

Village Council

Cc: Calvin Peck, Deborah Straub

May 17, 2010

Gentlemen:

Next year's proposed budget shows an increase of 29% when compared to this year's expenditures paid with current income. This substantial increase represents in large part the additional costs for legal, engineering and lobbying services related to the erosion of our beaches from the presence and maintenance of the Cape Fear River navigation channel. We agree that this step is necessary to protect our shoreline from other than natural forces. We appreciate the work and dedication of the Council and staff that reduced the current budget so that next year's increase is not even larger.

There will be a temptation to minimize the increase by turning once again to our reserves. However, in the past two years those reserves have been reduced by half, by more than \$4 million. For our island, those reserves are important for at least two reasons. First, they provide readily available resources to cope with emergencies, generally resulting from storms. Secondly, they are important for the role they play in preserving our village's investment grade bond rating. Without that rating, capital markets will be both more restrictive and more costly.

At the time of our last bond rating, our unrestricted reserves represented 60% of our operating budget. Year end projections indicate that, even without further depletion of the reserves, that percentage will have deteriorated to 36%. Another consideration in bond rating is total property values. We anticipate that our island tax base will be reduced by more than 30% at the revaluation that will take place later this year. This will result in an increase in the ratio of our debt to total property value.

The reserves must be increased to minimize the necessity of borrowing. If borrowing becomes necessary, we must have higher reserves in order to minimize the cost of that borrowing. As a first step, we recommend that for the balance of this year and next year the reserves be maintained at current levels and available exclusively for emergency response.

Further, we recommend that in future years, there be budgeted increases to replenish our reserves to fiscally prudent funding levels. Later this year, as we develop the next version of the Five Year Plan, we will recommend specific targets for those reserves.

In brief, we recommend using reserves only for emergencies. It is simply prudent to depend upon current revenues to support current expenditures.

Village Finance Committee

Jim Bonica Barry Kane John Knott , Chair Ken Miller David Ross Anita Schnog