



Montague Town Administrator's FY19 Budget Review and FY20 Revenue Projections

December 10, 2018

Overview

The Town Administrator's Montague Budget Review and Revenue Projections report is intended to provide the Town's Selectboard and Finance Committee with insight into the trajectory of the present FY19 budget year and to present current understandings of expected revenues, spending requirements, and financial opportunities and risks in FY20.

- I. Reflection on FY19 Budget
- II. FY20 Revenue Expectations and Preliminary Budget Plan
- III. Notable Budget Risks in FY20

I. Reflections on the FY19 Budget

FY19 Revenues

Following is a brief review of the FY19 budget as an exercise for considering the FY20 budget season. The FY19 budget saw a continuation of the Finance Committee's policy of taxing to the Levy Limit in order to sustain vital Town services, adequately support educational services, build stabilization funds in accordance with financial policy, and address overdue capital projects.

Bearing this policy in mind, FY19 was a positive year for the Town of Montague from the standpoint of General Fund revenues, but the Town's Water Pollution Control Facility (WPCF) sustained substantial losses with a corresponding impact on sewer user rates.

Observations:

- The Tax Levy component of the budget grew by just under 6% in FY19, driven primarily by "New Growth" (\$520,073), which was exceptional for a second consecutive year. Growth was driven by significant utility infrastructure investments and completion of residential housing projects in Montague Center and Millers Falls. Historically, New Growth more typically is in the range of \$125,000 - \$150,000 annually.
- State Aid grew by 3.8%, with Unrestricted General Aid, which is tied to state tax revenues, up by 3.8%. The Town received an increased payment for State-owned land, which presents as a positive, but also reflects ongoing purchase of land by the state, limiting future flexibility for development on those properties.
- Changes in revenue associated with Local Receipts are more difficult to assess during the year in which a budget is implemented, as some lines accrue incrementally over the course of the year. Further, these lines are conservatively estimated to preserve budget

flexibility and support taxation to the Levy Limit. Nonetheless, viewing these revenue lines, it is perhaps most notable that new Local Receipts (\$210,922) are anticipated due to lease and PILOT agreements for a 6MW solar field at the former Town landfill.

- The WPCF Enterprise Fund lost substantial revenue following closure of the Southworth Paper Mill (est. \$250,000/yr.) and the permanent stoppage of the Montague Process sludge reduction process (est. \$400,000/yr.). Compounding the challenge, Southworth left approximately \$250,000 in unpaid sewer user fees that are unlikely to be recovered, which served to deplete WPCF enterprise fund reserves.

FY19 Spending

The current FY19 operating budget—less debt-supported special articles—is \$23,621,075. This is an increase of \$426,833 from the May 5, 2018 Annual Town Meeting (ATM) budget. All additional spending was authorized at the October 10, 2018 Special Town Meeting (STM).

Some 80% of in-year budget growth resulted from required increases to the original WPCF budget, which had been trimmed substantially in an effort to limit sewer user rate hikes. The increase reflected the need to restore staff cuts per state requirements and to account for increased sludge disposal costs as the WPCF looks for more efficient solutions.

FY19 Operating Budget	ATM (5/5)	STM (10/10)	Current Total
Town Operating	\$9,400,018	\$6,000	\$9,406,018
Education	\$10,785,498	0	\$10,785,498
Airport	\$48,539	\$0	\$48,539
WPCF	\$2,017,231	\$379,148	\$2,396,379
Special Articles (non-debt)	\$899,206	\$85,435	\$984,641
Total	\$23,150,492	\$470,583	\$23,621,075

Viewing the current FY19 Operating Budget by budget area (next page), including those special articles not supported by borrowing; budget growth from FY18 to FY19 was 5.7%. The greatest increase among these lines was in education funding (6.7%). Within that line, the Franklin County Technical School budget increased 30.4% due to an increase in the enrollment of Montague students. This increase is likely to persist as that 9th grade class will be in the FCTS system for another three years and the school again was a popular choice for this year’s cohort of incoming 9th graders.

The Gill-Montague Regional School District assessment also grew substantially (5.7%) and in accordance with an established agreement that provides for the district by formula, granting the GMRSD 48.5% of all revenue available for the general operating budget. Despite this increase, the district saw some contraction in staff and programs, as revenue from other sources—tied in large part to enrollment level—remains problematic. Overall, GMRSD represents 91% of Montague’s total education spending.

FY19 Operating Budget	FY18	FY19	% Change
Town Operating	\$8,919,576	\$9,406,018	5.5%
Education	\$10,103,900	\$10,785,498	6.7%
Airport	\$49,925	\$48,539	-2.8%
WPCF	\$2,295,683	\$2,396,379	4.4%
Special Articles (non-debt)	\$981,458	\$984,641	0.3%
Total	\$22,350,542	\$23,621,075	5.7%

The Town operating budget grew by 5.5% total. The area of General Government grew 8%. Among the most notable changes was an increase in the Planning Department budget of 28% due to the addition of Montague’s new 0.5 FTE Cultural Coordinator, which was formerly a contracted and grant-supported position. The Town Clerk’s budget increased 20% to account for extra hourly staffing associated with three scheduled elections and to cover a retirement payout. Other operating budget changes include Employee Benefits (9.6%), Human Services (5.8%), DPW (5.2%), Culture and Recreation (3.6%) and Public Safety (3.1%). WPCF budget grew to 4.4%, largely due to increased sludge disposal costs. A school resource officer was added to the Public Safety budget, with partial funding from the GMRSD.

Spending on special articles remained in line with FY18, with expenditures focused on pay-as-you-go capital improvements, discretionary budget lines for plant and equipment, and funding of stabilization accounts. The Town continues to maintain recommended balances in its general stabilization account and is working toward developing strong capital and educational stabilization accounts. Maintenance of such reserves is essential to long-term budget stability and advantageous to the Town’s bond rating, which affects the cost of executing major capital projects, such as the planned Public Works Facility building project.

Impact on FY19 Assessments

It is important to understand how changes in the Town budget affect tax- and sewer rate-payers. Despite an increase in overall budget of 5.7%, FY19 tax rates moved only slightly higher, with the residential rate/\$1,000 valuation increasing 0.2% to \$17.13 and the commercial industrial rate increasing 1.0% to \$26.19. Of course, real estate bills for individual taxpayers may change at rates that differ from these percentages due to increased or decreased property value assessments. In general, Montague property values are rising and the Assessors’ Office reports that the year-to-year median residential home value increased 3.7% to \$202,562 in the present year.

In contrast to tax rates, sewer user rates rose sharply. The combined impact of sudden revenue losses and increased sludge disposal costs necessitated an increase in rates of 71%. Further increases may be necessary in FY20 due to the imminent bonding of debt associated with past sewer projects (pump stations and re-lining projects), but the Town is working diligently to create operational efficiencies that would avoid large increases in the future.

II. Fiscal Year 2020 Revenue Expectations and Plan

Following is an early look at expected revenue in FY20 by category. Note that two critical components of revenue, New Growth (local) and Unrestricted Government Aid (state) are not yet known and this forecast reflects estimates that the Town Administrator considers conservative, but appropriate. The FY20 budget should reflect a level service approach that acknowledges some strength with respect to revenue, but also the need for cost containment.

A. Property Tax Revenue

Massachusetts communities rely primarily on local property taxes to fund their budgets. The process of raising revenues through property tax is governed by Proposition 2 ½. This law establishes limits for total taxation and creates a “Levy Ceiling” of 2.5% of the full and fairly assessed value of all taxable real and personal property in a municipality. In Montague, the FY19 Levy Ceiling as calculated by the MA DOR is \$22,256,185. This represents the maximum allowable value of property tax revenue that could be raised for use in FY20.

Most relevant to Montague’s budgeting is the “Levy Limit,” which sets a limit for taxation that can be below, but never above, the Levy Ceiling. Once established by DOR, the Levy Limit for each succeeding year is equal to the previous year’s Levy Limit, plus 2.5%, plus the taxable value of any New Growth in taxable real and personal property in the preceding year. Towns can tax below the Limit, but can only tax above it if authorized through an override vote. It is through passage of overrides or experiencing a decline in property values that a municipality would approach its Levy Ceiling – a potentially perilous position.¹

The Montague Finance Committee has traditionally advised taxing to the Levy Limit and re-affirmed that strategy in fall 2018. Accordingly, the FY19 Limit (\$17,194,323) is the starting point for the FY20 budget and it provides a solid foundation. As presented below, current New Growth estimates are far below FY19. We expect this figure to increase somewhat, but not to FY18-19 levels. New growth is considered through March 1 each year.

The net levy increase is projected at 2.9%, which reflects the levy, less set aside for exemptions/ abatements chiefly attributable to continuing dispute regarding FirstLight Power Co. valuations.

Tax Levy	FY19	FY20	Change
Prior Year Limit	16,267,561	17,194,323	5.7%
2.50%	406,689	429,858	5.7%
New Growth	520,073	115,000	-77.9%
Debt Exclusion	742,178	739,268	-0.4%
Subtotal Tax Levy	17,936,501	18,478,449	3.0%
Less Allowance for A&E	(424,470)	(450,000)	6.0%
Net Levy	17,512,031	18,028,449	2.9%

¹ A helpful guide to understanding Proposition 2 ½ can be found on the MA Division of Local Services website at <https://www.mass.gov/files/documents/2016/08/oq/levylimits.pdf>.

It is possible that the estimated FY20 Tax Levy will increase further in the next two months due to an increase in excluded debt. Any increase in this line would be offset by a commensurate increase in the debt line of the budget (Debt 700), as it would represent the cost of new principal and interest payments associated with a bond expected to be issued in February 2019. It is possible that these expenses will not affect the Town budget until FY21, but the discussion remains ongoing. It is our intent to pursue the most economical long-term strategy, balanced against the near term interest in responsibly moderating near-term impacts on the tax rate.

The debt to be bonded is part of a larger issue that also includes bonding of some sewer projects that will be borne by the WPCF Enterprise Fund. The Town share of this issue is expected to include some \$585,000 associated with the “siphon” project, which repaired drainage passageways beneath the Turners Falls power canal (90% of the total expense) and an initial bond of \$2.5M to cover costs associated with the design and construction of the Town’s new public works facility (PWF). The decision to bond part of the PWF project immediately reflects concern regarding rising interest rates and the need to balance cash flow in FY20.

B. State Aid

State Aid figures appear on the “Cherry Sheet,” which summarizes sources of revenue and selected charges against the Town’s State Aid.² State Aid lines remain level funded in the preliminary budget as we do not yet have a solid basis for any other estimate. For budget purposes, the Unrestricted Aid and State Owned Land lines are the most important, as other significant lines are essentially pass-through funding that have offsetting expenditures. Note that State Aid equaled only 10% of the value of the Tax Levy in FY19.

The vast majority of funding is Unrestricted Aid. Governor Baker has followed a policy that ties Unrestricted Aid to a consensus estimate of projected state revenue growth developed in mid-January each year. Initial estimates are presented in early December and Montague adopts a conservative but credible figure as a budget placeholder. Unrestricted Aid grew by 3.5% in FY19, resulting in approximately \$50,000 in additional support to the town.

State Aid	FY19	FY20 (pending)	Change
Unrestricted Aid	1,481,823	1,481,823	0.0%
Veterans' Benefits	60,443	60,443	0.0%
Exemptions V/B/SS/Elderly	38,594	38,594	0.0%
State Owned Land	192,222	192,222	0.0%
Public Libraries	14,094	14,094	0.0%
less offset	(14,094)	(14,094)	0.0%
Subtotal Cherry Sheet	1,773,082	1,773,082	0.0%
Less State Charges	(97,873)	(97,873)	0.0%
Net State Revenue	1,675,209	1,675,209	0.0%

² To access Montague Cherry Sheet data, go to <https://www.mass.gov/lists/cherry-sheet-estimates#cherry-sheet-estimates-and-other-reports> and search the municipalities database for “Montague.”

The State Owned Land line grew substantially in FY19, increasing 30% (\$44,648). This growth was unusual and should not be expected again in FY20. It reflects an update in the state’s valuation of land it owns in Montague. According to the Assessors’ Office, the State purchased 377 acres in Montague during FY16-FY18, most of which is held by the MA Department of Fish & Game. The State owns approximately 4,500 acres in Montague, over 20% of the Town’s total land area.

C. Local Estimated Receipts

Local estimated receipts represent a significant portion of Town revenue, almost equivalent to State Aid. Some receipts can be very accurately estimated (e.g., a lease and other agreements) while others are estimated; usually conservatively to ensure against any potential revenue shortfall. Local Estimated Receipts can serve as a “safety valve” within the active budget year in the event that New Growth estimates or other aid lines are unexpectedly over-estimated.

Receipts are initially estimated during the budgeting process, but may be lowered the following fall when the tax rate is set as part of taxing to the Levy Limit. For this reason, year-to-year comparisons can be confusing and are not presented in the table below (to avoid comparison to an underestimated figure). When an estimated receipt is lowered for this purpose, it creates potential for a surplus of revenue at the end of the fiscal year. Any surplus comes back to the Town in the form of Free Cash, which is used to fund capital projects, non-capital articles, and—to a decreasing extent—to fund the operating budget.

Local Receipts	FY20 Estimated
Motor Vehicle Excise	725,000
Other Excise	1,000
Penalties & Interest	90,000
Local Option Meal Tax	20,000
PILOT	5,000
Charges for Trash Disposal	233,000
50% Kearsarge Lease (operating)	79,396
Other Charges for Service	50,000
Licenses & Permits	136,000
Fines & Forfeits	14,000
Investment Income	8,000
Miscellaneous Recurring	95,294
Misc. Non-Recurring	
Total Local Receipts For AA	1,456,690
<i>Other Local Receipts</i>	
FCTS SRO Reimbursement	66,016
GMRSD SRO Reimbursement	33,008
50% Kearsarge Lease (stabilization)	79,396
Grand Total Local Receipts	1,635,110

Motor vehicle excise, trash disposal charges, Kearsarge Solar lease payments, and licenses and permits are the most substantial lines within this budget. Miscellaneous Recurring Revenues are also significant and are comprised largely of intergovernmental reimbursement for administrative services provided by the Town to the WPCF, school districts, and other governmental entities.

Local Receipts includes a new line titled Local Option Meal Tax. This reflects Town Meeting's decision to adopt a 0.75% meal tax that is applicable to Montague businesses that serve meals as defined by the MA DOR. FY20 will see 10 months of receipts from the meals tax, as it was implemented July 1, 2018, but DOR collects and reports revenue on a May to May calendar each year. This line is conservatively estimated.

Montague may also begin to see benefits from the local option 3% marijuana retail sales tax in FY20. Realization of these revenues is pending completion and final operational approval of 253 Organic, which has a provisional license from the Cannabis Control Commission to cultivate, manufacture, and conduct retail sales of marijuana in accordance with a community host agreement adopted in April 2018. Final approval is expected following completion of a \$3.5M building renovation project in fall of 2019.

D. Stabilization

Development of an adequate General Stabilization account is a foundational element of the Town's financial policies, which specify that its balance should equal between 5% and 10% of the prior year's gross operating revenue. The Town is just over 5%, with a present balance of \$974,901. The Town also maintains a Capital Stabilization account (\$176,974), which has been bolstered by Kearsarge Solar lease revenue.

The Town WPCF Stabilization account was created in FY15 to support necessary plant and equipment upgrades for that very capital intensive operation, which has a primary plant and several pump stations of varying age throughout the community. The present balance is \$200,297. During FY18, Town Meeting rescinded an article that would have added another \$200,000 to this fund in order to stabilize sewer rates and no additional appropriation was requested in FY19 due to the looming crisis that would dramatically impact sewer rates in fall 2018. This fund is not addressed in the financial policies, but is lower than would be ideal.

Finally, the Town maintains a Franklin County Technical School Stabilization Fund, which is intended to serve as a hedge not only against unexpected capital expenses, but sharp increases in enrollment that can sometimes occur in this county-wide school district. This fund was relied upon in FY19 as a larger than typical number of Montague students chose to attend the school, reducing the balance from \$99,455 to a present value of \$46,021. It appears likely that Montague's portion of the school census will remain high in the coming years and the present balance of this account is likely not sufficient to carry that added cost burden moving forward.

E. Free Cash and Other Retained Earnings

Free Cash: The State Department of Revenue certified Montague's Free Cash at \$742,000 in FY19 and a balance of \$683,482 remained as of November 30, 2018. These resources are typically used to cover the cost of major capital projects and other special articles at winter Special Town Meeting and May Annual Town Meeting.

The Finance Committee has worked diligently over the past several years to reduce—with the goal of eliminating—the use of Free Cash to support the operating budget. Reliance on Free Cash to fund the operating budget declined from \$250,000 in FY17 (the last of several consecutive years at this level) to \$150,000 in FY19. The FY20 preliminary budget further reduces this appropriation to \$100,000.

Sewer (WPCF) Retained Earnings: The WPCF Enterprise Fund maintains an \$18,215 balance in its retained earnings account, having depleted its reserves entirely in FY18 to reduce sewer user fees. In fact, the lack of retained earnings and an apparent budget shortfall at the end of FY18 necessitated a supplemental end-of-year account transfer to ensure against a budget shortfall at the close of FY18. This highlights the risk of operating without a retained earnings balance. As it is unlikely that the Town will receive payment for some \$250,000 in unpaid sewer user fees from the former Southworth Company that might replenish retained earnings, this fund will need to be rebuilt over time.

Airport Retained Earnings: A balance of \$4,970 exists in the Airport Retained Earnings Account. Airport Manager Bryan Camden, hired in spring 2018, is working diligently to increase revenue opportunities for the airport that might reduce the operation's dependence on Town support and allow the operation to increase its retained earnings balance.

Colle Receipts Reserved - the Colle Operations account presently has a cash balance approaching \$345,525, but \$150,000 of that is allocated to building improvements that are presently in-process and are expected to be completed in late FY19. This leaves an effective balance of \$195,525 in that account, which provides some assurance against unanticipated expenses, but is not sufficient to address a variety of capital needs that are anticipated in the future. The Colle Building has thus far been a self-sustaining enterprise and the Town expects to renew the lease with the Center for Responsive Schools for another three year term beginning in June, 2019.

III. Notable Risks in FY20

The overall revenue outlook for FY20 is in most regards positive, but even in the context of a level services budget approach, there are matters that present risk to the town. These include:

- New Growth was exceptional in FY18-19, but the forecast for FY20 is less optimistic. In general, expectations related to new growth should be viewed cautiously for this and future years. It is essential that the Town continue to seek and support new opportunities to expand the tax base for future years.
- The Town is under order of the MA DEP to cap its former burn dump in FY20. This project would cost some \$2M, but the Town is working with Kearsarge Solar, which has proposed to cap the dump to DEP specifications in exchange for a commensurate break on the cost of a solar lease agreement. Failing this agreement, the Town would likely need to assume debt to perform this work. Design is underway and we expect to enter agreements during FY19 that would allow construction in calendar year 2019.
- The WPCF has experience dramatic changes in both its operation and its revenues following termination of the Montague Process pilot and loss of Southworth Company's sewer revenues. The operation appears poised to establish a new equilibrium, but is still working to implement waste disposal cost reductions that will offset the expense associated with bonding of existing debt that will impact the FY20 budget. WPCF officials are optimistic that efficiency can be attained to avoid another substantial increase, but the situation bears watching.
- The GMRSD assessment has risen in the vicinity of 5% each of the past two years in accord with the Town's growth and the Affordable Assessment calculation. Enrollment and revenue issues left those budgets inadequate to maintain district staff and programs. GMRSD has engaged in productive conversations regarding sustainability with officials from Montague and Gill, as well as other local school districts. Similarly, increases in the FCTS assessment present significant new costs that have increased overall education spending, with a commensurate strain on the Town budget.
- The Town remains in a holding pattern relative to the settlement of FY14-18 real estate and personal property tax valuations for FirstLight Hydro Generating Company. Despite a favorable ruling of the MA Appellate Tax Board (ATB) in December 2017 relative to the FY14 values, FirstLight still has the right to appeal the ATB decision after receiving the ATB's Findings of Fact, which have not yet been issued. The Town won't know FirstLight's intentions relative to appealing its FY19 assessment until April. For this reason an overlay account allocation of \$450,000 in the FY20 budget is strongly advised.
- Tax rate impacts of new bonding, including bonding of past sewer and public works projects, and an initial round of borrowing for the DPW, may impact the tax rate in the vicinity of 25-30 cents in FY20. While this does not directly affect the operating budget, it serves as an important consideration as spending is considered.