

THE TAX ATTACK

Chapter V

The preceding chapters of this series have dealt with organizational structure, operating process and Village income and expenses. If you have missed any of them, they along with the most current five-year cash flow projection can be found at the Village web site (www.gatesmillsvillage.com). The nature of governmental accounting is such that balance sheets like those of business entities are not generally maintained. Typically governments use cash basis accounting that focuses on liquidity. Rarely are assets such as real estate and motor vehicles valued over their useful lives or encumbered by loans. When money is borrowed it is against the “full faith and credit” of the community.

With that backdrop, now let’s look at Village solvency and liquidity. The good news is that the Village assets exceed liabilities by a significant amount, but because most of those assets are operating assets and operating real estate and improvements thereon which are held for use and not for sale, the Village continually must be attentive to issues of liquidity.

The critical financial statistics involve cash, easily monetized investments and debt, both general and project oriented. An important measure for a community such as ours is “free cash”, i.e., the cash in excess of short-term operating obligations and short-term debt repayment requirements. Best practice suggests that a community should have six months of operating cash on hand (\$2 million in our case) in addition to the funds necessary to satisfy extraordinary contractual commitments and to service all debt, i.e., pay the interest and principal as due. Because of investments in real estate in the last several years, currently Gates Mills’ free cash is only about \$400,000 or 10% of our budget.

The vast majority of communities fund their large capital projects by the issuance of notes and bonds. The term of notes may not exceed the life of the asset being purchased or constructed. Bonds typically have 20-year terms and generally require a sinking fund payment annually to insure that the bonds can be retired when they come due. Two-thirds of Gates Mills’ current debt (about \$6 million), both funded and unfunded, was issued in connection with the installation of City of Cleveland Water in the late 90’s. Water assessments and fees will ultimately provide the funds to satisfy those debts. In addition, the Village issued a note for street repair following completion of the municipal water project. The balance on that note is now \$1.6 million and is repaid at the rate of \$200,000 per year. Beyond those debts the Village owes about \$270,000 to the State of Ohio in connection with the wastewater treatment plant and another \$1.1 million on various capital projects.

The Long Range Planning Subcommittee of the Village Finance Committee (Council members and other residents) periodically prepares a five-year projection of Village cash needs. The operating cost component of that projection is built from the bottom up by each Village department and challenged by the Subcommittee, particularly as to the cost increase assumptions employed. The income projections also are based on historic trends and projections. Current projection reflects a consumption of our existing free cash in the near future and a shortfall at the end of 2012 of \$1.3 million, well below the best practice standard.

Recently, Village Council voted to place on the March 4, 2008 ballot a 2.9 mill five-year levy exclusively to fund road and culvert repair and replacement with payment beginning in January 2009. While it is important for Village Council to have unrestricted levies for the general conduct of Village business, this new levy, if approved, will insure a steady flow of funding for road and culvert replacement until 2014 at the rate of about \$642,000 per year. It is believed that even in the face of escalating costs for the raw materials required for these repairs and replacements this should insure safe conditions on our roadways for the entire period.

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