



## **Town of Amherst, Massachusetts**

### **Facilitation of Community Choices Committee Report to the Budget Coordinating Group**

#### **Hard Choices Ahead**

Committee Members:

Martha Hanner and Bob Saul, Co-Chairs

Isaac BenEzra

Alison Donta-Venman

Stan Gawle

Joan Golowich

Jerry Jolly

Irv Rhodes

Rich Spurgin

Katherine Vorwerk Feldman

December 1, 2008

## **Acknowledgements**

Many individuals aided us in our quest to understand Amherst's financial picture. We are indebted to the Town, School and Library staff who gave us their budget data and insights, including Bonnie Isman, Library Director, Larry Shaffer, Town Manager, John Musante, Town Finance Director and Assistant Town Manager, Rob Detweiler, ARPS Finance Director, and Wendy Kohler, ARPS Director of Curriculum and Program Development. Others who spoke to us include Andy Churchill, School Committee, Helen Vivian, ARPS Interim Superintendent, Rod Wright, Unicom-ARC, Patrick Brock, Chairman, Hampshire County Retirement Board, Jonathan Tucker, Planning Director, Jim Wald, Chair, Comprehensive Planning Committee, Alisa Brewer, Select Board, and Jere Hochman, former ARPS Superintendent.

We thank ACTV for televising and publicizing our Forums, Kris Pacunas, Town IT Coordinator, who set up our website, Stephanie O'Keeffe, Select Board liaison, who attended our meetings regularly and kept the Select Board informed of our progress, and Andrew Steinberg, BCG liaison, who helped set up the Committee and guided us on our way. Our special thanks go to John Musante, who patiently guided us through the maze of municipal finance, kept us focused on our task, and encouraged us as we struggled to see Amherst's future path.

Finally, we thank the many members of the community who listened thoughtfully to our presentations and studied the Library display and the documents on our website, and the 437 people who gave us their views by completing our questionnaire.

# The Facilitation of Community Choices Committee

Final Report December 1, 2008

Preface .....	1
Chapter 1. Summary of Recommendations Findings, and Conclusions .....	2
Summary Recommendations by the Facilitation of Community Choices Committee .....	2
Key Findings: Summary of Major FCCC Conclusions.....	4
Conclusion.....	8
Chapter 2. Committee Charge and Context .....	10
Budget History and Context.....	10
Budget Scenarios .....	12
Level Funding .....	12
No Increase in Revenue and 15% Decrease in State Aid .....	13
Level Services .....	13
Priority Restorations and Additions.....	13
Chapter 3. Outreach Program and Community Feedback.....	14
Community Education .....	14
Community Feedback and Development of the Questionnaire .....	14
Chapter 4. Potential Revenue Options for Closing the Gap .....	15
Chapter 5. Discussion of Pension and Health Care Liabilities.....	17
Pension Liabilities.....	17
Health Care Liabilities .....	20
Chapter 6. Questionnaire Results for Individual Budget Areas .....	22
Library Budget FY2010-FY2014.....	22
Municipal Government Budget FY2010-FY2014.....	23
Elementary and Regional Schools Budgets FY2010-FY2014 .....	28
Capital Budget FY2010-FY2014.....	32
Potential Capital Bond Measures .....	34
Chapter 7. Analysis of Potential Gap-Closing Measures from the Questionnaire.....	35
Economic Development.....	35
Payments in Lieu of Taxes (PILOTs).....	39
Increase in Local Meals/Lodging Option Taxes.....	41
Property Tax Override.....	43
Increase Fees for Services.....	45
Reduce Services/Expenditures.....	47
Additional Potential Gap-Closing Measures .....	49
Salaries .....	50
Adopting a Core Budget Approach .....	50
Comments on the Amherst Form of Government from the Questionnaire.....	52
Appendix 1. FCCC Handout and Questionnaire .....	54
Appendix 2. Calendar of Public Forums Conducted by the FCCC .....	63
Appendix 3: Detailed Discussion of Questionnaire Data .....	64
Appendix 4. Full Text of Open-Ended Responses to Questionnaire .....	72
Appendix 5. Budget Scenarios Provided by Town Officials .....	89

# **The Facilitation of Community Choices Committee**

## **Preface**

The Facilitation of Community Choices Committee was given a difficult assignment, made worse by the economic and financial events of the last several months. Nevertheless, we have attempted to rise to the challenge by maintaining a macabre fascination with how rapidly global and national events can impact regional and local circumstances. The fiscal problems of the Federal and State government are Amherst's fiscal problems too, and although it may take a year or two for the full effects of the housing, banking, and financial market disruptions to fully manifest themselves on the local level, these effects will eventually impact us directly. Any halcyon hope for budget business as usual is wishful thinking, and without extreme measures we do not see balanced budgets on the horizon within the time frame (FY2010 to FY2014) we've assessed.

Additionally, we collectively acknowledge that we are not the decision makers or elected officials who have to implement what will inevitably be difficult decisions. Consequently, our recommendations will be more general in nature. Additionally, our questionnaire results are not a statistically valid sample of Amherst's collective attitudes toward municipal, school and library services. We are reluctant to say: "this is what the community will support" with any real conviction. Nevertheless, we have worked very hard to understand the budget and discern public attitudes towards municipal service cuts and restoring cuts made in prior years, and we believe that our mandate demands that we make some judgments, recommendations, and concrete calculations regarding our fiscal future.

The world is changing, and Amherst floats in the soup of this changing world. We enter it with certain definite assets; a strong, involved and devoted community, and certain liabilities; a structural budget deficit, high expectations, and a general predilection to remain conservative with our personal resources. Amidst this community balance sheet, there are compromises to be struck among conflicting priorities. Strong, decisive leadership will be required. Our job is simply to present the facts, parameters, and best guesses about the troubling mathematical equations that lie ahead. It is up to our elected officials to make the hard, unpopular, but necessary, decisions about service priorities. We sincerely wish you good luck, good judgment, and good grace, as you grapple with these very difficult, and unprecedented fiscal challenges.

# Chapter 1. Summary of Recommendations, Findings, and Conclusions

## Summary Recommendations by the Facilitation of Community Choices Committee

*The Committee concludes that Amherst faces a serious and growing budget gap between projected revenues and the cost of providing the current level of Municipal, School, and Library services.* If State aid remains constant, the budget shortfall is approximately \$2.66 Million in FY2010, rising to \$10.2 M in FY2014. If State aid decreases by 15% next year, as in previous economic downturns, then the budget gap will be approximately \$5.2 M in FY2010.

**The budget gap for the next 5 years is of such magnitude that substantial cutbacks and restructuring will be required, and revenue increases in some form will also be needed.**

*Under the current economic conditions, the Committee recommends a Level Funding budget scenario for FY2010.* This means, regrettably, cuts, some severe, in all budget areas. We hope that a combination of reducing to a core budget in FY2010 and concerted efforts on the part of our elected officials to control costs and increase revenues will limit these service cuts to the near future. Community feedback overwhelmingly appears to support Level Services, with a moderate bias towards Priority Restorations for the School budgets. However, given the projected revenue shortfall, the uncertainty in State aid, and the pace of local economic development, we find it unrealistic to recommend a more optimistic scenario than level funding at the present time.

*The FCCC recommends that the Select Board, School Committee and Library Trustees define a core budget to fit within the anticipated revenues.* The Committee does not foresee that a balanced budget can be achieved by cutting all services equally, particularly if State aid decreases. Priorities must be set and difficult choices made. These priority budget decisions should be formulated at the Library, Municipal, Elementary, and Regional school levels, beginning immediately, so that the FY2010 to FY2014 budgets can be built upon the concept that the town must provide only certain core services and everything beyond the core must be carefully evaluated.

*The Committee recognizes that an override will probably be necessary at some point in the next 5 years to sustain even the most essential school and municipal services.* All members agree that an override will not solve Amherst's long-term budget gap and substantial cutbacks will be necessary regardless. Committee members hold a range of views regarding the timing of an override and the criteria that must be met before considering an override. Some members are against seeking an override vote for the FY2010 budget because they fear it would be an excuse to postpone difficult budget decisions. Others would favor keeping that option open *if* State aid decreases significantly. Others think an FY2010 override is necessary to preserve essential services while town leaders develop a restructuring plan. We recommend that if an override is put forward, a menu override approach be used to allow voters a choice of where to direct the revenues.

**The Committee has reviewed various options for closing the funding gap and we make the following recommendations to achieve the goals stated above.**

***The Committee recommends pursuing economic development, but notes that economic development will have, at best, a moderate financial impact in the next few years.***

***The Committee recommends that our elected officials pursue a local option meals tax and increased local option lodging tax.*** These taxes require action by the State Legislature. These taxes may have a significant impact on revenue, but it is beyond the scope of this Committee to assess the likelihood that they will be implemented. Additionally, the Committee recommends that town officials seek legislation to require that the Campus Center Hotel at the University be subject to the local option lodging tax.

***The Committee recommends that the Town increase fees and that some free services become fee based.*** The Committee finds broad support in the community for increased fees. Fees can help to sustain specific programs that might otherwise be cut, but they will have low impact on the overall revenue shortfall.

***The Committee recommends that our elected officials immediately start work to secure increased financial contributions from our three resident institutions of higher education –The University, Amherst College, and Hampshire College – through formal Payment in Lieu of Taxes (PILOT) agreements.*** In the spirit of neutrality and mutual cooperation, the Committee also recommends that our elected officials consider hiring an independent cost accounting firm to determine the cost of delivering specific services to these institutions so that such costs can serve as a guide in determining equitable financial contributions. The Committee is aware that these institutions have been negatively affected by the vaporization of the substantial financial gains of the past decades and acknowledges that any guarantee of payments in lieu of taxes has to occur in the context of mutual benefit for both the Town and these schools. Also, the Committee realizes that the schools provide substantial benefits that exceed those concrete benefits that can be counted as tax receipts or fees. However, in light of the magnitude of the budget cuts that will be necessary, and the threat to the Town's unique quality of public education, it seems appropriate that the three Amherst educational institutions find tangible, intangible, and extraordinary means to support the Town during a period of unusual budgetary stress. Once again, these institutions will be more likely to cooperate if they see the Town's decision-makers exercising discipline as they set budget priorities

***The Committee sees the need to hold personnel costs to a rate of growth in line with projected revenues.*** Personnel costs accounted for 86% of Amherst's spending in FY 09. The public sector is labor-intensive, so it is not surprising that employee compensation and other personnel-related costs make up most of the town's budget. Finding a way to limit the growth in personnel-related costs to a sustainable rate is therefore essential to the overall fiscal stability of the town. Once the FY2010 budget is brought into balance the town and the schools should each manage their personnel costs so that the combination of salaries, employee health benefits, and staffing levels grow at a sustainable rate. This can be achieved by four methods: a) continuing to make progress in achieving more cost-effective employee health insurance plan design, b) restricting future COLAs, c) reducing staffing, and d) some combination of the previous three.

***The Committee recommends that our elected officials develop a plan to reduce the Town's unfunded liabilities for pensions and retiree health care.*** Payments for pensions and retiree health care already

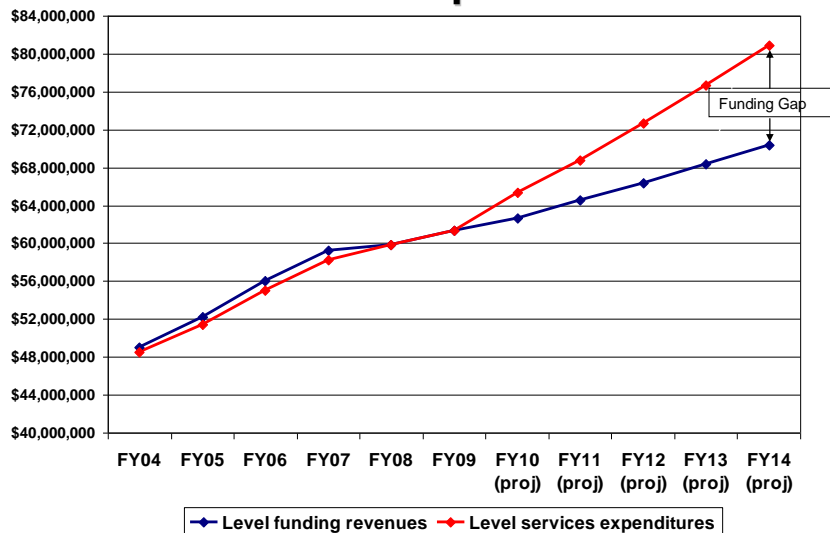
consume roughly 8% of total expenditures. These costs are projected to rise quickly over the next five years. Any solution to Amherst’s long-run budget problems must include a plan to manage these costs.

**The Committee recommends that the Select Board look carefully at the money allocated to the Capital budget, with an eye toward possible reallocation of a portion of these funds to other budget areas.**

**Key Findings: Summary of Major FCCC Conclusions**

**The cost of providing municipal services is rising at a faster rate than our revenues.** This trend will continue. The chart below shows revenue and expenditures for the Town from 2004 to 2009 along with the FCCC forecast of revenue and expenditures assuming the (1) tax revenues follow their current path and there is no Proposition 2 ½ override and (2) the Town maintains the current level of municipal and school services. The projected cost of maintaining current level of services rises at about 6% per year, while our revenues are expected rise at about 3% per year. Chapter 2 of this report explores the reasons for this finding in detail. The current budget for the Town, Schools, Library, and Capital Improvements is FY2009 is \$61 million.

**History and Projections of Total Town Revenue and Expenditures**



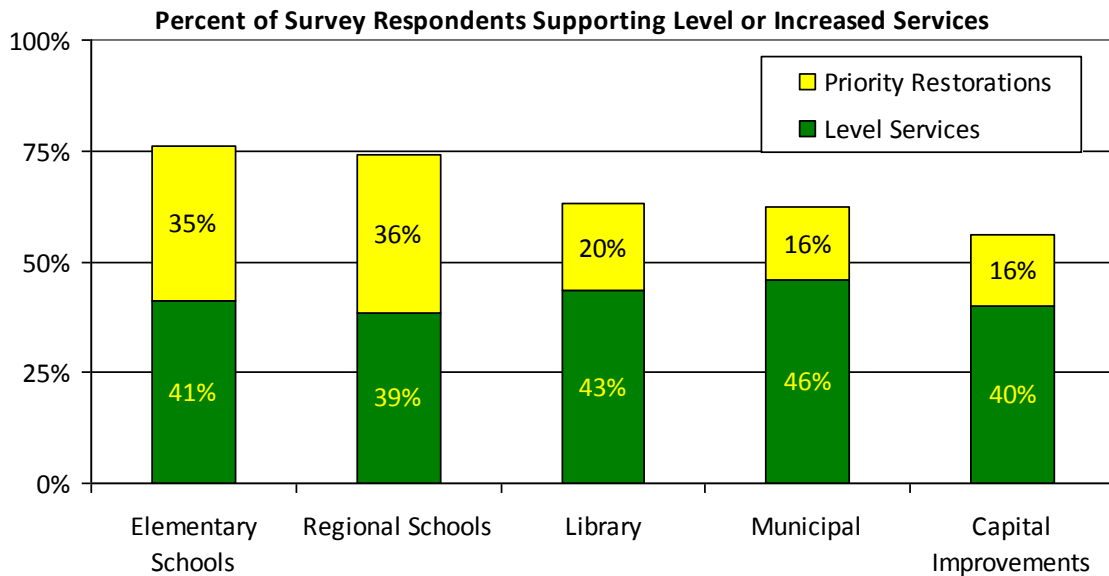
**If our forecasts are wrong, it is more likely that the deficit will be higher, not lower.** We identified a number of major risks in our budget forecasts. The largest of these is the potential for lower-than-expected State aid over the next five years. The prospect for a positive surprise from the State in coming years seems slim, while the odds of a negative surprise are growing as the economic crisis deepens. This topic is addressed in Chapter 2 of this report.

**A sizeable of the Amherst residents who completed our questionnaire prefer the Town to maintain (or increase) the current level or services.** An important part of our mandate was to present long-term budget forecasts to the local community and solicit feedback regarding the choices we face. There were

437 responses to the questionnaire. Our questionnaire asked residents to select one of the following three choices for each of the main budget sectors. The scenarios are summarized below:

Budget Scenarios Presented to Amherst Residents on Questionnaire		
<b>Level Funding</b>	Requires service cuts	No increased revenue required
<b>Level Services</b>	Maintains current services	Requires increased revenues
<b>Priority Restorations/Additions</b>	Restore core services cut in recent years and, in some cases, additional services	Requires substantial increased revenues

The chart below shows the percentage of respondents who chose to maintain or increase services. For example, 76% of respondents preferred to maintain the current level of Elementary School services (41% preferred to maintain current levels and 35% chose to increase services). The remaining 24% of respondents chose to reduce service levels. Support for avoiding cuts to schools was the highest, followed by library and municipal services. Only 56% of residents preferred to maintain the current level of capital improvements. These results are described in detail in Chapter 6. The FCCC also encouraged open-ended responses to our questionnaire. Comments that focused on town services are summarized in Chapter 6 and printed in their entirety in Appendix 3.





**The budget gap cannot be closed without a Proposition 2 ½ override or a sizeable increase in State aid.** The FCCC analyzed a number of potential sources of increased revenues. Of these, only State aid and a property tax override were deemed to have a high impact on the budget. The table below summarizes our conclusions regarding the potential impact of various options.

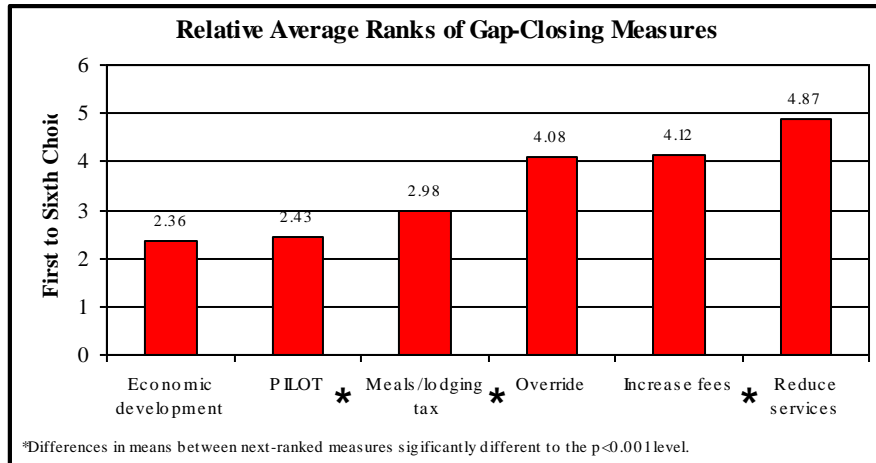
Potential Sources of Revenue and Estimated Impact on Amherst Budget	
Proposition 2 <sup>1/2</sup> Override	High impact
State Aid	High impact (positive or negative)
Local Option Meals/Lodging and Telecommunications Taxes	Moderate to high impact
Economic Development	Moderate impact
Consolidation/Regionalization of Services	Moderate impact
Increased Fees	Low impact
Payments in Lieu of Taxes (PILOTs)	Unknown impact

The table below summarizes our estimate of the *maximum* revenue that could be received from several of these options. Not all options were included in our estimates. PILOTs were excluded because estimates were deemed too uncertain. A proposition 2 ½ override was also excluded since there is no uncertainty about the amount raised by an override. The most revenue Amherst can expect from the sources listed below is 0.2 million in FY2010 and 2.0 million in FY2014. Since the budget gap is projected to be about 2.6 million in FY2010 and more than 10 million on FY2014, the FCCC finds that current service levels cannot be maintained without an override or a large increase in State aid. These topics are explored in more detail in Chapter 4 of this report.

Potential Gap-Closing Measures: Additional Expected Revenues per Year and Remaining Balance					
	FY2010	FY2011	FY2012	FY2013	FY2014
Economic Development	\$80K	\$160K	\$320K	\$320K	\$320K
NO Increase in State Aid	\$0K	\$0K	\$0K	\$0K	\$0K
Telecom. Tax Loophole			\$230K	\$230K	\$230K
Local Option Meals Tax			\$1.2M	\$1.2M	\$1.2M
Local Option Lodging Tax			\$25K	\$25K	\$25K
Low Impact Measures (total)	\$200K	\$200K	\$200K	\$200K	\$200K
<b>TOTAL POTENTIAL REVENUE</b>	<b>\$0.3M</b>	<b>\$0.4M</b>	<b>\$2.0M</b>	<b>\$2.0M</b>	<b>\$2.0M</b>
Total budget gap—Level Services (current projected revenues)	\$2.7M	\$4.2M	\$6.3M	\$8.4M	\$10.5M
<b>AMOUNT REMAINING (cuts, override, or a combination needed to balance budgets)</b>	<b>\$2.4M</b>	<b>\$3.8M</b>	<b>\$4.3M</b>	<b>\$4.0M</b>	<b>\$8.5M</b>
Total budget gap—Level Services (15% cut in State Aid FY2010)	\$5.2M	\$6.8M	\$9.0M	\$11.1M	\$13.3M
<b>AMOUNT REMAINING (cuts, override, or a combination needed to balance budgets)</b>	<b>\$4.9M</b>	<b>\$6.4M</b>	<b>\$7.0M</b>	<b>\$9.1M</b>	<b>\$11.3M</b>

**The Amherst residents who took our questionnaire prefer that the town pursue Economic Development and PILOTs over other choices for raising revenues.** We asked respondents to rank six potential gap-closing measures in order of priority to be used in hopes of closing Amherst’s future budget gap. A total of 347 people provided ranks for all six choices, representing 79.4% of all

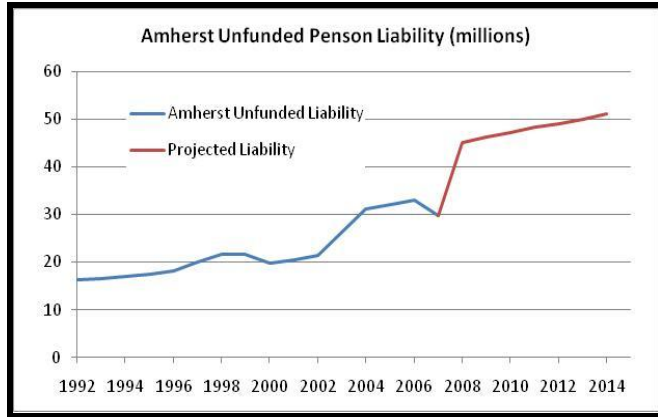
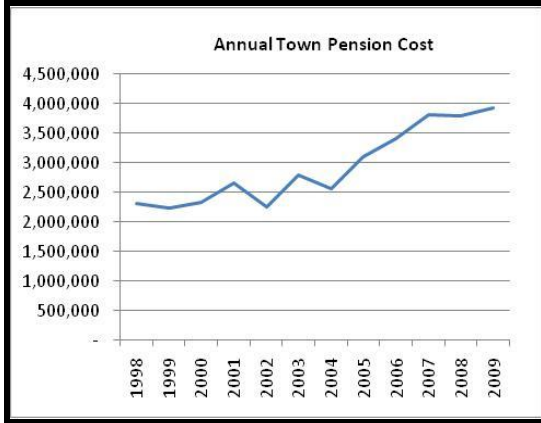
respondents. Responses were ranked from one (1) to six (6), where 1 is the first choice and 6 is the last choice. The chart below shows the average rank for each of the choices (lower average means higher preference).



The highest ranked measure was Economic Development (average rank of 2.36), followed closely by PILOT (2.43). An increase in the Meals/Lodging Tax ranked 2.98. The rank for Override and Increased Fees were nearly tied with ranks of 4.08 and 4.12, respectively. Ranked last, with an average rank of 4.87, was Reduce Services/Expenditures, exclusively. Detailed analysis of these choices is provided in Chapter 7, along with a large number of open-ended responses that dealt with budget-closing choices.

***The preferred methods of closing the budget gap cannot provide enough additional income to close the gap.*** Many people indicated on their questionnaire that they would like to maintain or increase service levels but indicated – through their ranking of budget-closing measures and their open-ended comments – that they would like this to be done without raising local property taxes and fees. The FCCC found that this is not feasible.

***Our analysis of the town’s pension obligations revealed a considerable risk that payments will increase substantially in coming years, in part due to the recent credit crisis which has dramatically lowered the value of pension investments.*** The chart below shows the annual contribution made by the Town to various pension plans since 1998. This cost increased from about 2.25 million in the early part of this decade to about 3.8 million today – an increase of more than 60%. Pension costs have been rising faster than the Town’s revenues for many years. Pension expenses now consume about 6.3% of our total budget. In five years we expect pension costs to consume between 7.5% and 9% of every dollar of town revenues.



In addition to higher annual pension contributions, the Town faces a large deficit in its pension plans. The chart above (right) shows that the current unfunded pension liability is about 30 million. This is project to rise to 50 million by 2014. The projected increase is mostly caused by the recent stock market decline, which reduced the value of assets in the fund but did not reduce the projected cost of providing pensions. Chapter 5 of this report analyzes this problem in greater detail.

***Amherst is not well prepared to shoulder the rising cost of providing health care to retired employees.***

The cost of providing health care to retirees is a large and rapidly growing liability. This year the combined cost of providing health insurance to retirees is estimated at \$2.8 million (or about 4.5% of total expenditures). Our actuarial consultants estimate this cost will rise to \$4.8 million in 2014 (6.8% of the projected 2014 revenues). These consultants recommend that Amherst begin setting aside money today in order to reduce the future cost of providing health benefits to retirees.

	Combined Liability (Town + 77% Regional)
Present Value Future Benefits	143,216,902
Unfunded Actuarial Liability	95,786,217
Annual Required Contribution	8,149,590
Expected Benefit Payments	2,831,124

The table above summarizes the recommendations of our actuarial consultants. “Expected Benefit Payments” of 2.83 million is the current cost health coverage for retirees. “Annual Required Contribution” of 8.15 million is the amount Amherst should be setting aside to meet both current and future obligations. The town currently has no plans to begin setting aside money to fund retiree health care benefits. More details about this topic can be found in Chapter 5 of this report.

## Conclusion

Since we began our meetings in May the financial outlook has changed, and not for the better. We desperately need our town officials and our town leaders to prepare a new vision for our community, a vision based upon the persistent, inconvenient fact that the town will be dealing with increasingly limited resources at least through FY 2014. Without thoughtful, proactive preparation, important

decisions, with repercussions that will last for years, might be made hastily under duress. To avoid this outcome, priorities need to be established and a plan of action needs to be developed. The efficient use of limited resources will need to quickly replace our collective expectations that there will be additional augmentations or restorations to our current level of services. "How to do more with less?" will require creative solutions to difficult problems. These are the urgent, immediate responsibilities of our elected officials and our town administrators.

## Chapter 2. Committee Charge and Context

Like many municipal budgets around the state and the nation, Amherst's budget has been under stress. Rising fuel and health care costs, limits on property taxes, volatile annual State aid contributions, and a general increase in expense of providing municipal services, have meant that costs are rising faster than revenues can keep up. Amherst cannot continue to treat each year as a new financial crisis; a long-range plan is needed based on realistic revenue assumptions. Against this backdrop, our Committee was created.

The Facilitation of Community Choices Committee was appointed by the Select Board in April 2008, following a recommendation from the Budget Coordinating Group. The Committee was charged with reviewing the five year budget outlook for Amherst, developing budget scenarios for the next five years, and soliciting feedback from Amherst residents regarding their budget priorities. Our committee represents a broad array of perspectives. We are not a monolithic group with a unified political viewpoint. However, we have unified around one concept: Amherst's financial future is challenging, and the sooner we all face it, understand it, and ultimately develop a plan for it, the better we will all feel about our community in the years to come. **Now is the time for difficult choices.**

### Budget History and Context

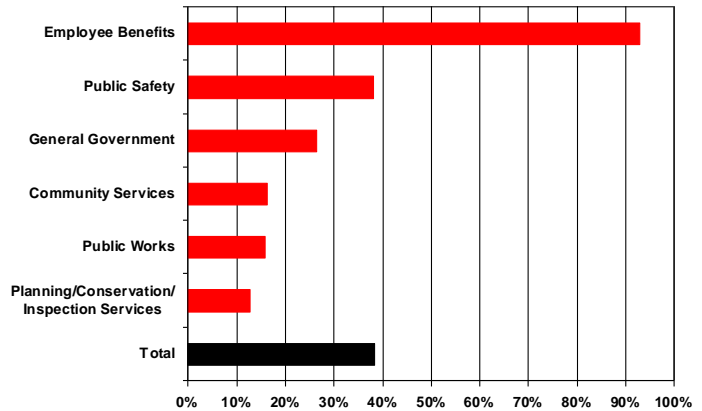
The budget gaps in recent years have been closed with an assortment of: cost cutting measures, use of reserves, and some positive surprises in State Aid and Lottery Revenue. One way to think about the problem of municipal finance is to realize that over the last 25 years, inflation and Proposition 2 and ½ constraints have caught up with the expense of providing local services. Every year, our property tax increases fall further behind inflation of wages, benefits, and other expenses.

In Amherst, in addition to the 2.5% increase in the property tax levy, new growth has averaged 1.5% per year during the past 10 years. Taken together, increases in property tax revenue have increased an average of 4% annually. However, because Amherst derives only 57% of its revenue from local property taxes, this 4% annual increase in the taxable base yields a 2.28% increase in overall revenue. This has not kept pace with increasing costs especially those associated with employee benefits as illustrated in the following chart. The remaining 43% of town revenue, including 28% of State aid, has been growing at an even slower rate than property tax revenues.

Fluctuations in State aid have been highly disruptive to the annual budget process. With a history of increases or decreases of 15% or more in a single year, the legislature has created an incentive for local authorities to avoid cutting services believing (often correctly) that more state aid was just around the corner. It seems unlikely that significant increases in State aid will take place until the State is able to increase its overall revenues. Amherst residents should expect at best a token increase in state aid until the legislature enacts a tax increase.

To compound this problem, the two fastest-growing portions of our budget – pensions and health care – are state-mandated programs that cannot be altered without legislative approval. The chart at right shows the percentage change in total cost for each sector of the Municipal budget. Employee benefit costs (principally health insurance and pensions) rose by almost 95% from 2000 to 2007<sup>1</sup>. As these costs outpace inflation and the general rate of increases in other expenses as shown on the black bar at the bottom, it draws resources away from other budget items.

**Total Percent Increase of Various Areas of the Amherst Municipal Budget: FY00-FY07**

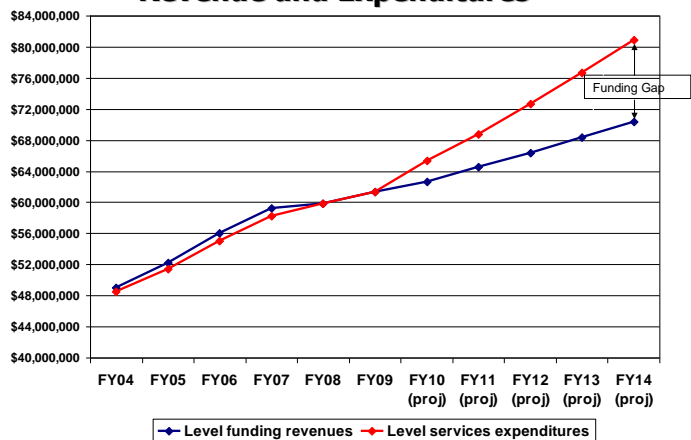


Additionally, there are certain unique structural stresses that constrain the budget in Amherst. These stresses are intertwined with our character as a community. Our primary industry is education—16.5% of the land is owned by our colleges and the university. Our legacy is agriculture and we value our rural setting—53% of our land pays reduced taxes as farm and forestland or it is permanently protected recreation or conservation land. We value a vibrant educational system for our children, and our collective values are progressive and forward looking. These collective community values give us an attractive, interesting, rural setting to live in. But, unfortunately, these positive community attributes have some financial repercussions. Most significantly, there is a lot of pressure on a limited tax base.

When all these factors are considered, the Town is looking at a growing funding gap even under moderately optimistic assumptions. This is the most optimistic view we dare propose for our future budget gap. It assumes that State aid remains flat. It is apparent that the hardest decisions appear to lie ahead of us.

The general economic environment is not getting any better. A slower State economy will hurt State tax revenues and likely undercut State aid to Massachusetts cities

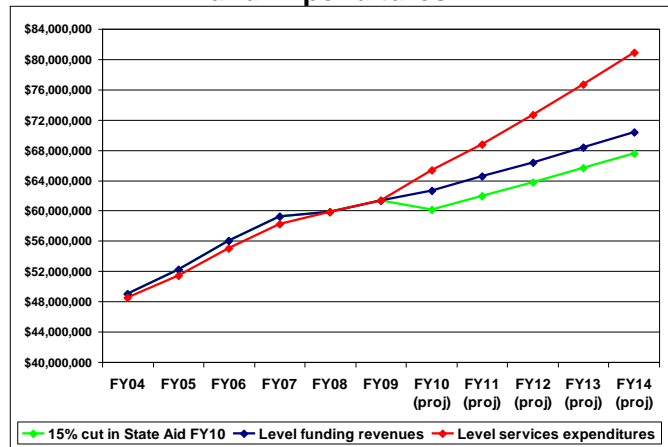
**History and Projections of Total Town Revenue and Expenditures**



<sup>1</sup> The Committee notes that, through the efforts of the Town’s Finance Director and other town officials, the rate of increase in health insurance premiums for existing employees has slowed considerably, and, in fact, the FY2009 costs were no higher than those in FY2008.

and towns. The most recent projection see a 15% cut in State aid in FY 2010, as shown in the following graph, and this downturn could last for several years. The chart below illustrates the effect of a one time cut of 15% in State aid. If the year-over-year cuts continue, these gaps could grow larger.

**History and Projections of Total Town Revenue and Expenditures**



Finally, if State Aid is the wild card in the annual budget process, then pension liabilities and retiree healthcare, the “unfunded liability” components of the budget picture, are the “really, really, wild” cards in the five year budget projection process. For this reason, we need to include a detailed description of this unknown, but potentially large and growing, liability. See Chapter 5.

This “best guess” slide does not include these growing shortfalls for our unfunded pension and healthcare liabilities. The potential magnitude of these liabilities has increased dramatically since our committee finalized these numbers two months ago, and it is not unrealistic to expect the FY 2012 gap, without action by the State legislature, to increase by several millions as mandatory payments to Town pension funds come due. The exact amounts are unknowable, and rather than speculate about their magnitude, which is largely a function of stock market performance, we’ve opted to describe the problem instead of quantifying it in this report.

## Budget Scenarios

The Committee has met nearly every Thursday, from 9 am to 11 am, beginning in May and continuing through November. Much of our early work consisted of receiving the various budget scenarios from each of the financial people in each of the municipal budget areas. Additionally, John Musante, the Assistant Town Manager and Finance Director, provided us with background behind each of the assumptions that drove the budget projections.

The Committee received input from the 5 budget entities: Library, Town, Elementary Schools, Regional Schools and the Joint Capital Plan. We are grateful to the Town, School, and Library staff members who devoted many hours to preparing their budget scenarios for us. For each of the five town budget entities we requested three distinct budgets: *Level Funding*, *Level Services*, and *Priority Restorations and Additions*. The Summary of the three scenarios for each of the 5 categories is described below. These scenarios were presented to the public. Our questionnaire asked specifically about these scenarios. Because of the changes in the fiscal landscape, we now view the *Level Funding* scenario as perhaps too optimistic to serve as a baseline. We recently added a new scenario incorporating a 15% decrease in state aid in FY2010 (as in the above graph). We did not request that town executives analyzed the implications of this new scenario.

## Level Funding

The term “Level Funding” is the best estimate for the future path of our present revenue streams, as prepared by the Town Finance Director in July, 2008. In preparing the *Level Funding* budget, town executives were asked to answer the question, “What level of services could we provide with the currently projected level of revenue.” The revenue assumptions we provided were based on the following assumptions:

- Property taxes continue to grow at the 2.5% limit per year
- 10-year average new growth of ~1.5% per year
- Chapter 70 state aid (for education) increases 1.5%/year
- Other types of state aid remain flat
- Other local revenue grows at a rate of 2.2% per year
- Other, smaller sources of revenue grow at a rate of 4.0% per year
- As of FY2010, the Town spends no money from the Reserve Fund

Level funding does not keep pace with the rising costs for the current level of services. Substantial cuts would be required.

### **No Increase in Revenue and 15% Decrease in State Aid**

The assumptions used for this scenario are below. The FCCC did not examine the specific cuts that would be required under this scenario, though they would be substantial. This option did not appear as a scenario on our questionnaire.

- Property taxes continue to grow at the 2.5% limit per year
- 10-year average new growth of ~1.5% per year
- All State Aid decreases by 15% in FY2010 and then flattens out
- Other local revenue grows at a rate of 2.2% per year
- Other, smaller sources of revenue grow at a rate of 4.0% per year
- As of FY2010, the Town spends no money from the Reserve Fund

### **Level Services**

In preparing the *Level Services* budget, town executives were asked to answer the question, “How much would it cost over the next five years to maintain current services (no cuts, no additions)?” Level Services assumes that resources will be allocated in the near future as they are currently. Budgets must still react to changes in the market, such as higher utilities and higher health insurance premiums, or to new state requirements. To fund the Level Services budget, additional revenue would be required

### **Priority Restorations and Additions**

We asked the staff from each budget entity to give us a list of their most pressing restorations to recent budget cuts and their priority additions, and to provide an estimate of the cost of each restoration. These are included in Appendix 1. These formed the basis for our most optimistic 5-year scenario. *Priority Restorations and Additions* would require substantial revenue increases from multiple sources, and such increases are not likely to occur in the next 5 years.



## **Chapter 3. Outreach Program and Community Feedback**

The Committee worked from October to early November to communicate our results to Amherst citizens. The committee's Outreach program had 2 main goals: 1) to educate a broad spectrum of the community regarding Amherst's 5-year revenue projections (including alternate revenue options) and budget scenarios, and 2) to provide the opportunity for Amherst residents to give us feedback regarding the budget choices for our town, schools, and library.

### **Community Education**

The FCC presented a series of open forums between October 2 and November 6, as listed in Appendix 2. The October 2 and October 28 forums were recorded by ACTV and rebroadcast several times in order to reach a wider audience. A web page [www.amherstchoices.org](http://www.amherstchoices.org) was developed, with the assistance of Kris Pacunas, the Town's IT Coordinator. Website visitors could view the FCCC presentations, study the financial reports our Committee received, and give their feedback via the online questionnaire. Other outreach efforts included: display in the Jones Library from October. 1-31, a table on the Amherst Common on Saturday, October 18th, interviews on ACTV and a public service announcement, a televised presentation before the Town Meeting Steering Committee, and numerous letters, editorials, and announcements in the Amherst Bulletin.

### **Community Feedback and Development of the Questionnaire**

The FCCC developed a questionnaire (see Appendix 1) allowing respondents to express a preference for one scenario for each of the five individual budget areas of Amherst: Library, municipal government, elementary schools, regional schools, and capital plan. Then they were asked to rank revenue options for supporting their selected scenarios. Open-ended comments were also solicited. The questionnaire was handed out at each forum, was available at the Jones Library, and on the website. All together, there were 437 responses to the questionnaire: 303 questionnaires were completed online and 134 were submitted on paper. Of those who completed the questionnaire, 239 (54.7%) submitted a response to the open-ended Question 8 which asked, "My idea for fixing the Town's budget problem is..." The summary of the questionnaire data appears in Chapters 6 & 7 and the verbatim answers to the open-ended questions appear in Appendix 4.

## Chapter 4. Potential Revenue Options for Closing the Gap

The FCC reviewed a number of potential options for increasing revenues in order to decrease the budget gap. These revenue options do not have equal financial impact -- and most of the options are not under local control. We discuss the options here in order of their financial impact. We define High Impact for revenue sources producing \$1 million or more each year, Moderate Impact for revenue generation of \$200,000 - \$900,000 a year, and Low Impact for additional revenue of \$100,000 or less per year. The table below illustrates the potential gap-closing measures presented to the public in the questionnaire, the potential increases in revenue that might result from these measures, and the resulting gap, both with and without the potential 15% cut in state aid.

<b>Potential Gap-Closing Measures: Additional Expected Revenues per Year and Remaining Balance</b>					
	<b>FY2010</b>	<b>FY2011</b>	<b>FY2012</b>	<b>FY2013</b>	<b>FY2014</b>
Economic Development	\$80K	\$160K	\$320K	\$320K	\$320K
NO Increase in State Aid	\$0K	\$0K	\$0K	\$0K	\$0K
Telecom. Tax Loophole			\$230K	\$230K	\$230K
Local Option Meals Tax			\$1.2M	\$1.2M	\$1.2M
Local Option Lodging Tax			\$25K	\$25K	\$25K
Low Impact Measures (total)	\$200K	\$200K	\$200K	\$200K	\$200K
<b>TOTAL POTENTIAL REVENUE</b>	<b>\$0.3M</b>	<b>\$0.4M</b>	<b>\$2.0M</b>	<b>\$2.0M</b>	<b>\$2.0M</b>
<b>AMOUNT REMAINING (cuts, override, or a combination needed to balance budgets)</b>					
Total budget gap—Level Services (current projected revenues)	\$2.7M	\$4.2M	\$6.3M	\$8.4M	\$10.5M
<b>AMOUNT REMAINING (cuts, override, or a combination needed to balance budgets)</b>	<b>\$2.4M</b>	<b>\$3.8M</b>	<b>\$4.3M</b>	<b>\$4.0M</b>	<b>\$8.5M</b>
<b>AMOUNT REMAINING (cuts, override, or a combination needed to balance budgets)</b>					
Total budget gap—Level Services (15% cut in State Aid FY2010)	\$5.2M	\$6.8M	\$9.0M	\$11.1M	\$13.3M
<b>AMOUNT REMAINING (cuts, override, or a combination needed to balance budgets)</b>	<b>\$4.9M</b>	<b>\$6.4M</b>	<b>\$7.0M</b>	<b>\$9.1M</b>	<b>\$11.3M</b>

### **Override of Proposition 2.5 Tax Limit** *High Impact*

An override of the Proposition 2 ½ tax levy limit is the most direct and effective way to decrease the gap in revenue, in order to maintain services. It is one of the few options under local control. In all likelihood, however, one override alone would not solve the 5-year budget gap.

### **State Aid** *High Impact (positive or negative)*

State Aid constitutes approximately 28 % of Amherst's overall budget and 34 % of the regional school budget. Thus, any change in state aid has a large impact on local budgets. The previous economic downturn, which reached a low point in the FY2004 state budget, resulted in a 15% drop in state aid to Amherst—approximately \$2 million. If a 15 % decrease in state aid occurs next year, Amherst's budget gap will jump to \$5.2 million.

***Local Option Taxes and Telecommunications Tax***      *Moderate to High Impact*

Under Massachusetts law, municipalities are not allowed to impose taxes other than the property tax and specific excise taxes. Any other potential revenue sources require action of the state legislature. The following three items have been introduced to previous legislative sessions, but have not been acted upon favorably. Among these, a 2% local option meals tax would have the largest revenue impact for Amherst; estimated to contribute up to \$1.2 million per year. Additionally, it is likely in next few years that we will see proposals to close the Telecommunications Tax Loopholes and this could bring in an average of \$230,227 per year. Additionally, it is somewhat likely that in the next few years a proposed 1% increase in the Local Option Lodging Tax could yield \$25,000 per year.

***Economic Development***      *Moderate Impact*

Economic development can have various benefits in stimulating the local economy, as well as expanding the tax base. The Town Manager's stated goal is to increase the tax base by roughly \$20 million per year over the next 10 years. Even this optimistic goal would bring in only an estimated \$320K in new taxes each year, a moderate impact compared to the overall FY2010 budget gap of at least \$2.66 million. However, even this moderate growth may not be realized in the current fiscal environment. To the extent that increased economic development increases the need for services, the positive revenue gain could be muted. In their questionnaires, 79% of the respondents favored economic development (Chapter 7).

***Consolidation and Regionalization of Services***      *Moderate Impact*

The Town Manager reported to our Committee on recent consolidation of functions within the Town government and possible sharing of functions with UMass and/or with surrounding communities. In a time of shrinking budgets, any money saved by consolidations can help to preserve services that might otherwise be cut. Among the proposed regionalizations, a regional dispatch system shared with UMass and Hadley seems to have the potential for the largest future cost savings. State funding may be available for the transition.

***Fee Increases***      *Low Impact*

The Committee foresees that fee increases will be a necessary part of the budget picture. Fees can help to sustain specific programs that might otherwise be cut, but they will have low impact on the overall revenue shortfall.

***Payment in Lieu of Taxes (PILOTs)***      *Unknown Impact*

Finally, education is our largest economic enterprise. The presence of UMass, Amherst College and Hampshire College brings many economic benefits to our community, but they also occupy 16.5 % of our land base. Currently, the State pays Amherst \$100,000 per year for the land owned by UMass. In 2007, the Town negotiated a strategic partnership agreement with UMass covering several areas, most notably that the University will pay the Town \$425,000 per year for the cost of fire and ambulance service. In 2008, Amherst College gave the Town a gift of \$120,000. Much more is possible -- greater cooperation in economic development, recovery of costs for police, or a payment in lieu of taxes agreement.

## Chapter 5. Discussion of Pension and Health Care Liabilities

### Pension Liabilities

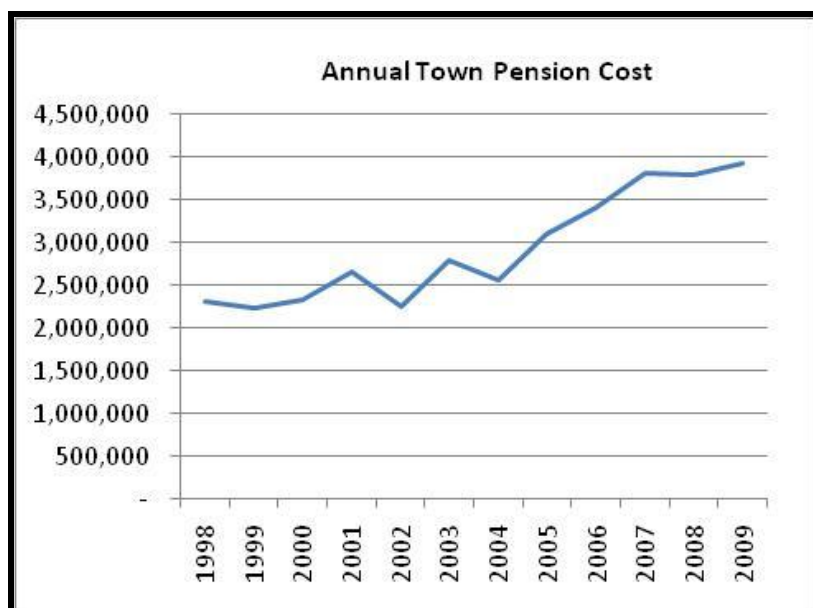
This section analyzes the status of the town's pension liabilities. The FCCC expressed concern that pension costs may continue to grow at a faster rate than the town's revenues. If this happens, cuts would need to be made from other town services. Our analysis of the town's pension obligations revealed a considerable risk that payments will increase substantially in coming years, in part due to the recent credit crisis, which has dramatically lowered the value of pension investments.

#### *Description of the Plans*

Amherst and the regional schools operate defined benefit pension plans for eligible employees. A defined benefit plan is a type of pension plan in which the Town is obligated to pay a certain amount of money to each retired employee for life, based on a the employee's age, years of service, and an average of three years of the employee's regular compensation. The plan also provides for job related and non-job related disability payments, death benefits, and termination allowances. There may also be provisions for payments to surviving spouses. In addition, there may be cost-of-living increases in the monthly payments.

Amherst's pension plan is operated by the Hampshire County Retirement System (HCRS). HCRS also manages the pension plan that covers regional school employees. For simplicity, this report combines those two plans. All figures that are quoted reflect 100% of the Amherst pension costs and 77% of the regional school pension costs (77% is the current portion of regional school costs borne by Amherst). These plans cover all Amherst and regional school employees except for teachers. The cost of providing pensions for teachers is borne by the state.

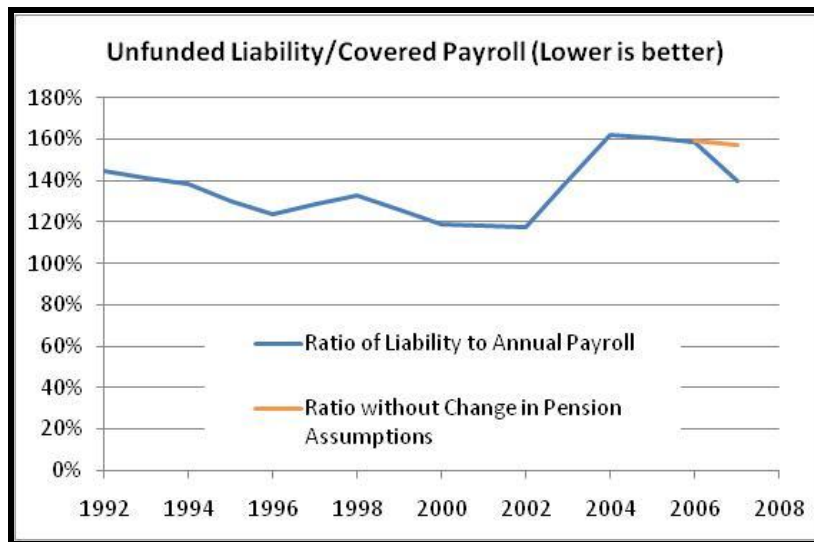
All data quoted here come from one of two sources: The Hampshire County Retirement System Valuation Report (2007), and the Hampshire County Retirement Board Annual Report (2008). Both of these reports are available at <http://www.mass.gov/perac/hampshire/hampshire.htm>



The chart above shows the annual contribution made by the Town for pensions since 1998. This cost increased from about 2.25 million in the early part of this decade to about 3.8 million today – an increase of more than 60%. There are two main reasons for the increase. First, pension contributions for current employees go up when salaries increase. Second, investment returns in the pension fund have been lower than expected since 2000. When this happened, the town was obligated to make additional contributions to its fund.

**Overall Health of the Pension Plan**

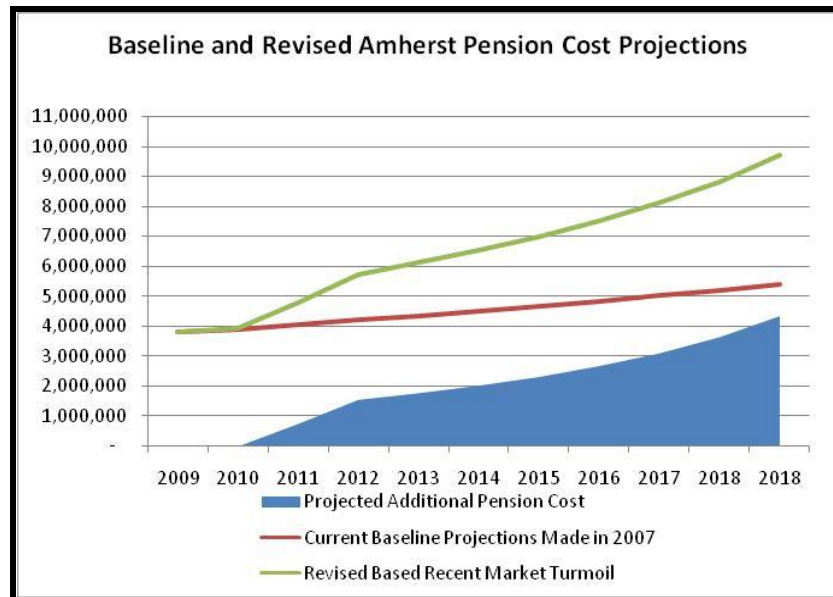
HCRS is half way through a 40 year funding program to change from a pay-as-you-go program where the town pays their share of the retirement benefit when the employee retires to a fully funded program where the town pays the “normal cost” for each employee so that their account is fully funded when they retire. At the start of 2008 Amherst’s share of HCRS was roughly \$56 million in its pension funds. According to HCRS’s actuary a fully funded system should have been \$87 million. The \$31 million deficit is called our unfunded pension liability. The chart below shows the unfunded liability as a percentage of the total payroll of all covered employees (this ratio is a standard measure of the health of a pension plan). Since 1992 the liability has ranged from a high of 160% of annual salaries (in 2004) to a low of 120% in 2002. It declined in 2007 because of a change in the pension assumptions. Without that change the liability would have remained at the high end of the long-run range.



**Impact of Financial Market Crisis on Amherst Pension Costs**

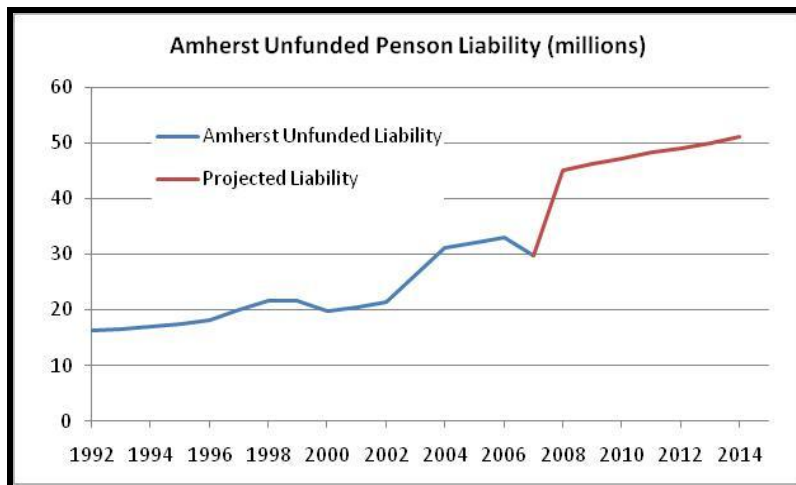
The recent decline in stock and bond markets has caused a significant decrease in the market value of the pension fund. This, in turn, increases the amount the town will need to contribute to the fund in coming years. The full impact will not be felt until FY2012. This is because pension contributions are determined almost two years in advance to allow for appropriate planning by the finance committee and town meeting. The chart below shows the estimated pension costs using 2007 estimates (red line). The green line above shows the likely contribution schedule given a 20% decline in the value of the investment portfolio in 2008. The blue area at the bottom shows the additional contributions that would be needed each year under present law, which requires full funding by 2028. Many pension leaders will ask their

legislators for relief from the impact of the financial crisis by extending in some way their required funding schedules. As of now the outcome of those efforts are unknown.



**Impact on the Unfunded Liability**

Recent declines in financial markets will cause a large increase in the unfunded liability. The chart below shows the liability from 1992 to 2007 (blue line) in millions of dollars. The red line shows the liability projected over the next five years (assuming a 20% decline in the value of the pension fund in 2008).



**Impact on FCCC Budget Estimates**

Each of the budget scenarios put together by the FCCC (in conjunction with town executives) uses the Current Baseline Assumptions<sup>2</sup>. The likely impact of the recent decline in asset prices is a multi-million dollar increase in annual pension contributions from FY2012 onward.

<sup>2</sup>For simplicity we have assumed throughout that Amherst accounts for 31.4% of the Hampshire County Retirement system. This figure represents about 25% for Town employees and 6% of Amherst's share of the Regional School costs.

## Health Care Liabilities

The cost of providing health care to retirees is a large and rapidly growing liability. This year the combined cost of providing health insurance to retirees is estimated at \$2.8 million. Our actuarial consultants estimate this cost will rise to \$4.8 million in 2014. Minimizing the long-run impact on our budget requires setting aside reserves to fund these liabilities in the future.

Amherst offers health insurance to retired employees and their spouses. The coverage for retired employees is the same as the coverage for active employees. When they turn 65, most retirees switch to a Medicare supplemental plan. Retirees pay between 18% and 25% of the cost, depending on the plan. Under the current rules, employees who are age 55 and have worked for the town for 10 years are eligible, as are employees under 55 who have worked at least 20 years for the town.

### Analysis

The following tables summarize the estimated liability for retiree health care. All data quoted here are taken from the GASB Actuarial Valuation reports for the Town and for the Regional Schools as of July 1, 2007. The illustrative chart at the end of this section is based on assumptions made in these reports, but is intended for illustrative purposes and not a forecast.

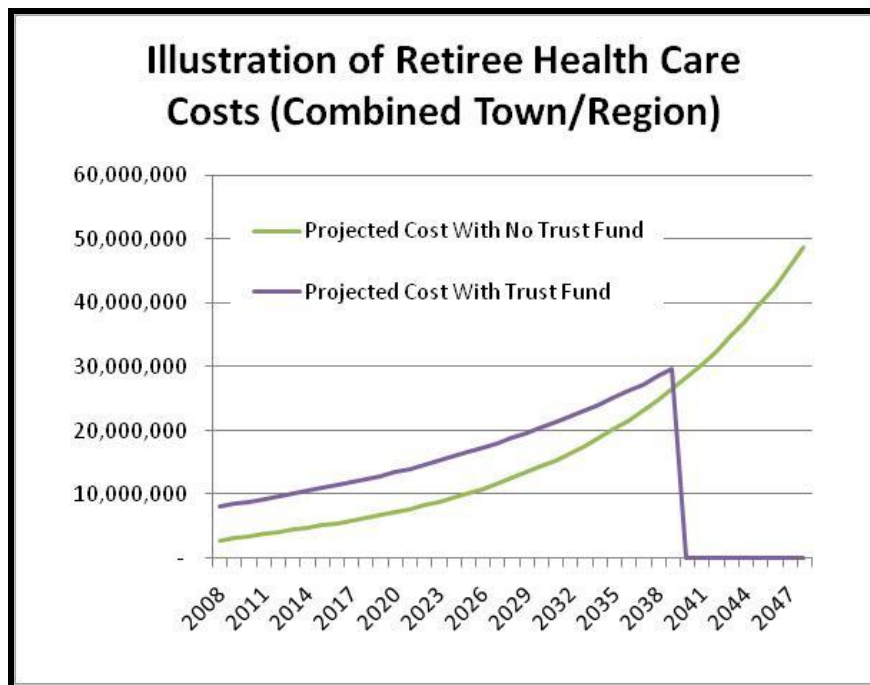
- *Present Value of Future Benefit Payments:* This reflects the current cost of retiree health care.
- *Unfunded Actuarial Accrued Liability:* This is the current cost if we apply pension fund accounting techniques (which assume that we build a trust fund to cover the future liabilities).
- *Annual Required Contribution (30 year amortization):* This is the amount we would contribute to this new trust fund in 2008.
- *Expected Benefit Payments:* This is the estimated cost of providing health care coverage in 2008 to current retirees.

<b>Liabilities for Amherst and the Regional Schools as of Valuation Date July 1, 2007</b>		
	<b>Town of Amherst</b>	<b>Regional Schools</b>
Present value of future benefit payments	\$101,823,473	\$52,757,700
Unfunded Actuarial Accrued Liability (UAAL)	\$68,990,212	\$34,800,006
Annual required contribution (30 yr amortization)	\$5,719,050	\$3,156,545
Expected benefit payments	\$1,938,267	\$1,159,555

*Explanation:* Using the Town of Amherst figures as an example, \$5,719,050 is the amount we are expected to contribute to this new trust fund in 2008. \$1,938,267 is the amount the trust fund would pay out to retired employees for health care coverage. The difference (\$3,780,783) would be left in the trust fund and invested to provide future benefits.

Combined Liability (Town + 77% Regional)	
Present Value Future Benefits	143,216,902
Unfunded Actuarial Liability	95,786,217
Annual Required Contribution	8,149,590
Expected Benefit Payments	2,831,124

The combined liability (Town + 77% of the Regional Schools) is given in the table above. These figures show that roughly 8.15 million is the expected combined cost needed to build a self-sustaining trust fund over a 30-year period. Combined retiree health care costs are 2.83 million in 2008 and are projected to grow at a high rate in coming years.



**Impact on FCCC Budget Estimates**

Each of the budget scenarios put together by the FCCC (in conjunction with town executives) assumes the Town continues to pay retiree health care costs out-of-pocket, and does not create a trust fund to pay for future costs. A decision to begin setting aside money to pay for future retiree health care costs would increase the budget shortfall that is projected by the FCCC in coming years.