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May 5, 2021

Dear Mayor and Council:

I formally present for your consideration, the Fiscal year 2021-2022 Recommended Budget for the Town of Chapel Hill. The total budget of \$116,746,903 is a 5% increase from FY 2021.

The past year has been a true test of our organization and our community. Ultimately, it proved to be a testimony to our resilience and fortitude. We have all experienced change and loss and the Town of Chapel Hill has responded with courage and compassion. Last year, we focused on protecting the Town's core services and establishing flexibility to face the unknowns brought on by COVID-19. It is our hope that we have emerged on the far side of this global pandemic, but we recognize that our recovery will not be immediate and that our new normal will not be a matter of simply picking up where we left off last March.

There is, however, reason for optimism. A municipal budget is an expression of a community's values and this year is no exception. While we are grateful for the opportunity to receive federal funding to address some of our immediate needs and to support our Town's interests, we must also focus on the long-term future of our community. Recovery will include immediate action with one-time funding as well as a return to our longer-term vision and 5-year plan for the ongoing budget.

Last year, we invested in our core services and were able to pivot to provide public safety, transit, affordable housing, and modified library, parks and recreation, and public works resources to our community. This year's budget seeks to restore some of the services that were limited last year, and to make investments in our future with our recurring revenues. We are putting the Town in a strong position to recover from the immediate impacts of the COVID-19 pandemic and to restore our focus on long-term priorities, especially those that will require an ongoing commitment, such as climate action, social equity, and infrastructure.

Recovery

The COVID-19 pandemic had unequal impacts on our Town's departments. Some of the most significant negative effects were loss of revenues in our Parks and Recreation department since recreational activities could not be offered as usual. Similarly, hotel occupancy tax revenues and parking fees were nearly eliminated by the lock-down. On the other hand, our sales tax collections were better than expected. In response to the emerging pandemic, we anticipated a 9.5% decrease in sales tax revenues in FY 21 and a 5% decrease in sales tax revenues in FY 22. For a variety of reasons this expected decrease in sales tax revenues never came to pass. In fact, the Town has seen greater than a 10% increase in sales tax revenues for the first seven months of FY22 over the same period of FY21.

As vaccination rates improve and businesses return to more normal operations, we have taken a cautious approach to projecting revenues, anticipating some return in programming and downtown activity. The one-time federal recovery funds are ideal for helping us support our businesses and our community as we transition to a more typical economy.

During the current year, we were able to use CARES Act funding passed through Orange County to the Town to address COVID-related needs, such as supporting our housing partners in the community, sheltering unhoused residents, providing food-bank support, purchasing and distributing personal protective equipment (PPE) in the community, and supporting our workforce with safety supplies, remote work, and operational shifts.

With the American Rescue Plan Act (ARPA) funds—which have federal limitations on eligible uses, we expect to be able to backstop some of our budget shortfalls and to invest in recovery efforts, such as the ReVive economic plan, so our community can bridge the gap from the pandemic year to a more typical year.

Restore/Replenish Operations

In North Carolina, counties are required by state statute to revalue real property at least every eight years. The revaluation process is designed to set tax assessments to a market value as of the appraisal date in order to equalize the tax base. Orange County recently completed the revaluation process that will go into effect beginning with the FY 2022 tax year. Overall, the real property value within Chapel Hill increased 13%. This is the combination of a 36% increase in commercial properties and a 9% increase in residential properties. As the result of the revaluation of property values, our property tax revenues—our main source of revenues for ongoing operations—would increase by \$5.2 million at the current tax rate of 54.4 cents per \$100 of assessed valuation.

State law requires the Town to declare, but not institute, a revenue neutral tax rate for the year a revaluation takes effect. The revenue neutral tax rate is calculated to generate the same amount of revenue that was generated in the tax year prior to the new revaluation assessments becoming effective. The revenue neutral tax rate for FY 2021-2022 is 49.4 cents per \$100 of assessed valuation.

The Council has expressed an interest in restoring some of the cumulative reductions the Town has made over time, to maintain our critical assets, and to be responsive to the interests of community members and property owners. The revaluation offers an opportunity for the Town to apply some of the property tax growth to priorities that we have struggled to adequately fund in the past.

In an attempt to balance the needs of the community with the impact of the revaluation increase on property owners, we have based this recommended budget on a tax rate of 52.4 cents per \$100 assessed valuation, to capture some of the natural increase in property values, while slightly lowering the tax rate.

Last year, to respond to the pandemic, the Town made a series of significant reductions within our budget in response to the pandemic:

- Other Post Employment Benefit (OPEB) prefunding contribution - reduced funding allocation by \$250,000
- Ephesus Fordham Tax Increment Financing (TIF) - eliminated funding allocation - \$445,100
- Street Resurfacing – reduced funding allocation by \$300,000
- Facilities Maintenance - eliminated funding allocation - \$472,200
- Fleet Replacement – eliminated funding allocation - \$525,000

- Pay-Go Capital – eliminated funding allocation – \$237,500

We know that continuing to defer maintenance of our capital assets will cause greater costs in the long run, so we propose replenishing those funds to the following levels in FY '22:

	FY 2021 Budget Reduction	FY 2022 Budget Restoration
Buildings	(\$472,214)	\$350,000
Streets	(\$300,000)	\$250,000
Pay-Go Capital	(\$237,500)	\$350,000
Vehicles	(\$523,908)	\$344,660

We also recognize that the Town has made commitments to decrease future liabilities, so we recommend reinstating the OPEB pre-funding contribution and the Ephesus-Fordham (EF) TIF budgets to the following level:

	FY 2021 Budget Reduction	FY 2022 Budget Restoration
OPEB Contribution	(\$250,000)	\$500,000
EF TIF	(\$445,100)	\$445,100

Recognize Town Employees

Last year, we did not provide Town employees with a pay increase and we instituted a hiring freeze on all vacant positions to save personnel costs. We were able to offer a one-time payment to employees mid-year, but we recognize that this has been an extraordinary year of sacrifice and hard work for our employees, many of whom were out in the community providing front-line service. We are fortunate that our safety protocols and the responsible actions of our employees resulted in very limited cases of COVID and nearly no work-place transmission of the virus. For that, we must thank the employees themselves. This year, I am recommending a 3% of market pay increase.

Our healthcare broker continues to negotiate our health insurance premium to ensure the best possible rate. The recommended budget includes a 5.5% increase in health insurance, which is higher than last year's 4% increase. The increase is due to a combination of significant claims experience from a relatively small number of high dollar claims and a general increase in the cost of healthcare.

Our goal is to retain and attract excellent employees in all areas of the organization. Last year, we paused the Class and Compensation study, due to a lack of funds to implement any findings. We have restarted that study and I am recommending \$400,000 to fund identified areas of need within the organization beginning on January 1, 2022.

One area of particular concern is in public safety where the competition for talent is considerable. We want to be in the best position possible to retain and attract the employees who make Chapel Hill a special place to live. We believe we can accomplish that goal by raising the starting pay and addressing the resulting compression of that increase in two phases, the first slated for FY 2022 and the other in FY 2023. We anticipate covering the costs of those increases with expected salary savings.

Return to the 5-year Budget Strategy

The Council Retreat in February 2021 focused on priorities for the future and how to pay for them. The Council reviewed the 2020-22 Strategic Goals and received an overview of the 5-year Budget Strategy. During the retreat, Council affirmed the overarching priorities of Environmental Stewardship, Economic

Development and Social Equity and discussed funding priorities for the upcoming year. The strategic initiatives funded in the recommended budget are listed below.

Environmental Stewardship

- **Climate Action:** On Wednesday, April 7, 2021, the Town Council voted to adopt the Town’s Climate Action and Response Plan. The Council also adopted a resolution declaring a climate emergency and requested that the Town Manager provide funding options as part of the Fiscal Year 2021-22 budget process. The recommended budget includes \$500,000 to begin implementation of the plan, which is roughly a half-penny on the tax rate.

Economic Development

- **ReVive:** This Recovery & Resiliency Plan offers a framework of goals, strategies and tactics that community leaders and volunteers can pursue to help Chapel Hill recover from the recession and lay a solid foundation for long-term transformation. This is a perfect use of one-time ARPA funding to help our downtown and other businesses bridge the gap between COVID and a more typical operating environment.
- **East Rosemary Street Parking Deck:** The recommended budget supports the construction of a new parking deck on East Rosemary Street using the Town’s Parking Enterprise Fund to pay the debt service for the cost of borrowing funds for the project.

Social Equity

- **Human Services:** The recommended budget increases the Human Services budget by \$100,000 to provide vital social services to low-wealth communities struggling with food and housing insecurity.
- **Reimagining Community Safety Task Force:** The recommended budget includes \$100,000 to implement recommendations from the Task Force to enhance our community safety initiatives, eliminate structural inequities in Town public safety systems; and enable all in the community to thrive.
- **Diversity Equity and Inclusion Officer:** The recommended budget includes \$143,250 to hire and support a Diversity Equity and Inclusion Officer for the Town. This position would report directly to the Town Manager and provide executive leadership on the Town’s racial equity goals and diversity initiatives.

Affordable Housing

- The Council continues to provide substantial annual funding for affordable housing and has approved leveraging Town-owned property to develop affordable housing. The recommended budget includes \$688,395 for affordable housing initiatives.
- The Town is expected to distribute the second half of the Affordable Housing Bond (approximately \$5 million) next year to assist with preserving and creating affordable housing units in Chapel Hill. We also anticipate utilizing ARPA funding to assist with housing assistance as folks continue to recover the financial impacts of the pandemic.

Refocusing on the Future

The recommended budget restores funding needed to continue to deliver high-quality core services to our residents, businesses, and visitors. The recommended budget also supports the Council’s strategic goal areas

from climate change to social equity and addresses critical workforce needs. Fiscal Year 2022 revenue projections are based on conservative assumptions about how funding levels will return to pre-pandemic levels. And in a revaluation year, the recommended budget establishes a municipal tax rate that captures a modest amount of property value growth.

Our community has weathered the dangerous storm of COVID-19 as well as any community in North Carolina. Our residents were determined to protect each other from infection and made significant sacrifices to do so. As we move cautiously into a better place, we know the goal is not to simply return to where we were before the pandemic but to learn from the experience and refocus our vision for a sustainable and equitable future. The pandemic exposed vulnerabilities in our community like food and housing insecurity and demonstrated the need for additional human services. And as the last year has also shown, our nation has much work to do to address our continued struggle with racism and its role in causing socio-economic disparities.

I believe this proposed budget offers the critical services and initiatives our community expects. It continues Chapel Hill's long history as a leader in addressing the critical issues of our times in a strategic, thoughtful and compassionate approach.

Sincerely,

Maurice Jones
Town Manager
Chapel Hill, NC

