FINANCE COMMITTEE REPORT

Dear Resident of Sudbury,

This report will assist you in understanding Sudbury's fiscal year 2012 ("FY12") budget – from July 1, 2011 through June 30, 2012 - and the related financial articles that will be presented to you at Town Meeting beginning on May 2nd. We believe, above all, the participation of an informed voter is essential for the success of Sudbury's democratic process and continued fiscal health.

The Finance Committee is responsible for reviewing budgets for the town and schools and making recommendations to the Board of Selectmen and to the taxpayers at Town Meeting. In this role, we have no authority to make spending decisions as that is the responsibility of our various elected bodies. Rather, our role is to examine those budgets on your behalf and make independent and informed recommendations regarding the budget and other financial issues. We do so by gathering data and asking numerous questions prior to forming a recommendation.

This diligence process happens throughout the year as we meet with the Town, the K-8 School System, and the High School in regularly scheduled Finance Committee meetings as well as in smaller liaison meetings between one or two FinCom members and the management teams for each cost center.

This report is the culmination of a six month budget process. In October 2010, the FinCom issued budget guidelines to the leaders of the three principal Sudbury cost centers - Sudbury Town Departments (the "Town"), Sudbury Public Schools ("SPS") and the Lincoln-Sudbury Regional High School ("LSRHS" or the "High School"). In preparation for the budget hearing process in February 2011, we asked each cost center to prepare two budget scenarios for FY12:

- a Non-Override Budget that allows for annual growth of 1.87% for each cost center and was based upon expectations regarding State aid and local receipts as of the date this warrant went to publication; and

- a Level Services (or roll-up) budget that assumes each cost center maintains the same staffing levels in FY12 as funded through their FY11 budgets, with the costs for FY12 based on the current contracts in place for their various collective bargaining units.

<u>What about the "4.5% budget" presented last year?</u>

As a matter of background, in early 2008 the Finance Committee concluded that the recent 6.5% per annum growth in the cost of operating the schools and the town was not sustainable and would likely lead to a series of no override votes that could have significant adverse consequences for the quality of our schools and other town services. After much discussion, in the fall of 2008 and in anticipation of the negotiation and renewal of all of the major Town and School labor contracts in 2009, the FinCom voted to recommend a spending growth limit of 4.5% per annum. This growth limit was meant to be a guideline for budget growth; a maximum, not a minimum. Moreover, this guideline was constructed prior to the onset of the international financial and fiscal crisis experienced in 2009 and 2010.

Unfortunately, like most communities in Massachusetts, Sudbury continues to feel the impact of the recent economic recession while confronting financial challenges caused primarily by decreasing state aid, lower local non-property related taxes and continually escalating employee costs, particularly healthcare and other benefits for both active and retired employees. As a result, while the FinCom recognizes that the current labor agreements were negotiated within the context of a 4.5% fixed growth budget, and in many cases provided a rate of growth well below the 4.5% maximum, those same agreements did not fully address the context of the fiscal crisis at the time and the accompanying uncertainty about future non-property tax revenues. Future budget guidelines beyond FY12 will need to carefully consider the likelihood that non-property tax revenue will most likely remain depressed over the next several years. As a result, sustainable budget growth is likely to continue to be constrained well below the previous 4.5% limit.

Recommended Non-Override Budget

For FY12, we are recommending only a Non-Override Budget of approximately $80.7 million at this time. The Non-Override Budget represents a tax increase of approximately 2.37% ($254) on the average assessed home value of $628,000, and a total increase in taxes of $1,600,339 including new growth and commercial property taxes.

The Non-Override Budget is in compliance with Proposition 2½ ("Prop 2 ½"), which was approved by Massachusetts voters in 1980 and first implemented in fiscal year 1982 (M.G.L. Ch. 59, sec. 21c). It limits the amount of revenue a city or town may raise, or levy, from local property taxes each year to fund municipal operations without the approval of taxpayers at the ballot box. Prop 2 ½ is not meant to be a "fiscally responsible spending benchmark". Exceeding this level should not necessarily be construed with negative implications towards a town's or a schools' financial management. It is meant to reflect a "check and balance" point at the local level: town officials cannot raise taxes more than allowed under Prop 2 ½ without an affirmative vote of the taxpayers. To spend more money, town officials have to "make their case" to the taxpayers who can apply their own test of reasonableness by their votes at Town Meeting and the polls.

The FY12 Non-Override Budget represents a 1.87% increase in the operating budget for each cost center compared to the FY11 budget. The difference in growth between the property tax increase of 2.37% and the allowable growth in the operating budgets of each cost center is due to continued projected declines in State Aid as well as stagnation in local non-property tax revenues. Sources of revenue and changes from FY11 are set forth below.

- Under Proposition 2 ½, the tax increase is limited to 2 ½% of the overall tax levy; for FY12, this increase is approximately $1.6 million.
- New growth, the tax on new and upgraded properties, is estimated to generate $350,000 of new revenue in addition to the allowed increase in the levy, down from an estimated $450,000 in FY11; this lower number assumes a continued reduction in new home construction and renovation activity related to the recent economic downturn.
- State aid revenue is estimated to decrease by 5% from FY11 levels, resulting in a decrease of approximately $420,000 (comprised of a 5% reduction in State Aid to Sudbury and LSRHS of approximately $277,000 and $143,000, respectively).
- Local receipts, primarily motor vehicle excise taxes and fees charged for certain town services, are expected to remain flat vs. forecast FY11 levels of approximately $3.7 million.

- The annual school debt reimbursement represents aid from the State and is the same as FY11 as this amount will not change for the remainder of the payments scheduled through FY21 (unless the outstanding debt is refinanced); this aid must be used to reduce the amount of school debt issued and is excluded from the normal Proposition 2 ½ tax levy limit.

	BUDGET FY11	BUDGET FY12	Increase/ (Decrease)	%
Tax Levy	67,418,506	69,018,845	1,600,339	2.37%
SBAB School Debt Reimbursement	1,702,597	1,702,597	0	0.00%
State Aid [(a)]	5,537,686	5,260,802	(276,884)	-5.00%
Local Receipts	3,652,860	3,657,581	4,721	0.13%
Sub-Total	78,311,649	79,639,825	1,328,176	1.70%
Enterprise Funds	1,012,397	1,156,844	144,447	14.27%
TOTAL REVENUE	79,324,046	80,796,669	1,472,623	1.86%

[(a)] Reflects State Aid for Sudbury only; LSRHS State Aid included in "Offsets/Re-apportionments".

Potential Override Budget Scenario

While we are not recommending an Override budget at this point in time, the FinCom has presented certain parameters for an Override budget to the Board of Selectmen for consideration. In summary, this potential scenario results in an Override Budget of approximately $81.7 million which represents a total tax increase of approximately 3.86% ($413) on the average assessed home value (inclusive of the amount previously discussed in the Non-Override Budget). The potential Override Budget scenario represents a tax increase over last year of $2,600,339, including new growth and commercial property taxes, and is comprised of the following three components.

1) $370,000 of additional funding to SPS which consists of approximately $175,000 to cover the gap from their Level Services budget request as well as an additional $195,000 to fund several critical needs that went unfunded due to the reductions resulting from three consecutive years of budget growth below 2% per annum. With this additional funding, the overall FY12 SPS operating budget would increase by 2.94% from the current FY11 budget.

2) $130,000 of additional funding for Town services in the form of an $80,000 increase to the operating budget of the Town departments and an additional $50,000 increase to the Capital Budget for specific capital items needed by the Town. With this additional FY12 funding, the Town operating budget and the Capital Planning budget would increase by 2.31% and 11.32%, respectively, from FY11 budget levels.

3) $500,000 of additional funding to LSRHS to help offset higher Special Education costs and mitigate some of the headcount reductions currently forecasted. With this additional funding, the overall FY12 LSRHS operating budget would increase by 5.70% from the current FY11 budget

As outlined above, unlike recent fiscal years the FinCom is not recommending the same percentage increase for each cost center as a disproportionate share of the override is targeted for LSRHS. As a result, the FinCom believes their override allocation should be tied to targeted savings that could be realized by restructuring the current health insurance plans offered at

LSRHS. Specifically, by moving all employees to a healthcare plan with an average cost of $19,422 per annum for family coverage and $7,296 for individual coverage (as compared to the current average plan cost of $22,842 per annum for family coverage and $8,592 for individual coverage), LSRHS could save approximately $400,000 due to lower health insurance premiums while their employees would collectively save approximately $173,000 in premium contributions. These projected savings are as compared to the costs projected in their current Level Services budget and would still provide employees with a generous healthcare package. In the longer term, we would like to see premiums for all town employees' plans remain or come down into the range more readily seen in the private sector of $14,000 to $18,000 per annum for family coverage and $5,000 to $7,000 per annum for individual coverage.

In conjunction with the proposed benefit changes, the FinCom suggests using $300,000 from the LSRHS's Excess and Deficiency Fund (similar to the Town's Stabilization Fund) to further bridge the funding gap. As demonstrated below, the sum of the proposed changes outlined in this potential Override scenario would address the significant funding gap at LSRHS.

	FY12
LSRHS Non-Override Budget Shortfall	$ (1,182,000)
Parameters for Potential Override Scenario	
1) Override Amount to LSRHS	$ 500,000
2) Savings from Health Insurance Changes	$ 400,000
3) Allocation from E&D Fund	$ 300,000
Total Adjustments	$ 1,200,000
Adjusted Budget Surplus / (Shortfall) =	$ 18,000

Moreover, the FinCom believes that concessions are warranted, in the form of the aforementioned benefit plan changes, in order to preserve one of the principles of the spending growth limit concept. Specifically, that absent major changes, such as a significant change in student population or new service mandates imposed by the State or Federal government, all cost center budgets should be growing at roughly the same rate. This is logical given that all three are labor-intensive services with 70-80% of their budgets consisting of labor-related costs. Limiting each cost center to the same percentage increase would:

- discourage overly generous labor contracts as the cost center with the larger contract settlement will have less money to spend on new hires (or reducing layoffs), technology, classroom materials, etc.;

- encourage each cost center to find ways to operate more efficiently by moving their budgets away from a "cost plus" approach as savings generated could be applied to better uses within that cost center as long as overall spending stays within the growth limit applied to all; and

- avoid the otherwise unfortunate result that one cost center might receive a bigger piece of the pie, over time, without any change in their relative contribution to town services.

As of the date this warrant was submitted for publication, no changes had been agreed to by the LS School Committee and their collective bargaining units regarding healthcare benefits. That said, the FinCom is hopeful that discussions are ongoing and will proceed in earnest so that we might have the opportunity to provide a formal recommendation concerning a potential Override Budget at Town Meeting.

<u>Conclusions</u>

Over the past several years, the Town's fiscal situation has been severely constrained by increases in the cost of wages and benefits, costs which have risen much faster than the rate of inflation. Moreover, with one of the highest levels of households with school age children in the State, we have a much higher demand for education services relative to other communities. On a comparative basis, Sudbury has amongst the highest per capita spending on education in the entire State. That said, our spending on schools and services as measured on a per student basis is in line with, or lower than, many of our peers.

However, our cost structure is constrained by the fact that our revenue structure is heavily dependent on property taxes with only 7% of Sudbury's total revenues coming from commercial property taxes and 70% coming from residential taxes. As a result, residents bear the brunt of any tax increases.

In the short-term, it is unlikely that our non-residential tax revenues will see any meaningful increases given the current economic climate and the potential continued decreases in state aid and stagnation of local receipts. For the past three years, these non-residential tax revenues have decreased substantially. As a result, the Finance Committee believes the Town will increasingly be confronted with three alternatives:

- additional overrides needed to fund our ongoing level of services given current organizations and cost structures;

- reductions to staff, and therefore services, within our current organizations and cost structures in order to fit within the constraints of Proposition 2 ½ and avoid overrides; or

- changes to our current organizations and cost structures that enable our Town to deliver substantially (but perhaps not completely) the same level of services at a lower overall cost.

The Finance Committee believes that achieving the latter of these three alternatives is imperative if we are to avoid or limit either of the former alternatives. To that end, we encourage the Selectmen and the School Committees to continue their efforts to reduce our structural costs. Several initiatives have already been implemented - including reductions in the rate of growth of Town and SPS employee health insurance, enhanced cooperation among school administrations, and sharing of staff with neighboring communities to reduce overall costs. However, more is needed.

In addition to these cost initiatives, we support the Selectmen's on-going efforts to sustain and grow our commercial sector by moving forward with efforts to fund the development of a wastewater treatment plant to serve the Route 20 area. Over the long-term, diversifying our tax base and securing revenue opportunities beyond the traditional residential property tax is critical.

We strongly urge you to be informed on the budgets being presented for your consideration. You have several avenues to increase your understanding of how each budget will affect the level of services, schooling and quality of life in Sudbury. Please review the Finance Committee Report section of the Town Warrant; attend budget forums; watch the Finance Committee budget hearings, which will be rebroadcast on Channels 8 (Comcast) and 31 (Verizon) during March and April; and review the vast array of budget materials available on the town and school websites. Also, do not hesitate to ask questions of your elected officials and committee members.

Whether or not you agree with our findings and recommendations, please make sure that when you cast your vote, it is an informed one.

Lastly, the Finance Committee would like to recognize and extend thanks to the employees of the Town, SPS and LSRHS, and the various committees for their support and contributions during the preparation of the FY12 budget.

Respectfully yours,
Sudbury Finance Committee

Jim Rao, Chair
Joan Carlton
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