

Town Manager's
FY10 Fiscal Summary
(July 1, 2009 – June 30, 2010)

Executive Summary

The challenge of balancing the FY10 operating budget took no one by surprise. The inevitable School Choice shortfall has long been anticipated. In last year's fiscal summary the shortfall was cited for FY10 and early comprehensive fiscal planning was suggested. Such planning did occur in meetings during the past summer with the Board of Selectmen, School Committee and Finance Committee participating. The magnitude of the fiscal challenge was quantified and directions to mitigate that challenge were given.

The estimated shortfall for FY10 was nearly \$1.7M. Based upon an agreed upon apportionment of anticipated new property tax revenues allowed by Proposition 2 ½ the shortfall attributed to the Schools was \$650,000 and the Town \$1,050,000. Ironically, our national economy dramatically worsened after the Town's summer fiscal planning meetings. Despite the fact that this widespread economic decline heightened the need to minimize the municipal tax burden, it coincidentally brought with it lowered gas prices. This helped minimize the estimated budget shortfall. By utilizing existing fiscally conservative policies and generally budgeting more tightly the Town's general government was able to formulate a FY10 budget which eliminated entirely its expected shortfall. The Schools reduced their estimated FY10 budget shortfall to \$558,873. Due to the reduction from the Commonwealth of 10% of Chapter 70 school aid, the operational override required to offset the shortfall in FY10 is a total of \$630,000. If this override is presented to Town Meeting and approved, it would have the effect of increasing the Town's tax rate by 10 cents. The resulting annual impact on the average Chatham taxpayer would be \$60.

For the past several years the Town's payments on its debt for capital projects has declined. This "debt drop off" has been appropriated and used to fund small capital projects and to replenish the Town's stabilization fund. This budget plan proposes not to appropriate that debt reduction in FY10 and thereby allow the corresponding tax savings to be used to offset the cost of the School shortfall override. The debt reduction available for this purpose in FY10 is \$670,000. As a result, even if an override of the magnitude suggested passes, then the impact on the tax levy will be entirely offset. The tax levy for FY10 will stay within the allowable 2 ½% growth limits.

This report details not only the budgets being offered to the Town for its consideration, but the process by which the budgets were balanced. Every effort was made to minimize service reductions in the formulation of the FY10 budget; the budget reductions made are clearly enumerated in this report.

Description	08 Actual	09 Approp	10 Dept Req	Proposed Budget FY10	%
Expenses					
Operating Budgets					
General Government	\$ 1,835,116	\$ 1,950,882	\$ 1,945,314	\$ 1,945,314	-0.29%
Public Safety	5,304,333	4,909,894	4,871,683	4,871,683	-0.78%
Community Development	752,976	805,110	752,600	752,600	-6.52%
Health & Environment	820,558	844,953	828,510	828,510	-1.95%
Public Works & Facilities	3,704,483	3,865,631	3,907,242	3,907,242	1.08%
Community & Social Services	915,701	952,408	941,265	941,265	-1.17%
Education	9,002,755	9,126,983	10,087,144	10,087,144	10.52%
Employee Benefits	3,014,185	3,492,885	3,709,041	3,709,041	6.19%
Undistributed Ins. & Reserve Fund	348,560	333,902	351,097	351,097	5.15%
Debt Service	<u>5,094,473</u>	<u>5,118,384</u>	<u>5,363,490</u>	<u>5,363,490</u>	4.79%
Operating Budget Total	<u>\$ 30,793,139</u>	<u>\$ 31,401,032</u>	<u>\$32,757,356</u>	<u>\$32,757,356</u>	2.31%

Introduction

The Town of Chatham had advanced notice of its fiscal challenge in FY10. The following is an excerpt from last year's Town Manager's Fiscal Summary:

"The Town has relied upon its School Choice receipts to subsidize its school budget in a manner which is not sustainable. The inevitability will become apparent not in FY09, but certainly in FY10. Candid discussions and co-operative fiscal planning must occur in the immediate future amongst the Board of Selectmen, School Committee and Finance Committee in order to successfully address this challenge."

The meetings recommended above were held during this past summer. The magnitude of the FY10 fiscal challenge was quantified and possible mitigation efforts were identified. Administrators from both the Town and Schools set to work to prepare their respective budgets for FY10.

The Town has recently been commended for its on-going efforts to plan its future needs in a manner which is both thorough and fiscally innovative and sound. The following is a second excerpt from last year's Town Manager's Fiscal Summary:

"When Standard & Poor's recently awarded the Town of Chatham an improved bond rating, their independent fiscal analysis pointed to sound financial planning and strong management practices as the key elements in their decision to do so. For more than a decade our community has been able to limit the tax impact on its citizens within the restraints of Proposition 2 ½. What an independent bond rating agency, neighboring communities, and anyone else observing objectively, may have found remarkable about this community's achievement is that while maintaining a low property tax rate Chatham has improved municipal services and made significant progress towards replacing its aging municipal infrastructure.

As we planned our FY09 budgets, the Town continued to enhance its fiscal planning. Conservative fiscal policies incorporated into our planning for some time now are being increasingly relied upon due to the recent economic downturn. Pre-payment of debt and stockpiling of reserves will enable our community to continue to provide excellent municipal service levels and to continue to replace and expand our capital facilities. In addition, the Town of Chatham continues to move forward in an attempt to resolve its single greatest environmental challenge by expanding its sewer system. It is doing so in a fiscally conservative manner considering foremost the taxpayers who can least afford any additional tax burden."

The Town of Chatham could take this much deserved pat on the back and rest on its laurels as it faces the significant fiscal challenges of FY10. Instead, it has chosen to set an example for municipal organizations by formulating an operating budget which continues to provide exemplary municipal services while keeping in the forefront of its planning those taxpayers least able to afford an increased fiscal burden. The community has done so by adhering to and strengthening of its conservative fiscal policies (Attachment #1).

One such policy allows growth in municipal services in accordance with identified need and Board of Selectmen's goals in positive economic times. New revenue sources allow new expenditures, which are added only while coincidentally buffering reserves. The corollary of this fiscal policy must also be implemented when economic times suffer. The reserve buffer allows this transition to be measured and smooth.

The FY10 budget herein proposed represents the implementation of this fiscal policy: it shrinks costs as revenues shrink in a measured fashion with minimal loss in municipal services and an affordable increase in the tax burden.

Background

Proposition 2 ½, so called, was passed by the Commonwealth in 1979 and was implemented in 1980. This law limits the growth of a municipal tax levy to a 2 ½% growth above its previous levy limit without specific authorizations known as overrides. Overrides can be for capital projects or for operational expenses. This strict 2 ½% levy growth can be annually subsidized by new taxable property growth. This law has assured reasonable property tax growth in the Commonwealth. However, since external economic growth factors oft times make it challenging for municipalities to keep its budgetary growth to within the 2 ½% limit, municipalities have expanded non-property tax revenue sources in order to balance the budget. The statute has also demanded innovation by communities in order to properly fund demanded services.

A common misunderstanding about Proposition 2 ½ is that as home values grow so does tax revenue. So in prosperous economic times more tax funds are available. With the exception of "new growth" as described above, that is categorically untrue. A municipal tax levy is defined by the following formula: Levy = Value x Rate. A tax levy can not increase outside the restraints of Proposition 2 ½. Therefore, as values grow tax rates correspondingly decrease. Therefore, no new tax levy or tax windfall results. Tax levy is strictly controlled by Town Meeting and/or electoral votes.

The result in Chatham, which has experienced significant value increases in the past decade, is a reduced tax rate. The tax rate has become the lowest on the Cape and one of the lowest in the Commonwealth. Since the Town of Chatham has strictly and intentionally monitored its municipal expenditures, then the Town's tax rate relative to those of other communities has been more dramatically reduced. As our economy continues to lag, the Town's tax rate may increase as values decline, but will do so relative to neighboring communities. As long as spending or levy is controlled, then our tax rate should continue to rank amongst the lowest in the State.

Each year the Town determines how much additional revenue is available within the limits of Proposition 2 ½ in order to balance its operating costs. In FY10, the following new tax levy was available:

2 ½ Allowable	\$520K
New Growth	<u>250K</u>
Total	\$770K

Since the passage of Proposition 2 ½ and the 1993 Education Reform Act schools have lost their fiscal autonomy. Therefore, a method of apportioning an appropriate share of available revenues for the schools needs to be determined. A mechanism for this apportionment, or a school formula, was devised by the State. This formula assured that a minimum amount of funds were available to fund school budget increases. This formula became unworkable for the Town of Chatham two fiscal cycles ago and a comparable and equitable formula has since been developed specific to Chatham. Maintenance of a spending formula, in a manner determined to be fair to local schools, is a cornerstone of municipal finance. With a formula a fair share of municipal growth revenue is apportioned to the School Department and other Town departments. A copy of Chatham’s local formula is addended to this report as Attachment #2.

Based upon the Town/School distribution formula, the following funds were determined to be available to balance the FY10 budgets respectively.

Town = \$468,369
 School = \$301,631

Annually the Town of Chatham roughly estimates anticipated budget growth versus available funds to determine the magnitude of its fiscal planning challenge. This year it was anticipated that the School deficit would be magnified by a known \$270K deficit in School Choice revenues.

School Choice funds are non-property tax funds which are available for the schools to balance their budget. Since Chatham schools have such an outstanding reputation, the number of students choosing to attend Chatham schools from neighboring communities has increased. School Choice fees are fixed by the Commonwealth for non-special needs students at \$5,000/yr. Despite increased School Choice revenues, increased School spending has finally in FY10 outstripped the Town’s School Choice reserves. This was anticipated. The amount of the School Choice deficit in FY10 is \$270,000.

At meetings held this summer the Town was able to quantify the anticipated FY10 deficit for both the Town and the Schools. These deficits are shown below:

<u>Town</u>		<u>School</u>	
Salaries, Steps	\$ 400K	School Choice deficit	\$270K
5 year Staffing	-	Salaries	205K
Health Insurance	250K	Health Insurance	225K
Pension	125K	Pension	15K
Utilities, Gas	200K	Supplies	40K
Transfer Station	300K	Other	<u>150K</u>
PD/O.T.	50K		\$905K
Fire/O.T.	100K	Available	<u>\$270K</u>
Union Salaries	<u>100K</u>	Deficit	\$635K
	\$1,525K		
Available	<u>480K</u>		
Deficit	\$1,045K		

During the summer fiscal planning meetings not only were these anticipated deficits quantified, but possible mitigation efforts were identified. Interestingly, as the national economic situation worsened at the end of the summer and fall, oil prices coincidentally began to decline. Lower fuel prices relieved some of the deficit pressure, but increased the Town's need to curtail tax spending for the average homeowner now struggling in a recession.

Municipal Budget Categories

Prior to any budget review it must be understood that an annual municipal operating budget consists of many categories and in some cases warrant articles. All budget components must, combined, fall within the restraints of Proposition 2 ½ or be exempted from it. In Chatham, each budget category has a determined funding source and a corresponding fiscal policy. Budget categories are enumerated and briefly explained below.

- Annual Operating Budgets (general and water)
These budgets are the two chief operating budgets for the Town in the upcoming fiscal year. The General Government operating budget is funded by the tax rate and includes all Town departments, including the Schools. The Water Department operating budget is funded by water revenue.
- Cost of Living Increases
A separate warrant article funds cost of living increases for all municipal employees, unions and non-union, except School employees who are funded within the School Department's operating budget. These costs are funded by property tax revenue.
- Five Year Capital Plans
Both a General Government and Water Department capital plan are funded each year. The capital budgets are funded by free cash and water revenue reserves each year contingent upon availability of funds.
- Capital Facility Budget
Large capital purchases are funded by exempt borrowing authorizations. Capital borrowing costs, to date, though exempted from the limits of Proposition 2 ½ and have been funded by "debt drop off" thus not increasing the property tax rate.
- Surtax Expenditures
Each year funds are allocated from either or both the Land Bank surtax or the Community Preservation surtax for specific, designated purposes. Expenditures from these sources do not effect the tax rate.
- Stabilization Fund
A reserve or stabilization fund has been generated by the Town in order to address emergency expenditures or to act as a bank for small capital purchases in order to avoid borrowing costs. This fund should not be used for recurring expenses and has overlay reserve funds as its funding source.

Three budget categories or programs have not been integrated into the FY10 budget planning due to the weakened state of our local economy. They are as follows:

- **Five Year Staff Plan**
This plan is used to identify staffing deficiencies in order to adequately address future needs and Board of Selectmen's goals. This planning component facilitates funding challenges.
- **Mid-Range Capital Plan**
This plan identifies and prioritizes smaller, less essential capital projects, which if funded would increase the tax levy.
- **Conceptually Planned, Unreserved**
This plan identifies large projects the need for which has been minimally vetted. Funding source would more than likely be the tax rate. The plan may be used as an overall fiscal context for future needs and tax impact planning. This plan is added to this report as Attachment #3.

FY10 Saving Initiatives

During the fiscal planning meetings this summer, a number of areas were identified which could lead to budget savings. These cost mitigation efforts were undertaken in order to help address the predicted \$1.7M budget deficit. Some of these concepts proved cost effective and will be implemented; others were explored and rejected. One major reduction in the project's budget deficit was due not to the Town's initiative but due to the market reduction of oil prices.

- **School/Town Operational Cooperative**
The areas of Information Technology, Building Maintenance, and Finance were explored with minimal opportunities for cost savings found.
- **Reorganization**
This concept may have proven most effective in achieving budgetary savings without reducing services than any other explored. A full administrative order which details these savings is hereby submitted included as an addendum to this report as Attachment #4. Savings and reorganization effects multiple Town departments.
- **Transfer Station Costs Shifted to Tax Rate**
This concept was rejected since it was determined that it would result in an increase in volume at the existing Transfer Station. However, during the review it was determined that existing private haulers had no objection and, in fact, support an increased commercial recycling effort. Proposed maintenance improvements at the Transfer Station will expedite this in the future.
- **Parking Revenue**
The discussion of downtown parking revenue has started but needs to be publicly vetted at much greater length. The renovation of the most significant downtown lot has been delayed due to lack of matching State funds. However, sticker parking on Bridge Street will commence this season. It is anticipated that additional parking revenue should significantly offset the reduced costs of the Lighthouse Beach operational staffing. Additional funds should be available for appropriation in FY11.

- **Golf Lease**
An expectation of greater revenue from the recently re-bid contract for the management of the Town's golf course did not materialize. The Board of Selectmen expressed interest in raising golf fees in the future if non-tax revenue continues to be a need.
- **General Fees**
Both Board of Health and building inspection fees have been modified to create additional revenue. Mooring fees, perhaps the last remaining fee of significant revenue generating capacity which has not been adjusted to the market, have not been raised and are being held in reserve as a future revenue source for increased dredging costs.
- **Hiring Freeze/Early Retirement**
The hiring freeze was an extraordinarily effective practice. It will continue into FY10. Whenever a position became vacant an analysis was made about the position's need and alternatives were explored regarding alternative service provisions of the components of the job description. The added benefit to the freeze was the opportunity to decrease FTE's without the necessity of layoffs. Service reduction was thereby minimized. Exploration of early retirement opportunities was largely unfruitful due primarily to the lack of a State/County incentive and declining interest/investment rates which made lump sum buyoffs unattractive.

General Operating Budget

The budget reductions described thus far in this report have been unusual inasmuch as this level of communication, public input, need identification and mitigation measures are not normally part of the budgeting process. However, FY10 fiscal challenges certainly warranted this effort. The effort has been innovative and has proven fruitful, with the result being the elimination of more than half of the Town's anticipated general government deficit. The Town of Chatham has made a determined effort to address the challenges of a volatile economy while preserving both municipal services and their affordability to the taxpayer.

Board of Selectmen Goals

The next step in compiling an affordable, service driven municipal operating budget is to complete the requisite annual scrutiny of operating expenses. A municipal operating budget is required to adequately fund certain essential services such as for schools, fire, police and highway maintenance. However, in Chatham, the goals of the Board of Selectmen are used to drive the emphasis on these and other service needs. The annual Board of Selectmen goals are used to provide the requisite prioritization of services in light of the shrinking municipal dollar.

The goals of the Board of Selectmen which are used to drive this budgeting process are added to this report for your consideration as Attachment #5.

Budget Cuts

The next step of the process after the broad initiatives of the summer and the goal-setting of the Board of Selectmen is the more mundane search for efficiencies and budget cuts. The magnitude of the FY10 fiscal challenge demanded even more due diligence. This year the budget balancing challenge was placed squarely on the back of department managers and line staff. The response was extraordinary and innovative. In any municipal operational environment no matter how thorough a review is conducted by a financial oversight group or by elected officials, no one can pinpoint and suggest efficiencies better than those individuals who are charged with providing those services. The effort, or buy-in, this year by staff to bring in a budget that maximized service and minimized cost was extraordinary. Staff members dedicate entire careers to provide service to the community. They also uniquely appreciate as taxpayers themselves the need to do so affordably. They understand that if budget cuts are not done with a full understanding of their impacts, staff will be the one's from whom services will be demanded, but for which they cannot provide.

The following non-staff budget cuts have been made in the FY10 operating budget.

- Transfer Station costs minimized by purchasing trailers, saving money in transportation contract
- Transfer station tipping fee increases delayed to FY11
- Health insurance savings due to deletion of one of two indemnity programs and hiring freeze
- Utilities, Transfer Station hauling fees due to lower gas prices
- Shellfish propagation fee offset larger percentage of budget
- North Beach elimination of patrols
- Chamber of Commerce reduction due to loss of Executive Director

Inevitably, however the Town's goal of eliminating all of its \$1M deficit was not going to happen if reductions in staff did not occur. The hiring freeze preserved vacancies so that re-assignment of duties could be maximized and layoffs of existing staff minimized. In all slightly in excess of eight FTE positions have been reduced from the general government workforce in the FY10 operating budget. The positions deleted were as shown below:

- Water and Sewer Department, 1 FTE Administrative Assistant
- North Beach, .5 FTE Patrol
- Landing Officer, .25 FTE (plus reduction in grade of supervisor)
- Community Development, .75 FTE Secretary (two positions) and .5 FTE Inspector
- Town Manager, .1 FTE Administrative Assistant
- Council on Aging, .75 FTE Outreach Coordinator
- Finance, 1 FTE Assistant Treasurer
- Police Department, 1 STE Sergeant
- Highway, .25 FTE Seasonal Laborer
- Fire Department, 1 Firefighter
- Health and Environment, 1 FTE Lab/Assistant Conservation Agent

In FY10 the reduction in full time employees as shown above effectively reduces from 140 the number of full time employees on the general government payroll by 5%. However, the necessity of doing so in the FY10 budget has been accomplished with minimal loss of service capacity by reassignment of duties. This staff reduction is in keeping with the overall fiscal policy of the Town which allows staff growth as the economy and revenue grow, yet demands staff reductions as the economy and revenue shrink. The chart below illustrates the extent of staff growth in the past decade as our economy and service demands increased. This past growth enables staff reductions such as those recommended in this budget to only minimally impact service provision.

<u>Department</u>	<u>2000</u>	<u>2004</u>	<u>2009</u>
Town Manager	4	3	3
Human Resources	-	3	3
Accounting	2	2	4
Assessors	4	4	4
Treasurer/Collector	6	5	4
Information Systems	1	2	2
Town Clerk	2	2	2
Permits	-	1	1
Municipal Buildings	3	4	5
Police Department	29	27	28
Fire Department	20	24	28
Shellfish	1	2	2
Harbormaster	2	4	4
Coastal Resources	1	1	1
Highways	8.25	8.5	8.5
Solid Waste	4.75	6.75	5.5
Water and Sewer	4	4	4
Community Development	11	7	11
Health	-	3	3
Lab	1	4	5
Council on Aging	3	3	2
Parks and Recreation	<u>9</u>	<u>8</u>	<u>10</u>
	116	128.25	140

The growth of 24 FTE positions during a ten year period seems significant. However, upon close examination it becomes apparent that the bulk of the new positions were added in order to address certain service demands. For example,

- 8 positions were added in the Fire Department to expand shift coverage and reduce response times.
- 7 positions were added in the Community Development (plus Health and Environment) Departments to address increased inspection needs, wastewater planning and project management.
- 3 positions were added in IT to begin to televise meetings and expand computer capability.

- 2 new janitorial positions were added due to restroom construction and building expansion.
- 2 new positions were added in Parks and Recreation to expand programs in the new Community Center and to address older youth counseling needs.
- 2 positions were added to the Harbormaster Department, paid for by mooring fees, to improve the Town's Mooring Management Program.

The FY10 staffing reduction will continue the Town's policy of shifting resources towards areas of need and gaining efficiencies in existing departments.

New Budget Initiatives

Due to fiscal restraints there is only one new budget initiative being offered in FY10. The bulk of the explanation for this initiative for Lighthouse Beach public safety staffing may be found later in this report since a separate warrant article is being proposed for that purpose. However, during the discussion of the waterside safety effort on Lighthouse Beach and due to the lessons learned from recent water related rescues, funds have been placed in the Harbormaster's budget in FY10 sufficient to add a second person seasonally in the patrol boats for either side of Town. This cost has been minimized by utilization of Fire Department personnel with the dual purpose of cross training of emergency response staff.

Water Department Operating Budget

The Town has a separate Water Department operating budget which is funded by revenue generated from water receipts. The Water operations are sub-contracted to a private contractor (as is the Sewer operations) which is supervised by the Town's Water and Sewer Director. Currently, three administrative staff positions are funded by the Town shared between both departments. In FY10 one of these administrative positions has been deleted from the budget. In addition, the supervision of the Department has been transferred to the Town's DPW. The operations contract for FY10 has increased, however, the total for FY10 has been increased only slightly due to this reorganization. The FY10 Water Department budget, therefore, will be balanced without the need for a water rate increase.

Cost of Living Adjustment

Cost of living wage adjustments for both union and non-union employees, except School Department employees, is funded in a warrant article separate from the operating budget. This is a long-standing practice of the Town in order to highlight pay raises for employees. School Department pay increases are contained within the School budget. Cost of living adjustments are given annually in accordance with the annual increase in the consumer price index. A 2% cost of living increase has been placed in this budget warrant article for non-union employees. Fire

Department union employees have been funded for a 3% cost of living increase for the second year of a three year contract, plus a market adjustment increase of 2% on July 1, 2009 and 2% in January, 2010. This market adjustment has been awarded based upon a salary survey of Cape fire department's wage scales and in an effort to maintain a local salary at the market average for Cape departments.

Stabilization Funding

During the past decade the Town has accumulated a balance of more than \$2M in its stabilization fund. This fund is a reserve fund, or a rainy day fund, and is set aside in order to be available for emergency expenditures. In the case of an unforeseen expenditure a community with a Stabilization Fund balance may use the available fund balance rather than spiking its property tax rate. The tax rate may be therefore "stabilized". Bond rating agencies rate municipalities more highly if they maintain a healthy reserve balance in this and other reserve accounts. The Town has set an arbitrary goal of \$2M for this account. This goal has been achieved, primarily by appropriating the overlay reserve balance each year. The overlay reserve, funds remaining after all tax abatements have been paid, will continue to be available to replenish and add to the Town's Stabilization Fund.

In addition to the use of the Stabilization Fund balance for emergency expenditures, it may be used for small capital expenditures in order to avoid borrowing costs. A municipality needs to be extremely cautious about using a stabilization fund balance, or any reserve balance for a recurring expense, since such a practice would eventually deplete a reserve balance resulting in a non-funded recurring obligation or deficit.

FY10 was a particularly challenging year in which to balance the Town's budget. Review of certain departmental requests revealed that certain budgetary increases requested would be short term and not perpetually recurring. Increased expenditure in both the Police Department and Fire Department overtime accounts were due not simply to increased service demands, but due to injured on leave status of several officers or 111F payment obligations. These payments will continue into FY10, but will thereafter diminish. A similar situation has presented itself regarding funding for the Library. The Town funds a significant portion of the costs associated with Library services. However, the balance of the Library budget is funded by the interest generated from an endowment fund. Our national economic decline has reduced this endowment's fund balance and, as a result, the interest, if any, which will be generated and available to fund the Library's FY10 budget.

Both the increased need for funding in the Town's public safety overtime budgets and the Library budget could be addressed by increasing the Town's tax levy. In FY10 such an increase in the levy would need to be added to a proposed override. However, it is the Town's expectation that all of these budget requests will be non-recurring. Injured officers will either retire or return to duty and the economy will improve and interest once again will be generated and available to subsidize the Library budget. If the tax levy is increased and the budgetary obligations disappear, then the excess tax levy could be absorbed by routine future budget requests.

What is proposed for FY10 is an appropriation of approximately \$100K for those various purposes from the Stabilization Fund. This appropriation will “stabilize” the budget until either the expenses are eliminated for the Police and Fire Departments or the revenue flow is re-established for the Library. Since the Town has a recurring revenue source for its Stabilization Fund, this inherent risk in this funding approach is minimized. If more than one budget cycle is required to reverse these budgetary needs, then the Reserve Fund has a sufficient balance not to be depleted dramatically; if the budgetary needs reverse themselves within the upcoming budget cycle, then the appropriated funds will not be used and will return to the Stabilization Fund.

Lighthouse Beach Staffing

Considerable discussion has taken place during the fall regarding an adequate staffing plan to assure the public’s safety at the Lighthouse Beach. A plan has been developed and approved by the Parks and Recreation Commission and the Board of Selectmen and is being presented in a separate warrant article. These costs will be recurring and will eventually be incorporated into the Town’s operating budget. This year, however, this new program will be highlighted in a warrant article for ease of discussion at Town Meeting.

The funding for the plan will be in two parts: an operating expense and a capital expense. The operating expense for FY10 has been incorporated into the Town’s budget planning and will fall within the funding limits of the Town’s formula allocation of available funds within the limits of Proposition 2 ½. The Board of Selectmen has recently authorized sticker parking along Bridge Street. In future years this additional revenue is estimated to largely offset the annual increased costs of this program. Most of the capital component costs of the program are start up costs. Insufficient funding is available for these costs in the Town’s free cash funded five year capital plan. The program capital costs will therefore be funded with the Stabilization Fund balance. Replacement capital costs in future years for this program will be incorporated into the standard five year capital plan.

Override Implications of Operating Budget

Since the original fiscal planning discussions this past summer, it was apparent that for the first time in more than a decade the Town may be faced with a request for an operational override in order to balance its operating budget. Based upon an accepted formula distribution of anticipated additional funds available within the limits of Proposition 2 ½, it was determined that the Town budget deficit was projected at \$1,045,000 and the School budget deficit was projected at \$655,000. The subtotal of \$270,000 of the School deficit was due entirely to a known shortfall in School Choice funds.

The Town was able to offset its entire deficit in a manner described in this report. The Schools were able to partially reduce its formula share of the deficit to \$558,873. If this remaining deficit is funded through an operational override, its passage will increase the tax rate by \$.10. The annual impact on the average homeowner, with a home valued at \$600,000, will be \$60 if the override is sought and passed.

Five Year Capital Plan

The Town's five year capital budget is funded either from free cash, other available reserves or project balance turnbacks. Free cash is generated by revenue from non-property tax sources received in excess of estimates and from budget turnbacks. As expected and due to our economic decline, the amount of free cash available to fund this plan is less than in previous years. This budget consists primarily of annual maintenance accounts such as for buildings and roads, vehicle replacement and small projects. Fiscal policy has been established to enable this budget or program to be used as the Town's first hedge against economic decline. This hedge allows the Town to not immediately be forced to cut operating budgets and services. Certain maintenance balances cannot be fully replenished in this program or projects or vehicle replacement can be delayed. This hedge, or flexibility, can allow time to pass for the economy to recover and revenues to increase.

In FY10 most projects were delayed to an out year in the five year capital plan. Some vehicle purchases were delayed. However, one major maintenance project for the Transfer Station was included in the plan. Routinely, a project of this magnitude would be funded by a capital exemption. Instead, it was funded by free cash in order to eliminate a property tax impact.

Water Department Five Year Capital Plan

The Water Department has a separate capital budget. This budget is funded not from free cash, but from revenue from water charges. The Town has been aggressive in this capital plan in order to systematically replace and expand its water infrastructure. This year the Town proposed to replace the chemical feed component of its South Chatham wells. The project cost of \$1,000,000 will be funded 50% from water surplus and 50% through borrowing. The amortization costs of this borrowing will be paid by revenue reserves anticipated for this purpose. No water rate increase will be necessary.

Stabilization – Transfer Station Trailers

For the past several years, the Town has paid for the costs of its capital facility replacement plan by the increased funding available as amortization costs from previous capital projects decline. The result has been that new projects are funded without increasing the tax rate. A secondary benefit has been that funding is available each year for small projects or purchases as capital exemptions are passed by Town Meeting. The level of payment for annual debt costs remains stable.

In FY10, the use of this "debt drop off" by a capital exemption has been forgone.

The project scheduled for a capital exemption for FY10 is the purchase of four replacement trailers for solid waste transportation at the Town's Transfer Station. The costs to replace these trailers in the past has been borne by the contractor in our annual hauling contract. Purchase of the trailers by the Town reduces pass through interest payments and has allowed the Town to reduce its FY10 Transfer Station budget.

Two funding sources will be used for this \$280,000 purchase. A total of \$130K in Overlay Surplus funds which is normally used annually to replenish the Town's Stabilization Fund, will be applied for this purpose. The balance of the purchase price will be paid for by the Stabilization Fund balance.

"Debt Drop Off"

The fiscal policy of using "debt drop off" to fund the Town's Capital Facility Plan has been very effective. Its result has been the replacement of the Town's aging infrastructure without increasing our tax rate. This fiscal policy has been in place long enough to complete all but the payment of the costs for the replacement of the Fire Station and the partial payment of our replacement wastewater treatment plant.

Each year the funding level for debt payment remained stable by raising funds through a capital exemption. You will have noted in the paragraphs above that the two scheduled items for a capital exemption in FY10, the first year of the Transfer Station maintenance plan and the purchase of Transfer Station trailers, were funded by other sources. The result will be a reduction in the levy of more than \$670,000. This has been done in order to offset the increase in the levy by a nearly comparable amount of the School override. The result will therefore be, in FY10, an operational override of \$630,000 which will not have the effect of increasing the Town's tax rate.

Although, this is good news for the taxpayer in FY10, it will have an impact in future years. From this point forward, all capital projects will become "pay as you go". If and when the Town replaces its Fire Station, then the entire cost of the project will impact the tax rate. The Town will no longer be able to offset capital project costs by its "debt drop off", since this funding source will be used on a recurring basis to fund the FY10 deficit in the School budget.

This "debt drop off" allocation and the new "pay as you go" fiscal policy will be felt immediately, since the first capital expenditure for the wastewater upgrade is being prepared for consideration at the upcoming Annual Town Meeting.

Summary

This has been an arduous process to prepare a budget for FY10 which provided adequate services at a minimal cost. In many respects the paragraphs above illustrate that the costs of the proposed override can be entirely mitigated, but at the expense of future savings on important capital projects. In essence the Town will call in the chits of its good fiscal planning for the past decade to pay for this override.

I am confident that in future years new fiscal policies can be put in place that will further contain costs. However, the service reduction costs will be more dramatic. This year, owing to a hiring freeze and the resultant opportunities for reorganization of existing staff, the Town's costs were contained. It has become apparent during this process, however, that additional or future cost containment would result in the layoffs of positions that are currently filled. The Town should maintain its hiring freeze indefinitely in order to preserve that same latitude in the future.

The fiscal challenge which we are facing will not end in FY10. Even if the local and national economy improves more quickly than has been predicted, we need to continue and re-emphasize our fiscal planning. Can both the Town and the School commit to living within the limits of the distribution formula of the allowable increases of Proposition 2 ½? Should we diligently pursue other non-property tax revenue such as an expanded Hotel/Motel tax and meals tax? We benefited this year by having our elected officials meet jointly to discuss fiscal issues both broad and specific early in the fiscal year. We should do so again in the future.