



Small Town Financial Viability Case Study: Town of Ahoskie, North Carolina

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Ahoskie, North Carolina

Public finance is a significant factor in determining the viability of local government. Without sound financial management systems, municipalities have a hard time maintaining infrastructure and providing valuable services to their citizens. This case study focuses on the steps that were taken by the Town of Ahoskie, located in rural Hertford County in North Carolina, to work towards a sound financial future. There are 5,000 people who live in Ahoskie¹, but it hosts a daytime population of around 15,000 people who come to the town for its various amenities, including a hospital, various dining establishments, and businesses. To put the surrounding area in perspective, out of the four-county region that Ahoskie lies in, there is only one Bojangles, one McDonalds, and one Burger King that are the only chain restaurants that are not in the town itself, with the only Walmart located in Ahoskie as well. The town's importance to the region in terms of economic activity serves as significant source of revenue for its water and wastewater utilities.

Early Spending and Debt Accumulation

In 2005 a newly elected town council was intent on investing in large capital projects to update the infrastructure of the town. Some of these infrastructure improvement projects included the following:

- Construction of a new police station.
- Construction of new fire stations and purchasing of 2 new fire trucks.
- Construction of a new wastewater treatment plant.
- Street repair and repaving.

While all these projects can be considered necessary endeavors for a town to undertake, the amount of money that was spent had significantly surpassed the revenue that had been generated over the course of the next 10 years. To finance these improvements, the town incurred \$21.2 million dollars of debt. By the end of June 2017, the town council recognized that Ahoskie was

in a very difficult financial situation. At that time, Ahoskie's available General Fund balance had been declining for three consecutive years. Also, in the 2015-16 fiscal year the town needed to pull from reserves in order to meet operating budget for the General Fund, and they had to transfer approximately \$200,000 from General Fund to the Water & Sewer Fund. The General Fund and Enterprise Funds should be self-sustaining, not requiring transfers from either to the other. Repeated transfers between the Funds can indicate to the Local Government Commission (LGC), which assesses the financial condition of the town and approves or declines any debt that local governments in the state incur, that the Fund is not financially viable. This can impact the town's ability to access funding through subsidies, bond issuances, and loans. Refinancing existing debt obligations to reduce the portion of each payment that goes toward principle or interest can help municipalities ease short-term budget pressures and free up cash for essential government operations. However, this strategy becomes difficult to implement if the municipality is deemed not financially viable by the LGC.

An excessive amount of debt can also affect the financial viability of a town's water and wastewater utilities. In 2017, erasing the debt by reducing other expenses was the town's main priority, meaning that any additional capital improvements to its water and wastewater infrastructure were to be postponed. That year, Kerry McDuffie was hired as the new town manager, and was asked to help analyze expenses and set a path for recovery. With the approval of the elected officials, McDuffie and others took a hard look at spending and figured out ways to reduce expenses to pay off the debt.

Paying Down \$21 Million in Debt for a Town of 5,000 Residents by Cutting Expenses

The Town comprehensively examined all its expenditures across many departments and identified multiple ways to reduce costs while maintaining services for its residents.

Assessing Staff Needs

As the town first started focusing on cutting extraneous expenses in 2017, third party assessors such as the Environmental Finance Center (EFC) at the UNC School of Government and the LGC were asked to help examine the efficiency of various functions of its departments and determine how many workers were needed to operate the wastewater plant. One of the first dramatic decisions made was to cut about 15% of the staff across departments, in a manner that preserved the town's ability to provide essential functions to the public and did not impact the quality of the work conducted by the local government. The town went from 60 employees to 51, which helped reduce expenses and pay off more debt. This included eliminating the entire Parks and Recreation Department, with the maintenance responsibilities absorbed by Public Works and the program management taken over by volunteers. Using volunteers for running programs proved to work well and was well-received by the community. There were also other departments that needed an assessment of the size of their staff. By evaluating workflow and essential function, the town reduced an additional position at the wastewater treatment plant and

at Town Hall. Ahoskie also took advantage of the LEAD for North Carolina Program offered by the University of North Carolina's School of Government. The town applied for an intern through the program, who worked on revitalization projects and conducted research on outsourcing governmental function. The funding for the intern was shared by Ahoskie and the UNC School of Government, which cut back on full time expenses such as salaries and benefits.

Assessing Water/Wastewater Expenses

The North Carolina Rural Water Association was brought in to assess the energy efficiency of the wastewater treatment plant. The major finding from the assessment was that the rate code that Dominion Energy was charging the town led to higher-than-needed charges. Ahoskie decided to switch the rate code from a basic commercial user to a time-of-use account. This time-of-use rate structure allows for the utility to control its energy costs by operating energy-intensive equipment during the hours when time-of-use rates are lower. A time-of-use bill is more complex to calculate than a basic bill but can be determined by multiplying the amount of electricity consumed during certain hours of the day by the rate specific to those hours. While Dominion was reportedly not amicable to this decision, after a couple months the town and the energy company reached an agreement. Through switching the rate structure and implementing the other findings that the Rural Water Association reported, the wastewater treatment plant achieved annual energy cost savings of approximately \$36,000. Another expense that the town discovered it was significantly overpaying was its leases for various equipment. For example, printing costs for utility bills were lowered by offering contracts to copier companies. Prior to outsourcing this job, the town was paying roughly \$12,000 per year to lease a folding machine to stuff envelopes and purchase postal stamps. Instead of continuing to lease this equipment, the town contracted with a company called Arista which owns software that interacts with postal service systems. By paying Arista to print the bills instead of leasing expensive pieces of equipment and paying for stamps to send out utility bills, the town had a net savings of \$13,000 per year.

In North Carolina, some wastewater utilities have been using spray fields to discharge treated effluent since 1998. These fields are planted with cover crops that uptake the nutrients contained in treated effluent. The cut hay from the spray field that Ahoskie's wastewater department was using was being sold for livestock feed and other agricultural uses. For years, the utility had been mowing the spray field themselves. They were obtaining some revenue, \$30,000 per year, from selling this hay. However, the expenditures involved in mowing the spray fields, including fuel, equipment, and personnel costs, exceeded those revenues. Hay mowing was outsourced, and other operations at the plant were changed to help the wastewater treatment plant run more efficiently, ultimately leading to a reduction of 5 staff positions within the department. Although this led to a reduction of income in hay sales, the town reduced equipment, fuel, labor, and associated costs for a net savings of over \$300,000 per year on a permanent, on-going basis.

Labor time was also targeted by the Public Works department. The town decided to install automatic dialers at several sewer lift-stations. North Carolina state laws require an individual to visit every sewer lift station every day unless there is an automatic dialer installed

at the station. The installation of automatic dialers reduced labor time enough to reduce one position in Public Works. Another reduction in staff expense was changing the uniforms of Public Works employees. The town changed the Public Works uniforms from collar dress type shirts to high visibility t-shirts. This together with using the state contract for uniforms saved over \$7,300 per year while providing employees safer, highly visible uniforms.

Assessing General Town Maintenance and Services

As town manager, McDuffie was responsible for looking at nonessential and overpaid expenses across all departments. For instance, Ahoskie was leasing a street sweeper which had to be driven to Raleigh whenever an oil change was needed. This expense amounted to \$10,000 a year in maintenance and a lease payment with 5% interest. The town instead elected to exit that lease and buy a street sweeper outright in the pursuit of long-term savings.

An example of another expense that the town was able to reduce before McDuffie's hiring in 2017 was a maintenance contract for watering hanging plants on street poles. Originally the contractor was charging \$20,000 per year to water the plants and cut grass on Main Street. To reduce costs, the town decided to eliminate the contract, remove the potted plants, and assign mowing the grass to its Public Works department.

Around 2013, Hertford County, Ahoskie, and neighboring Town of Murfreesboro built a joint 911 dispatch center with the County funding the construction of the facility and both towns paying a per-capita based amount of money to run 911 services. Ahoskie was paying \$100,000 per year on average. In 2019 the state law changed on 911 services, now requiring all counties to run a police dispatch for municipalities that elected not to run one on their own. In July of that year, Ahoskie gave notice that it would no longer be running the service, relinquishing responsibility to the County. This resulted in savings of about \$96,000 per year. After moving the dispatch center to the County, the town further examined its expenses within the police department. For example, running a 911 dispatch requires a T1 level of internet connectivity to guarantee a large bandwidth and that no calls would be dropped. Paying for this resulted in large internet bills for the police department, approximately \$1,300 per month. Ahoskie had stopped paying for the dispatch costs but still had T1 internet at the police station. The argument was made that while the police need a good and secure internet system, T1 could be replaced with a regular cable modem, which would bring down monthly internet bills to \$199. The town went ahead with this decision, resulting in savings of about \$1,100 per month.

Overall Reduction of Costs

Ahoskie's experience with debt taught the town employees across departments to examine their expenses and analyze alternatives that could lower costs while maintaining services. After a comprehensive review and finding adequate alternatives, the town was about to generate the following annual cost savings, in addition to one-off savings or revenue generation:

Service/Department	Expense	Annual Savings
Wastewater	Energy Rate Structure	\$36,000
Wastewater/Water	Printing Utility Bills	\$13,000
Wastewater	Hay Cutting on Spray field; increased efficiency at WWTP and elimination of positions.	\$300,000
General	Street Sweeper	\$10,000
General	Street Plants	\$20,000
General	911 Dispatch	\$13,200

Table 1. Examples of savings from various cost-reducing measures

Paying Down Debt

After reducing operational expenses, the town used the savings to partially pay down its debt burden. Since 2017, the town has paid off nine loans amounting to around \$4 million in part by using the cost savings achieved over this time period.

Public Response

In 2017, many residents of the town were aware of the financial situation that the municipality was facing. Both the public servants and the population at large understood that expenses had to be cut in order to reduce the debt. However, a number as high as \$21 million raised suspicions around the legitimacy of the expenses that were being claimed as the reason that the debt was so large, which led to speculations of possible corruption among the elected officials.

One of the strategies used to increase transparency and understanding was to hold public town halls. At these town halls, a 4x8 foot bulletin board was used to show the different sources of debt using multicolored pieces of paper (Figure 1). Under each source of debt were characteristics such as the annual payment, the payoff date, and the payoff amount. Behind each one of these sheets of paper was another sheet that had the original amount of the debt in 2017 and the words “paid in full”. As each one of the debts was paid off, this sheet would become exposed.

By showing the public what the sources of debt were—a new fire station, an upgraded wastewater treatment plant, street repairs, etc.—and how they amounted to \$21 million, fears of corruption were stamped out. They focused on paying off the small debts first and the board worked to communicate to the public the direction that the town was heading.

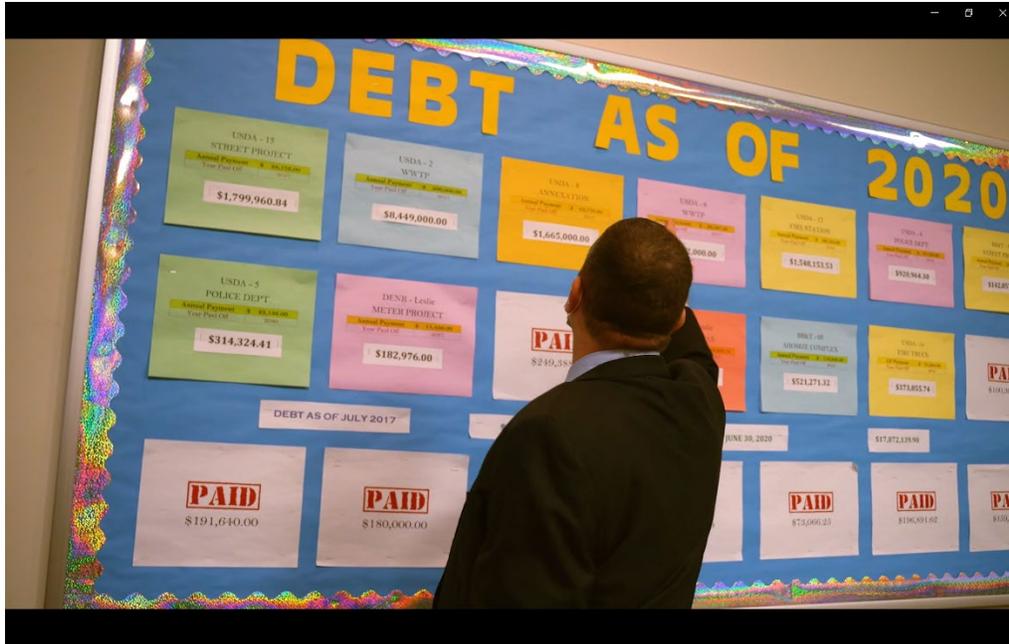


Figure 1. Bulletin Board in Town Hall showing the various sources of debt, Kerry McDuffie points to the board (Photo by Angelina Katsanis)

Ahoskie's Financial Health Today

Improved Fund Balance and Lowered Debt Burden

Through examining town expenses and rates that were being paid to third party groups, the town was able to conduct a series of responses to build the town's fund balance and reduce the debt. The cost reductions enabled Ahoskie to pay off 9 loans, reducing the debt owed now to around \$17.8 million. With those 9 loans paid off, \$560,482 in principal and interest payments has been freed up in 2021. The town's Water and Wastewater Enterprise Fund balance as a percent of expenditures had increased between 2017 and 2019, from 1.49% to 16.88%. 2020 has been the only year in the past four that Ahoskie has not had a noticeable increased fund balance. During the 2019-2020 fiscal year, the town's General Fund repaid the Water and Wastewater Enterprise Fund previous years' transfers. Now that this has been repaid, the town can continue building its Enterprise Fund balance.

The town's conscious efforts to cut down costs through a careful examination of expenses and identification of lower-cost alternatives that would maintain adequate levels of service has not only allowed the town to pay down a sizable portion of their debt burden, but also increased their reserves for responding to emergencies—such as the changing operational conditions during the COVID-19 pandemic.

Today, the Water and Wastewater Enterprise Fund balance is independently supported with a positive balance. During fiscal year 2020, operating revenues were 18% higher than operating expenses, meaning that the rates were sufficient to cover the costs of operations and

depreciation for the fiscal year. The water and wastewater fund's debt service coverage ratio, which measures a water/wastewater system's ability to pay its debt service using its operating revenues in a given fiscal year, has been increasing since 2015 and was at a healthy level for FY2020, at 1.20. Debt service coverage ratio provides a broad perspective on financial sustainability over the course of an entire fiscal year.

Improved Financial Resilience of the Water/Wastewater Enterprise Fund

Demonstrating the growth in financial reserves in the water/wastewater Enterprise Fund, the days cash on hand was 0 at the end of fiscal years 2016, 2017, 2018, but then increased to 33 days in fiscal year 2019 and 165 days in fiscal year 2020. This is representative of the unrestricted cash on the last day of the fiscal year, which is a snapshot in time. While the amount of unrestricted cash can fluctuate daily, the increase in 2019 and then again in 2020 shows an increasing reserve which Ahoskie can count on in case of emergencies or unexpected expenses. This is especially important, as it protects them from borrowing money from another fund for a one-time emergency.

When businesses were forced to shut down during the COVID-19 lockdown, the town's consumption of water and wastewater significantly declined. Ahoskie saw an increase in residential water usage between March and July 2020, compared to 2019 levels. However, with businesses shutting down or reducing operations during the lockdown period, reducing water consumption significantly, Ahoskie experienced a massive \$22,000 monthly loss in water and wastewater revenues from commercial usage. In addition, Ahoskie lost approximately \$8,500 per month for three months in late fees and penalties from residential customers. This loss was attributed to the fact that under the Governor's Executive Orders 124 and 142, local governments were no longer allowed to charge late fees and penalties or disconnect customers for non-payment of water/wastewater bills from April through July 2020. If allowed to signal cut-offs for customers that were behind on their water/wastewater bills, 180 households would have lost their water and wastewater services, resulting in approximately \$55,000 in back bill amounts. It should be noted that most of the customers with delinquent accounts were also customers who had trouble paying their bills before the COVID-19 pandemic. While many people in the town lost employment or income during the pandemic lockdown, it appears that many residents used their unemployment benefits and social assistance to pay for their water bills. After the Executive Orders' moratorium on disconnections for non-payment expired at the end of July 2020, customers were required to pay their bill arrears over time. As of April 2021, Ahoskie has collected payments on late bills from almost all 180 of their delinquent customers.

Adjusting Water/Wastewater Rates

Ahoskie's water and wastewater rates are relatively higher than most of the utilities of similar size in North Carolina. When the LGC examined Ahoskie's debt in 2017, they recommended that the town implement a 10% rate increase every year for the next three years, followed by an evaluation. The town complied with this recommendation in the first year, however in the second and third years it increased rates by 5% and 0%, respectively. Ahoskie was able to meet its debt reduction goals through reducing expenditures rather than increasing

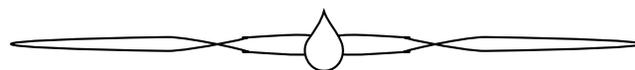
rates and revenues. Otherwise, rates could have become increasingly unaffordable for a town that already is charging its customers more than the state average for water and wastewater. As of 2021, the combined water and wastewater residential bill at a consumption rate of 5,000 gallons is \$102.51/month, compared to the state median of \$80. Households making the median level of income in Ahoskie would spend 3.85% of their income on water and wastewater bills at that level of consumption.

Refinancing Debt

In April 2021, the Ahoskie Town Council received approval from the LGC for a refinancing agreement that will be used to pay off two previously issued utility system General Obligation bonds held since 2011 by the United States Department of Agriculture (USDA). USDA-Rural Development was the financing agency that handled the loan that was used to construct the Wastewater Treatment Plant. The original loans had an interest rate of 4.125% and was scheduled for 40 years until 2051. The interest rate on the new 20-year refinancing loan is 2.86%, and the loan closing is scheduled for May 5, 2021. Although this plan will increase debt service payments by approximately \$40,000 per year, because of the shorter loan term, it will lower the number of annual payments from 31 remaining years to 20 years, and along with the lower interest rate, will save the town about \$3.5 million over the life of the loan. While it cannot be said for certain, Ahoskie could have missed out on this refinancing agreement if they had not made the financial strides that were accomplished in the past three years to gain LGC's approval for a new debt issuance. By finding and cutting costs that proved to be extraneous to the necessary functions of a town, they have proven that they can handle a shorter loan term with higher monthly payments.

Outlook

Ahoskie has improved its financial stability since 2017, yet the town still needs to pay off its debts and prioritize raising reserves, especially for its water/wastewater utilities. In early 2020, Sharon Edmundson, Director of the LGC's Fiscal Management Section, wrote a letter addressed to the mayor of Ahoskie, commending "the town for the significant improvement in the General Fund balance for the second year in a row"². Ahoskie is mitigating what was a serious financial concern for the town through the implementation of effective financial practices. With \$17 million remaining in debt, there is still a long way to go to pay off all debts. The work that has been done in the past few years is encouraging and the signs are showing that if Ahoskie can continue its budget tightening practices, it can build the Fund balances and achieve long-term financial viability.



¹Population: <https://datausa.io/profile/geo/ahoskie-nc>

²<https://www.roanoke-chowannewsheald.com/2020/03/27/ahoskie-praised-for-financial-recovery/>