

To: The Honorable Harwich Board of Selectmen
From: James R. Merriam
Town Administrator

Date: January 7, 2008

Re: Submission of the Fiscal Year 2008-2009 Annual Budget

In accordance with the Harwich Home Rule Charter, Chapter 9 Financial Provisions and Procedures, Section 2-4 through 6, I hereby submit to you the FY 09 Annual Budget recommendations with supporting documentation. This budget has followed the instructions outlined in your budget message to me dated October 1, 2007. As I cited in my first budget message to you one year ago, the Harwich Home Rule Charter date for submittal, is in my humble opinion, at least thirty days premature. The submittal date should be revised to re-align with vital information provided with the Governor's Budget, scheduled for release on January 23rd. Within days following the Governor's House 1 Budget, the Department of Revenue and Department of Education calculate and post on their respective web sites specific data relating to Cherry Sheets and Educational local minimum contribution requirements that become an integral component of building a local budget. As has become my longstanding custom, I submit a budget to you within the context of the larger world around us.

US Government

As we welcome in a new year, Americans who have heard national candidates from both major political parties debate and attack one another over international and domestic issues at last get to vote in their respective State caucuses and primaries with a goal of electing a new President. The Iraq war is one of the most debated topics of these candidates as the war continues without Congressional bipartisan agreement over when American troop withdrawal can be achieved. Other hot topics include immigration, access to and affordability to quality health care and global terrorism / nuclear proliferation as Al Qaeda regains strength in Northeast Pakistan. On the domestic economy, investors lost confidence in risky subprime mortgages which caused credit to tighten and house prices to fall to a 12 year low.¹ Predatory lenders are blamed for offering "teaser-rate" mortgages to borrowers for mortgages they could not afford on the promise that they could refinance their mortgages later to avoid a steep rise in interest

¹¹ "Home sales fall to a 12-year low" Boston Globe December 29, 2007 by Associated Press

²"America's economic perfect storm" Boston Globe December 21, 2007 by Robert Kuttner

rates.² Consumer spending is falling and wages have been flat or declining since 2000. Medical costs keep rising. Former Federal Reserve Chairman Alan Greenspan believes the approximately 3 percent of consumer spending between 2000 and 2005 was funded by home equity loans and credit cards, but with house prices falling and credit tightening, these consumer options are no longer available. The Federal Reserve believes that Americans have accumulated \$920 billion in credit card debt.³ Banks are becoming worrisome over Americans ability to juggle growing and expensive credit card debt with more delinquencies and defaults expected after the holiday shopping season. More than two million home foreclosures are now pending, which further depresses home prices, consumers net worth and discourages new home construction. Massachusetts' communities, with the levy constraints of Proposition 2 & ½, rely heavily upon new construction to generate additional revenue to fund local services.

New home sales have dropped by 34.4 percent nationally over the past year, the biggest decline since 1991. The Federal Reserve's response has been to lower interest rates three times in 2007 to bolster the economy, which has weakened the value of the dollar and increased inflation. Alan Greenspan has described the economy as "getting close to stall speed."

The Federal budget deficit for FY 07 was reported at \$162.8 billion, but would have been reported at \$275.5 billion if the accrual method of accounting had been used. The accrual method reports expenses when they are incurred, not when paid. The U.S. Treasury Department and the President's Office of Management and Budget reported last month that there is a \$45 trillion shortfall between the Federal benefits programs of Social Security, Medicare, Railroad Retirement and Black Lung Program and projected revenues over the next 75 years. According to Comptroller General David M. Walker, "Our government has made a whole lot of promises in the long term that it cannot possibly keep." ⁴Congress is aware of the pending urgency to address the unfunded liability as 78 million baby boomers approach retirement.

Commonwealth of Massachusetts

Massachusetts currently has \$2.3 billion set aside in its Stabilization Fund but has overestimated its Lottery receipts by \$119 million for FY 07 and projected to do so again for FY 08. Governor Patrick has just completed his first year in office but has had very little success in achieving his goals. One of the few "victories" in his Municipal Partnership Act was having legislation approved for municipalities to join the State's Group Insurance Commission (GIC) for group health insurance, yet the municipal unions lobbied to set the bar at 70 percent local union approval through a process called coalition bargaining, which voided any real consideration, except for eight local governmental units. The Legislature must amend the law to provide municipalities a real chance of local acceptance and meaningful cost savings. Governor Patrick's effort to secure additional revenue from three casino licenses, closing corporate tax loopholes and raising meals and lodging taxes have met stiff opposition by the Legislative Leadership. Patrick

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³ "Debt load grows in US" Cape Cod Times 12/24/07 by Rachel Konrad and Bob Porterfield Associated Press

⁴ "Report lists benefits shortfall at \$45 trillion" Boston Globe 12/18/07 by Martin Crutsinger

Administration officials are contemplating the inclusion of casino license revenues within their FY 09 budget to the Legislature.

The Federal Government is withholding \$1 billion in matching highway funds from the Commonwealth because Massachusetts has not set aside sufficient resources to invest in its bridges and roads.⁵ Governor Patrick has filed a new three year Transportation Bond bill which would provide \$500 million in Chapter 90 funds, of which \$150 million would be for FY 08. The Patrick Administration has estimated that there is a \$19 billion upkeep backlog for the Commonwealth's roads and bridges.

To further complicate the Commonwealth's fiscal woes, supporters of a ballot question to eliminate the State's income tax have gathered the required number of signatures to place the question on the 2008 ballot. Currently, the State Income tax generates approximately \$11 billion annually or 40 percent of the State's total revenues. Governor Patrick is quoted that the proposed ballot question is "just a dumb idea."⁶ In 2002, 40 percent of voters voted in favor of repealing the income tax, 48 percent voted against the question and 12 percent left the question blank. This does not bode well for this year's ballot question given that the voters have so few opportunities to reduce their costs and the connection from State Revenues to Local Government services is not readily apparent.

The Massachusetts School Building Authority accepted 400 letters of interest from communities interested in funding school construction projects and voted to move forward with the first 83 projects, though none from the Cape. The Massachusetts Municipal Association continues to lobby for a new revenue sharing plan based upon a fixed share of 40% of state tax collections from personal income, corporate excise and sales.

Cape Cod

The Cape Cod Chamber of Commerce sponsored two economic summits in October and December with demographer Peter Francese, in which Harwich was well represented. Mr. Francese provided a number of Cape demographic trends that he entitled "challenges and opportunities." He cited that the Cape is losing its year round residents, its working age adults, their children and early retirees. The Cape has one of the highest median ages (45.7) in the nation. He noted that all Cape towns have declining school enrollments (down 13 %), yet school budgets are increasing (up by 26 %) supported by property tax revenue from single-family units with few occupants, many of whom are retired. He advocated for more workforce housing and rental units for young adults to support year round workers or families with children in order to sustain the Cape communities long term. He advocated for regional governments to reduce governmental costs, to stop purchasing more open space that increases housing costs and to form incubator businesses for job creation.

The Cape Cod business community has expressed concern over the U.S. Citizenship and Naturalization Services refusal to accept any more H-2b visa applications for the balance

⁵ "US denies matching funds for highways" Boston Globe December 2007 by Noah Bierman

⁶ "Patrick says eliminating income tax would be ruinous" Boston Globe December 2007 by Steve LeBlanc

of this fiscal year. Cape employers rely upon foreign workers to supplement their seasonal workforce.

The independent auditor for Cape Cod Regional Transit Authority recently revealed that the Commonwealth has not reimbursed the CCRTA for the FY 07 State Share of the Flex bus (\$968,334), which serves 7 lower Cape towns including Harwich. (Harwich's share of the FY 07 State share is \$243,536.) The lower Cape towns face the prospect of paying the State Share, losing service or both. Just last week, Harwich received an amended Cherry Sheet Assessment of \$62,000 for the omitted FY 07 local assessment for the Flex bus after the tax rate has been set. If State funding is not forthcoming by the end of January, the 7 lower Cape Towns must move to suspend service. Even with State funding, the mismatch between Flex bus low ridership and its large mostly empty busses must be quickly addressed.

Harwich

Harwich is relatively fortunate fiscally compared to most Massachusetts communities. As our local Chamber of Commerce proudly markets, "Harwich has it all." Our service levels are high and our tax rates and average tax bills are lower than the statewide average, which is achievable through a total assessed value in excess of \$5 billion.⁷ We must continue to demonstrate fiscal prudence in order to maintain these relative advantages.

I wish to publicly thank the Finance Team, which consists of Town Accountant David Ryan, Assistant Town Administrator Nan Balmer, Assistant Assessor David Scannell, Treasurer/ Collector Dolly Parkhurst, School Superintendent Carolyn Cragin and School Business Manager Gary Costin. The Finance Team developed both the Revenue projections and supported the variable school and municipal revenue sharing formula after fixed costs were deducted. Dave Ryan, Nan Balmer and I together scrutinized every municipal account in the Munis budget prep program.

The FY 09 Budget

The Town Administrator budget, as recommended, is balanced! Departmental requests originally exceeded projected revenues by \$1,695,930. Revenues are estimated at \$49.8 million, which represents an increase of 2.5% above FY 08. Projected revenues do not include a General Override or the use of the million-dollar Stabilization Fund. Expenditures are recommended at \$49.8 million. State Charges and the Overlay Account are estimated to increase by 5.7% and Fixed Costs are estimated to increase by 1.2%. The operating budgets were originally submitted in November based upon FY 07 salary and wage rates. With the ratification of 5 out of 6 municipal union contracts, the departmental budget requests were resubmitted with the new FY 09 rates. (The Special Town Meeting scheduled for February 11th is intended to fund the FY 08 raises through transfers from existing Insurance accounts.) Since the school and municipal contracts expired last June, management's priority has been to eliminate this fiscal year the costly Blue Cross Master Medical and Carve out A plan options for employees and retirees and for next fiscal year,

⁷ 2007 State average single family tax bill \$4,232 Municipal Financial Data 37th Edition Massachusetts Taxpayers Association ; 2007 Harwich single family tax bill \$2,938 DOR

to join the Cape Cod Municipal Health Group, a self funded regional collaborative which represents all Cape municipalities except for Harwich and Bourne.

Attached are several documents that provide you with details of the budget recommendations. First, there is a summary sheet entitled Sources Uses of Funds. The column dated January 4, 2008 provides the various revenue sources on the top half of the page. The Charges and fixed costs follow the revenues. Finally, the variable municipal and school budgets are stated at \$16,439,552 and \$14,423,616 respectively, equating to a balanced budget. The second chart is entitled Municipal / School Revenue Sharing Formula. The formula is based upon an equitable methodology of splitting revenues after fixed costs are subtracted.

Electricity and natural gas accounts have been increased by 10% over their FY 08 base or FY 07 actual if the base appeared either over or under-budgeted. The bulk fuel was redistributed to the respective operating budgets to reflect the actual cost center (especially for benchmarking) and to motivate Department Heads to conserve fuel through downsizing new vehicle requests. Harwich was one of the first communities to convert to bio-diesel fuel for its fleet.

Harwich School Budget

The Harwich School Committee and Administration prepared a progressive budget that advances learning at all levels. It is program driven and strives to improve performance as a distinctive district while acknowledging the competitive nature of Choice and Charter options. Proposals include application technology, improved instruction, visual arts, expansion of Spanish into higher grades and a strong science curriculum.

The FY 09 School Budget recommendation is \$14,423,616, which represents a 5.6% increase over FY 08. However, when the FY 08 budget is adjusted to include the School related articles for Maintenance, Technology and PCC, then the FY 09 TA recommended increase is 4.47%. The FY 09 TA recommended School Budget includes the same dollar amount as that approved in separate articles in FY 08 for Maintenance, Technology and PCC. Since the School Department FY 09 request for these three items is \$230,243 higher than what was approved in separate articles in FY 08, then these increased costs should be requested in a separate article and funded from Free Cash.

	<u>FY 08</u>	<u>FY 09</u>
Facilities Maintenance	87,350	171,520
Instructional technology	54,306	200,379
PCC	12,000	12,000
Total	153,656	383,899

Cape Cod Tech

The budgeted amount is \$914,144, which represents a \$99,483 or 12.2%, increase over the current year. School Business Manager Bob Sanborn is awaiting the DOE minimum contribution calculation before refining this request. This request is based upon the highest potential assessment and is most likely to decline by the end of January.

The next document lists the Departmental budgets as approved by Town Meeting for FY 08, as requested for FY 09 by Department Heads and as Recommended by the Town Administrator. It includes the centralization of Vehicle Maintenance within the Department of Public Works (one new mechanic position), a new Emergency Telecommunications budget, the merging of Computer Hardware/ Software and Channel 18 into a new Information Technology budget, a new Jim Noonan Human Services budget, and new budget requests for Cranberry Festival public safety details for \$15,000 and \$3,000 from the Agricultural Commission for the Farmfest. These last two new requests are not recommended within the Operating Budget but are suggested that they be resubmitted separately as articles for inclusion into the Annual Warrant.

Having recently completed a course in Performance Based budgeting, I am pledging to convert our current line item budget into a Program Budget over the next year, and then transform it into performance based budgeting. This will re-align cost centers and provide better-organized information relative to the merits of each program. This effort should be coordinated with Town Accountant David Ryan's task of creating a new Munis Chart of Accounts.

In an effort to become more efficient and to better control costs, a Human Resources/ Personnel Director and a Purchasing Agent position were requested in the FY 09 municipal budget but sufficient revenues have not yet been identified to fund them. Discussions continue with School Administration to collaborate over sharing of resources for Human Resources, Purchasing, Technology and Building Maintenance. These four programs should be prioritized if additional revenue is identified. With regard to technology, both the Town and Schools are striving to improve our web sites to become more informative and interactive. As a convenience to our customers, some of whom own second homes here and others who travel south during the winter, we would like to accept more on line payments. We are also collaborating with our local Chamber of Commerce through its web site to sell the many attributes of Harwich to prospective businesses to improve our tax base.

The Treasurer's Budget includes \$20,000 for parcels in Tax Title in order to reduce the list of outstanding accounts. This financial commitment should be budgeted every year. When processed through foreclosure, some of these properties may have value for re-sale and could be placed back onto our tax rolls, lessening the burden for everyone. Other parcels may be strategically located and added to the Town owned list for Municipal or Conservation purposes without having to expend money to purchase. However, as forewarned by Demographer Francese, Harwich must carefully scrutinize every future land purchase that it has a meaningful public purpose so as not to become a further tax debt burden and make the Cape less affordable for everyone. Our current strategy to purchase finite amounts of land that is about to be developed has increased remaining land and existing house prices and exacerbates the affordable housing crises.

Of equal concern is our current affordable housing strategy. Affordable units that are either tax exempt or under taxed (payment in lieu of taxes) simply shifts their cost of local services to the balance of property owners. Given the Cape's demographic trends, existing homeowners should not be asked to bear this additional tax burden. A successful

strategy would be to build taxable affordable units in which the residents pay for their own services. Examples of this strategy include private developer Chapter 40B construction, Section 8 vouchers, Housing Authority low income rental assistance programs, Inclusionary zoning and accessory apartments.

The FY 09 Debt budget includes \$2 million in authorized but yet unissued debt for roads, Police Station design and wastewater planning, all of which were approved last May. Treasurer Dolly Parkhurst continues to monitor the market for an opportune time to bond this debt. There was \$77,860 in additional debt added to the FY 08 RECAP, so our FY 09 total debt is actually \$8,154 less than the current year's debt.

	<u>FY 09 Debt</u>	<u>Credits</u>	<u>Net Taxable</u>
General	2,352,931	92,250	2,260,681
School	1,419,062	1,352,679	66,383
Water	226,835	209,172	17,662
CPA	860,486	860,486	0
Total	4,859,315	2,514,588	2,344,727

HEA Classification Study

The Harwich Employees Association negotiated a classification study within its previous contract and the study results are due by the end of February. The recommendations are to be incorporated into the FY 09 Operating Budgets through an amendment.

Capital Budget

The Capital Outlay Committee has worked diligently and will be submitting its recommendations to you under separate cover. Dave Ryan and I have attended most of their meetings and worked closely with them. I have recommended a few changes that should improve the process over time. Firstly, I recommended that the Departmental request be retained in a separate column, so that there is a historical record of the requested amount. Secondly, I've asked that the dollar threshold of a Capital request be reduced from \$100,000 to \$25,000 so that these smaller requests also are reviewed. Thirdly, I've asked that the Capital Budget Committee focus more on funding sources with less of an emphasis upon the tax rate.

For FY 09, the single largest project is the construction of a new Police Facility that will be physically joined to the existing Fire Station on Sisson Road forming a Public Safety complex with shared functions. The \$10 million dollar cost will be bonded over 20 years if approved by the voters, as Debt exclusion. The replacement of the 2001 ambulance has been advanced to the February 11th Special Town Meeting in order to address the Commonwealth's concern about its current condition and the fact that there is at least a 6 month lead time for delivery of a new ambulance. The funding of the \$192,000 ambulance would be through a one time only Capital exclusion, if approved by the voters on February 5th. The balance of recommended projects totals \$893,000, all of which would be funded from non recurring Free Cash, which is anticipated to be certified at \$1.765 million by DOR this week. The Water Department Capital budget is funded through the Enterprise Fund with water rates adjusted accordingly.

The Capital Budget Committee is rightly concerned about the future financing of a potential new High School as well as addressing the Town's Wastewater requirements. In both cases, Peter Francese's advice regarding regional solutions has already been contemplated. MSBA classified their review of the High School letter of interest with a regional response. The new MSBA legislation requires cities and towns to bond only the local share of school debt, not like the previous program in which all debt was bonded and reimbursed by the Commonwealth annually for twenty years. This method cuts local debt for schools substantially.

Senator Rob O'Leary has filed a bill that would provide zero interest loans through the State Revolving Loan Program to assist the Cape and all communities finance their sewer projects at lower costs. The zero interest SRF bills have been filed annually by MMA for more than ten years running. A provocative amendment to the Community Preservation Act to allow sewer financed debt to be paid with CPA funds would greatly assist Cape Communities fund this massive Capital cost as their Land Bank debt declines.

I have recommended that the Town fund only \$200,000 from Free Cash for roads rather than the \$750,000 as recommended in the Capital Outlay's printed report. The rationale is that the \$1 million authorized last May is scheduled for paving work this upcoming season, mostly on Route 39. For FY 09, there is a balance of \$70,000 uncommitted in Chapter 90 funds plus \$300,000 in the Highway Revolving Account. With the Governor's Bond Bill, we can anticipate approximately \$488,000 in new Chapter 90 funds by April 1st. All together, with this additional \$200,000 from Free Cash, there should be approximately \$1 million available for the FY 09 paving season.

The Capital Budget Committee worked closely with Harbormaster Tom Leach and the Waterways Committee to identify their capital needs and develop a program to address their infrastructure improvements over time. The Allen and Saquatucket Harbors will require costly inner harbor dredging over the next several years, so capital planning for this work is very important. Coastal Engineering is working with Town officials to locate potential disposal sites for the dredge materials. The ultimate disposal site will determine how costly these projects may become. We will need to search for funding sources, including Federal and State Grants to assist in these inner harbor dredging projects. The Capital Budget Committee is recommending an engineering study for Saquatucket Harbor this coming year to identify potential improvements, including fixed platform loading rather than floating dock access for the Freedom Cruise line.

The channel dredging projects over the past year, combined with beach nourishment, has resulted in much improved beaches that residents and visitors alike were genuinely thrilled with. The channel dredging and beach nourishment program will require annual capital investments.

Unlike my recommendation to submit the Operating Budget later, I recommend that the Capital Budget be submitted earlier than the Charter date of December. Capital budgeting should be first and prioritized with specific revenue sources prior to submittal of the

Operating budget so that the Town annually invests in its infrastructure and the Capital Budget is not competing with the Operating budget for scarce revenues. Some communities actually earmark a certain percentage of available revenues for Capital budgeting purposes.

Conclusion

While the FY 09 budget is balanced without a General Override, it has been a challenge to do so and maintain current service levels. With your Board's support, we were able to submit the Town's first 5 year Financial Plan and look beyond the one- year timeframe. Standard and Poor's should be pleased when we return to the market for a new bond rating. With this budget submittal, we will automatically update the 5 Year Plan. The longer- term financial view should give us time to amend public policies and practices accordingly. It will also give us an opportunity to collaborate with the Schools for greater efficiencies such as with building maintenance, technology, personnel and purchasing functions, and to centralize functions like vehicular maintenance, merge services like joint Public Safety dispatch, and regionalize services as we have proposed by joining the Cape Cod Municipal Health Group.

The Harwich Home Rule Charter authorizes the creation of a Municipal Finance Department without having to follow the lengthy statutory Chapter 43C, section 11 ballot question process. Having created one of the first Municipal Finance Departments in Massachusetts in the mid 1980's and a second in 2004, I strongly recommend that Harwich follow its Charter and merge its financial functions into one Finance Department.

As with the four budget amendments processed last year as new information became available, I would anticipate that there would be further amendments to this year's recommendations. Surely, we will learn more specifics at this week's Massachusetts Municipal Meeting in Boston and with Governor Patrick's Budget in the next two weeks. Now that the Board of Selectmen's goals have been catalogued and tracked, we will have the opportunity to incorporate these goals into the budget process as we transition toward performance based budgeting.