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Swampscott Financial Forecast: Users' Guide and Assumptions

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Table of Contents

Introduction	1
Revenue Projections	2
Property Tax Levy.....	2
State Aid Cherry Sheet.....	2
Chapter 70.....	2
Unrestricted General Government Aid (UGGA).....	3
Veterans Benefits and Exemptions for Veterans and Elderly	3
Aid to Public Libraries	3
Local Estimated Receipts	3
Enterprise Funds	4
Water/Sewer Budget and Indirect Costs.....	4
Available Funds/Other Financing Sources	4
Available Funds for Operating Budget	4
Free Cash	4
Free Cash for Strategic Reserves and Capital Projects	4
Expenditure Projections	6
Municipal Departments.....	6
Schools	6
Swampscott School Department	6
Essex North Shore Agricultural and Technical School	6
Debt Service.....	6
Existing Non-Exempt Debt	6
BAN Interest- Non-Exempt Debt.....	6
Existing Exempt Debt.....	7
Retirement.....	7
Retirement	7
Insurances.....	7
Unemployment	7
Health Insurance	7
Property/Liability Insurance.....	7
Workers Compensation	7
Medicare.....	7
Enterprise Funds	7
Water and Sewer Direct Charges -	7

Overlay	8
State and County Assessments	8
Free Cash/Other Available Funds	8
Free Cash for Strategic Reserves and Capital Projects	8
Process to Update Forecast	9
Description of Worksheets.....	9
Steps to Update.....	10

INTRODUCTION

The object of the Town of Swampscott's financial forecast is to conservatively project revenues and expenditures five years into the future (FY2020-FY2024). The forecast is intended to provide policymakers with the information they need to make informed decisions around the Town's financial strategies and policies, long-term financial and capital planning, and long-term contracts or obligations.

Revenue and expenditure forecasting is a powerful financial planning tool that can be used to isolate the impact of particular future events and determine their effects on the Town's financial picture. The forecasting model is designed using reasonable assumptions about a wide variety of future events and, by using these assumptions along with known facts, a comprehensive view of the Town's fiscal outlook emerges. Though potential exists that any one item in the forecast may be less than accurate, when taken as a whole, a well-built model presents a fair representation of the Town's future finances.

The approach used in the forecast model for the Town of Swampscott assumes that current staffing service levels will be maintained in the future years of the forecast. The model also assumes that existing Massachusetts General Laws and regulations will remain unchanged over the forecast period. However, as new information becomes available here forward, the assumptions and estimates used in the current projections will need to be regularly reevaluated by Town officials to determine if they are still appropriate and reasonable.

The forecast is structured as a series of Excel worksheets. Revenues are projected in detail in the "Revenue Projections" worksheet and expenditures are projected in detail in an "Expenditure Projections" worksheet. The totals from the detailed revenue and expenditure projections flow into a "Summary" worksheet which reveals projected future operating surpluses or deficits. More detailed sheets are available for more in-depth analysis of issues like new growth (Growth), debt excluded from Proposition 2½ limits and all other non-excluded Town debt ("Non-Exempt Debt Summary" and "Exempt Debt Summary") and local receipts (Local Rcpts). An additional worksheet estimates the impact of cost-of-living increases ("COLA") for collective bargaining agreements and salaries.

REVENUE PROJECTIONS

PROPERTY TAX LEVY

Annual tax levy growth is constrained by Proposition 2½, the Massachusetts General Law that limits the annual growth in a municipality's total tax levy to 2.5%, plus an allowance for certain new construction and other additions to the tax rolls. The law also allows a city or town to increase taxes beyond this annual levy limit with voter approval. An override of this limit by voters becomes a permanent part of the tax levy calculation in future years and is best used for recurring expenses in the regular operating budget.

A debt exclusion may also be approved by voters to increase the levy limit temporarily to fund capital projects. Generally, these projects are financed by borrowing and the annual debt service is added to the levy limit each year until the project is paid off.

The FY2020-FY2024 forecast for Swampscott projects new growth to be \$500,000 per year. This is a blend between the five-year New Growth average and the eleven-year average. New growth is reported to the State each year on Form LA-13 which is typically submitted in late summer or early fall prior to setting a tax rate.

Swampscott has approved a number of debt exclusions in the past. As debt is issued and the annual tax rate set, the Town Treasurer/Collector and Town Accountant complete the State DE-1 schedule to calculate the annual debt service that can be raised outside the Proposition 2½ limits. The existing exempt debt will be retired at the end of FY2027.

Levy limit information is published each year by the Division of Local Services (<https://dls.gateway.dor.state.ma.us/gateway/Login>) and should be reviewed by Town officials periodically in late summer and early fall as growth is certified.

STATE AID CHERRY SHEET

Chapter 70 – Chapter 70 education aid is determined each year by the State Department of Elementary and Secondary Education (DESE) using a complex formula. The formula entails calculating a foundation budget for each municipality or school district based on the number and characteristics of the pupils (e.g., low income, bilingual, or vocational) in the district. The foundation budget represents the minimum level of spending necessary to provide an adequate education in each district. Generally, in communities with sufficient resources, required school spending (aka, “net school spending”) is well above the calculated foundation budget, reflective of historically high education spending. In communities with fewer resources and lower historical spending on education, the formula seeks to maintain required net school spending at a level at least as high as the foundation budget.

To determine the relative contributions from municipal revenues versus state Chapter 70 aid necessary to meet required education spending levels, DESE calculates target levels of local (municipal) contribution and target levels of (state) Chapter 70 aid. These calculations are based on the total income of a municipality's residents and the total property wealth of the municipality. For example, if a community has sufficient income and property wealth to cover 60% of the foundation budget, then the State aid

target is 40% of foundation. Income is measured using State Department of Revenue total income by community from state tax returns and property wealth is measured using equalized property values for each community. Equalized property values are determined by the state every two years and control for differences in local assessing practices. In cases where a municipality has a low ability to pay, less is required from the municipality and state Chapter 70 aid fills the gap between the foundation budget and the required local contribution.

Swampscott provides public education locally at three elementary schools, one middle school, and one senior high school. The Town receives Chapter 70 state school aid to offset some of the costs to educate these pupils. In FY2018, state Chapter 70 aid contributed \$3.47 million to Swampscott. The forecast assumes that this revenue will increase by 1% throughout the term of the forecast. In addition, Swampscott's high school pupils attend the Essex North Shore Agricultural and Technical School.

Past state aid has ranged widely from \$25 per pupil to \$65 per pupil, and it is recommended that Town officials revisit the projection of Chapter 70 funding as the State budget process progresses. However, DESE only publishes detailed Chapter 70 numbers for the Governor's budget and the final State budget on its school finance page under the Ch. 70 heading: <http://www.doe.mass.edu/finance/chapter70/>.

Unrestricted General Government Aid (UGGA) – Swampscott is anticipating receiving \$1.34 million in this category in FY2019 compared to \$1.29 million in FY2018 for an increase of \$45,259 (3.5%). UGGA is projected to grow at a rate of 2.5% for this projection.

To keep UGGA and the other cherry sheet accounts up to date, Town officials will need to monitor the local aid estimates published by the Division of Local Services at each juncture of the state budget process: <http://www.mass.gov/dor/local-officials/municipal-databank-and-local-aid-unit/cherry-sheets/>. The first of these estimates will come after the release of the Governor's budget each year in late January followed by the House Ways and Means Committee budget in mid-April, the final House budget in late April, the Senate Ways and Means budget in mid-May, and final Senate budget in late May. The Conference Committee's budget, which resolves differences in the two legislative versions of the budget, is typically issued in late June. Final cherry sheets reflect any vetoes by the Governor and/or any legislative overrides of these vetoes.

Veterans Benefits and Exemptions for Veterans and Elderly – These accounts consist of reimbursements for veterans' benefits and certain local property exemptions for qualified individuals. In FY2019, the Town will receive \$70,373 in reimbursements compared to \$79,707 in FY2018. This forecast assumes level reimbursements.

Aid to Public Libraries -- This item is a cherry sheet offset and may be spent without an appropriation by the Town's library. This account has no impact on the forecast since it is also raised on the expenditure side, essentially pulling these revenues out of the general revenue mix for direct use by the library.

LOCAL ESTIMATED RECEIPTS

Local estimated receipts are locally-generated revenues, other than real and personal property taxes. Examples include motor vehicle excise, investment income, payments in lieu of taxes, penalties and interest on taxes, departmental revenue, fines, and permit fees. Swampscott reports on 13 categories of local receipts. The history of local receipts versus actual receipts is shown on the local receipts section of

the Revenue Projection worksheet tab in the forecast file. The Town has a practice of conservatively budgeting these items and routinely collects approximately \$400,000 more than was budgeted. As a result, local receipts in excess of estimates have been a primary factor in the Town's positive year-end results and free cash certifications

In FY2019, the Town anticipates collecting \$5.6 million in local receipts versus \$4.6 million in FY2018 for an increase of \$1 million (22%). The actual total local receipt collected in FY2017 was \$5.9 million. Motor vehicle excise revenue projected for FY2019 is \$2.45 million while FY2017 actual collections were \$2.4 million. This is the Town's largest local receipt constituting about 43.8% of the total estimated receipts. Other significant local receipts include license and permits, fees, and other departmental revenue. The Town has adopted the State-authorized meals tax, generating \$244,801 in FY2017. For forecast purposes, motor vehicle excise is anticipated to grow by 3% per year through the term of the forecast. The room/meals tax is projected to increase 2% per year. Other Departmental Revenue, Licenses, and Fines are projected to grow by 1% per year. All other items are projected to remain stable. This results in a net projected increase of 1.48% per year.

ENTERPRISE FUNDS

Water/Sewer Budget and Indirect Costs - The Town utilizes an enterprise fund for its Water and Sewer services. Revenues generated are used to cover costs, including capital outlay and indirect costs. Revenues listed in this section are used to cover all of the costs projected in the expenditure section. Approximately \$822,407 of indirect costs from other departments that provide support to the enterprise is also included in the revenue projection tab. As part of the tax rate setting process, the Town Accountant completes a form submitted to the State that details all water and sewer revenues and expenditures.

AVAILABLE FUNDS/OTHER FINANCING SOURCES

Available Funds for Operating Budget- This line item represents funds that are dedicated to offset expenditures in the expenditure section. Included in the FY2019 budget and in recent prior years, the Town has used recurring revenue from the General Enterprise Fund Offset items and Free Cash to balance the annual budget. In addition, in prior years, revenue from Overlay surplus has been used to reduce the tax levy.

FREE CASH

Free Cash for Strategic Reserves and Capital Projects-

In prior years, the Town's capital has used Free Cash to both support the General Fund budget and to strengthen reserves. In FY2019, the Town allocated \$250,000 each to OPEB funding and capital improvements. In addition, \$500,000 has been allocated to the General Stabilization Fund, to maintain the Town's liquidity and protect against downgrading of the bond rating. The forecast continues allocating Free Cash to these items at the same levels.

The Town also uses Free Cash to support the ongoing General Fund operating budget. \$1,000,000 has

been used for this purpose. Best practice suggests that the Town should not continue this practice. Rather than disrupt service delivery in the next few years, the forecast has a gradual phase out of Free Cash supporting the operating budget. The amount is phased down and eliminated all together by FY2024.

EXPENDITURE PROJECTIONS

MUNICIPAL DEPARTMENTS

In the forecast, Town departments have been grouped by major categories consistent with Town budget and state expenditure reporting. The department budgets are reported as follows: General Government, Public Safety, Public Works, Health, and Human Services and Cultural Services. The Enterprise departments (Water and Sewer) are reported separately.

For projection purposes, the impacts of wage settlements beyond FY2019 have also been factored into the COLA salary worksheet for the five- year forecast. The forecast utilizes a 2% COLA, but this is intended as an example of cost impact moving forward and not a recommendation for any wage settlements. The Town of Swampscott utilizes a salary step system. Therefore, the forecast utilizes a 0.5% step increase across the board. Cost impacts have been included in the Expenditure worksheet within each Salary and Wages line item. The COLA worksheet allows for simulation of other wage agreements and step amounts.

Departmental operating budget accounts have been projected to increase by 2% per year, which is a beginning guideline. As the budget review proceeds each year, adjustments can be made in the forecast.

SCHOOLS

Swampscott School Department – The Swampscott School Department, under the jurisdiction of the Swampscott School Committee, provides education services at three elementary schools, one middle school, and one senior high school. The FY2019 Public School budget is approximately \$29 million. The forecast utilizes an inflation factor of 3.5% per year for both the public-school system and the regional school system. The FY2017 student enrollment was 2,131.

Essex North Shore Agricultural and Technical School – Swampscott has sent students to the School, and its percentage of the total yearly assessment was based upon the ratio of Swampscott student enrollment to the total student enrollment. For the purposes of the forecast, it is assumed that the Town will decide to withdraw. Regional School costs are projected at a 3.5% annual growth.

DEBT SERVICE

Existing Non-Exempt Debt - Debt Service costs in this category are funded within the limits of Proposition 2½. FY2038 is the last year for debt payments for existing bonded projects, as they will all be paid off in that fiscal year.

BAN Interest- Non-Exempt Debt - During construction/acquisition and before long term debt is issued, the Town may borrow funds for cash flow purposes and/or market timing. The interest rate is lower on these short-term borrowings and this budget item is a projection of these interest costs.

Authorized/Unissued- Non-Exempt Debt - The Town has a number of projects that have been approved by Town Meeting, but for which long-term Debt has not yet been issued. The projected debt costs for

these projects are shown.

Existing Exempt Debt - Debt Service costs in this category are funded outside the limits of Proposition 2½. FY2035 is the last year for debt payments for existing exempt bonded projects.

RETIREMENT

Retirement - Town pension costs are projected based on the estimated appropriations issued by the Public Employee Retirement Administration Commission (PERAC). The appropriation letter from PERAC breaks down the assessments between the Town, Enterprise Funds, and the Town Housing Authority, and shows the percentage of the total borne by each entity. The allocation for Swampscott is detailed in the Retirement worksheet. The forecast utilizes the latest actuary analysis so as to achieve full funding by FY2031.

INSURANCES

Unemployment – Unemployment cost for FY2019 is \$10,000. This variable is level-funded throughout the term of the forecast.

Health Insurance – The town receives its health insurance through the State’s Group Insurance Commission or GIC. The forecast includes an 8.0% increase in rates in FY2020. Rates are estimated to phase down in the out years to 5% in FY2024. The health insurance market is volatile and subject to extreme changes. As such, this variable should be reviewed and adjusted on an annual basis to reflect current trends

Property/Liability Insurance - This insurance covers municipal building and contents, motor vehicle and public official liability insurance. These costs have been relatively stable in recent years and have been forecast to grow modestly at 3.0%. As additional building or building improvements are added to the property portfolio, this variable will need to be adjusted upward.

Workers Compensation – Swampscott’s FY2019 appropriation is \$276,500 to support Workers Compensation claims. It is anticipated that this cost will increase by 2% per year through the term of the forecast.

Medicare – The Town/School appropriation for FY2019 is \$493,500. Medicare has been projected to increase by 2.5% per year, or whatever final COLA settlement is reached.

ENTERPRISE FUNDS

Water and Sewer Direct Charges - The Water and Sewer Enterprise Funds are a self-sufficient operation. All of the direct costs for water and sewer expenses are included in this category. The combined cost for FY2019 is slightly less than \$6 million. The indirect costs are budgeted within the various operating budgets and are allocated in the enterprise report submitted to the State when the tax rate is set. As a self-sufficient operation, all of these costs are offset by water/sewer revenues in the revenue detail

worksheet. This forecast model does not attempt to project future revenue needs and expenditure costs for the water or sewer operations.

OVERLAY

Allowance for Abatements and Exemptions - The overlay account has been projected to be 0.8% of the annual levy. In a revaluation year, a community typically has more abatement requests, so a good practice is to increase the overlay to reflect the risk of additional abatements. This model should be updated to reflect the update year.

STATE AND COUNTY ASSESSMENTS

All State assessments included in the forecast are based on the Cherry Sheet estimates published by the Division of Local Services. The most significant of the State assessments in Swampscott are the Massachusetts Bay Transit Authority (MBTA), representing 36.3%, and Charter School Sending, representing 48.5% of all State Assessments. All State Assessments are anticipated to increase by 2.5% per year through the term of the forecast.

FREE CASH/OTHER AVAILABLE FUNDS

Free Cash for Strategic Reserves and Capital Projects - In prior years, the Town's capital commitment was funded through debt service (both non-excluded and excluded) and pay as you go non-discretionary and discretionary projects. Free Cash would be used to fund the General Stabilization Fund and other reserves such as for OPEB. Phasing out Free Cash as a revenue to support recurring services allows the adoption of a new strategy for Free Cash use. Assuming conservatively that prior year-end Free Cash will be approximately \$2 million per year, and Free Cash use is phased down and finally out by FY2024, this non-recurring source of revenue can be matched against non-recurring expenditures such as snow deficits, OPEB, and capital improvements.

OPEB Fund - Other Post-Employment Benefits (mainly retiree health insurance) are a significant future cost for municipalities in Massachusetts and across the U.S. Unlike Massachusetts retirement law, there is no requirement to put money aside for these future costs that are being incurred as employee work. State law does provide a mechanism for municipalities to set aside funds voluntarily in a special fund to accumulate money to pay for these future costs. Swampscott has established such a fund and has appropriated Free Cash, when available, to this fund. Beginning in FY2020 and beyond, it is anticipated that the Town will annually contribute to this fund by a minimum of \$250,000 per year.

PROCESS TO UPDATE FORECAST

Description of Worksheets

The Swampscott Revenue/Expenditure Forecast file has a number of independent and interconnected worksheets. The following describes the worksheets which include:

- Summary
- Revenue Projections
- Growth
- Local Receipts
- Expenditure Projections
- COLA
- Retirement
- Capital Investment
- Town Budgets Proposed and Appropriations
- Existing Debt Summary Schedule
- Projected Debt Service for Authorized/Unissued Bonds
- Tax Levy Limit chart
- Free Cash/Stabilization Fund chart

Summary – This worksheet rolls up from the Revenue and Expenditure forecast details to provide a quick overview of the five- year plan.

Revenue Projections – This worksheet is used to list the details of the various revenue categories and the assumptions that are used in the projections. The Final Recap column will require manual data entry each year to input actual revenues collected. Future year projections are calculated utilizing the straight-line percentage change column on the far right. If no growth is expected, a 0 should be input in the “percentage projection” column. If a revenue is not projected to grow linearly, the revenue expectations should be input manually into the forecast. Once the final tax recap is approved, any changes in the revenue detail must be made in this worksheet.

Growth – This worksheet is a summary of the new growth taxes that the Town can raise within the limits of Proposition 2½ for the fiscal year. Once the final growth amount is calculated by the Assessors, the Selectmen set the tax rate, and the tax recap is approved by the State, the final amounts will need to be added to the worksheet. When updating the forecast each year, the finance team should discuss any changes in the growth projections.

Local Receipts – This worksheet details the history of local receipts and is updated at the close of each fiscal year and at the time of the tax rate submission to the state. It plays a valuable role in the preparation of revenue estimates for the upcoming budgets.

Expenditure Projections – This worksheet lists the details of the various departments and other expenses categories that are in the Town Administrator’s budget. In addition, it lists all the non-departmental financial appropriations. Finally, it lists other expenditure categories that do not require town meeting appropriation but that are expenses that must be included in the tax rate setting process. The wage line for each department is automatically changed when the user enters information into the COLA worksheet.

The user must also enter manually or use the cost increase straight-line factor for the other cost items listed.

COLA and Wages – This worksheet provides the user with multiple “what if” scenarios on COLA and step increases. Factors entered into the COLA and/or step cells automatically update the department wage line in the Expenditure Projections detail.

Retirement – This worksheet lists the current PERAC retirement appropriation for Essex County and Swampscott’s share. The funding schedule is updated by an actuary hired by the County every three years, and information will be provided to Swampscott to update the forecast.

Capital Investment– The capital worksheet brings together the Town’s existing general fund debt service, estimated debt for projects approved by Town Meeting and other capital appropriations with the funding anticipated to be available for the Town’s developing capital plan. The underlying assumption in this worksheet is that a minimum of \$300,000 will be available on a recurring annual basis to finance capital items and a minimum of \$100,000 will be appropriated annually to the Capital Stabilization fund. The worksheet also calculates the Town’s annual general fund capital investment as a percent of net revenues, which excludes the enterprise fund. The Town’s FY2017 capital investment as a percent of net revenue is 4.23%. Going forward, the Towns investment increases by FY2020 to 5.78% of net revenue as a result of the new debt for the Town hall renovation. It is anticipated the new CIP debt projects that are contemplated in the FY2018-FY2022 CIP will maintain the Town’s investment at a minimum of 5.78%. This tab can be used on an iterative basis to identify the amount of capital investment needed to reach the Town’s target for capital as a percent of prior year revenues, as will be established in the Town’s financial policies.

Town Budgets – This worksheet duplicates the budget line items that are submitted to Town Meeting and can be utilized to roll up to the expenditure detail worksheet.

Existing Debt Summary – This worksheet summarizes all of the Town’s existing debt service by fiscal year by funding source. This worksheet must be updated whenever the Town issues permanent debt. The Town Treasurer and the Financial Advisor play an invaluable role in maintaining the detail debt schedules for this summary.

Projected Long Term Debt Service for Authorized/Unissued Debt – This worksheet projects the timing and estimated debt service for projects that have been approved by the Town Meeting but have not yet been permanently borrowed. The Financial Advisor, Treasurer/Collector, Town Accountant, and Town Administrator work together to time the issue and principal amount based on needs, budget impact, and the market.

Steps to Update

The process for updating the forecasting spreadsheet to reflect a new base year must be done systematically and with care as changes to certain data and formulas will be needed. As a result, it is strongly recommended that users save a separate back-up file of the spreadsheet before any changes are saved in the spreadsheet they are updating.

Generally, the updating of the Revenue and Expenditure spreadsheets should occur after the end of the

current fiscal year after the Town's budget for next year has been adopted by the Town Meeting and final cherry sheets are issued. Both spreadsheets must be updated one final time when the tax recap approved by the State.

This final step will update the structure of the forecast to make room for a new Year 5. To do this, insert a column to the right of the last FYXXX Projection year in both the Revenue and Expenditure spreadsheets and copy the data and formulas from the prior column. This step will add the data for the last year of the five-year forecast. This same process should be followed for all tabs of the worksheet.

Data for what was previously the base year of the forecast must also be updated with actuals. For the FY2018-FY2022 forecast, the base year was FY2017 and included revenues and expenditure expectations approved in the Town's adopted budget. These must now be replaced with actual revenues and expenditures. The new base year will then need to be updated using that year's approved budget. The first update will change the forecast to FY2019-FY2023 and FY2018 will become the base year.

After the base year has been updated, the user is now ready to prepare the five-year forecast working with the appropriate individual worksheets. To forecast the first-year revenues or expenditures, a percent change is applied to the base year to yield the projected amount. To project the second year, the percent change is applied to the first forecast year as the base. In other words, the selected percent change is applied to each year of the forecast. This is accomplished by modifying, if appropriate, the percentage change column to reflect recent experience and new information and expectations.

In some instances, the user may find that it is easier to simply enter values for certain items. This is fine as long as the user remembers to replace the formulas later if they want to determine the projections based on percent change in other years.

ABOUT THE CENTER

The Edward J. Collins, Jr. Center for Public Management in the McCormack Graduate School of Policy and Global Studies at the University of Massachusetts Boston was established in 2008 to improve the efficiency and effectiveness of all levels of government. The Center is funded by the Commonwealth and through fees charged for its services.



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