

# **Ocean Pines Association, Inc.**

## **RECOMMENDED BUDGET**

### **Fiscal Year 2019-2020**

#### **Executive Summary**

**January 25, 2019**

**General Manager, John S. Bailey**

#### **Introduction**

The Recommended Budget for Fiscal Year 2019-2020 will accomplish many things that will be new to the association's budget and very good for the long-term health of the Association. That's the upside; the downside is that to fund those items, there is now recommended to be a significant increase in the annual assessment. In order to understand these major considerations, and to generally understand the entirety of the budget, one must look strategically at what the recommended budget accomplishes and how it creates a foundation for a healthy future – financially and for an improvement in the maintenance, and thus value, of the community's assets.

It should be noted that this budget includes the full, properly calculated reserve contributions; updated and current depreciation calculations; funding of over \$600,000 in new capital (for the Police Department/Admin building; and a room addition at the Sports Core pool); deferred operational maintenance; and drainage. It does not arbitrarily attempt to avoid addressing OPA issues in favor of assessment calculations. This approach provides the community with the opportunity to participate in the decision process and allows the Board of Directors to specifically identify which areas will not be funded, if any, and why, in the next fiscal year.

The budget development process is one of collaboration – by many of your fellow members, in addition to the OPA staff. The Budget & Finance Committee members, those who are specifically dedicated to helping manage the financial affairs of the community, have spent many hours of volunteer time reviewing the operating budget and the reserves. The B&F Committee conducted three days of intense and detailed budget meetings. Their effort was followed by two days of budget discussions by the Board of Directors. Those five work sessions yielded a lot of modifications and questions that created further significant changes to the Proposed Budget and have now led to the Recommended Budget.

## The Details – Interim Changes

The original Proposed Budget, issued January 4, 2019, began with an assessment of \$951. As a result of many review meetings and discussions with the Budget & Finance Committee, we increased the proposed assessment by \$31 to \$982, a 3.3% increase. This figure was presented at the membership budget hearing on January 12. What changes caused the \$31 increase?

• Added net revenue to Marina	(\$ 10,000)	(\$ 1.18)-
• Fire / EMS Capital Replacement Contribution	\$133,000	\$15.74+
• Add for Legal Services	\$ 50,000	\$ 5.92+
• Additional Funding for Deferred Maintenance	\$ 40,000	\$ 5.37+
• IT Redundancy, Depreciation	\$ 50,000	\$ 5.90
		<b>\$31</b>

## Recommended Budget Changes

Conversations and discussions have continued over the last two weeks at the Board level and with additional input from the General Manager, the B&F Committee, the Treasurer, and the Assistant Treasurer. As a result of everyone's collaborative effort, we have made some additional recommended changes to the budget as of January 24, 2019.

<b>Deficit Recovery*</b>	\$237,038
<b>Capital Reserve Contributions</b>	\$650,136
Replacement Capital Reserve	\$ 89,548
Road Reserve	\$400,000
Road Depreciation	\$225,000
Road Contribution	\$175,000
Bulkhead Reserve	
All Lots	\$160,000
<i>Waterfront Lot Bulkheads \$465</i>	
<b>New Capital Debt Service</b>	\$ 25,000

\$200,000 for Room Addition to Sports Core Pool – Borrow from 3<sup>rd</sup> Party @ 6%

\$400,000 for Expansion of the Police/Administration Building – Borrow from Reserves @ 3%

### **Deficit Recovery\***

The complete recovery of the deficit of \$1.6 million (as of April 30, 2018) from the prior two fiscal years is desired to be completed as soon as possible, and practical. The current fiscal year will see the deficit reduced to approximately \$1 million. The Recommended Budget includes a plan to apply \$337,098 to deficit recovery and thus eliminate the debt that we owe ourselves in three years.

This approach is financially healthy and very worthwhile, however, this level of funding for deficit recovery does have a corresponding impact on the recommended budget. While there is no additional increase to the assessment for deficit recovery, the amount of funding available for the new items in the recommended budget had to be off-set by cuts in other line items or paid for through increased assessments, or a combination thereof.

### **The Recommended Budget provides new spending in the operating fund for:**

Drainage	+\$178,000
Deferred Maintenance ( <i>non-reserve funding</i> )	+\$160,000
Pay Study Adjustments, 2% labor increase, 10% benefit inflation	+\$275,000

The Recommended Budget also includes the following increases in spending:

Drainage ( <i>Road Reserve funding</i> )	\$620,000
Deferred Maintenance ( <i>Replacement Reserve funding</i> )	\$305,000

**Total spending on Drainage** is proposed to increase by \$798,000; from \$117,000 in FY18-19 to \$915,000 in FY19-20.

**Total spending on Deferred Maintenance** for this coming fiscal year of 2019-20 is proposed at \$465,000.

### **Deferred Maintenance**

This is to cover many repair and maintenance projects that have not been addressed over the years. It includes \$305K worth of capital items to be paid from the Replacement Reserve Fund. This effort also includes \$160K to be paid for out of the Operating Fund. Examples of Deferred Maintenance are:

*The guard shack at the Beach Club Parking Lot*

*Many exterior signs throughout the community*

*Mulch for all of the playgrounds*

*Additional stone dust for trails*

*Small playground equipment*

*Basketball goals and backboards*

If approved, many of these deferred maintenance projects are desired to be completed by Memorial Day weekend, 2019. Obviously, however, with so much to do, the completion of these long-deferred items will be accomplished on a rolling basis throughout the year.

### **Replacement Capital Reserve Contribution**

The annual contribution to the Replacement Capital Reserve is recommended to increase by \$185,404. Depreciation for FY19-20 will be increasing as a result of the amount of assets put in service this year and next. The Replacement Reserve Fund consists of monies set aside to replace and preserve our community's physical assets; these are projects that need to be done and have needed to be done on a regular basis, but for which we have not followed the reserve expenditure plan in prior years. This has led to much of the deferred maintenance and lack of upkeep of our major assets.

#### **Replacement Reserve Expenditure**

\$4,196,079

*The depreciation calculation, plus an added inflation factor of 3.8%, indicated that the association should increase the annual assessment contribution from \$1,677,000 to \$1,862,749.*

### **Road Reserve Contribution**

Currently, the only revenue streams for funding the Road Reserve are the casino funds (\$325K per year) and a small amount of interest earned on the Road Reserve fund itself. The Association has not been funding Road Depreciation, nor have we been making any other general assessment contribution to the Road Reserve. The cost to maintain, repair, and replace pavement has certainly risen over the years, just as our outside revenue stream has gone down. We need to be making an annual contribution from the assessment to Roads in order to meet this discrepancy.

#### **Road Reserve Expenditure**

\$1,253,000

Roads \$633,000

Drainage pipes under roads \$620,000

*(The Road Reserve allows for specific costs associated with road drainage to be paid from this reserve.)*

If approved, Requests for Proposals will be issued this spring, with work to commence based upon scheduling with the selected contractors.

### **Bulkhead Reserve Expenditure**

\$1,619,057

***The Recommended Budget includes the \$19 contribution that was waived last year for common property bulkheads. The annual contribution only paid by those members with private bulkheads also will continue at \$465.***

If approved, the Requests for Proposals will be issued this spring, with work to commence after the boating season in the fall of 2019. A possible exception to that timeline would be for bulkhead improvements for general association-owned bulkheads.

## **New Capital**

The Recommended Budget funds three New Capital items. There is \$6,500 for Police Department-specific software. The other two New Capital items are bold measures to improve the assets of the community.

First is a room addition to the Sports Core Pool. The idea for this addition is to build a room to generate new revenue streams by conducting after-school programming and other revenue producing activities. The business plan supporting this addition estimates an annual revenue stream on the investment such that the ROI will cover the full cost of the construction over a period of years. The estimated cost for this project is \$200,000 and it is recommended that we pay for it by borrowing the full amount from a third party, i.e.: the bank. We would be seeking a \$200,000 loan at approximately 6% interest with a 5-year term. Conversations are on-going, and if approved, the Association would work to secure the funding and finalize plans such that construction could begin in the fall of 2019.

The second major new capital project that is recommended to be funded is an expansion of the Police/Administration building. The Police Department facilities are, and have been for quite some time, outdated and deplorable. The physical space for the PD is to be increased from 1,770 square feet to 5,300 square feet. Initial design for the PD facility has been done with advice from criminal justice facility design experts. To get the PD to the 5,300 square foot dimensions, the PD will take up most of the existing building; thus, the need to expand the building to provide for the displaced area used currently for Administrative Services. The estimated cost for the new, extension of the building is \$400,000. Funding for the new capital portion of this project is recommended to come from the Replacement Reserve as a loan to ourselves over a ten-year term at 3% interest. The Request for Proposals for this project was issued on January 24 and the deadline for submissions is Friday, February 22. The Board will consider action on this proposal on March 9.

It should also be noted that other New Capital requests totaling \$225,714 have not been funded. The issue that everyone needs to remember about New Capital is that we have no funding mechanism for anything new except for increases in the annual assessment, reductions in current spending, or borrowing – either by third party or internally from the reserves. Either approach only leads to fluctuations in an annual assessment and/or other consternation on how to fund such items. Thus, it is important for the Association to create a policy and procedure in FY19-20 on how to fund new capital projects.

## **Payroll**

The Recommended Budget fully funds the pay adjustments identified in the Pay Study. The study found that we had 35 positions that are currently under funded, thus the Recommended Budget includes approximately \$128,000 to bring those positions into better alignment with the competing marketplace. Payroll adjustments include a 2% labor pool increase to be distributed based on merit achievement. Medical benefit costs are budgeted to increase 10% based on the advice of the insurance professionals.

**User Fees & Fee-Based Amenity Departments**

The Recommended Budget increases most user fees an average of three percent. There are no subsidy level increases proposed for the fee-based amenity departments (Golf, Aquatics, and Racquet Sports).

For more details on the budget, please see the attachments that are included with this summary.

**All of the above leads us to a recommended assessment of \$1,078. This would be a \$127 increase or 13.4% over the current amount of \$951.**

**Recommended Assessment Increase of \$127**

**Major Components of New or Increased Expenditures**

Drainage	\$178,000	\$21.06
Deferred Maintenance	\$160,000	\$18.93
Bulkheads (all)	\$160,588	\$19.00
Road Reserve Contribution	\$400,000	\$47.33
Legal Services	\$ 50,000	\$ 5.91
New Capital Debt Service	\$ 25,000	\$ 2.96
Payroll	\$275,000	\$32.54
Offsets within Budget	(\$175,210)	<u>(\$20.73)</u>
		<b>\$127</b>

As the budget schedule indicates, this is a process, a collaborative one. We started with staff and the General Manager to create multiple drafts leading to a Proposed Budget. We have had three Budget & Finance Committee budget work sessions, a member hearing on the Proposed Budget, two Board of Directors budget work sessions, and lots of effort by many members, committees, and staff. We now have a Recommended Budget. The Board of Directors will conduct a member hearing next Saturday, February 2, in the Assateague Room. The hearing will begin at 10:00 am. The Board of Directors will hear your comments and will then take two weeks to provide the General Manager with budget adjustments they would like to consider. Amendments to the Recommended Budget will be voted on by the Board on February 16, at which time the Board of Directors will adopt the Final Budget and set the annual assessment for the next fiscal year. Please do share your thoughts with the Board by attending the member hearing and/or by email at [directors@oceanpines.org](mailto:directors@oceanpines.org).

**Attachments:**

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|-----------------------|----------------------|---------------|
| Assessment Detail     | Capital Reserve List | Road Plan     |
| Deficit Recovery Plan | Drainage Plan        | Bulkhead Plan |