City of Chelsea

“Renewal”

Five Year Financial Forecast
for Fiscal Years 2012-2016
and
Preliminary FY’12 Budget Overview

to be Presented to the City Council

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Five Year Financial Forecast
Revenue and Expenditure Summary

	FY'12	FY'13	FY'14	FY'15	FY'16
REVENUES	$113,339,344	115,659,251	117,990,280	120,550,292	123,174,453
% CHANGE	(5.17%)	2.05%	2.02%	2.17%	2.18%
EXPENSES	$115,143,568	117,097,324	119,107,366	121,557,838	124,153,130
% CHANGE	(3.66%)	1.70%	1.72%	2.06%	2.14%
SURPLUS (DEFICIT)	($1,804,224)	(1,438,073)	(1,117,086)	(1,007,546)	(978,676)
FREE CASH AFTER FY VOTE	$5.5m	$4.6m	$4.0m	$3.5m	$3.0m

Budget Pressures

SUMMARY

- The economic recovery is not providing relief for the City budget.
- The chronic State budget crisis continues to impact revenues!
- The City is controlling discretionary spending, but employee benefits (health insurance and pensions) continue to rise at multiples of inflation.
- Cost-cutting measures are exhausted, unless the City considers, for examples, closing the senior center or taking a fire piece out of service (neither of which are under consideration).
- Regionalism is underway but not providing immediate financial benefits.
- The City will seek cost savings in benefits (health) and language (overtime) through the collective bargaining process.
- The City is adding police (2), DPW (2) and finance (1) positions through City funding and fire (4 – for a total of 15) through federal grants. The Schools plan on eliminating 5-25 positions.
- In addition to prudent fiscal management, excise tax increases, economic development activities and reserves are keeping the budget balanced.

Budget Pressures

SUMMARY – (continued)

- Non-school Local Aid losses this decade are $21.9m, in constant dollars, and $40m, adjusted for inflation. Non-school Local Aid is down 40% since FY'01 highs, although School Aid is up 54% during that same time.
- Despite aid increase, Schools must cut spending to balanced the FY'12 budget.
- As reserves dwindle, the City's financial flexibility becomes more restricted.
- The City needs to continue to:
  - Control spending,
  - Promote new revenue growth through economic development and entrepreneurial activities, and
  - Lead state debate on local aid, health insurance, pensions and regionalism.
- Otherwise, the City faces the potential of:
  - A depletion and maybe elimination of stabilization balances,
  - Deep service cuts in public safety,
  - A Proposition 2 ½ override,
  - Something worse!

Understanding the Numbers

REVENUES

- LOCAL AID
  - General Gov't – OUCH – FY'12 – assumes another 7% CUT ($500k).
    - Non-school Local Aid is $4.2m below FY'01 high ($10.6m), unadjusted for inflation (DOWN 40%!).
    - Non-school Local Aid is $7m below FY'01 high, adjusted for inflation (OFF 53%).
  - Schools – assumes Gov.'s recommendation, providing a 2.7% ($1.4m) increase in Chapter 70 (but a 100% reduction in Ch. 70 stimulus funding and a $2.4m drop in Federal stimulus funding).
  - Since '00, non-school aid is down an average of 3.7% a year, while school aid is up an average of 3.4%.
  - It is hard to predict any significant increase in Local Aid in the out-years because of State's own budget issues.

- OTHER MAJOR IMPACTS
  - Payments around late taxes (down 23%), Interest (down 41%), Medicaid Reimbursements (down 48%) and School Loan Payments (down 100% - there is a corresponding expense decrease as well) create significant financial burdens on the budget.

Understanding the Numbers

REVENUES

- OTHER (continued)
  - Tax Levy is projected to grow by 2.5% ($919k) plus New Growth ($700k). The New Growth is lower in FY'12 than more robust growth numbers in the previous years (FY'10 - $1.24m) and likely more reflective of what expectations should be for the out-years.
  - Overlay provision remains at the reduced level of 1.5% of the prior year levy ($551k).
  - Fines & Forfeits will see growth from nighttime parking enforcement and Licenses & Permits are expecting no change.
  - Trash fees are expected to rise in the area of 5% yearly ($79k).
  - Meals (down 9% - $25k) and Hotel Taxes (down 14% - $40k) reflect reduced expectations from higher previous year estimates.
  - Motor Vehicle Excise Tax is up substantially (11%, or $500k) and is the main reason why a balanced budget is within reach.

Understanding the Numbers

EXPENSES

- Total spending is projected to be down 3.7% in FY'12 (down $4.4m).
- School spending is projected to increase by 1%, or $730k, while all other spending is down 9.9% ($5.1m).
- The cost of core municipal services (also known as "discretionary spending," which excludes schools, debt service, employee benefits and assessments) is up 0.8% ($200k) in FY'12.
- The School Department, despite an increase in Chapter 70, has had to make significant cuts, as revenue growth is insufficient to keep up with expanding costs and loss of federal stimulus money.
- Wage increases are assumed to be 0.5% FY'12, and then 1%, 1% , 2% and 2% from FY'13-'16.

Understanding the Numbers

EXPENSES (continued)

- Health Insurance rates are up 7.0% in FY'12, resulting in a $420k impact on the municipal budget and a $350k impact on the school budget. Pending legislation at the State House might provide relief on rates, which have averaged a 10% increase over the last decade.

- Retirement costs – The City continues to follow the recommended funding schedule, which results in a 4.5% increase in costs ($250k to $5.8m) for FY'12.

- The City is making its first payment for OPEB (other post employment benefits) related costs. Although the City is not presently required to fund the $227m outstanding liability for retiree health insurance, it is expected that sometime in the future such a requirement will exist. To lessen that burden, a burden which is similar to what the City now experiences with Retirement contributions, the City is proactively placing $150k into a fund the Administration will ask the Council to establish. Standard & Poor's has regularly cited the City's lack of such a fund as a shortcoming of the City's overall financial management, a notation that could have an impact on the City's bond rating (which was reaffirmed this past year at A+).

Understanding the Numbers

<u>EXPENSES (continued)</u>

- Debt Service is down 64% as a result of :
  - The City making a conscious effort to avoid adding too much new debt during this period of fiscal uncertainty. That decision does reduce general infrastructure spending, and increase pay-as-you-go expenses in the operational budget.
  - The early payoff of schools loans which resulted in a net overall benefit to the City of $2.5m. Because the City has previously forecasted a positive net effect from school loan repayments from the State, and because the City has set aside the net overall benefit for future school capital needs and overall city budget reserves, the annual budget’s operational deficit has grown as a result of the refunding decision.

- In the out-years, debt continues to decline. This is again reflective of a conscious decision to avoid adding too much debt by paying for more capital projects through a pay-as-you-go process.

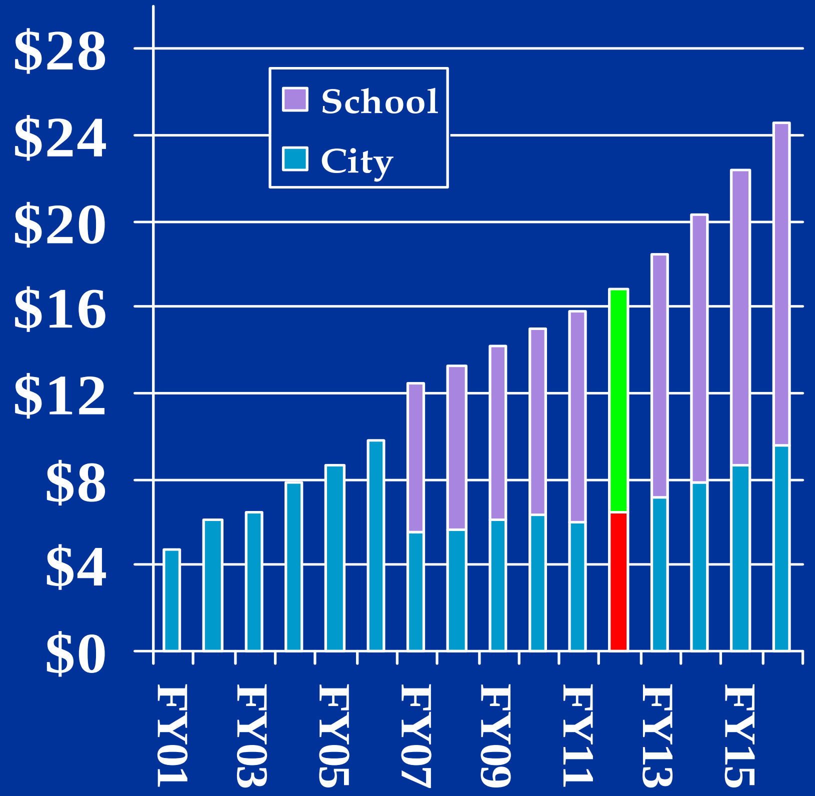
Budget Pressures

Expenditures:

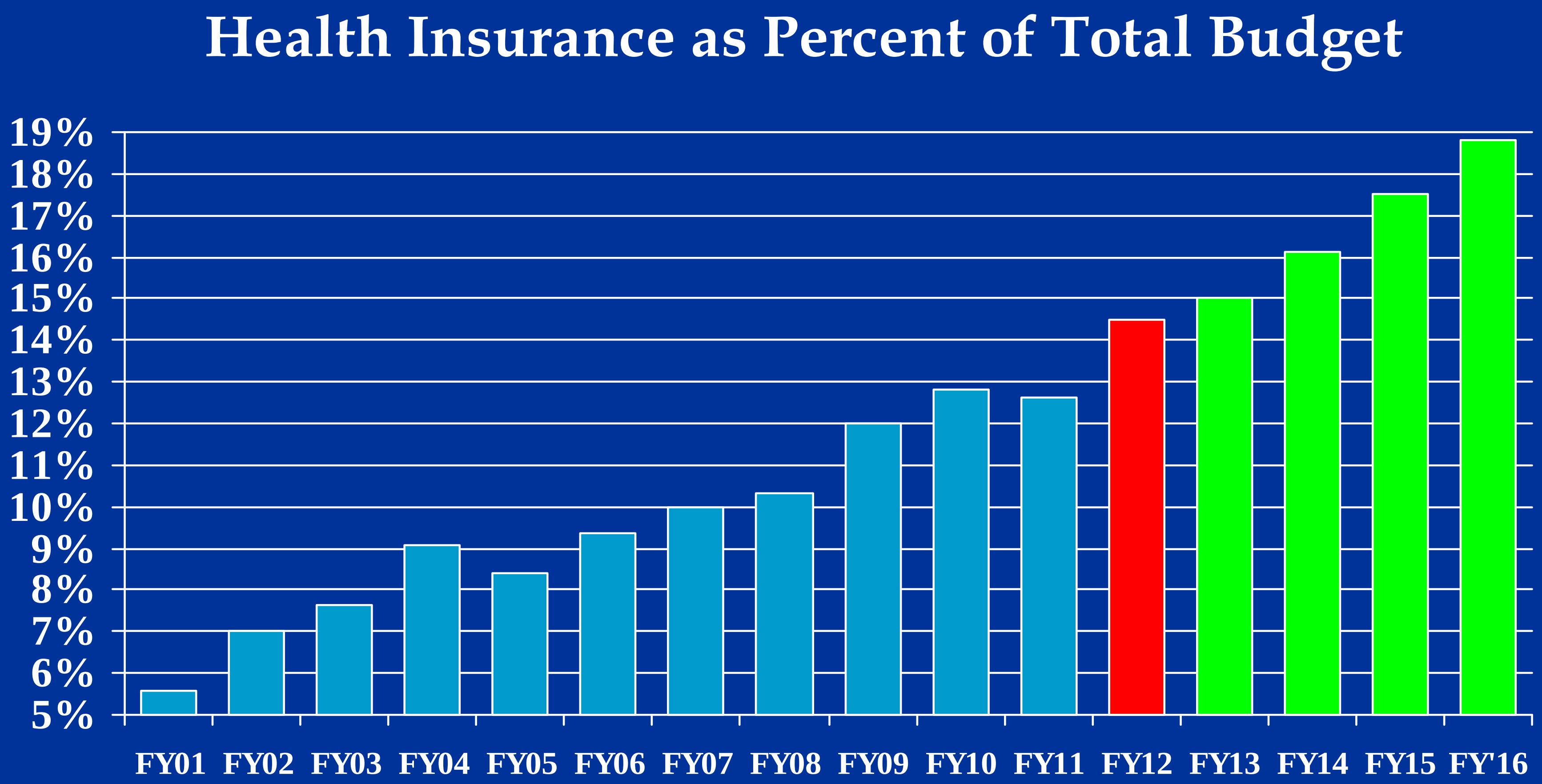
- The City secures health insurance through the City of Boston to have a bigger pool for premium negotiations with insurers.
- The City is negotiating with unions to pay the same 82.5% for HMO coverage that the Schools and City retirees receive. All get 75% for Indemnity and Medex costs.
- Health Insurance costs to the City and Schools have risen $12.1m since FY'01.
- Since FY'01, the average premium increase is 10%, and the average budget increase is 7%. (The difference reflects employee premium shares increasing and a reduction in positions.)
- Premiums are up 7% for FY'12 (resulting in a 6.3% budget increase) and assumed to increase by 10% from FY'13-'16.
- If municipal and school employees were covered by the State's health insurance system, it is estimated that the City, Schools and employees would save $2.5m - $3.5m in premium payments in FY'12, although higher co-pays would ultimately reduce the savings.
- Legislative action is expected in CY'11 to address municipal health insurance costs.

Health Insurance Costs

amounts in millions - net of employee contributions



Budget Pressures

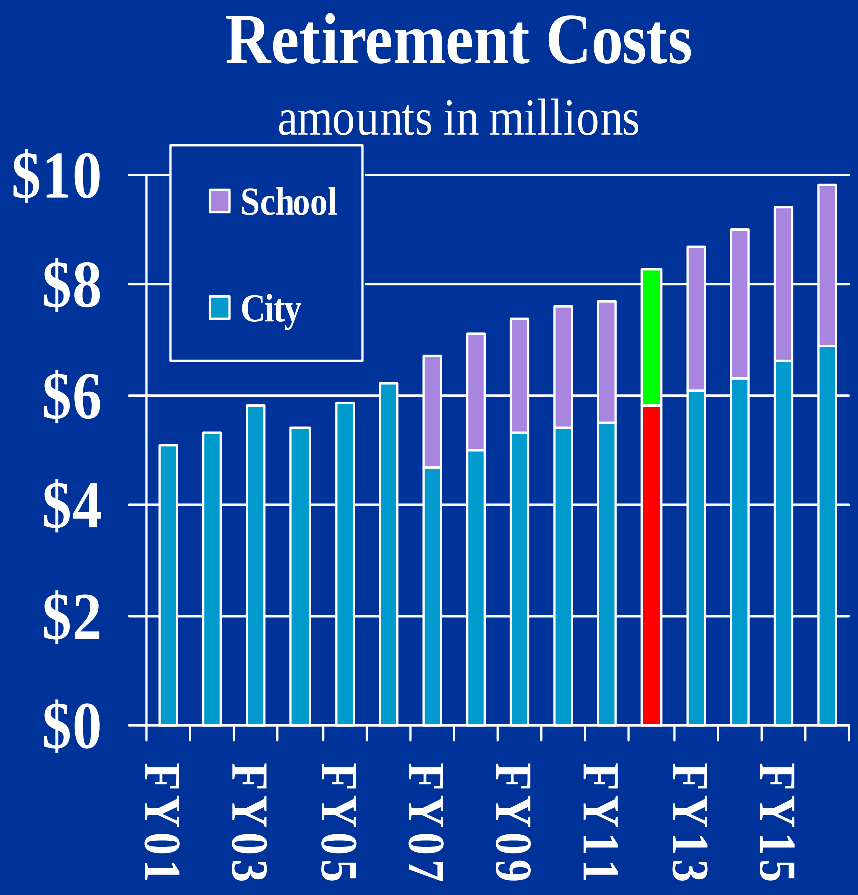


Reflects combined City and School expenditures

Budget Pressures

Expenditures:

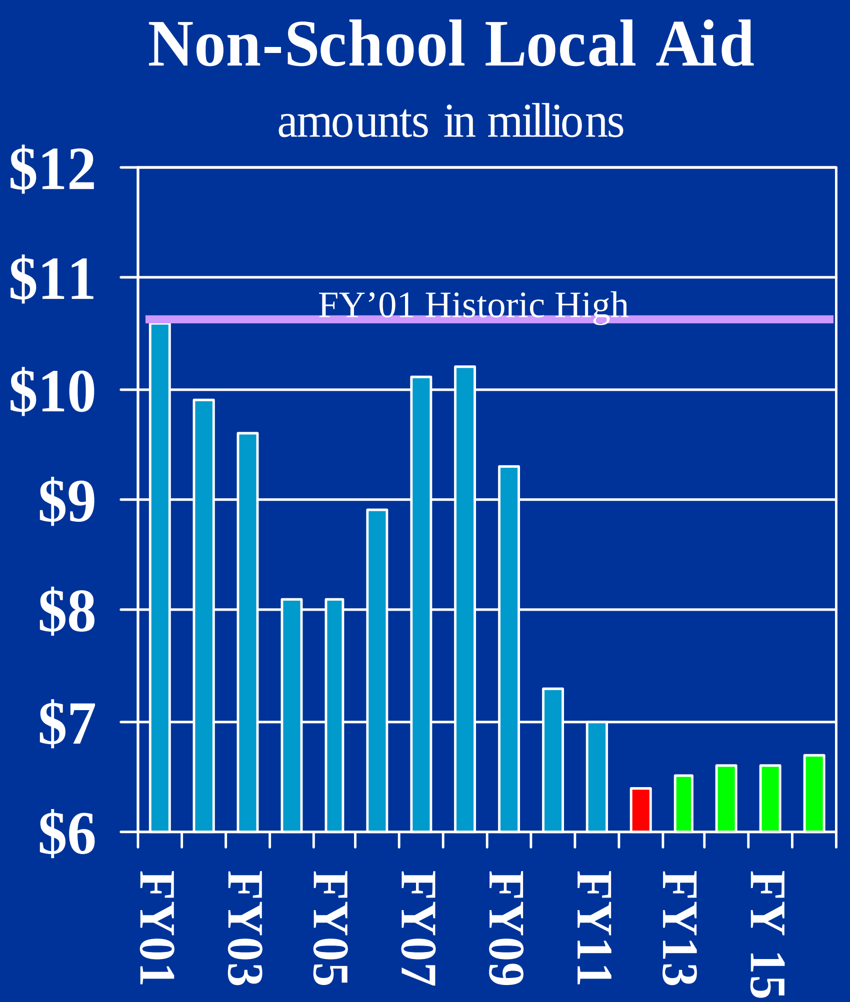
- The City voluntarily entered the State's system for pension asset management.
- The State determines the amount needed for the City to fully fund the retirement system by 2029, 11years ahead of the maximum allowed by the State.
- The School Department pays its portion of the retirement appropriation through its budget.
- Approximately 75% of annual charges reflect catch-up payments to provide for the decades that no payments were made into the system.
- Catch-up payments grow into 2029, including approx.$6m in FY'12 and almost $11m in FY'29 combined for the City and Schools.
- Retirement costs, Schools included, increased by an average of 4.5% from FY'01 to FY'11, and are projected to rise at three times the rate of overall budget growth in the out-years.
- Teacher retirement costs are paid through a statewide system and are not reflected in the School's calculation.
- The City is making its first payment into a retiree health fund in FY'12 of $150k. It is estimated that the fund is underfunded by $227m.



Budget Pressures

Revenues:

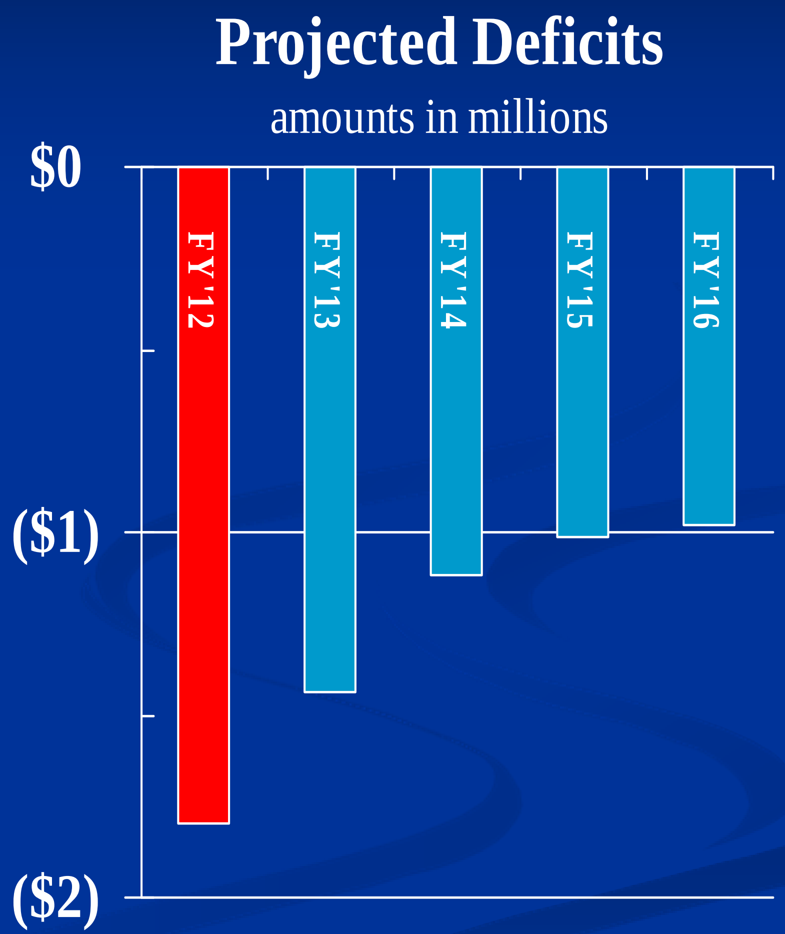
- Non-school Local Aid (LA) is Unrestricted General Gov't Aid, which was established as the combination of Lottery Aid and Additional Assistance by the State in FY'10.
- This forecast assumes a 7% cut ($500k) in LA.
- For FY'12, LA of $6.4m is $4.2m less than the FY'01 high of $10.6m, or 60% of the historic LA high.
- The cumulative loss in LA from FY'01-'12 is $21.9m (meaning $21.9m in Free Cash/cuts have been used to make up for LA shortages).
- Adjusted for inflation since FY'01, LA is down $7m for FY'12, far eclipsing the City's proposed deficit ($1.8m).
- The cumulative loss of inflation-adjusted LA from FY'01-'12 is $40m.
- Since FY'01, LA is down 40%.
- No scenarios exist for a quick return to the historical high levels of LA.



Budget Pressures

FIVE YEAR DEFICITS:

- Deficits, driven by reduced non-school Local Aid and skyrocketing Employee Benefit costs, exist in four of the next five years:
  - FY’12 ($1.80m)
  - FY’13 ($1.44m)
  - FY’14 ($1.12m)
  - FY’15 ($1.01m)
  - FY’16 ($0.98m)
- The cumulative deficit for 5 years is $6.3m, down from an estimated $9.9m made in CY’10.
- The City is not alone in projecting deficits. Many other municipalities are experiencing similar budgetary pressures, or worse.
- Prudent City management has led to fund balances that are offsetting deficits. More expenditure cuts or revenue growth will be required, though, to avoid the complete elimination of reserves.



Projected Use of Reserves

	FY12	FY13	FY14	FY15	FY16
General Fund					
Free Cash Certified at Previous Year's End	7,400,000	5,500,000	4,600,000	4,000,000	3,500,000
Free Cash (Used) or Generated	(1,800,000)	(1,400,000)	(1,100,000)	(1,000,000)	(1,000,000)
Supplemental Appropriations of Free Cash	(1,100,000)	(1,000,000)	(1,000,000)	(1,000,000)	(1,000,000)
Years Net Activities Affecting Free Cash	1,000,000	1,500,000	1,500,000	1,500,000	1,500,000
Free Cash Estimated at Year End	5,500,000	4,600,000	4,000,000	3,500,000	3,000,000
Stabilization Balance at Start of Year					
General *7020*	4,284,597	4,434,558	4,589,767	4,750,409	4,916,673
Capital *7022*	995,328	1,030,165	1,066,221	1,103,538	1,142,162
Planning and Development *7021*	166,338	172,160	178,158	184,422	190,877
Operational (School Refunding) *7023*	3,105,000	3,213,675	3,326,154	3,442,569	3,563,059
School Capital (School Refunding) *7024*	2,375,729	2,458,879	2,544,940	2,634,013	2,726,203

assuming a 3.5% investment return

Potential Future Budget Impacts

<u>ON THE POSITIVE</u>

- The City does not anticipate a need for a Proposition 2 ½ override during the next five years and beyond.

- Switching to the State's health insurance system could save 15-20% of health insurance premiums, estimated to be more than $2.5m for the City, Schools and employees, and lead to smaller annual increases going forward.

- The City is active in statewide policy discussions that could lead to reduced impacts from health insurance, retirement and charter school costs, as well as the regionalization of services to maintain and improve efficiencies.

- Promising economic development could lead to further increases in building fees, property taxes, hotel/motel excise taxes and motor vehicle excise taxes.

- Entrepreneurial activities around excise tax and loan refinancing have strengthened the City's overall bottom line.

- Reserves, if combined with additional cuts and revenue enhancements, do provide a method to assure balanced budgets for at least the next 5 years.

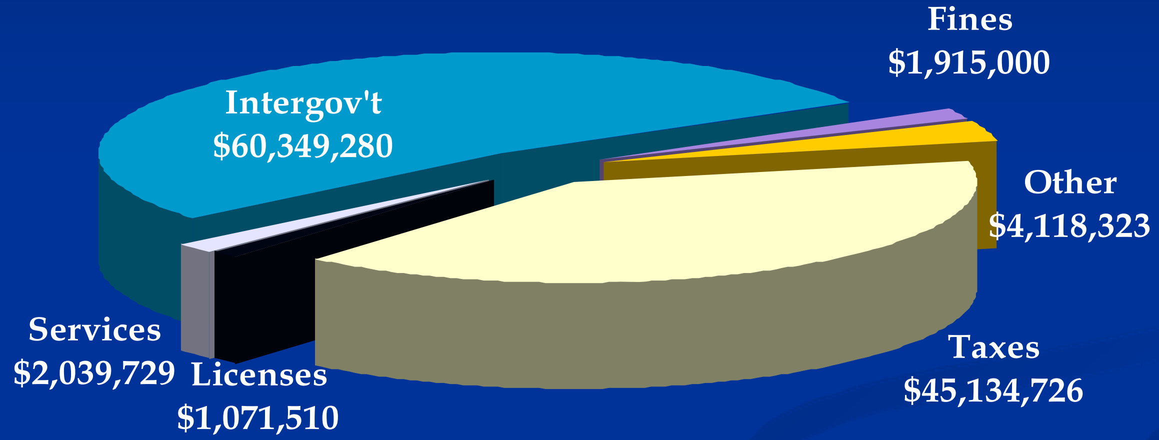
Potential Future Budget Impacts

<u>ON THE NEGATIVE</u>

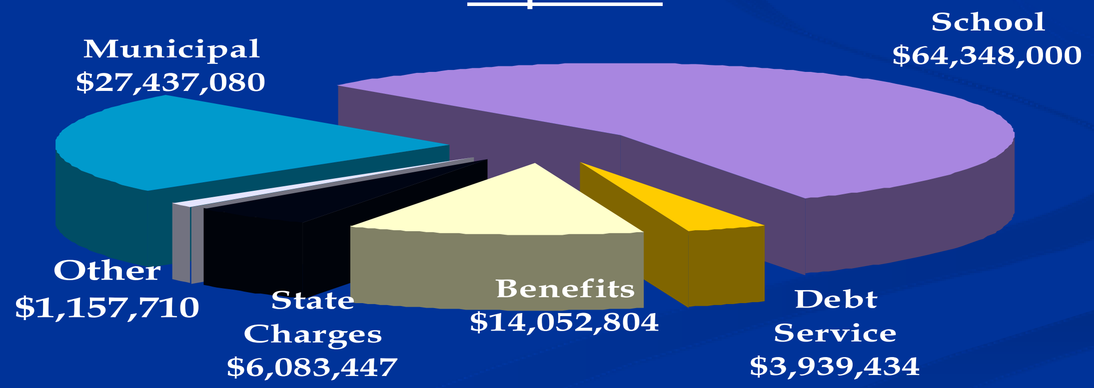
- The City's aggressive economic development agenda that has help avoid even more substantial budgetary gaps in the past has components that are now stalled.
- The lingering State budget crisis could lead to further local aid reductions and other revenue impacts.
- Motor Vehicle Excise Tax receipts could be reduced if local airport related parking is negatively impacted by future airport and airline issues, or if consumers continue to put off buying new or newer vehicles.
- The adoption of the meals and hotel taxes have produced nominal revenue increases that have not made up for deep local aid cuts.
- Federal reductions in Medicare reimbursements could result in funding shortfalls to support necessary school health programs.
- Fuel and energy costs are placing additional impact on the budget.
- Infrastructure needs are substantial and costly.
- Federal support for police and fire needs appears to be reducing, which will force the City to make some tough decisions on public safety services in the out-years.

FY'12 Budget
General Fund Revenue & Expenses

Revenue

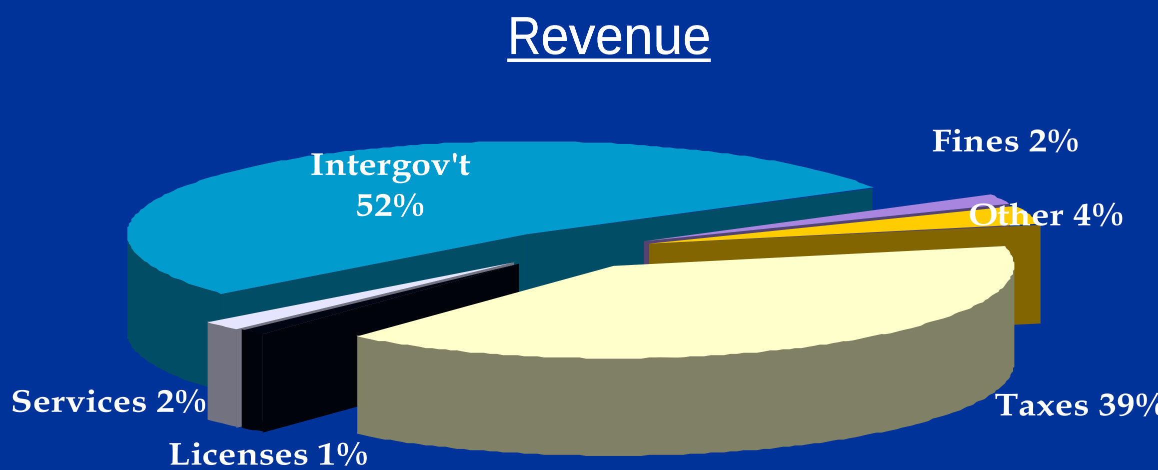


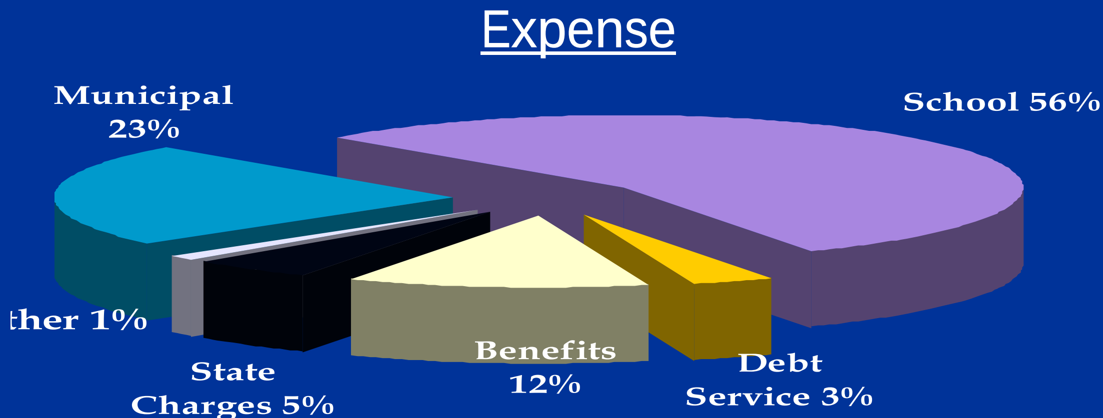
Expense



FY'12 Budget

General Fund Revenue & Expenses





School Department Budget

- With loss of $2.4m in federal stimulus funding, net revenue is down $197,000 from FY’11.
- New spending, including funding for salary adjustments, health insurance and other benefits and transferring stimulus positions onto the School payroll require $2,124,820.
- A funding gap of $2,322,043 existed as the School budget was put together.
- To close the gap, Schools have had to make cuts in operations/maintenance budgets, raise fees on programs, appropriate additional funds out of revolving accounts, and eliminate a minimum of 5 and up to 25 positions (depending on ongoing collective bargaining negotiations).
- Health Insurance reform could save the Schools $1.5m or more in costs.

Water and Sewer Enterprise Funds

- Enterprise Funds recover costs for providing Water & Sewer services. Those funds project slight surpluses going into FY'12.
- User fees account for 98% or more of the revenues.
- The MWRA Assessments accounts for between 55-60% of costs.
- The preliminary assessments from MWRA is for a 1.4% increase, relating to new population estimates that reflect a lower count for which the MWRA basis assessments, as well as the MWRA's overall lower rate of increase for its members communities (in the 3.5% range).
- Other charges to the funds include direct expenses to pay the RH White maintenance contract, indirect expenses to pay for other employee allocation costs of the General Fund and debt services to pay for the continuing update of water and sewer infrastructure.
- The City seeks to keep costs down by controlling debt service, but must also update a system that still has significant age to it.
- Local charges are about average when compared to other MWRA users communities.

Municipal Costs Affordability Index

- The City reviews data from 7 neighboring cities (Boston, Everett, Lynn, Malden, Revere, Somerville and Winthrop) to chart a Municipal Costs Affordability Index. Below, the chart refers to those communities anonymously, but lists out average property tax and water & sewer bills for the average single-family owner occupied unit in each city in FY'12.
- The data below indicates that municipal charges are less in Chelsea than all other cities.

City	Average Tax Bill	Combined Water & Sewer Bill	Combined Homeowner Costs	% Above Chelsea Cost
G	$4,333	$1,597	$5,930	72.1%
E	$3,372	$1,592	$4,964	44.1%
C	$3,615	$1,138	$4,753	38.0%
F	$3,342*	$1,380	$4,722	37.1%
D	$3,549*	$1,002	$4,551	32.1%
B	$3,741*	$674	$4,415	28.1%
A	$3,155*	$1,096	$4,251	23.4%
Average	*$3,400*	*$1,229*	*$4,629*	*34.4%*
Chelsea	$2,091*	$1,354	$3,316	

Conclusion

- The current municipal finance environment, of trouble for the last ten fiscal years and the most severe since the Great Depression, continues to threaten the viability of municipalities throughout the commonwealth and country.
- Despite that, the City is succeeding at managing through these tough times.
- Out-years are severely impacted by reduced non-school Local Aid and growth in non-discretionary spending areas, most notably, health insurance and pensions. The City has played a significant role in raising the statewide debate about these three “Budget Busters.”
- With about 52% of the City’s revenue coming from Local Aid (down from 67% in FY’01), the lagging State budget crisis continues impacting the City’s budget. In FY’12, non-school Local Aid will provide only 60% of that from FY’01.
- In FY’12, the City will receive $4.2m less in non-school Local Aid since its $10.6m high in FY’01. That reduction, when adjusted for inflation, is $7m. Cumulatively, non-school Local Aid reductions have cost the City $22m from FY’01-’11; $40m when adjusted for inflation.
- The School budget requires cuts, as modest increases in funding are not sufficient to cover contractual increases and a rise in health insurance and pension costs. Necessary budget cuts will result in increased class sizes and the elimination of some programs and positions.

Conclusion

- Central to City's deficit reduction plans is the development of more than 1,200-units of housing. Progress toward achieving that goal has slowed as a result of the economy, putting more pressure on reserves and requiring more austerity measures, including position eliminations.
- A municipal tax and fee study examining property tax and water & sewer fees for the City and seven neighboring communities finds that the City is the least expensive place to be a single-family owner occupant.
- With no local Proposition 2 ½ overrides projected, the City's relative affordability should remain as such, but the City will struggle to maintain and expand core municipal services.
- There is little margin for error, or, more likely, little margin for additional impacts from a State budget in crisis or a further decline in the economy. Any further substantial impact will potentially result in a disastrous local result.
- The City saved in "good times" to have reserves to fund operations in "bad times." Those reserves have been counted upon to provide budget stability during these tough financial times, while the City looks for cost savings and revenue enhancements elsewhere to continue budget stability into the out-years.
- Absent a sustained recovery, additional actions, on top of the judicious use of reserves will be required to maintain budget stability in the out-years and beyond.