



REPORT OF THE FINANCE COMMITTEE

March 21, 2014

BUDGET OVERVIEW

The proposed total spending for Town operations (Article 5) is \$25,889,157 for FY2015, an increase of 2.6% over FY2014. This number includes the Town's contribution to the School Department. In the discussion below we provide a thorough analysis of both Government's and the Schools' numbers.

The proposed budgets for the Water and Sewer Enterprise Funds (Articles 5A and 5B) total \$3,450,796, a decrease of \$30,974 or 1.0% from last year. These funds are covered solely by water and sewer user fees and are, therefore, separate from the main operating budget and don't affect the tax rate.

The proposed Capital Spending Items (Articles 6, 6A and 6B) total \$1,370,260. The proposal for Town Operations (Article 6) is \$596,060. The proposal for the Enterprise Funds (Articles 6A and 6B) totals \$774,200.

KEY FINANCIAL DECISIONS FOR VOTERS

In addition to the normal requests for approval of routine budget items, there are a few key items for voters to understand this year:

1. The proposed budget includes an unusually large increase in funding for the schools. This is necessary to adequately fund the schools and to eliminate the necessity for a Proposition 2½ override.
2. Separately, the Board of Selectmen, School Committee and the Finance Committee recommend the establishment of a SPED Stabilization Fund as described below. This significantly reduces the uncertainty the School Committee faces in its budgeting process.
3. There are several waterfront projects proposed for this year. Most are expected to be funded by FEMA to the extent of 75%. The process is complicated, but the Finance Committee is recommending their approval.
4. Payments for debt service will increase substantially over the next few years. This assumes that no future debt issues are approved after those in today's articles which is very unlikely.

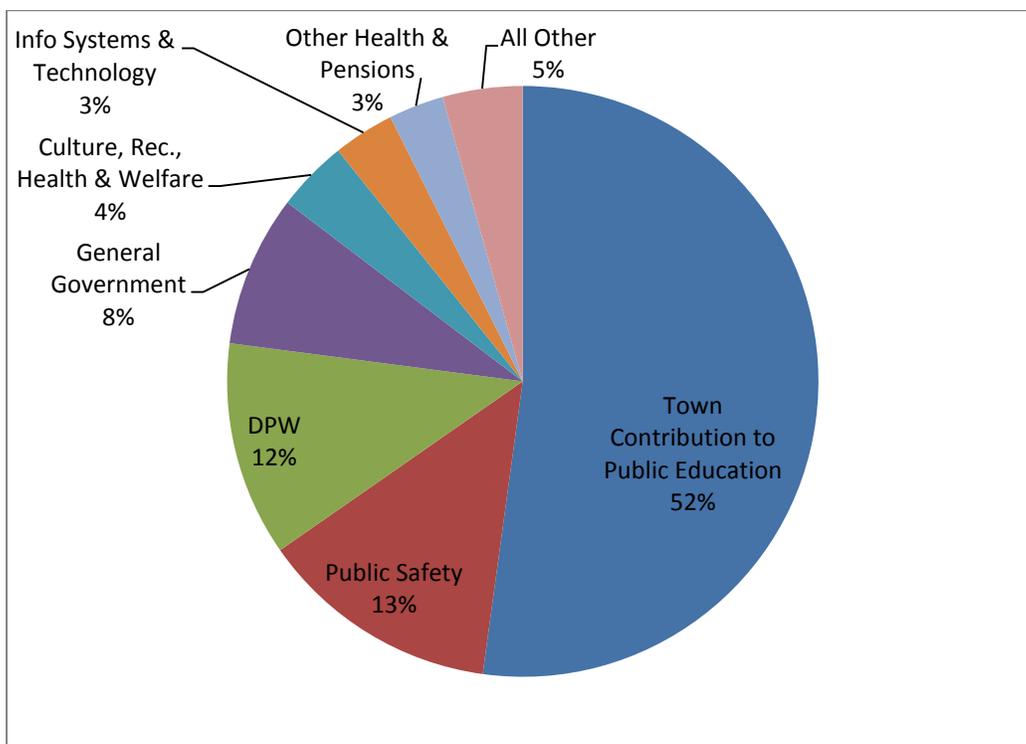
OPERATING BUDGET HIGHLIGHTS

The numbers below show summaries by categories. They represent the total spending of the departments plus the full allocation of employee benefits and debt service attributable to each. In the case of the Schools, the amounts below represent only the Town's contribution. The Schools also receive state and federal grants as well as other monies. In the case of Information Systems and Technology (IS&T) spending, this was previously comprised of separate departments in General Government and the Schools. For FY14 the Town decided to centralize the IS&T departments to have greater coordination and efficiency in this important function. The historical numbers below for FY13 and FY14 have been restated for comparability to transfer the spending from Schools to General Government department.

There are several items in the numbers below that should be noted:

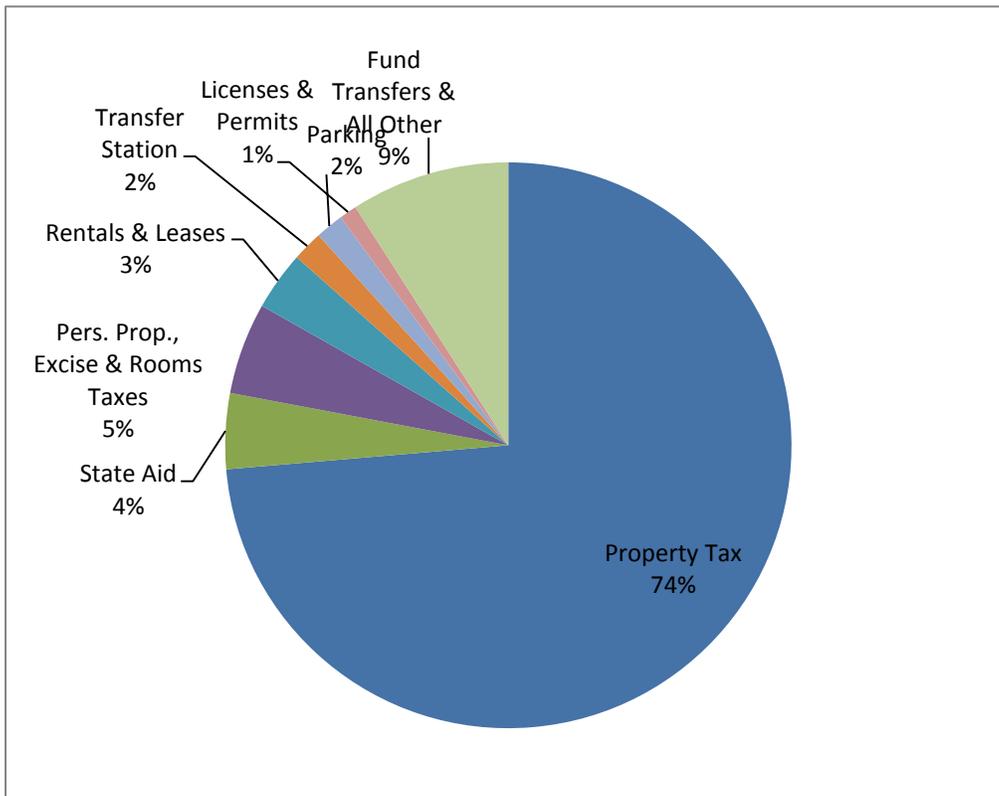
1. The Finance Committee recommends that the Town's contribution to the Schools be \$275,000 more than what it otherwise would be. This will be a permanent increase in the level of base funding for the Schools. In FY14, the Town provided a one-time special funding of \$253,000 to cover extraordinary Special Education (SPED) expenses that year. This is not needed for FY15. See more about this in the Public Education paragraph below.
2. Information Systems' expenses will grow by \$241,707. Some of this increase reflects consolidation of spending for software, telephones and copiers from other operating departments to this department. In total, \$62,351 of spending has been reduced in various other departments and transferred to IS&T. Additionally, the town-wide capital projects authorized in FY14 will add \$128,000 in debt service to the department. Finally, there are two staff members who are now taking health insurance, adding additional departmental costs.
3. After negotiations with our health insurance carrier, they agreed to no increase in premiums for FY15. Other towns are experiencing increases of 5-7% this year and an increase of this magnitude would have amounted to an increase of approximately \$200,000 to \$280,000 annually. Clearly, if this type of increase were to occur next year, actions would need to be considered to reduce such an increase. The Town will consider moving to the GIC benefit levels allowed by state law. Managing this important cost area is complex as it involves 6 union contracts as well as non-union employees, all of whom share a common plan.

Total Operating Expenses			
	2013	2014	2015
Town Contribution to Public Education	\$ 12,503,104	\$ 13,195,463	\$ 13,504,241
Public Safety	\$ 3,119,335	\$ 3,347,363	\$ 3,405,816
DPW	\$ 3,125,622	\$ 3,030,293	\$ 3,041,233
General Government	\$ 2,026,151	\$ 2,174,933	\$ 2,144,554
Culture, Rec., Health & Welfare	\$ 967,160	\$ 998,309	\$ 1,014,022
Info Systems & Technology	\$ 659,690	\$ 625,711	\$ 867,417
Other Health & Pensions	\$ 636,400	\$ 739,924	\$ 779,601
All Other	\$ 1,145,061	\$ 1,129,580	\$ 1,132,273
Total Budget - Article 5	\$ 24,182,522	\$ 25,241,576	\$ 25,889,157



State law requires that the budgets of cities and towns in the Commonwealth be balanced. Revenue sources must be equal to or greater than budgeted spending. The table below shows revenues that are generated locally by the Town or aid that is provided by the state to offset some of the costs. These revenues contribute to decreasing the costs the Town is required to raise from property taxes.

Revenues			
	2013	2014	2015
Property Tax	\$ 18,640,816	\$ 18,963,509	\$ 19,693,859
State Aid	\$ 1,203,936	\$ 1,150,094	\$ 1,148,728
Pers. Prop., Excise & Rooms Taxes	\$ 1,354,268	\$ 1,321,500	\$ 1,391,500
Rentals & Leases	\$ 598,307	\$ 689,829	\$ 894,670
Transfer Station	\$ 378,730	\$ 426,925	\$ 463,900
Parking	\$ 368,449	\$ 337,474	\$ 424,666
Licenses & Permits	\$ 257,732	\$ 226,700	\$ 268,350
Fund Transfers & All Other	\$ 2,478,369	\$ 2,235,234	\$ 2,413,790
Total Non-Tax Revenue & State Aid	\$ 6,639,791	\$ 6,387,756	\$ 7,005,604
Total Revenue	\$ 25,280,607	\$ 25,351,265	\$ 26,699,463



There are several items in the revenue figures above that should be noted:

1. There are three components of the increase in Property Tax revenue. One is the increase in taxes on existing housing stock, which is limited to 2.5%. Secondly, the tax levy may be raised by overrides or debt exclusions. Third, there are taxes based on "New Growth" which is the additional assessed valued of new or renovated properties.

2. Parking Revenue, consisting of meter and parking sticker revenues plus parking fines, shows a large increase, reflecting the increased meter rates recently implemented and supported by the new meters. The Police Department studied the results of the pilot test of new electronic meters in 2012 and concluded that the credit card feature resulted in considerably more revenue per meter than the old ones. Over 100 of these new meters will be in place in the future and we forecast that they will result in increased revenue.
3. Rentals and Leases consist primarily of Long Beach and cell tower leases. The Town owns the land under the cottages on Long Beach. The Selectmen recently decided on new 10-year leases. This means that rental revenue will increase about \$150,000 per year over that period.
4. Some examples of Fund Transfers & All Other are expense reimbursements from the Enterprise Funds, Ambulance Revenues and Mooring Fees.

PUBLIC EDUCATION

The Finance Committee recommends that \$10,452,560 be authorized in Article 5 for support to the Schools' operating budget. In addition, \$178,596 is recommended for tuition payments to Rockport students attending the North Shore Vocational Technical Schools. Additional costs generated by the school system, but included in other sections of the Table of Estimates include Debt Service and Pensions & Benefits shown at the end of the Article 5 Table of Estimates. They are shown as expenses of the Town. Here we will analyze the total school operations including all expenses and sources of revenue. The total school expenses proposed for this year are \$15,689,374. The Town provides a large portion of this, but there are several other sources of funding that are very important. In summary, the funding sources are:

- a. Town contributions of \$13,930,061, of which \$1,311,376 is expected to be reimbursed by the state and federal government, making the taxpayer contribution be \$12,618,685.
- b. Independent revenue of \$1,820,768 is not sourced from the Town taxpayers. Most of this revenue comes from School Choice, Fees, State and Federal Grants. See below for more detail.

Under state law, the School Committee has control of the entire budget after the Town contributions are voted by Town Meeting. To assist the voters of Town Meeting to better understand the financial situation of the schools, we are providing the following analysis. This analysis itemizes all expenses and sources of revenue regardless of who controls them. In the current year, FY14, the Schools are responsible for educating 1012 students, 802 of whom are Rockport residents.

Expenses: Listed below are all expenses associated with educating the students of Rockport and School Choice students. When reading these items, please refer to the table below.

1. Most of the day-to-day expenses are comprised of Labor and Operating Expense. These categories also include the expenses of educating SPED students who remain in our schools.
2. Some SPED students need more specialized instruction than can be provided by our school system. These expenses are designated as SPED Outside Services.
3. As in other Town departments, the annual cost of debt service for school-related borrowing is allocated to the Schools. This also applies to Pension & Benefit expenses of current and retired employees.
4. Some Rockport students attend North Shore Vocational Tech and Essex County Technical Institute. The expenses for these Rockport students are shown in the chart below as a school expense paid by the Town.

Sources of Revenue: As mentioned above, not all of these expenses are paid by the Town's taxpayers. We have identified two types of revenue below.

1. Town Contributions:

- a. The amount of \$10,727,560 will be voted for appropriation for the School Department this year.
- b. The Town will pay the debt service and pensions & benefits of the whole town, regardless of where they are generated. The amounts of these payments which pertain to the school are expected to total \$2,598,085.
- c. The Town will pay \$425,820 to the state directly for retired teacher health insurance that it will provide in FY15.
- d. The Town will pay \$178,596 for tuition at North Shore Vocational Tech, and Essex County Technical Institute.
- e. This year Town Meeting is being asked to approve \$65,000 from Free Cash to fund certain capital outlays in Article 6.

2. Independent Revenue:

- a. School Choice Receiving – The Rockport School Committee agrees to a certain number of openings in each class that are available for Choice students. The Schools receive a little over \$5,000 per student from the sending school system when their students opt to go to the Rockport schools.
- b. The State reimburses Rockport for a percentage of the most extraordinary individual SPED expenses it incurs above a threshold amount (Circuit Breaker).
- c. The Schools receive a number of grants which offset some of the costs of delivering specific education programs and initiatives.
- d. The Schools receive fees for athletics and transportation.
- e. The School Committee can use reserves to cover additional expenses. They estimate that the reserve balances will be \$510,000 at the end of FY14.

Rockport Public Education			
Expenses	FY13	FY14	FY15
Labor	\$ 9,356,755	\$ 9,650,211	\$ 9,955,131
Operating Expense	\$ 853,294	\$ 870,580	\$ 817,826
SPED Outside Services	\$ 1,384,687	\$ 1,875,188	\$ 1,713,916
Needed to Operate - Direct Expenses	\$ 11,594,736	\$ 12,395,979	\$ 12,486,873
Other School Expenses Paid by Town:			
Debt Service (700)	\$ 274,075	\$ 168,575	\$ 215,884
Pensions & Benefits (900)	\$ 2,304,519	\$ 2,379,633	\$ 2,382,201
North Shore/Essex Voc. Tech.	\$ 143,838	\$ 162,217	\$ 178,596
Retired Teacher Health Insurance	\$ 284,947	\$ 352,998	\$ 425,820
Total Other Expenses	\$ 3,007,379	\$ 3,063,423	\$ 3,202,501
Total School Expense	\$ 14,602,115	\$ 15,459,402	\$ 15,689,374
Revenue			
Town Contributions:			
Base Funding - ATM Appropriation	\$ 9,780,672	\$ 10,232,038	\$ 10,727,560
One-Time SPED Expense Contribution		\$ 253,000	
Debt Service (700)	\$ 274,075	\$ 168,575	\$ 215,884
Pensions & Benefits (900)	\$ 2,304,519	\$ 2,379,633	\$ 2,382,201
Retired Teacher Health Insurance	\$ 284,947	\$ 352,998	\$ 425,820
North Shore/Essex Voc. Tech.	\$ 143,838	\$ 162,217	\$ 178,596
Total Town Contributions	\$ 12,788,051	\$ 13,548,461	\$ 13,930,061
Independent Revenue:			
School Choice	\$ 924,927	\$ 1,155,000	\$ 1,150,768
Circuit Breaker	\$ 207,805	\$ 240,991	\$ 320,000
Grants	\$ 418,445	\$ 300,000	\$ 275,000
Fees	\$ 103,349	\$ 120,000	\$ 75,000
Total Independent Revenue	\$ 1,654,526	\$ 1,815,991	\$ 1,820,768
Total School Revenue	\$ 14,442,577	\$ 15,364,452	\$ 15,750,829
Note: The Town receives Chapter 70 from the State, and Medicaid payments from the Federal Government. It pays School Choice Sending.			
Total Town Contributions (from above)	\$ 12,788,051	\$ 13,548,461	\$ 13,930,061
Less Chapter 70 Reimbursement	\$ (1,304,118)	\$ (1,324,168)	\$ (1,377,981)
Less Medicaid Assistance - SPED	\$ (88,522)	\$ (60,000)	\$ (88,000)
School Choice Sending	\$ 102,676	\$ 164,069	\$ 154,605
Funded from Tax Levy	\$ 11,498,087	\$ 12,328,362	\$ 12,618,685

Members of the Finance Committee worked closely with the school department and members of the School Committee to come up with the following recommendations. Our objectives were to:

1. Adequately fund the needs of the schools;
2. Develop a plan for predictable increases in base funding for the schools; and
3. Provide for sudden and unexpected changes in needs for SPED spending.

Accordingly, the Finance Committee recommends that Town Meeting:

1. Approve a funding level change that is \$275,000 higher than the regular increase appropriated for the schools in the past, and
2. Approve Article K which establishes the SPED Stabilization Fund at the initial level of \$200,000. Most of this will come from Free Cash.

SPED Stabilization Fund: This is a stabilization fund that can be used only for changes in SPED Outside Services (a line item in the chart above), which are unexpected, uncontrollable increases in the budget. In future years, the School Department may request a withdrawal in the amount equal to the increased expense level over budget for that year. Alternatively, if actual expenses are lower than the budgeted SPED costs, the schools will request a deposit in the amount equal to the SPED savings into the account. Since this will be a stabilization fund under state law, all deposits and withdrawals would need a 2/3rd vote of Special Town Meeting in April, or Fall Town Meeting in September.

The expectation is that this fund will serve as a buffer against SPED costs that cannot be anticipated during the budgeting process. As a result, the School Committee will not request a Proposition 2 ½ override this year. The School Committee, Finance Committee and the Board of Selectmen expect to work together on an ongoing basis to accomplish both objectives of adequately funding the schools while keeping increased costs to the taxpayers to a minimum.

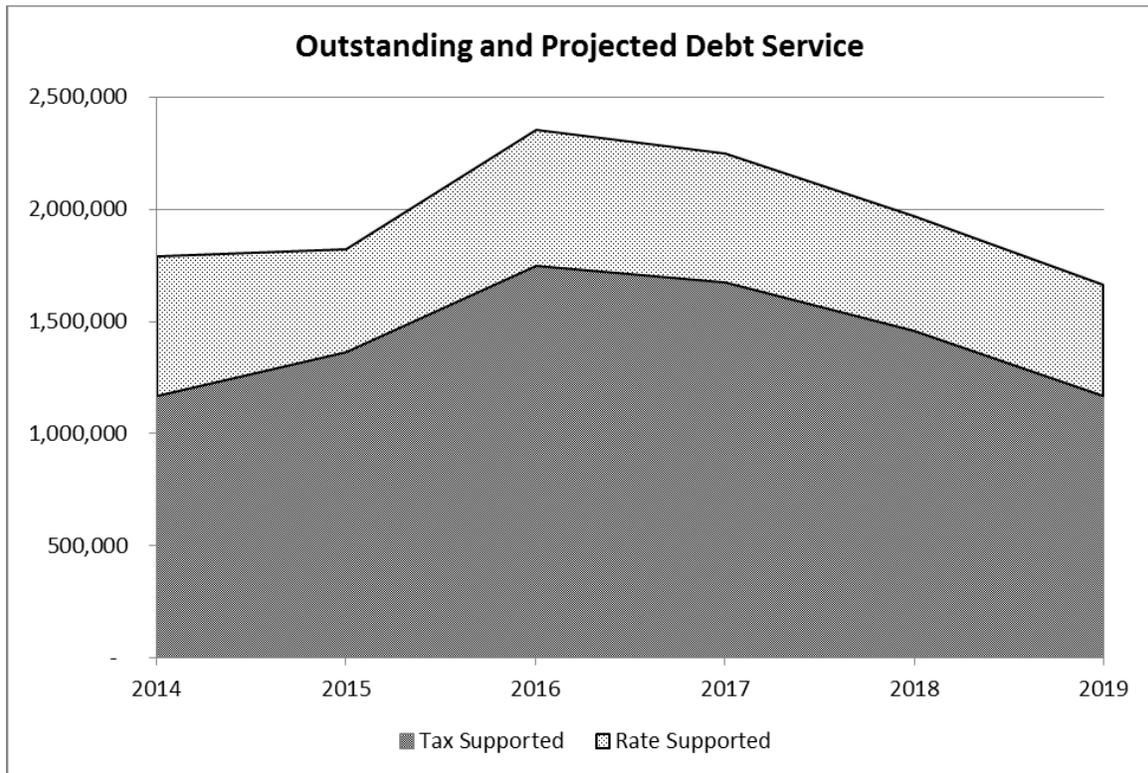
ENTERPRISE FUND HIGHLIGHTS

The Water & Sewer Enterprise Funds each operate separately from the Town’s operating budget. These expenses are covered by water and sewer rates billed to the users, and thus do not affect the tax rate.

Enterprise Fund Budget Expenses			
	2013	2014	2015
Water Fund - Article 5A	\$ 1,498,587	\$ 1,562,939	\$ 1,649,200
Sewer Fund - Article 5B	\$ 2,122,678	\$ 1,918,832	\$ 1,801,596

CAPITAL OUTLAY EXPENDITURES (ARTICLE 6, 6A AND 6B)

The Capital Improvement Planning Committee (CIPC) receives requests for capital items from the operating departments and the enterprise funds. It meets with each department and then prioritizes the requests before making a recommendation to the Board of Selectmen and the Finance Committee. Once the Finance Committee decides what it wants to recommend it presents it to Town Meeting these articles to Town Meeting. Looking ahead, there are a number of large projects that will need to be addressed. These include Town building repairs, Old Harbor dredging, a pumper truck for the fire department, heavy equipment for the DPW, and numerous waterfront projects as they become necessary. The Town will need to control expenses, find additional non-tax revenue, borrow money, or increase taxes temporarily with an override to meet these needs. The Finance Committee recommends that future borrowing be kept to a minimum. The chart below shows that debt service in the next few years will increase merely by funding out existing temporary debt and by borrowings recommended at the ATM this year.



UNFUNDED PENSIONS AND BENEFITS & OTHER FUTURE REQUIREMENTS

There are two significant categories of unfunded liabilities that the town must eventually address. The longer we wait, the more difficult it becomes to deal with these:

1. **Retirement Fund.** The town is part of the Essex Regional Retirement System which includes 19 towns and several dozen regional schools and authorities. Its auditors have determined that the system is underfunded by \$323 million as of a year ago. Rockport's share is 5.26% or \$17 million, so we can expect that our payments will be increasing significantly over the next twenty years. These are funds set aside to fund future retirement payments to both active and retired employees. Retirement payments are important for Rockport's employees because municipal employees are not eligible to be part of the Social Security System, and will receive no payments from it. Rockport does not have control over the funding level or the investment policy of the ERRS. It does, however, have the ability to review the level of retirement benefits of our employees.
2. **Other Post Employment Benefits (OPEB).** These are primarily health insurance benefits to retirees and their spouses. The annual cost of this set of benefits is included as part of the health insurance expense in the operating budget. As is the case with retirement benefits, these are obligations of the town, and will be paid on behalf of our retirees for many years into the future. The state will require that the expected future costs be included as a liability on the Town's balance sheet soon. This will make it a very serious issue for us to deal with. We do not have an organized plan for funding process for OPEB, although we are recommending a deposit of \$79,618 into the fund this year. As it stands today, these payments will increase as our retirees live longer and as health insurance premiums rise. This has the potential to grow significantly, and possibly reduce the town's ability to fund other expenses or require additional tax increases. Rockport must work to control the growth of health insurance, and as a result, OPEB.

STABILIZATION FUNDS

The town has two funds to help it cope with future uncertain needs.

1. Stabilization Fund - \$1,338,593
2. Capital Reserve Stabilization Fund - \$175,202

As discussed above, we are recommending a third stabilization fund and asking this Town Meeting to create it as a special SPED Stabilization Fund and fund it with \$200,000 this year.

YOUR REAL ESTATE TAX BILL

There are several factors that go into the determination of your real estate tax bill:

1. The amount of spending in the operating departments;
2. Plus the retiree pension and health insurance payments;
3. Plus debt service;
4. Less the amount of local revenue; and
5. Less the amount of state aid.

The result is the amount of the real estate tax levy. Under Proposition 2½, this levy is limited to:

1. Last year's levy limit plus 2½% growth;
2. Plus additions to the levy known "new growth" which is generated when a house is new or significantly renovated causing an increase in assessed values and, thereby, creating an increase in the tax base; and
3. Plus any Proposition 2½% overrides previously approved by the voters.

Once the year's levy is established, the tax rate is determined by dividing the levy by the total assessed value of the Town's taxpayers' real estate. Therefore the change in the tax rate is determined by both the change in the levy and the change in the total assessed valuation. The resulting tax for your property is the product of its assessed value and the tax rate.

For FY14, the total assessed value of Rockport's real estate was \$1,694,188,700. To raise the \$19,093,509 that was billed this year, the rate of \$11.27 was required. Therefore, a house assessed at \$500,000 would pay \$5,635.

FREE CASH

The Town has \$829,618 available Free Cash in the General Fund. Because this amount varies greatly from year to year, the Finance Committee supports using it for one-time capital expenditures, for one-time emergency payments and for building up our reserves rather than for funding on-going operating expenses. By using Free Cash for capital outlay, the Town is able to limit additional borrowing. The Finance Committee recommends using \$253,400 to finance Article 6 Capital Outlay items, \$120,000 to fund computer equipment under our five-year plan and and \$407,552 to support Special Articles in the 2014 STM & ATM Warrants. This \$407,552 includes the \$79,618 to be deposited into the OPEB Trust Fund and \$152,934 of the \$200,000 that will be deposited into the new SPED Stabilization Fund. The unspent balance of Free Cash will be \$48,666.

The Free Cash of the Enterprise Funds totals \$384,253 (\$67,951 Water & \$316,302 Sewer). The Finance Committee recommends using \$67,100 and \$307,100 respectively to finance Articles 6A (Water) & 6B (Sewer) Capital Outlay items.

BUDGET UNCERTAINTIES

State Aid revenues are estimates and reflect the Governor's proposals to date. Final State budgets are not adopted until after our Annual Town Meeting and adjustments to our budget will be made at the Fall Town Meeting.

By state statute and Town By-Law, the Finance Committee works directly for you the voters. We are charged with providing you with the best possible information so that you can make informed decisions. We hope you find it so.

The Finance Committee wishes to thank all the Town of Rockport's staff and volunteers for their diligence and patience throughout this year's budget process. Their dedication to the citizens of Rockport in maintaining and improving services is truly appreciated.

We also wish to thank all those who contributed directly to the preparation of this document.

Wally Hess, Chairman

Laurene Wessel, Vice Chair

Frank Hassler

Michael Hughes

June Michaels

Michael Lamoureux

William Wagner

Carl Engel

David Coyne