. The asset management initiative was designed to assess the value of some underutilized Town assets and leverage them in addressing critical core needs or Council Goals in facilities. This program has also led to opportunities for public-private cooperation and other creative reuse options.

- **523 East Franklin** - The recent sale of 523 East Franklin has generated about \$1.7 million that will be used for the planning and design of the new multi-function complex that will house the new Police Headquarters.
- **Hamilton Road Fire Station Site** - The Council approved a Memorandum of Understanding for a public-private redevelopment project for the Hamilton Road Fire Station, including a new fire station and private development, subject to subsequent approval by the Council of the development in its regulatory role. The arrangement will provide the Town with a new fire station and other economic benefits through the redevelopment of an underutilized site.
- **DHIC Project** – Repurposing underused Town properties can also serve to further Council Goals, such as affordable housing. The use of 10 acres of Town owned land as the site of a Low Income Tax Credit project has made it possible to add about 140 units of much needed affordable housing.



Capital Program Management

The Town has a significant backlog of capital projects that were deferred during the fiscal crisis. The delay provided an opportunity to refine priorities through the master planning

process. Now that the Town has capacity building in the Debt Management Fund we can start to implement the Town's Capital Improvement Program.

In addition to the \$40.3 million of General Obligation (GO) Bonds authorized in the November 2015 Referendum, the Town's CIP includes almost \$60 million of installment financing, pay-go and two-thirds bonds projects that we will be trying to fund in the next 7-10 years. In addition to Town financed projects, the Capital Program also includes the Rogers Road project that will be financed by the County with the Town paying a portion of the debt service. The following table is an estimate of the sources and uses of funds for the CIP in the next 7-10 years.

FUTURE CAPITAL PROJECTS Use of Funds & Source of Funds

Use of Funds:	Referendum Bonds	Installment Financing	Two-thirds Bonds	Pay-go
Referendum Projects	\$ 40,300,000	\$ -	\$ -	\$ -
Ephesus Fordham Phase 2-4		5,200,000		
Public Safety Projects		29,500,000		
FY17 Various Projects			1,700,000	
FY17 Pay-go				898,434
Bus Replacement		21,000,000		
Total	\$ 40,300,000	\$ 55,700,000	\$ 1,700,000	\$ 898,434

Source of Funds:				
Debt Management Fund	\$ 34,400,000	\$ 24,500,000	\$ 1,700,000	
Stormwater Fund	5,900,000			
Asset Management		5,000,000		
Synthetic TIF		5,200,000		
GF Operating Transfer				898,434
Transit Fund		21,000,000		
Total	\$ 40,300,000	\$ 55,700,000	\$ 1,700,000	\$ 898,434

- **Pay-as-you-go (pay-go) funding** – Annual General Fund transfer used for small and/or recurring projects that can be accomplished within the fiscal year. Projects may include on-going costs for major maintenance of facilities and projects that can be divided into small annual segments.
- **Two-thirds Bonds** - Used for eligible high priority projects that have relatively short timelines and are too large for pay-go. Projects may include major equipment purchases, facility and infrastructure improvements.
- **Installment Financing** - Used for priority projects that are essential and for which adequate collateral is available. In cases where collateral for an installment financing is sufficient to cover multiple projects, combining financing is a useful tool to fund projects that would otherwise be problematic to fund. Projects may include construction, renovation or major repair of essential facilities and major equipment and vehicles purchases.

- Public Safety Projects are generally considered “essential” for financing purposes and thereby can be funded by an installment financing using the new facility as collateral.
- **GO Bond Referendum** – Voters approved the November 2015 referendum, passing all five bond orders by wide margins. The Town now has the authority to issue these bonds within the next 7-10 years. The \$40.3 million of authorized referendum bonds include \$34.4 million of General Fund Projects and \$5.9 million of Stormwater projects.
 - **Bond Orders** - The approved bond orders (categories of projects that will be presented on the ballot) include projects that have been prioritized through the Town's internal review process. The bond order categories and project dollar amounts are as follows:
 - **Streets & Sidewalks**

▪ Bicycle & Pedestrian Safety	\$ 7,800,000
▪ Sidewalk Construction	2,000,000
▪ Street Infrastructure & Bridge	3,400,000
▪ Downtown Streetscape	<u>3,000,000</u>
Total	\$ 16,200,000
 - **Trails & Greenways**

▪ Morgan Creek Trail	\$ 3,000,000
▪ Bolin Creek Trail/Tanyard Branch	<u>2,000,000</u>
Total	\$ 5,000,000
 - **Recreation Facilities**

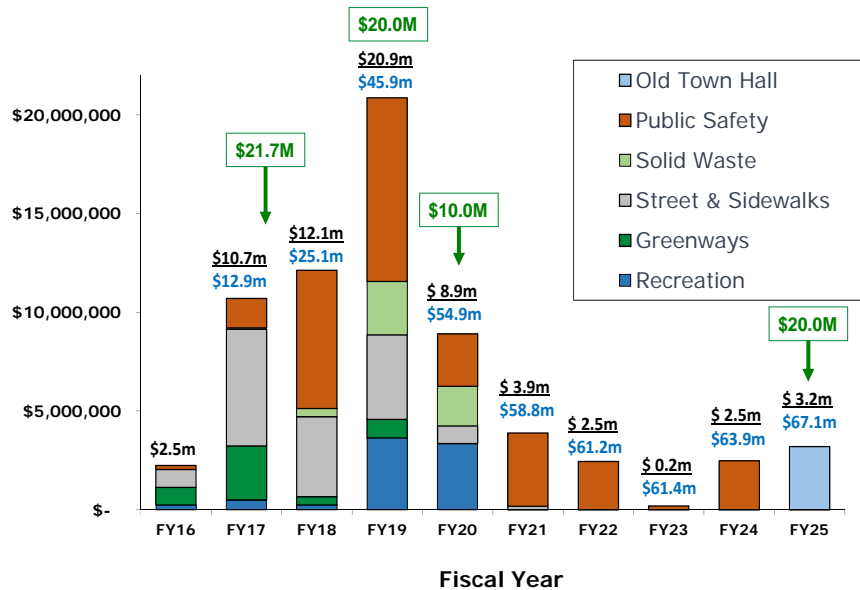
▪ Administration Building	\$ 3,600,000
▪ Cultural Arts Building	3,400,000
▪ Park Renovations	<u>1,000,000</u>
Total	\$ 8,000,000
 - **Solid Waste Facilities** **\$ 5,200,000**
 - **Stormwater Improvements** **\$ 5,900,000**

Note: the projects noted above are for planning purposes only. Council has the discretion to change projects within the dollar amount and stated use for each bond order.

Unfunded Projects

The following graph represents the planned cash flow for debt funded projects for the 10 year period beginning FY16. The bars represent the planned expenditures by use of funds and the dollar amounts at the top of the bars are the annual and cumulative expenditures. The green numbers in the box are the planned debt issues. This plan is designed to pay for maximum amount of the capital program without exceeding the current capacity of the Debt Fund. In other words, this scenario does not necessitate a tax increase.

Planned Projects Cash Flows



This scenario only includes projects that are currently in the capital plan. It does not include the following projects which are being considered:

- Fire Station 4 and Training Center Replacement
- American Legion Property
- 415 West Franklin Project
- Glen Lennox Public Improvements
- Police Station Coal Ash Mitigation

The estimated total dollar amount of these projects is well over \$30 million and there is currently no additional capacity to absorb these projects unless significant changes are made to the priority of existing projects or the Debt Fund tax is increased.

Employee Compensation

The Town is a service based organization that relies on a skilled and flexible workforce to deliver a broad scope of governmental services. Personnel related costs account for 71.1% of the FY17 General Fund Adopted Budget. The costs of maintaining a high performing workforce are increasing as the competition for labor increases. In recent years we have seen increased turnover including a significant increase in retirements. The Town's Turnover rate (about 8%) is typical for local governments in our region. The Town can stay competitive in the labor market by maintaining its comprehensive benefits package and through annual salary adjustments.



The FY17 Budget includes a salary adjustment that is split into two parts, with a 2% increase in July and another 1.5% increase in January. By splitting the increase we

reduce the annual cost and also set the stage for implementation of a pay for performance system by separating future pay adjustments and pay for performance increases. Moving toward a performance based pay system and maintaining salaries that are competitive with the market are consistent with the recommendations of the Compensation Task Force.

	Pay Adjustment	One-time Payment	Health Ins. Increase
FY2008-09	3%	0	10.0%
FY2009-10	0	0	17.1%
FY2010-11	0	\$800	13.9%
FY2011-12	0	\$800	10.1%
FY2012-13	3%	0	(3.0%)
FY2013-14	2%	0	4%
FY2014-15*	3%	0	7.0%
FY2015-16*	2% - 2%	0	(8.5%)
FY2016-17*	2% - 1.5%	0	15.5%

* Increase calculated from market (mid-point) for each grade

Living Wage

The FY17 Adopted Budget includes additional funding to pay for changes to the Town’s Living Wage Policy that Council amended to comply with the Orange County Living Wage (OCLW) standard. The policy changes mostly affect seasonal, part-time and temporary workers in the Parks and Recreation Department. New employees in the effected positions will have a minimum starting wage of \$10.00 per hour. After 90 days on the job these employees will be subject to a \$12.75 per hour minimum pay rate. The budget impact of these changes add about \$140,000 to the Parks and Recreation Budget for FY17. A portion of this cost will be offset by increases in fees.

Employee Health

As shown in the following graph, after several years of moderate increases including an 8.5% reduction in FY16, our rates will jump significantly for FY17. While this reverses the favorable trend over the past 4 years, it does not negate the progress made in the Town’s Wellness @ Work Program. The spike in rates is due mostly to a small number of high cost cases rather than an increase in usage for the plan membership as a whole. This is encouraging for long-term prospects of controlling healthcare coverage costs, but in the short-term a 15.5% increase is significant budgetary setback.

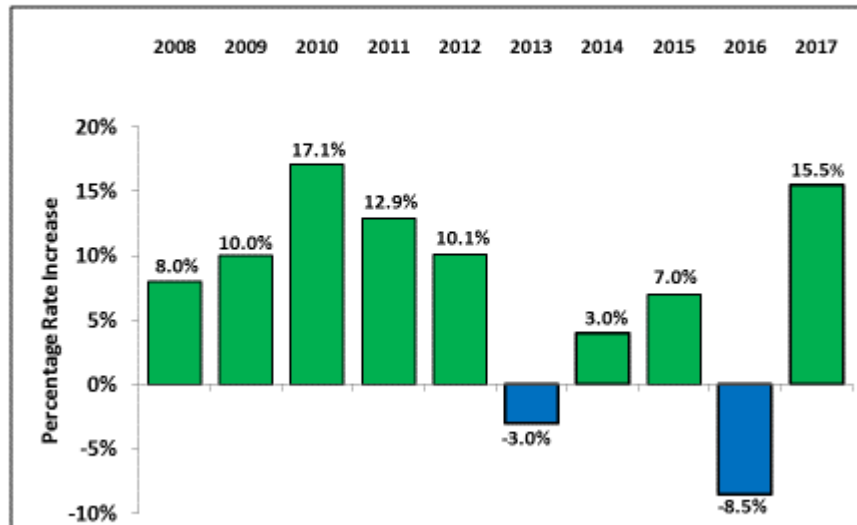
After several consecutive years of double digit increases the Town needed to find a way to control healthcare costs. The easiest and quickest path to controlling costs would have been to ration healthcare for our employees. This is a path that many other businesses and local governments have taken, basically solving the problem by transferring the cost to their employees. While this may have been an effective solution financially, the long-term impact on the Town’s workforce would have been detrimental. Rationing healthcare simply does not create a more healthy and productive workforce. In fact it does the opposite. Rather than taking the easy short-sited approach, the Town embarked on a wellness initiative designed to identify and treat chronic illnesses, reach-out to

employees who may be medically underserved, and help make our employees make good healthcare and lifestyle decisions.

The Chapel Hill Wellness @ Work Program is a comprehensive wellness program for the employees of the Town of Chapel Hill. The program is a partnership between the UNC Health Care Department of Family Medicine and the Town of Chapel Hill. The success of this program is a direct result of this partnership and the work of the Wellness @ Work Committee.

The recent reversal of a positive trend in medical insurance premiums is disappointing, but improving employee health is the most important outcome of the program. The FY17 adopted budget continues these efforts by encouraging participation in the HRA program by giving a discounted employee medical insurance rate for program participants.

Medical Insurance Cost Increase from Prior Year



Performance Agreements

The Town’s operating budget includes funding for performance agreements with outside agencies that provide services consistent with the Town’s goals and values. We have maintained approximately the same overall level of funding for these agreements over the past 6 years. For FY17 we have allocated an increase of \$74,400 in the funds that are allocated based on the recommendations from the Human Services Advisory Board.

Applications for human service agencies are processed through a joint application process with Orange County and the Town of Carrboro. The human service agency applications are evaluated by the Human Services Advisory Board who make

recommendations to Council for funding. All other agencies are evaluated by a cross-departmental staff team. The adopted amounts are shown below.

Performance Agreements with Outside Agencies	2015-16 Adopted Budget	2016-17 Adopted Budget
Human Services	\$ 337,100	\$ 411,500
Environmental	1,000	1,000
Arts	20,500	23,000
Affordable Housing	361,238	379,557
Economic Development	260,000	280,000
Total Performance Agreements	\$ 979,838	\$ 1,095,057

The affordable housing agency funding includes a \$328,561 allocation to the Housing and Land Trust. This represents an increase of \$28,147 from the FY16 performance agreement. This increase is based on the interlocal agreement, authorized by Council April 13, 2015, with the Towns of Carrboro and Hillsborough and Orange County formalizing the long-standing relationship with the Community Home Trust. The purpose of the Agreement is to: 1) clarify the responsibilities of the Towns, the County and the Community Home Trust; and 2) provide a formula to provide financial support of the Home Trust’s administrative operations based on the number of Home Trust units in each jurisdiction.

We have discussed the Agreement with our partners and with the Community Home Trust. We believe that the Agreement provides sufficient guidance for our partnership with the Community Home Trust and do not recommend changes at this time. We will continue to review the agreement on an annual basis and recommend modifications for consideration as appropriate. In addition to the performance agreement amount, the Community Home Trust has also been allocated \$50,000 of the Town’s FY17 CDBG funds.

The economic development agency funding includes \$200,000 for the Convention and Visitor’s Bureau, an increase of \$25,000 from FY16. Their contract includes a clause that increases their funding if the Town’s Occupancy Tax receipts exceed \$950,000 for the fiscal year. The Bureau will receive 50% of all receipts in excess of \$950,000. Also included in economic development agencies is a \$70,000 allocation to the Downtown Partnership for services in the Downtown Municipal Service District (MSD). The Downtown Service District Budget also includes \$120,000 for services in the (MSD).

Technology Initiatives

The use of a Technology Pool funding mechanism for technology projects and creation of

a Business Analyst position in IT to evaluate and facilitate technology projects has allowed a more thoughtful and deliberate investment in new technologies. The most recent allocation from the Technology Pool included funding for projects ranging from an upgrade to Library management software to equipment that counts the number of users on Town trails. Both of these projects interface with the public and help maximize the use and utility of Town assets.

One of the Town's on-going technology challenges is to effectively support a diverse and growing base of over 650 users. This has become more challenging as we deal with competing demands for higher levels of security to protect confidential information and the need to embrace open data concepts to provide higher levels of transparency by making Town data available to everyone. To assist in the coordination of security and user-support efforts, two technology positions in the Police Department will be moved to Technology Solutions. This change is reflected as an increase in the personnel costs in Technology Solutions and a decrease in Police.

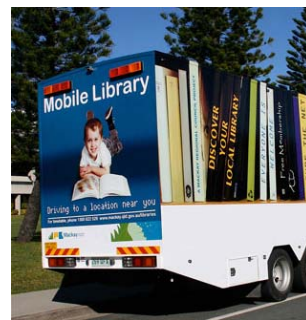
Closing the digital divide – getting all Chapel Hill residents online – has been an ongoing priority that requires a multipronged approach. The key to effectively leveraging our fiber assets to create a more level digital playing field is to build relationships with organizations that share our interests, such as UNC, the School District and Carrboro. Through these partnerships Chapel Hill is working on a variety of fronts to ensure residents have access to internet, access to computer equipment, and access to digital literacy educational opportunities.

Library Operations / Youth Services

User Experience – In FY17, the Library will implement a year-long, \$100,000 federal grant project focused on improving the User Experience (UX) at the Library and giving staff skills to continue to do so after grant cycle complete. Focusing on UX helps achieve the goals of the Library: increase access, decrease barriers, raise awareness, develop customers, and become a place for everyone.

Open Data – Public libraries are trusted community institutions who make information freely available to all. As such, CHPL is shepherding the creation of an Open Data Portal for the Town. We anticipate an internal launch in May and public launch in June.

Library Outside the Library – In addition to longstanding outreach services to schools and community partners, we are focusing on ways to get out into the community even more. Exploring external funding options for a “Pop Up” Library/21st century bookmobile.



Youth Services – In our FY16 Business Plan, we identified teens one of our key constituencies to focus on. Here's what's happening:

- **Teen UX** – As part of the UX project, CHPL has been collecting data, observing behavior, and directly engaging teens. In FY2016, we have refined our understanding of their wants, needs, and interests, and in FY2017 we will begin making improvement to the collections, services, and spaces we offer them based on that understanding.
- **Teens of Chapel Hill** – A working group of TOCH staff who work with teen populations, facilitated by Stephen Ashley, Teen Engagement Coordinator. Comprised of key staff from Library, Parks & Rec, Housing & Community, and Police, the group meets monthly. Goals are increased communication and collaboration. They are currently working with CAPA on a website to provide information to teens about Town-sponsored events and opportunities.

Transit Sustainability

Chapel Hill Transit (CHT), like most transit systems, relies heavily on State and Federal funding in order to maintain operations. The lack of reliable Federal funding for bus replacement has created a critical maintenance issue for CHT. Currently 42 of the 99 fixed route-buses are beyond their useful life and all of the 19 demand response vehicles are beyond their useful life. In order to maintain CHT without significant reductions in fleet size and service levels, an alternative to Federal funding of bus replacements is being implemented. By borrowing funds and spreading the cost of new buses over their useful life, we can begin the process of bringing the average fleet age within industry standards, thereby reducing breakdowns and maintenance costs.

Beginning with the FY15 budget, funds have been set-aside in the Transit Capital Reserve funding to pay debt service for the financing of new bus purchases. The FY17 Transit budget includes \$967,000 for financing bus replacements. The successful negotiation of long-term commitments for debt repayment with CHT's funding partners makes the financing of buses a feasible strategy to renew the fleet. The recent Council approval of a Bus Purchase Agreement and the Bus Financing Agreement have paved the way for a major purchase of new buses which will be delivered in FY17.

The FY17 CHT Budget shows a 1.9% reduction in expenditures compared to the FY16 budget. This is due to the unexpected receipt of \$934,000 in State grants and the adjustment of cost estimates based on current year actual numbers.

During FY17, we will also begin serious discussion with UNC and Carrboro about the sustainable financial future of public transit in our community. Our partnership has reached the point when we must review all of our financial and governance arrangements in light of today's financial stresses. The results of these discussions could have tremendous effect on future budgets.

Stormwater Fund

In order to keep pace with needed stormwater improvements it became necessary in FY14 to begin increasing the stormwater fee to meet current and future needs. Prior to FY14 the rate had not changed since the inception of the fund in 2004, despite a 40% increase in the operating budget. Also, the size of the Equivalent Rate Unit (ERU) was reduced in FY14 from 2,000 to 1,000 square feet.

For FY16 an additional \$1.40 per ERU was added to the Stormwater Fee to help address capital needs, including the need to pay debt service on General Obligation Bonds that were approved in November 2015. For FY17 there is no increase in the Stormwater fee because of the need to complete subwatershed studies before major capital projects are undertaken.

Fund Balance

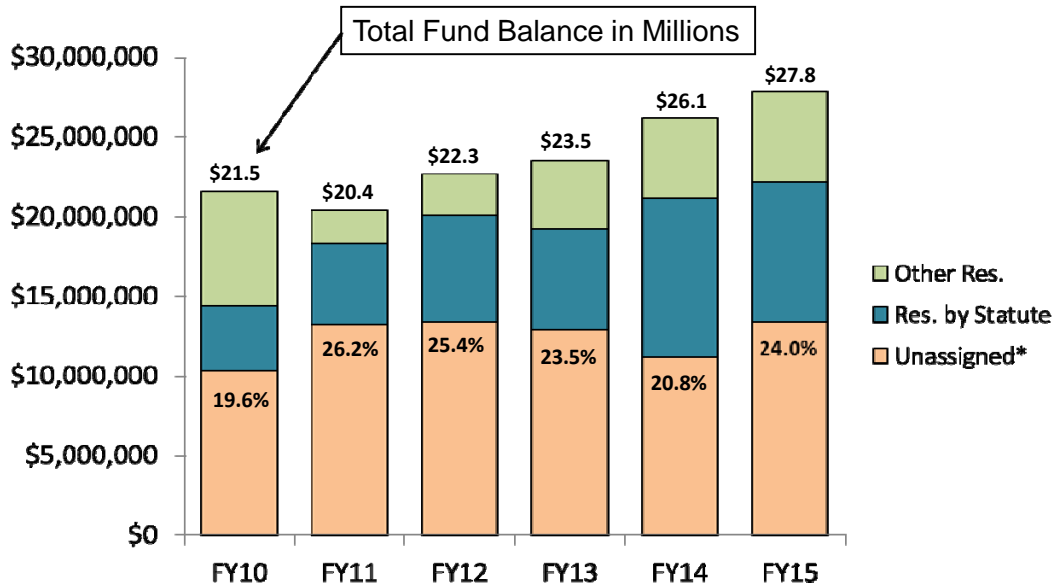
The Town has maintained a strong and consistent General Fund fund balance (see graph below) over the last 7 years. In order to help address the Town's capital needs and to create a funding mechanism for the Town's long-term liability for retiree healthcare, we recommended in FY15 that unassigned fund balance (the portion of fund balance available for appropriation) over 22% be split between high priority capital investments, such as Rogers Road, and funding for the retiree healthcare liability (OPEB).

The establishment of 22% as a fund balance "floor" for the purpose of allocating excess fund balance is based on the following:

- 22% fund balance (\$11 million) would provide about 2.5 months of operating funds for the Town's General Fund.
- Based on the timing and dependability of Town revenue sources, 22% provides adequate operating funds to avoid borrowing for operating cash flow needs.
- Although 10% has generally been considered the floor for purposes of satisfying the Local Government Commission and bond rating agencies, the experience of many municipalities during the fiscal crisis has demonstrated that 10% is insufficient.

Total GF Fund Balance

FY10 thru FY15



* Unassigned fund balance is calculated as a percent of expenditures and other uses per audited financial statements

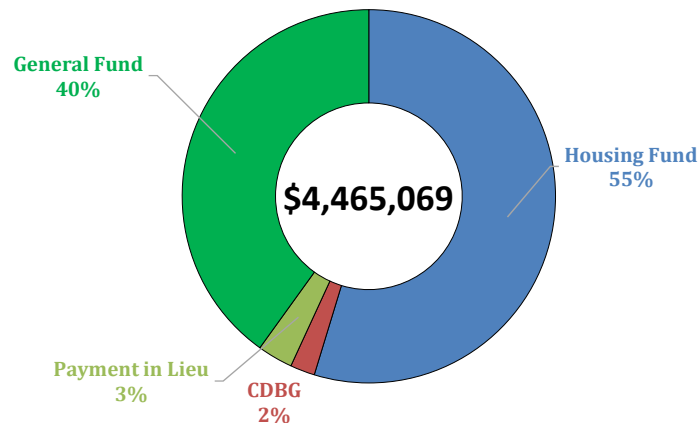
Maintaining an adequate level of fund balance is critical to meet the cash flow requirements of this municipal corporation and to provide an emergency fund to safeguard the Town against the costs of recovering from unforeseen economic, emergency and natural disasters. The Town’s high fund balance levels are a positive factor in assigning credit ratings to the Town’s debt. The Town has continually received the highest possible rating for its general obligation bonds.

The FY17 Adopted Budget seeks to keep the use of fund balance to a manageable level and uses \$2.7 million of fund balance, about 4.3% of total revenues, to help balance the budget. We believe that this is an appropriate and sustainable level of fund balance use.

Affordable Housing

The Town’s total investment in affordable housing for FY17 is \$4,465,069 as shown in the following graph. This includes all planned expenditures for Public Housing Fund, the Housing and Community Department, grant funds and performance agreements with outside agencies.

FY17 AFFORDABLE HOUSING INVESTMENT



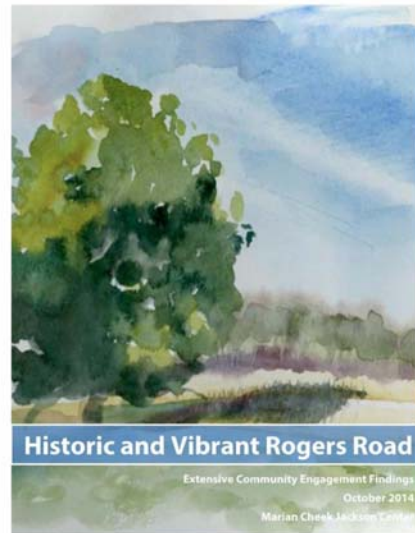
Recently initiated affordable housing projects include:

- **Northside Community** - Leaders from the Town of Chapel Hill and the University of North Carolina at Chapel Hill (the University) announced in March of 2015 a major investment in the future of the Northside neighborhood. The investment - a \$3 million no-interest, 10-year -loan from the University and annual funding from the Town of Chapel Hill for administration of that investment – will allow Northside and community partners to achieve a shared vision for the historic neighborhood: a family-friendly, socially-connected community where long-term residents, new owners, renters and students can live together.
- **Penny for Housing** - The Town of Chapel Hill's adopted FY17 Budget includes \$688,395 to support affordable housing development and preservation, an amount equal to nearly one penny of the property tax rate. These funds will be allocated through the Affordable Housing Development Reserve (AHDR) consistent with the Town's Affordable Housing Strategy.

We plan to embark on an effort to work with Council to establish performance measures for critical high priority Council Goals as a way to set a clear path, evaluate results and focus resources. Because of the critical importance of the affordable housing goals for our community, we intend to begin there and apply what we learn in the process to other Goals.– We also hope to start with affordable housing because of the opportunities generated by the Rosen study underway for critical areas in our Town and the renewed commitment by our housing professionals in the nonprofit and governmental sectors to work together to learn from our past experiences and apply that learning to new initiatives. These opportunities for initiatives and thinking differently are provided by community first planning in the development of the Rogers Road area, including the Greene Tract, as well as the assessment of the Town's inventory of public housing neighborhoods.

Rogers Road

The Town has contributed about \$610,000 toward the construction of the Rogers Road Community Center and preliminary engineering (phase 1) and sewer engineering design (phase 2) for extension of sewer service to the Rogers Road community. The engineering and easement acquisition work will be completed in FY17 and the award of the construction contract should also take place in FY17. The financing plan calls for the County to borrow the cost of construction and connections, approximately \$6.6 million, with a 20 year payback term. A basis for distribution of the costs of construction and connections is currently being worked out. It is estimated that the project will take a minimum of two years to complete.



Parking Fund



The FY17 Parking Fund Budget is balanced with the use of \$26,349 in fund balance. This is the second year in a row that the fund has been at or close to break-even after several years of significant deficits following the issuance of debt for the 140 West parking structure. A period of fund balance spend-down was expected in the transition of Lot 5 to 140 West, however the addition of unexpected capital repair costs and a slower ramp-up of revenues from new facilities prolonged the period during which the fund ran budgetary deficits.

In FY16 the practice of transferring excess on-street parking revenue to the General Fund was stopped and these funds are being used to support off-street parking operations. While the Parking Fund has achieved a balanced operating budget there are still major capital improvement challenges to be addressed, including repairs to the Wallace Deck roof to fix ongoing water infiltration problems.

In order to meet changing parking demands in the Downtown, the Parking Enterprise needs to look at different strategies and service delivery models to better match parking supply with demand. The experience of parking should not be a barrier to people visiting downtown. With the assistance of the Downtown Partnership and other parking stakeholders, the Parking Enterprise, under the supervision of the Police Department, will continue to engage the community and industry experts to fulfill their goal of building a sustainable parking system that supports the commerce and vitality of Downtown.

Conclusion

A major focus of the FY17 Adopted Budget is the implementation of a comprehensive capital program that addresses public facility and infrastructure needs that have been underfunded in the years subsequent to the financial crisis of 2008. In many ways the Town is playing catch-up in key capital areas such as replacing public service facilities, providing bicycle and pedestrian amenities in the public right-of-way and replacing buses. While we move forward to address these needs, new needs and opportunities arise challenging our ability to prioritize from among numerous worthwhile projects and stretching our capacity to fund high-priority projects.

The development of an annual budget requires equal parts thoughtful reflection and hard work. The reflection part takes the form of planning, strategizing and assessing past results. The work part entails building the thousands of individual assumptions, estimates, and calculations into a cohesive whole that represents a positive step in the direction articulated by Council. These two activities coexist in an inclusive process that culminates in this document, the Adopted Budget. It is sometimes easy to lose the thread that ties Council goals to the minutia of an operating budget as it attempts to bind strategy to initiatives to service delivery to outcomes using only words and numbers. In FY17 we will be working to strengthen that connection between Council goals and the results of our efforts by identifying and tracking key indicators that help us measure our progress toward the future expressed in those goals. To assist us in that effort we will be asking Council to help us think about what success looks like and what how movement toward our goals will change specific characteristics of Chapel Hill.

The budget is the tool we use to move toward a future based on our shared vision. But, moreover, the budget is about choices. Choices dictated by factors both within and outside of our control. Our ability to understand, manage and anticipate these factors is greatly enhanced by our ability to build trust and respect through open communication and the participation of the public in our planning, goal setting and decision making processes. The choices reflected in the Adopted Budget represent our best efforts to move forward toward achieving Council Goals. The 2016-17 Adopted Budget keeps the Town on its path toward sustainably achieving the long term goals of the community.

Respectfully Submitted,

A handwritten signature in black ink, appearing to be 'R. S. D.', written in a cursive style.

