

Winchester Finance Committee Report on the Town's Financial Condition and Options for FY03

The Finance Committee is pleased to present to you, the members of Town Meeting and the citizens of the town, our Annual Report on the Town's finances. It sets forth:

- the basics of our current financial condition in fiscal years 2002 and 2003;
- our funding sources and our current expenditures;
- an assessment of the reasonableness of our tax burden and our spending; and
- the committee's conclusion that the Town must either reduce staff or raise revenues via a Proposition 2 ½ override.

Unlike our budget analysis each spring, this report addresses the key factors and policy issues facing the Town and not the detailed line item analysis so essential to the Town's cost management. The spring budget process is essentially a bottom-up analysis, the Finance Committee believes a top-down, strategic analysis is also necessary.

As the town's official fiscal watchdog, our primary mission is to advise and make recommendations to Town Meeting on the budget and other areas of finance. The analyses and charts herein are offered to you in that spirit.

by Winchester Finance Committee

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What fiscal issues does the Town currently face?

Winchester, like most other towns in Massachusetts, finds it difficult to maintain current levels of service while keeping costs matched to the rate of increase in revenues. Key factors affecting revenues and expenses follow.

On the revenue side:

Under Proposition 2½, the Town's total property tax revenues can rise by only 2.5% on existing property absent any tax overrides. (New construction and improvements are counted as "new growth" and may increase total tax receipts.) Including "new growth," McCall & Lincoln debt exclusions and Chapter 110 water & sewer debt, the Town's tax levy has grown at an average of 4.8% annually over the past 5 years. Excluding the debt overrides and the water and sewer debt, the growth has been 4.0% annually for the same period.

The tax base has a low and declining percentage of business property. Businesses require a different mix of municipal services – perhaps more fire, police, and public works, but no school, hence they are proportionately less expensive. While the Planning Board has been diligently working on land use planning, particularly for North Main Street, any redeveloping of those re-zoned areas, and any significant benefits upon the town's finances, are years or decades away.

The current State budget crisis means State Aid, presently 12% of the budget, is likely to decrease.

There are no new sources of revenue on the horizon. New construction is down with the current economic climate, and Winchester has little room for significant new construction in any event.

Since the town no longer has the option of selling capital assets, such as the Woburn Loop, to meet capital requirements, it is seriously under-investing in capital.

On the expense side:

The Town has cut most non-personnel spending, leaving employee costs at 68% of the budget.

Health care costs on these employees are growing 16% or more a year, exacerbating the problem.

The school population declined from the peak in the 1970's, but has been rising throughout much of the 1990's. This creates a need for more teachers, pure and simple, costing more than just the wage increases discussed above.

While productivity has increased significantly in Town operations, we are running out of obvious ways to reduce staffing and still get the job done. A snowplow does not need a crew of two (as was once required by contract in Winchester), but it does need a driver.

Normal cycles of capital life will require continued funding for maintenance, replacement for major school, road and other projects, such as flood control.

Winchester Residential Taxes Pay Most of the Town's Expenses

The Town's revenue for the fiscal year ending June 30, 2002 is projected to be \$54.9M, with an additional \$4.3M from Water & Sewer charges, which are accounted for separately.

73.9% is from Real Estate Taxes, Chapter 110, and Debt Exclusions (McCall and Lincoln).

Chapter 110, which represent 5.1% of revenue, shifts the residential portion of capital costs for Water & Sewer to the tax levy. This allows taxpayers to deduct these costs as part of their Itemized Deductions (Schedule A) on their Federal Income Tax, thus saving Winchester homeowners collectively almost \$1,000,000.

2.4% is previously approved debt exclusion overrides for Immediate School Repairs and rebuilding McCall and Lincoln Schools. These taxes will be eliminated as the state reimburses us for a portion of the cost and the bonds are paid off.

State Aid is 10.7% of the budget, plus 1.9% reimbursement for School Building projects (primarily McCall in FY02), for a total **12.6%** from the Commonwealth. State Aid has more than doubled over the last 10 years, but this is probably the high water mark. Cuts in state aid and the School Building Assistance program are likely due to the current State budget crisis and the Cellucci-Swift state income tax initiative, which is not yet fully phased in.

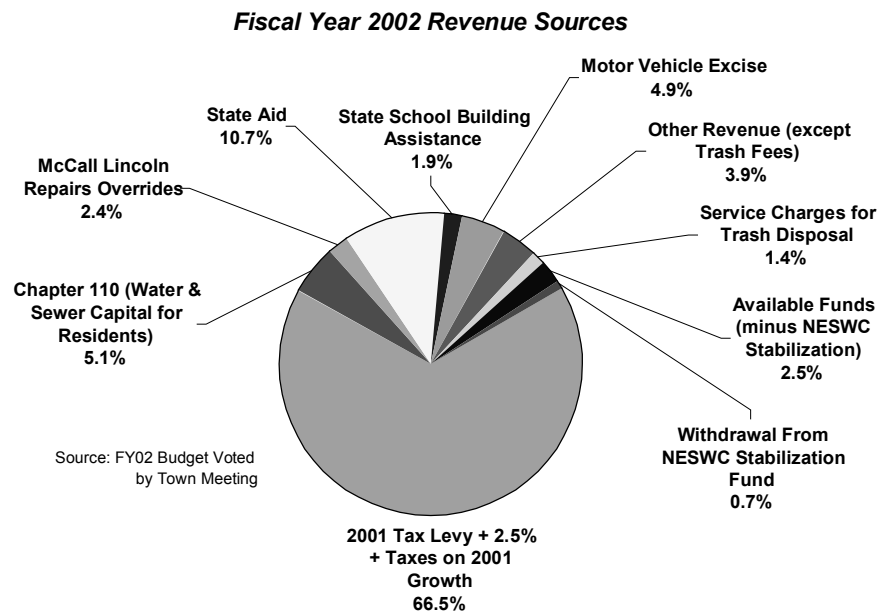
All other revenue sources total **13.5%**.

Motor Vehicle Excise taxes are 4.9% and could decrease if new car sales decline.

Other Revenue of 3.9% (excluding Trash Fees and NESWC Stabilization) includes about 1% from investment income, which could decrease as investment returns have declined.

Available funds (excluding NESWC Stabilization) are 2.5% of revenue and include Free Cash accumulated in previous years, which can vary widely from year to year.

While we get 1.4% of the budget from transfer station fees and permits, we are also drawing down the NESWC Stabilization Fund (to the tune of 0.7%) to pay for our participation in a Trash-to-Energy project. The total for this category is 2.1%.



How Your Tax Dollars Are Spent

Overall spending for the Town increased 6% from FY01 to FY02. Significant increases or decreases include:

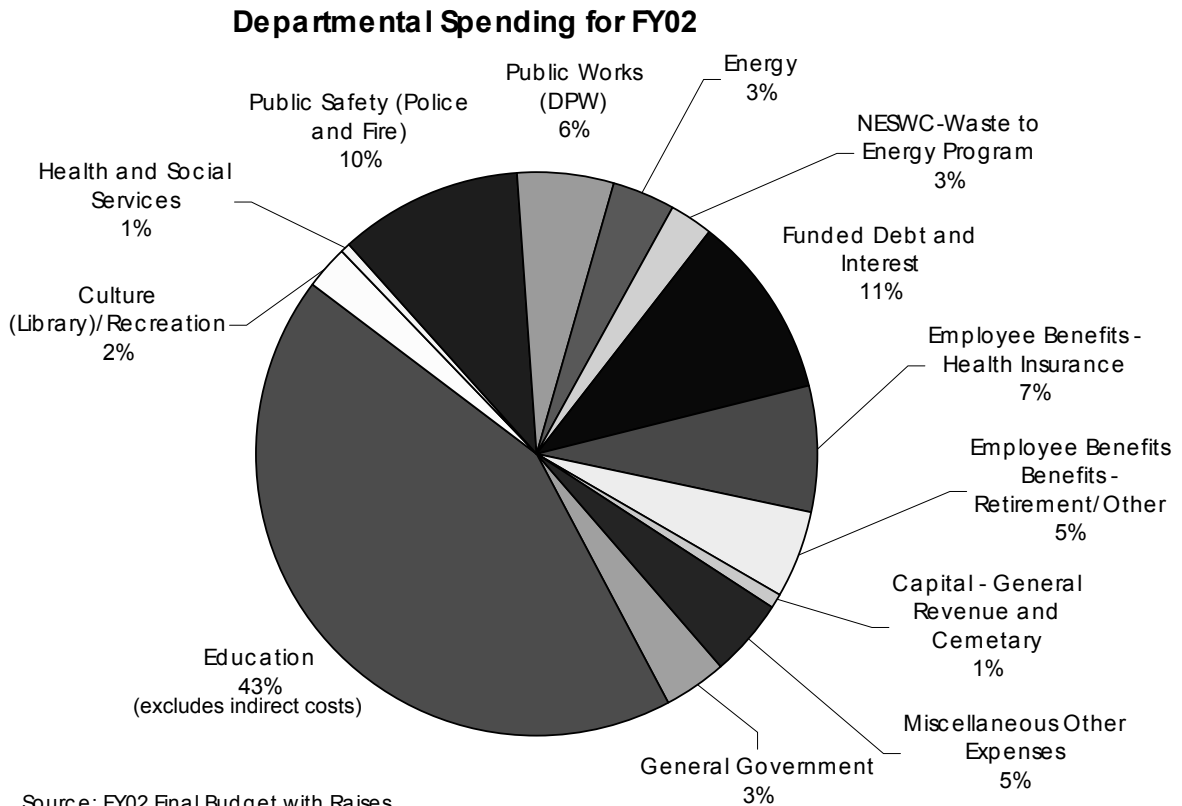
Energy: 33% increase due to price increases in the cost of fuel and electricity for town buildings (including schools) and plants.

Funded Debt and Interest: 28% increase in FY02 for interest payments on Lincoln and McCall building renovations.

Health Insurance: 16% increase in premiums over FY01 to more than \$3.7M for FY2002. This has been growing much faster than inflation (or our revenues under Proposition 2 ½).

Other Expenses: 37% increase due to an increase in the reserve fund; the commencement of payments for environmental remediation at McCall School and DPW facilities; and the snow and ice deficit from FY01.

Revenue Financed Capital Improvement: 58% decrease reflects reducing capital expenditures to fund current expenses.



Salaries and Benefits Represent the Largest Expenditure

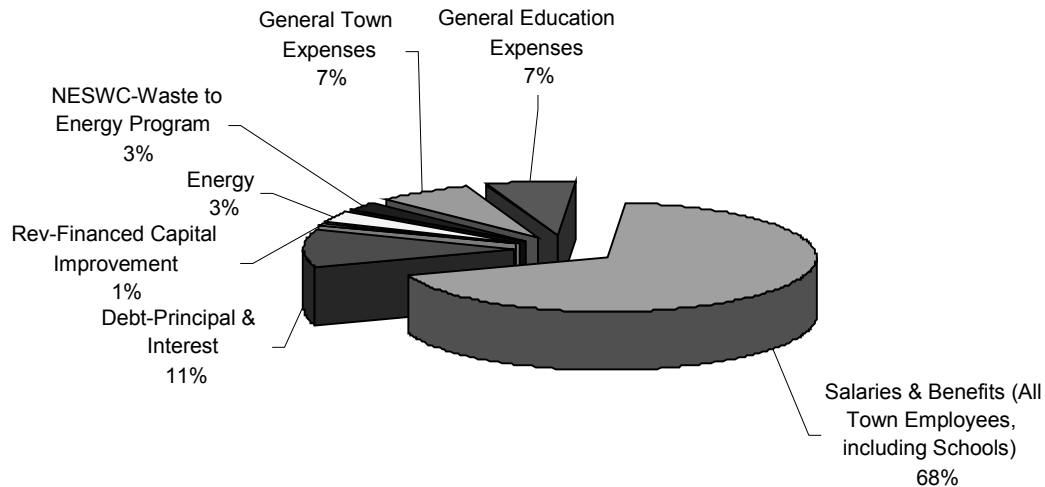
Salaries and Employee Benefits are 68% of Town expenses.

Over 70% of the more than 700 Town employees are members of the 8 unions that govern salaries and benefits and include increases for “step and track”, inflation, and seniority. While the pay packages are competitive to similar towns; these costs are growing faster than inflation. In addition, the union increases usually influence non-union pay packages.

School Department staffing (including teachers) has increased roughly 3% from budgeted FY01 to budgeted FY02 to staff SPED, improve student/teacher ratios, and accommodate the increase in student population. Other Town Departments have either decreased or remained constant in staffing levels.

A freeze or cut in salary spending will necessitate a reduction in staff levels and probably require a layoff of Town employees (some retirement and attrition can be expected).

Town Spending on Salaries and Benefits - FY02



Education is the Largest Town Service

The direct Education budget is 43% of the town budget, which does not include the cost of the building, energy, and employee benefit expenses. Fully allocated, Education is in excess of 60% of the Town's budget (excluding Water & Sewer).

While the total school population increased only 2% from 2001 to 2002; the Special Education (SPED) population increased 6% during this same time period. SPED represented 13% of the student population in 2001; 14% in 2002; and is expected to increase to 15% in 2003.

As knowledge of learning styles and disabilities have expanded, Special Education mandates have been imposed:

MA Public Education Law Section 28

Federal Individuals with Disability Act (IDEA)

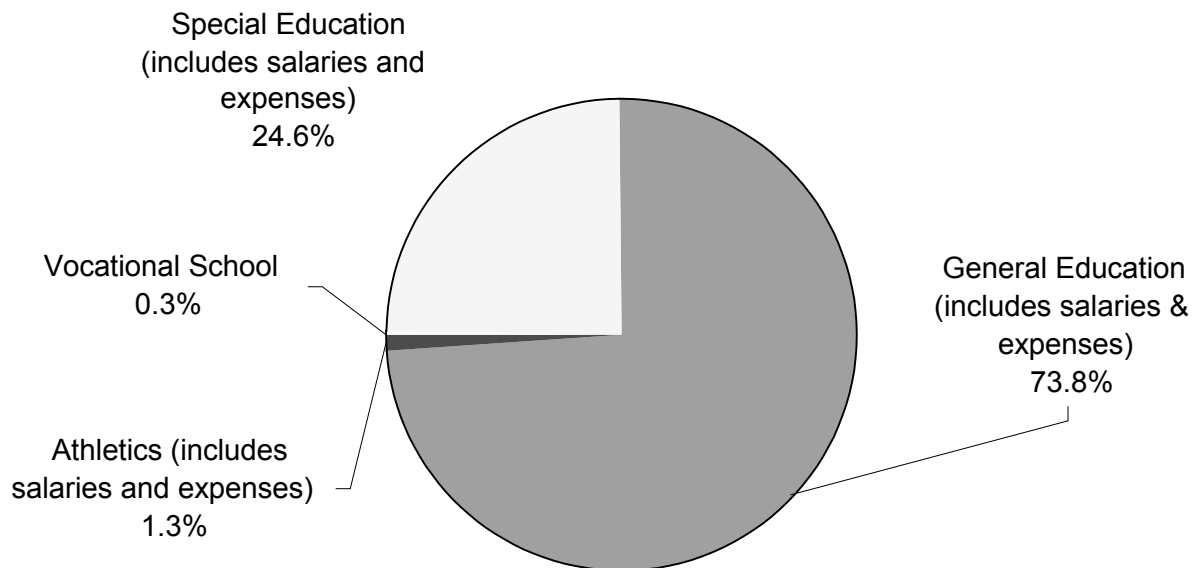
Americans with Disabilities Act: 1990

Federal Rehabilitation Act: Section 504

SPED is currently 24.6% of educational spending and difficult to control due to the strict state & federal regulations and oversight. Parents can (and sometimes do) appeal or sue to have a determination of a child's SPED plans changed, with the town picking up both the legal and SPED costs.

In an effort to control SPED spending, the School Department has introduced new programs at the elementary level; and has diverted in-town versus out-of-town placements with a total cost savings estimated by the School Department of \$374K. This resulted in only a 3% increase in SPED spending for FY02 over FY01.

Educational Spending for FY02



Winchester Spends Slightly Less Than the Average of Comparable Towns

The Finance Committee selected six benchmark towns from the FACTS list of 22 towns to compare the relative use of local tax dollars. We defined selection criteria that would identify towns with similar economic structure, and avoided measures that we believed might bias the analysis. Our final selection criteria were:

Population between 10,000 and 35,000

School Enrollment less than 10,000

A K-12 school system structure

Reliance on revenue derived from residents at 70% or more. This includes residential taxes, fees, excise taxes and other revenue derived from residents

Population density (population per square mile) at 1,500 or more

The following towns are the six towns of the FACTS 22 towns that met all five criteria:

	Population 2000	FY2000 School Enrollment	School Structure	Population Density	FY01 Percent Rev. from Residents
Reading	23,708	4,193	K-12	2,402	76%
Belmont	24,194	3,559	K-12	5,271	84%
Wellesley	26,613	3,684	K-12	2,648	80%
Melrose	27,134	3,463	K-12	5,737	73%
Needham	28,911	4,330	K-12	2,313	77%
Lexington	30,355	5,809	K-12	1,842	75%
Winchester	20,810	3,218	K-12	3,527	87%

Source: Population, population density, school structure from Mass DOR, At-a-Glance Reports as of 1/3/02; Percent Revenue generated from Residents calculated from DOR data; Enrollment from Mass DOE Long Term Enrollment Trends report of 2/1/02.

Spending Analysis Methodology

Analyzing spending across towns can be tricky because, while towns might provide similar services, they might report spending under different categories. Using detailed "Schedule A" financial reports from the Massachusetts Department of Revenue for FY2000, the most recent available, we:

compared Municipal spending on a per capita (per resident) basis.

compared Education general fund spending on a per student basis, excluding programs not funded by local taxes, such as school lunches or grant-funded programs such as Metco.

excluded spending for expenditures not incurred by all towns, such as electric power production and MBTA assessments.

excluded capital spending for major bonded construction projects that have large current year cash outlays.

The net deficit or surplus (receipts less expenditures) of each town's special revenue programs is included in our analysis, to reflect the portion of those programs funded by the general fund.

Winchester spends 5% less than the benchmark town average on non-school services, and 6% less than the average on school services

Winchester spending is somewhat higher than Reading & Melrose, similar to Needham, somewhat below Belmont, and well below Lexington and Wellesley.

While spending is not the only determinant of education test scores, MCAS (Mass. Comprehensive Assessment System) test rankings appear to correlate with per pupil spending for these towns.

	Non-School Spending Per Capita (All Sources)	Winchester Percent Diff Versus Towns		School Spending Per Pupil (General Fund)	Winchester Percent Diff Versus Towns	MCAS Rank 2000
Reading	\$1,363	+14 %		\$5,973	+10 %	24
Belmont	\$1,836	- 16 %		\$7,127	-8 %	2
Wellesley	\$1,766	-12 %		\$8,209	-20 %	8
Melrose	\$1,322	+17 %		\$6,091	+8 %	89
Needham	\$1,567	- 1 %		\$6,377	+3 %	4
Lexington	\$1,906	- 19 %		\$7,944	-18 %	5
Benchmark Towns Average	\$1,627	- 5 %		\$6,954	-6 %	
Winchester	\$1,549			\$6,553		12

School Enrollment as a Driver of Expense

Most of the major drivers of costs experienced by Winchester are common to all Massachusetts towns, with the exception of the most important - school enrollment growth. Some towns have seen rapid growth with the “baby boom echo” and others have actually seen declines. Below you can see the variation in enrollment growth experienced by the benchmark towns.

	Winchester	Reading	Belmont	Wellesley	Melrose	Needham	Lexington	6-Town Average
School Enrollment								
1990	2,756	3,560	2,795	2,892	3,782	3,587	4,387	3,501
1995	2,969	3,833	3,263	3,271	3,481	3,888	5,076	3,802
2000	3,218	4,193	3,559	3,684	3,463	4,330	5,809	4,173
%Chg past 5 yrs	8%	9%	9%	13%	-1%	11%	14%	10%
%Chg past 10 yrs	17%	18%	27%	27%	-8%	21%	32%	19%

When school enrollment is growing, this adds financial pressure beyond inflation. All benchmark towns except Melrose have experienced this pressure, in addition to the other pressures cited in earlier sections. **All of the benchmark towns, except Winchester, have passed one or more general operating budget overrides since the inception of Proposition 2 ½ in 1981 – as per the Massachusetts Dept. of Revenue, Division of Local Services Municipal Data Bank.**

Options for Winchester

As a result of the factors and trends identified above, Winchester can no longer afford the same level of staffing and services at the budget levels forecasted for FY03 and beyond. Simply put, the alternatives in the near-term are essentially two:

Reduce staffing, or

Increase taxes using an override.

The staff reductions necessary to balance the FY03 budget without an override would be about 20-25 full-time-equivalents, or about 4% of the town's workforce. Other non-staff repercussions currently being proposed include decertification of the library.

We conclude that there are no significant pockets of money available to allow current staffing levels to be maintained, and that current levels of expenses are in line with those of appropriate peer-group towns. The ultimate decision on which path to take will be up to the town's voters.