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MEMORANDUM

TO: Board of Selectmen
Finance Committee
Residents and Taxpayers

FROM: Andrew J. Sheehan, Town Administrator

DATE: March 13, 2014

RE: **FY 2015 BUDGET NARRATIVE**

Consistent with the budget timeline the departments, boards, and committees have submitted their budget requests for the FY2015 budget which runs from July 1, 2014 to June 30, 2015. Since that time the Town Accountant, Kim Fales, and I have compiled those requests and have developed this first budget draft. As will be noted, there remain some unknowns on both the revenue and expenditure side. For this reason, the budget will change and evolve as we approach Town Meeting on May 6, 2014.

As I wrote in my budget message in December, the outlook for FY15 contains substantial uncertainty. Care must be taken to ensure we continue to live within our means while providing the necessary services. As has been noted in prior years, Town departments have largely been living with level funded budgets for several years. This is an unsustainable practice as costs continue to rise and departments, though level-funded, fall further behind due to normal inflationary pressures. Unfortunately, with few exceptions this will continue in FY15.

Budgeting requires that we make certain assumptions with respect to revenues and expenditures. This is an inexact science, but conservative and reasonable assumptions minimize surprises. Several of the assumptions that we must make can fluctuate from year to year. On the revenue side the most unpredictable is State aid to cities and towns (local aid). On the expense side the largest cost centers are regional school assessments and employee benefits, specifically health insurance and retirement.

In simplest terms, Townsend has a revenue problem. As will be detailed below, local aid is at FY2006 levels and is well below the peaks we saw prior to the Great Recession. We would have

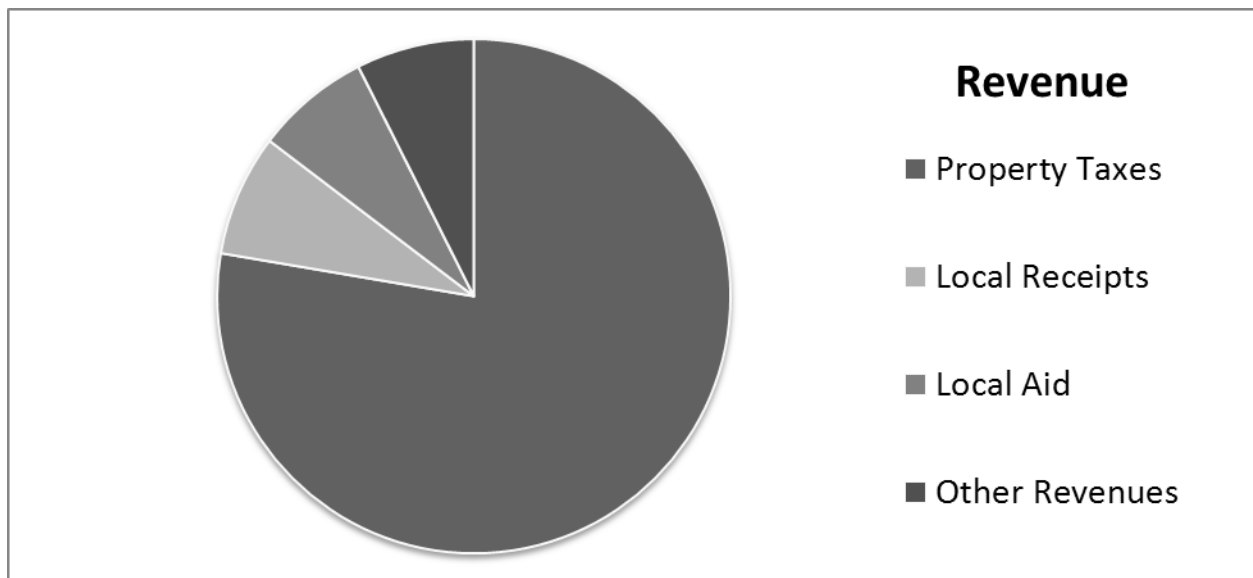
much greater flexibility in both the operating and capital budgets if we were receiving the local aid we received in FY08 or FY09. However, we must play the hand we are dealt and the draft budget I am putting forth does that.

Revenues

There are four revenue categories. The property tax levy is the largest portion of revenue. The levy consists of last year's levy, the allowed annual 2 ½% increase, and new growth. It also includes amounts approved by Proposition 2 ½ overrides and debt exclusions. The tax levy is proposed to increase by the statutory 2 ½ percent. The 2 ½% increase for FY15 is \$351,429. As will be shown below, this increase is more than taken up by the regional school assessments. In FY15 the levy limit will be \$14,977,307.

Local receipts, which include things such as license fees, permit fees, and excise taxes, are estimated at \$1,475,000. Local receipts trailed off during the recent economic downturn and are only now approaching pre-recession levels. We are continuing our conservative approach with local receipts in FY15.

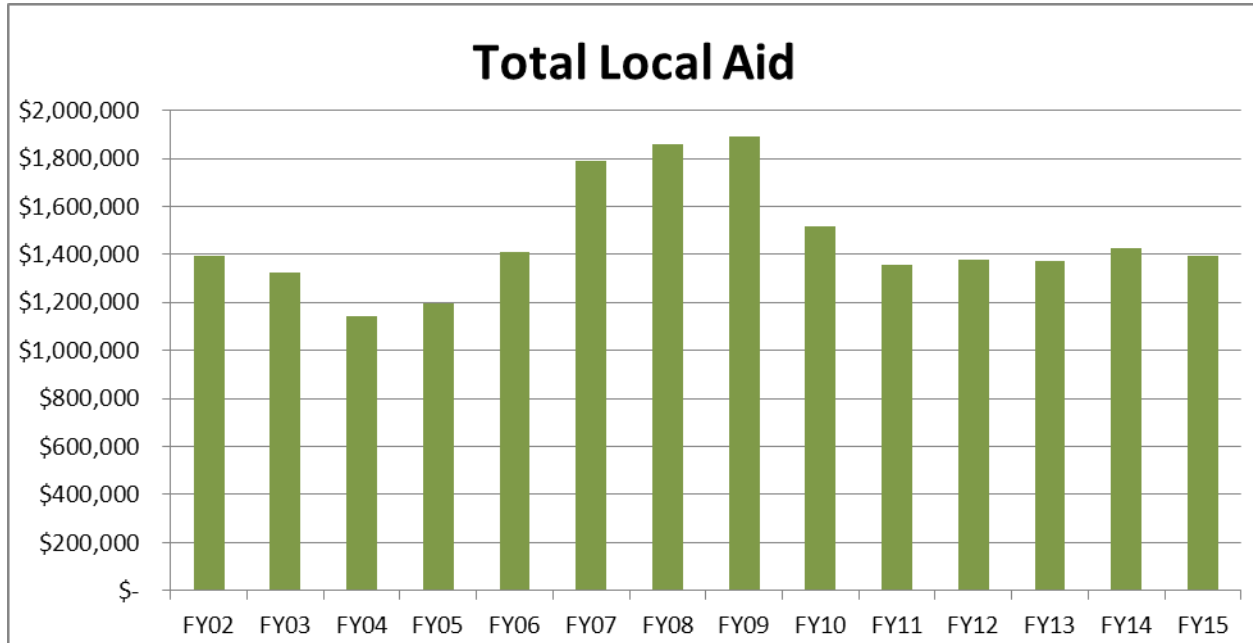
Another revenue category is other revenues. This category includes transfers from other departments (Ambulance, Water, cable franchise, etc.), overlay surplus, and transfers from stabilization or free cash to cover debt service. This category totals \$1,432,159.



Local aid from the State is the final revenue category. We are assuming local aid will be level funded at FY14 amounts. Our largest source of local aid is Unrestricted General Government Aid (UGGA). UGGA topped out at \$1,454,476 in FY08. In FY15 we are assuming UGGA at \$1,137,900. This is equal to what we received in FY14. Other local aid accounts, including State Owned Land, Quinn Bill, Public Libraries, Veterans' Benefits, and Elderly and Veterans Exemptions, remain uncertain. In FY14, these other accounts totaled \$285,671. In FY15 we are using the Governor's numbers, which are slightly lower than FY14. For the purposes of this budget draft, total local aid is estimated at \$1,395,947. However, comments from the State House lead us to remain hopeful that the Legislature will provide local aid higher than the Governor's

budget. If local aid changes to the positive prior to Town Meeting we may amend the budget and restore some items that are currently not included.

As I mentioned in the introduction, Townsend has a revenue problem more than a spending problem. The primary culprit is local aid. As shown in the table below, total local aid from the State peaked in FY09 at \$1,892,874. We project total local aid in FY15 to be just \$1,395,947, a drop of \$496,927. It is easy to imagine how much different our fiscal picture would be with an additional half-million dollars.



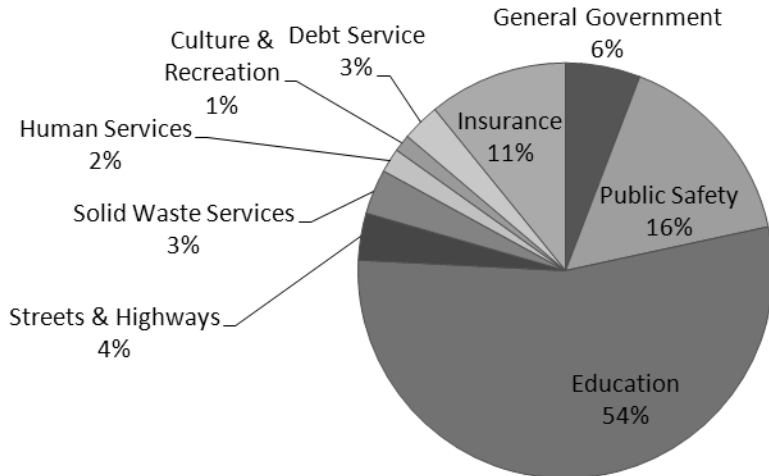
Expenditures

Expenditures are the other piece of the budget puzzle. The following are some expenditure highlights:

Education: Public education is our largest expenditure at 54% of the General Fund budget. The Nashoba Valley Technical High School (NVTHS) approved a budget that was 5% higher than FY14. Townsend’s assessment is \$1,034,072, an increase of \$61,549 over FY14. The North Middlesex Regional School District (NMRSD) certified its budget with a 2% increase. This resulted in an assessment of \$8,989,357, an increase of \$406,235. As noted above, the school assessments more than exhaust our allowable 2 ½% increase under Proposition 2 ½. This makes funding non-school budgets challenging. We must remember that school budgets are heavily dependent on State mandates. Decisions made at the State level will almost certainly alter our position. As we remain hopeful for additional local aid we also remain hopeful that the Legislature will increase school aid and regional transportation aid which will help the overall budget.

Municipal Spending: Forty-six percent (46%) of the budget belongs to non-school or municipal functions. The largest of these is public safety at 16%, insurance at 11%, and general government at 6%. The remaining 13% of expenditures is shared among streets and highways, solid waste, human services, culture and recreation, and debt.

Expenditures by Functional Area



County Retirement Assessment: Last year saw a 36% increase in our Middlesex County Retirement assessment. This was necessary for the system to fully fund its obligations by 2040 and bring average annual growth assumptions in line with market performance for the years prior to FY14. Our FY15 assessment is \$673,724, a 4.4% increase. Recent years have seen strong performance in equity markets and we hope this will bode well for our assessments in future years.

Health Insurance: Employee health insurance is another significant cost center. At this time we are budgeting a 7% increase over FY14. We continue to work with our insurance pool, the Massachusetts Interlocal Insurance Association (MIIA), and our benefits advisors, Cook & Co., to find savings in our employee health insurance budget. We are hopeful we will identify further cost savings in health insurance.

Curbside Trash Collection: The Town's curbside trash collection program is a large cost center and one over which we have some control. Due to restrictions on the number of bags or barrels residents can put out for collection we have seen reductions in tonnage. In FY15 each household will be able to place two 35 gallon bags or barrels out for pick up, down from three in FY14. This is expected to result in further tonnage reductions, saving us tipping changes.

Personnel Costs: Personnel costs are a large piece of our budget. I am not proposing any reductions to current employees for FY15. There may be opportunities to reduce costs as positions become vacant and we will continue to explore options while maintaining services. The Board of Selectmen made a commitment to employees with the compensation and classification plan. Increases of 2 ½% for non-union personnel are factored in. Most collective bargaining units are scheduled for 2% increases.

Other Post-Employment Benefits: Funding of other post-employment benefits (OPEB) is a huge nationwide problem. Cities and towns are scrambling to fund their OPEB liabilities. Among area communities the lowest OPEB liability is \$5.5M and the largest is \$168M. As noted previously, Townsend does not provide retiree health insurance and therefore does not have an OPEB

liability that needs to be funded. We are fortunate to be in this position. However, we are carefully watching the Legislature as a bill currently under consideration could dramatically alter this landscape.

The current general fund budget is projected to be \$18,495,248, 4.6% above FY14. As noted above, this number is certain to change as we are still early in the budget cycle. As the remaining revenue and expenditure numbers become clearer the budget will evolve and be finalized for the May 6, 2014 Annual Town Meeting.