

BOROUGH of CHATHAM

STRATEGIC FINANCIAL MANAGEMENT PLAN

(Change the financial planning model from an annual process to the multi-year process)

Chatham Borough Finance Committee

Original – January 27, 2014

Revised - October 13, 2015

Revised - October 11, 2016

Revised - September 11, 2017

Situation Analysis

In October 2012, the Chatham Borough Finance Committee discussed the concept of developing a strategic financial management plan. Before embarking on the plan preparation phase, the Finance Committee and the Administrator identified the plan goal and the measurement systems for the achievement of the plan goal. The goal of the strategic management plan is: “Change the financial planning model from an annual process to the multi- year process.” Recognizing the importance of developing a multi-year strategic financial management plan, the Chatham Borough Finance Committee and governing body have stated their commitment and understanding that the traditional annual preparation of the municipal budget is a short term financial planning tool and there is a need to explore the benefits of developing a multi-year strategic financial management plan.

The municipal government is required by New Jersey law to collect the taxes that fund Chatham Borough, Chatham School District and Morris County operations. The Chatham Borough Council does not have statutory authority for input or oversight for that portion of the total tax levy that funds the Chatham School District and Morris County operations. The strategic financial management plan does not include the tax projections for the schools and county. Each year the Chatham Borough budget presentation includes one slide that depicts a one dollar bill that is divided into three parts. The three parts are the percentage of the tax dollar that is apportioned to the schools, Morris County and the Borough of Chatham: 63.32% for schools, 19.53% for the Borough of Chatham (includes Open Space) and 15.15% for Morris County. The strategic management plan is focused on municipal operations and capital improvements, that portion of the property tax bill that the Chatham Borough Council does have the authority to decide:

- Residential property taxes
- Types of services
- New debt
- Borough infrastructure improvements & maintenance
- Future financial liabilities
- Debt obligations and the annual debt service payments
- User based fees to determine if the fees adequately cover the actual expenses that are necessary to support current service levels

Keep in mind that the strategic financial management plan is a systematic method to avoid the financial cliff through measured financial performance over time. Absence of a strategic financial management plan may eventually lead to any one or a combination of the following:

- Unexpected immediate employee terminations
- Reduction of municipal office hours
- One time revenue sources from the sale of Borough assets, applied to the current year budget for the purpose of reducing taxes
- Service reductions
- Lowering of the municipality's bond rating

The strategic financial management plan is designed to identify potential future financial issues, which will allow the governing body to adequately develop alternatives that will avoid the need for emergent chaotic reactions.

Municipalities that are similar to Chatham Borough that are fully developed have limited opportunities for ratable expansion. Developing municipalities have the benefit of adding new ratables annually. Chatham Borough has and should continue to limit expanding government services during the ratable expansion periods.

Budget, Debt & Taxes

The municipal budget is the backbone for municipal operations and services. The budget is the municipality's financial plan for the current year. The municipal budget is divided into two components: revenues and appropriations. The sixty percent of Chatham Borough's budget is supported by property taxes. The Finance Committee recognizes that property taxes generate the largest revenue component of the Chatham Borough budget.

The Finance Committee decided that the current process for the preparation of the annual municipal budget is a short term financial planning method. Business accounting systems are "accrual accounting", any debt including pension obligations are counted as an expense. Broadly speaking, government accounting systems are "cash accounting"; expenses are not actually counted until cash is paid. New Jersey has adopted "modified cash accounting", expenses are actually counted when incurred and revenue when cash is received. Over the last five years; states, counties, cities and local governments have been faced with pension liabilities that are underfunded. One of the reasons is that the government accounting system did not recognize future liabilities and did not plan for or identify the revenue streams that would support those liabilities. In other words and for the most part, **the government accounting system is blind when it comes to future liabilities.** Most government accounting systems are designed to focus on fraud. The systems are inherently

short term and short sighted. The preparation of the multi-year strategic financial management plan should not be thought of as a rigid rule based document designed for control and fraud detection, but rather a budget planning document that identifies future financial trends that are not based on past data.

The Finance Committee recognizes that multi-year financial management planning is an excellent model to anticipate the future financial conditions that would affect municipal taxes, operations and Chatham Borough's current Aaa bond rating. The Borough's strengths to maintain the current Aaa bond rating are:

- Strong wealth levels
- Strong cash and financial reserves
- Moderately sized tax base with proximity to New York City
- **Development of a multi-year strategic financial management plan**
- Current revenue sources other than property taxes

The challenges are:

- Weather related expenditures
- Consecutive draw downs of financial reserves
- Restricted revenue raising ability due to the statewide 2% tax levy cap
- New revenue sources

The factors that could cause the Borough's bond rating to go down are:

- Ongoing economic and tax base declines
- Multi-year operating deficits that continue to reduce Current Fund reserves
- Significant increase in debt burden
- Artificially holding the tax rate to levels that will create future tax rate spikes

Evaluation, Analysis and Monitoring

The following financial information was analyzed and evaluated:

1. Multi-year department budget forecasting. (personnel, operating and capital expenses)
2. Future debt service and budget impact.
3. Future fixed costs. (health & pension expenses)
4. Surplus & Reserve for Uncollected Taxes. (past & future)
5. 2015 Audit Report.
6. Debt comparisons of other municipalities.

7. Continued annual monitoring systems design. (annual comparative analysis of projected costs to actual expenses, the graphs that follow are the monitoring mechanisms)

Chart #1 – Reduce the five year annual average for capital spending from \$2,030,622 to \$1,000,000 or 50%, reducing the total debt over ten years (2015-2023) approximately \$4,764,636 or 31%

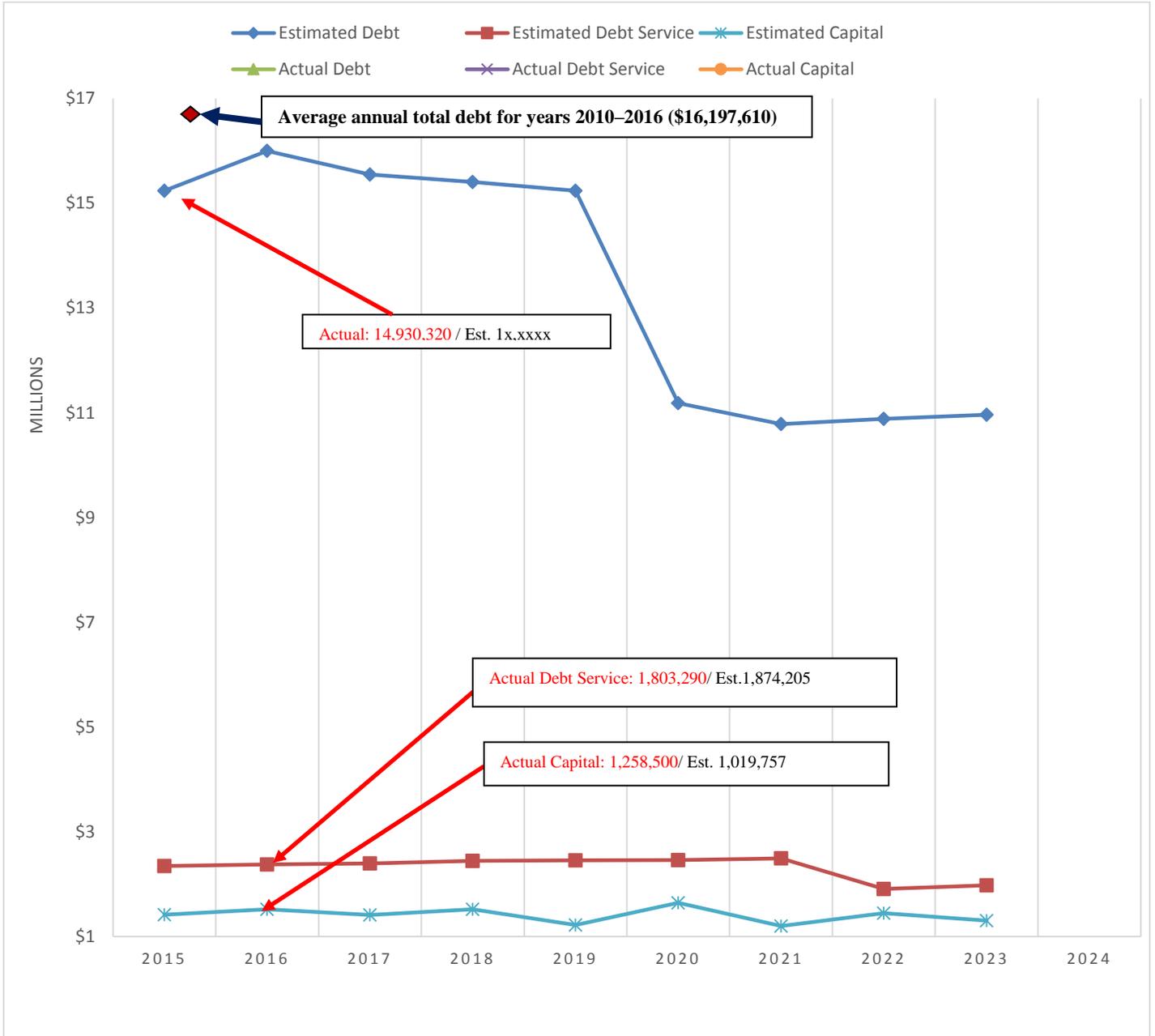
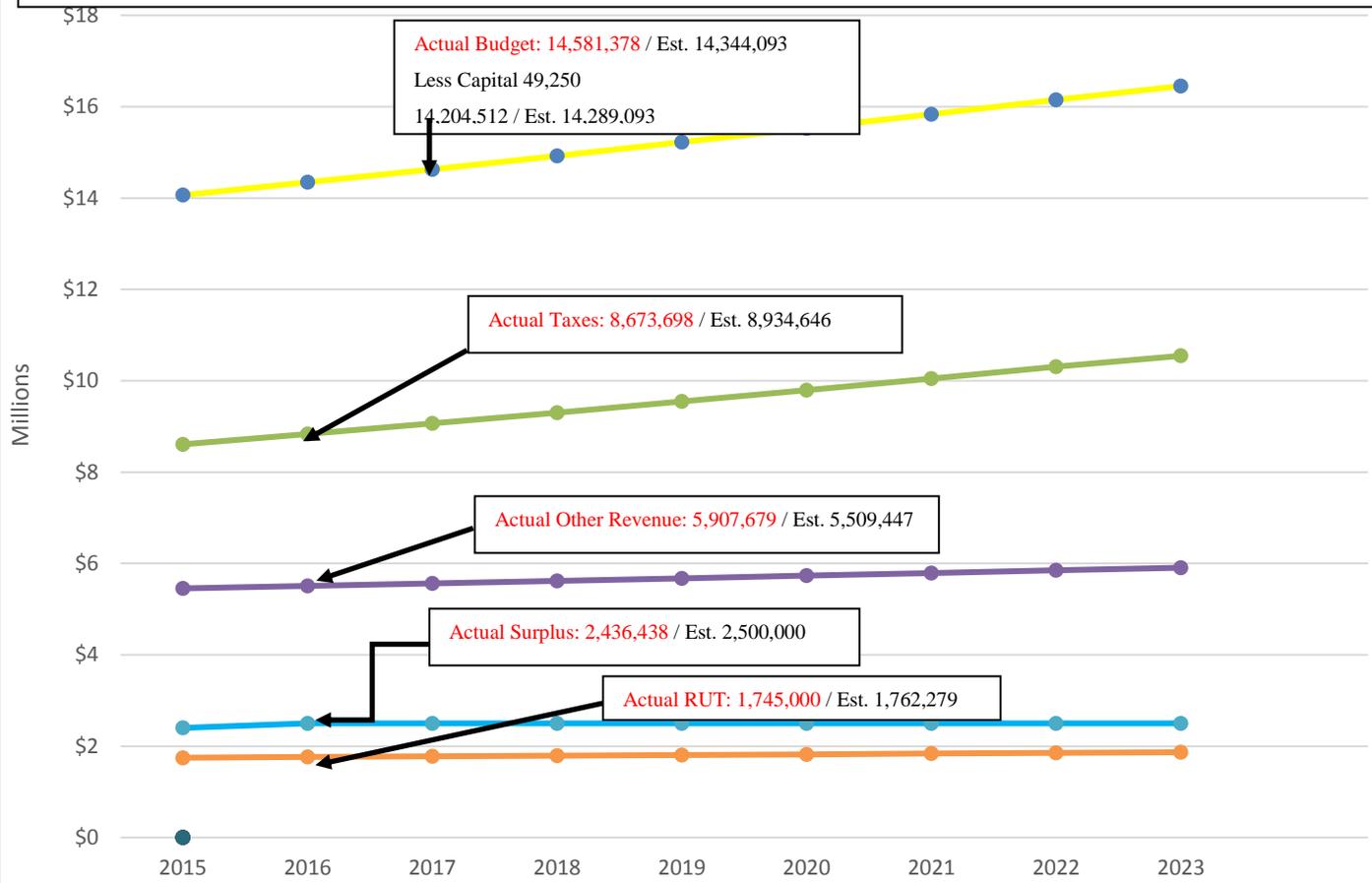


Chart # 2

Amount to be raised by taxation

Except for the debt service schedule, the annual budget increase assumption is 2%. To establish the amount to be raised by taxation, the general revenue assumption (1% annual increase assumption included for each year) is deducted from the total budget. The difference is the amount to be raised by taxation. Surplus is anticipated to increase from \$2,000,000 in 2014 to \$2,500,000 in 2023 – **Approximately an increase of 25%**



- Estimated Budget
- Estimated Taxes
- Estimated Other Revenue
- Estimated Surplus
- Estimated Reserve for Uncollected Taxes
- Actual Budget
- Actual Taxes
- Actual Other Revenue
- Actual Surplus
- Actual Reserve for Uncollected Taxes

Referenced: New Jersey Department of Community Affairs

Chart #3

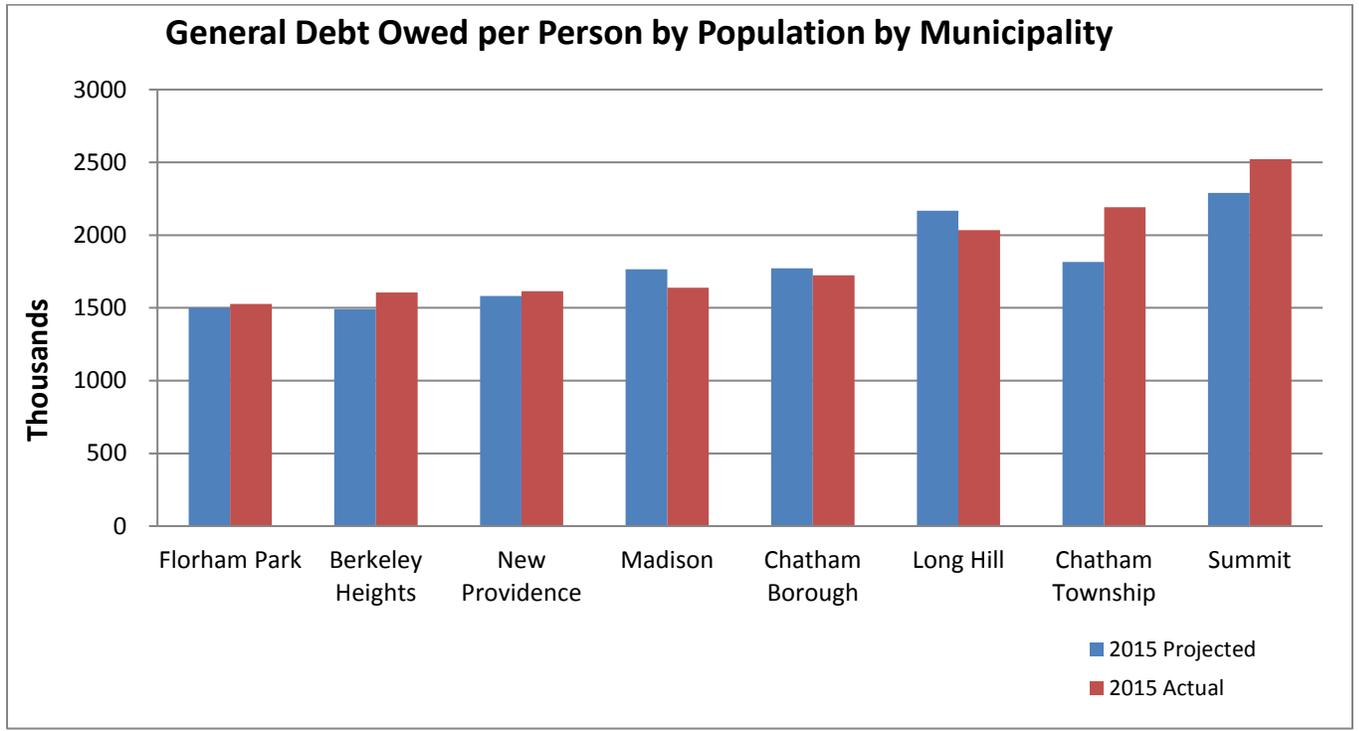


Chart #4

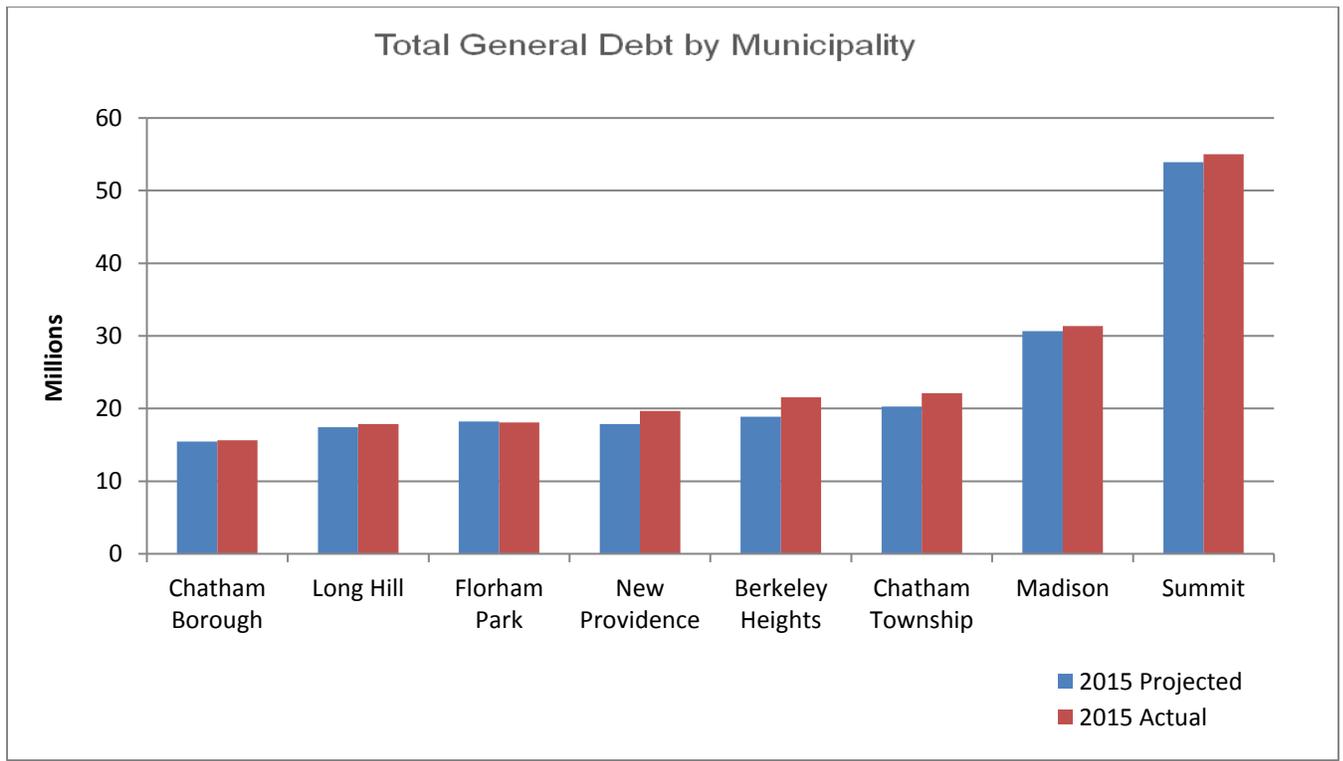
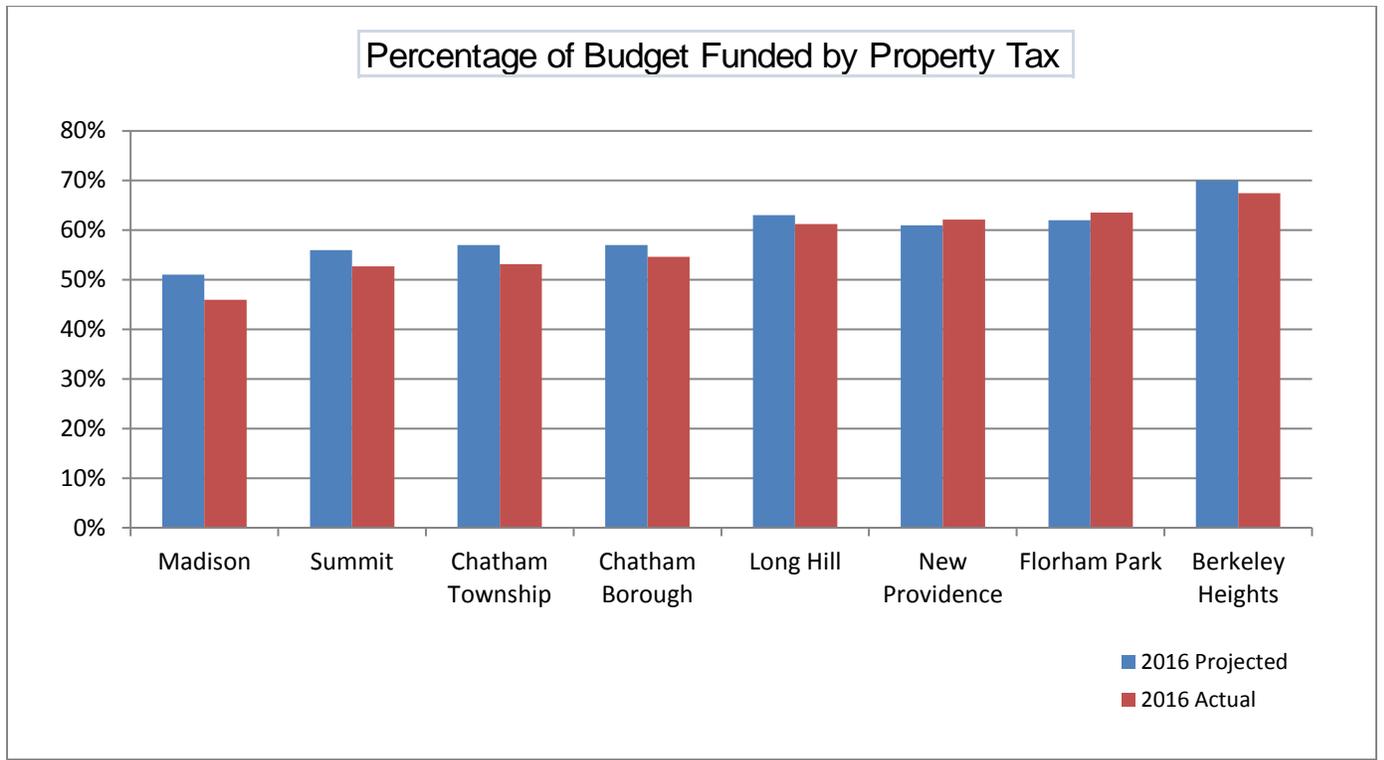


Chart # 5



Chart#6

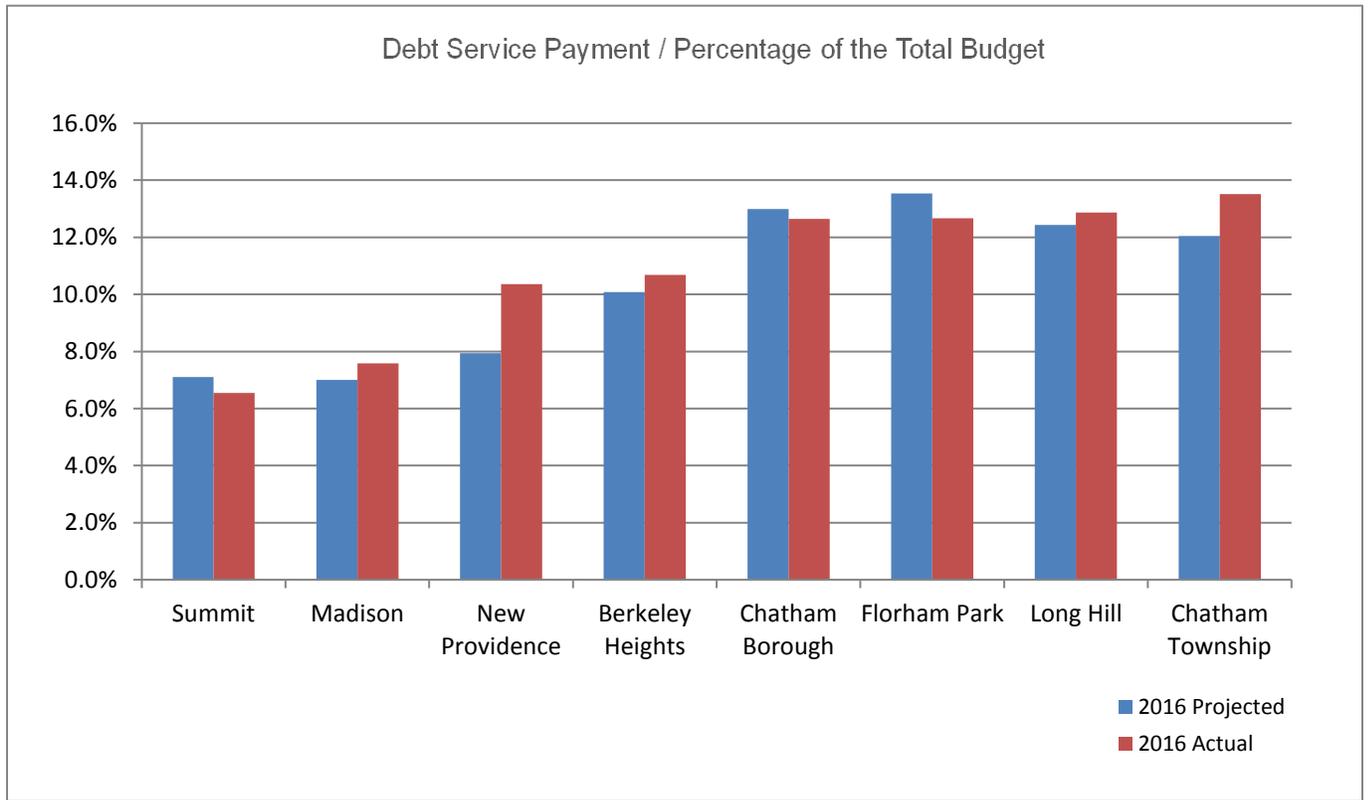
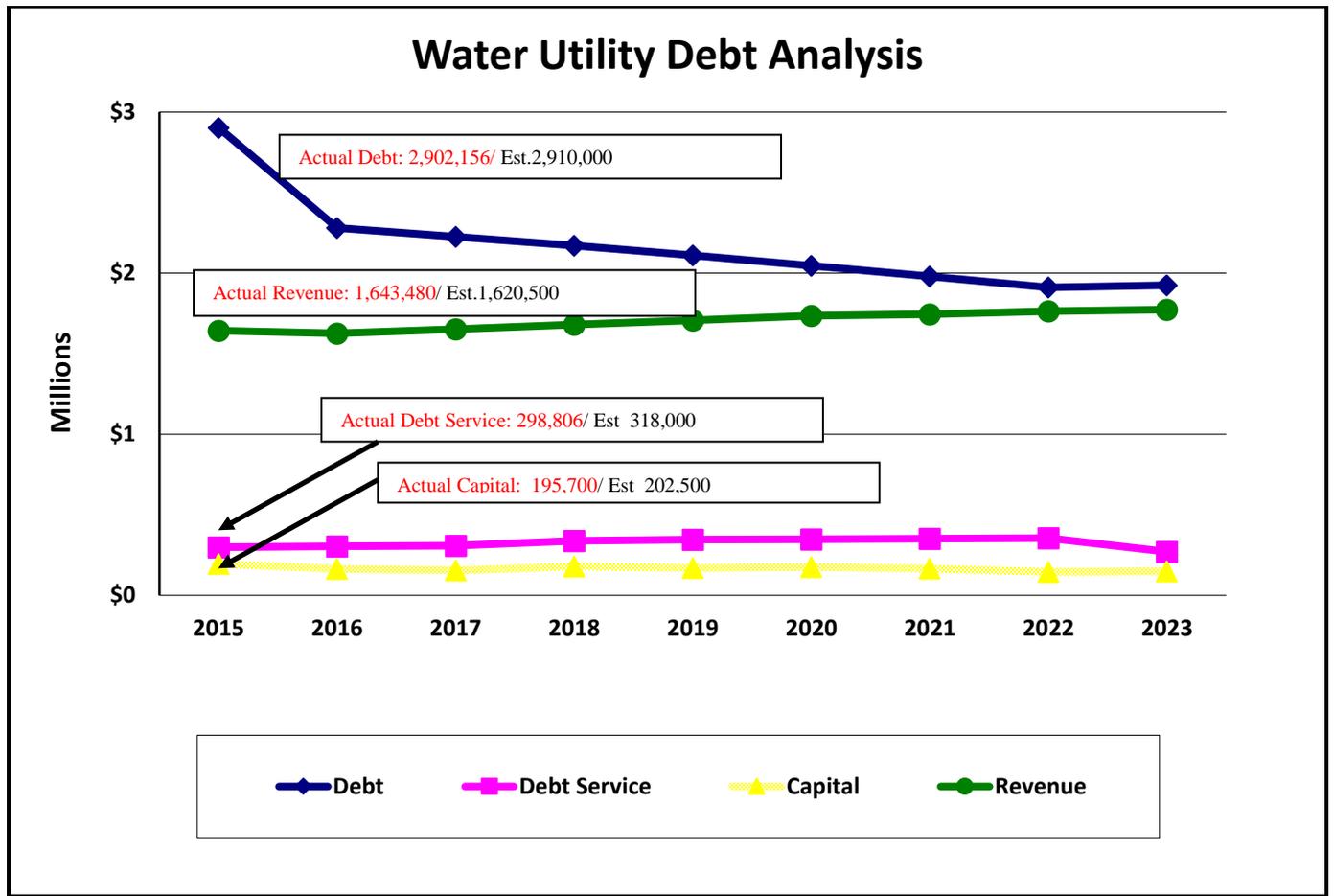


Chart # 7



Recommendations

The goal of the strategic financial management plan is to change the financial planning model from an annual process to the multi-year concept. The strategic financial management plan is designed to connect budgetary systems to municipal operations and services. The Finance Committee recommends that long range financial management planning should span ten years. The plan should be updated annually. Annual comparative analysis of the actual financial performance to the anticipated performance is essential.

The Chatham Borough Council has the responsibility and authority to determine the tax levy for municipal operations only.

General

1. Reduce the previous five year annual average for general capital purchases from \$2,030,622 to no more than \$1,000,000 annually. (reduction of \$1,030,622 or 50%)
2. By 2023, reduce the total debt by \$4,764,636. (reduction of total debt 31%)
3. Limit annual increases for personnel and operating expenses to no more than 2%.
4. Annually review revenue streams to ensure that the fee charged for each service is at least adequate to cover the actual expenses incurred by the Borough to provide the service.
5. Continue to identify new shared services opportunities to offset expenses.
6. Identify and rezone areas to encourage new businesses to locate in Chatham Borough to increase the ratable base.
7. Identify and develop new mass transit opportunities, including parking and access.
8. Extend the useful life of equipment, facilities and infrastructure through aggressive preventative maintenance programs.
9. Maintain the Borough's Aaa bond rating.
10. To measure financial performance, annually review and update the strategic financial management plan. Include the review and updating as one of the annual goals and report the achievement status.
11. The Finance Committee recommends that the Borough Finance Committee and Board of Education Finance Committee meet annually to review draft budgets and discuss the impact that each budget would have on the tax rate.
12. Develop a plan that will fund the Open Space debt and fund new Open Space projects.

Utilities

1. Limit water utility capital spending to \$175,000 annually.
2. Annually review water & solid waste rates to determine that the rates are adequate to fund future personnel, operating and capital improvements that are necessary for the efficient operation of the Chatham Borough Water Utility and solid waste collection services
3. Reduce the water utility debt by a minimum of \$50,000 annually.
4. Pay for Capital Improvements from Utility Surplus and not borrow funds. This provides a cost savings to the Borough and a deduction in the Utility outstanding debt.

References:

1. *Reinventing Government, David Osborne and Ted Gaebler, page 243*
2. *United States Census Bureau*
3. *Wikipedia*