APPROPRIATION COMMITTEE
TOWN OF LEXINGTON

REPORT TO THE
2020 ANNUAL TOWN MEETING

RELEASED MARCH 25, 2020
UPDATED MAY 11, 2020

APPROPRIATION COMMITTEE MEMBERS
Glenn P. Parker, Chair • Sanjay Padaki, Vice Chair • Alan Levine, Secretary
Carolyn Kosnoff (ex officio; non-voting) • John Bartenstein • Eric Michelson
Meg Muckenhoupt • Albert Nichols • Lily Manhua Yan

Contents

Summary of Warrant Article Recommendations

Abbreviations

EF	Enterprise Fund	CPA	Community Preservation Act
GF	General Fund	DSSF	Debt Service Stabilization Fund
RE	Retained Earnings	IP	A motion to Indefinitely Postpone is expected
RF	Revolving Fund	TDM	Traffic Demand Management

Article	Title	Funds Requested	Funding Source	Committee Recommendation
4	Appropriate FY2021 Operating Budget	*See below*	*See below*	**Approve (8-0)**
5	Appropriate FY2021 Enterprise Funds Budgets	**$10,745,775** **$10,846,234** **$3,015,408**	**Water EF** **Wastewater EF** **Recreation EF**	**Approve (8-0)**
6	Establish Qualifications for Tax Deferrals	**None**	**N/A**	**Approve (8-0)**
7	Petition General Court to Amend Legislation Regarding Tax Deferrals	**None**	**N/A**	**Approve (8-0)**
8	Short Term Rental Impact Fee	**None**	**N/A**	**Approve (7-0-1)**
9	Establish and Continue Departmental Revolving Funds	*See below*	**RF**	**Approve (8-0)**
10	Appropriate the FY2021 Community Preservation Committee Operating Budget and CPA Projects	**$5,400,225**	**CPA**	**10(a-c,e-o) Approve (8-0)** **10(d) IP**
11	Appropriate for Recreation Capital Projects	**$180,000**	**Recreation EF** **Retained Earnings**	**Approve (8-0)**
12	Appropriate for Municipal Capital Projects and Equipment	**$6,842,022**	*See below*	**Approve (8-0)**
13	Appropriate for Water System Improvements	$2,000,000 $200,000 **$2,200,000**	**EF Debt** **EF Rates**	**Approve (8-0)**
14	Appropriate for Wastewater System Improvements	$1,301,200 $100,000 **$1,401,200**	**EF Debt** **EF Rates**	**Approve (8-0)**
15	Appropriate for School Capital Projects and Equipment	**$1,299,246**	**Free Cash**	**Approve (8-0)**

Article	Title	Funds Requested	Funding Source	Committee Recommendation
16	Appropriate for Public Facilities Capital Projects	$1,736,285 $5,300,152 $208,962 **$7,245,399**	**Free Cash** **GF Debt** **Tax Levy**	**Approve (8-0)**
17	Appropriate to Post-Employment Insurance Liability Fund	$750,000	**Tax Levy**	**Approve (8-0)**
18	Rescind Prior Borrowing Authorizations	**None**	**N/A**	**IP**
19	Establish, Dissolve and Appropriate To and From Specified Stabilization Funds	*See below*	*See below*	**19(a,b) Approve (8-0)** **19(c) Approve (6-2)**
20	Appropriate From Debt Service Stabilization Fund	**$124,057**	**DSSF**	**Approve (8-0)**
21	Appropriate for Prior Years' Unpaid Bills	**None**	**N/A**	**IP**
22	Amend FY2020 Operating, Enterprise, and CPA Budgets	**$658,950**	**State CPA matching funds**	**Approve (8-0)**
23	Appropriate for Authorized Capital Improvements	**None**	**N/A**	**IP**
24	Reduce Legal Expenses (Citizen Petition)	*See below*	*See below*	**Disapprove (2-6)**
25	Purchase of Land/Eminent Domain	**$177,000**	**GF**	**Approve (8-0)**
34	Authorize Special Legislation—Development Surcharge for Community Housing (Citizen Petition)	**None**	**N/A**	**Pending**

Preface

This preface describes the structure and stylistic conventions used in this report. It is followed by an introduction discussing changes in the Town's financial status since the previous Annual Town Meeting, along with issues pertinent to the Town's general financial situation. The main body of this report contains article-by-article discussions and recommendations on those articles that, in our opinion, have substantial financial relevance. The report references several appendices at the end of this document that provide a deeper explanation of particular financial issues.

The discussion for each article presents the prevailing view of the Committee, as well as any other considerations or cautions that we feel Town Meeting should be informed of. If one or more Committee members are strongly opposed to the majority position, we summarize the opposing perspective. Each article discussion concludes with the most recent vote of the Committee prior to publication. The vote is summarized by the number of members in favor, followed by the number of members opposed, and lastly (when applicable) the number of members abstaining, e.g. "(6-2-1)" indicates six members in favor, two opposed, and one abstaining. It is not always possible to collect a complete vote for every article from nine voting members. In such instances, the total number of votes and abstentions published will be less than nine. For convenience, Committee votes are also summarized on the preceding pages.

This report does not replicate information readily available to Town Meeting members elsewhere. Key documents that inform our analysis and provide a more thorough picture of the Town finances are:

- The Town Manager's *Fiscal Year 2021 Recommended Budget & Financing Plan* (the "Brown Book"), dated February 21, 2020, fully describes the annual budget of the Town. The Brown Book also summarizes budget laws and bylaws (Appendix B) and includes a glossary of financial terms (Appendix D).
- *The Level Service and Recommended Budget of the Superintendent and School Committee* as voted February 4, 2020 (hereafter the "LPS Budget Book", which details the budget plan for the Lexington Public Schools.
- Capital Expenditures Committee (CEC) Report to the 2020 Annual Town Meeting, which provides recommendations on appropriation requests for capital projects.
- Community Preservation Committee (CPC) Report to the 2020 Annual Town Meeting, which details requests approved by the CPC and funded using revenue from the CPA surcharge.

The LPS Budget Book is available online at:
`https://sites.google.com/lexingtonma.org/lps-finance-and-operations/fy-21-budget`

All other reports for this Town Meeting will be available online at:
`https://www.lexingtonma.gov/town-meeting/pages/2020-annual-town-meeting`

Acknowledgements

The content of this report, except where otherwise noted, was researched, written and edited by Committee members who volunteer their time and expertise, and with the support of Town staff. We have the pleasure and the privilege of working with Town Manager James Malloy; Assistant Town Manager for Finance Carolyn Kosnoff (an *ex officio* member of our Committee); Budget Officer Jennifer Hewitt; the Capital Expenditures Committee; the Community Preservation Committee; the School Committee; the Permanent Building Committee; the Planning Board; Superintendent of Schools Dr. Julie Hackett; Assistant Superintendent for Finance and Operations David Coelho; and the Lexington Select Board. We thank the municipal and school staff, Town officials, boards and volunteers who have contributed time and expertise to help us prepare this report. Last but not least, we thank Sara Arnold, who records and prepares the minutes for our meetings.

Introduction

The Appropriation Committee is required to create a report with a review of the budget as adopted by the Board of Selectmen, including an assessment of the budget plan and a projection for future years' revenues and expenses. This report includes the Committee's analysis and recommendations regarding all appropriations of Town funds that are anticipated in the Town Warrant, and other municipal matters that may come before Town Meeting. This report is normally published and distributed to the members of Town Meeting as a printed document and as an electronic document via the Town website. *This year, printed copies will be limited due to the public health emergency.* The Committee also makes presentations during Town Meeting, including recommendations on appropriations and other matters for which the Committee's formal position was pending at the time of publication.

Committee Membership

There have been no changes to the Committee's membership since the 2019 Special Town Meeting #1. The Committee still has one vacant seat, for a total of 8 voting members.

Schedule of Budget and Report Publication

In prior years, the timing of the official budget approval process required Town Meeting to defer considering financial articles until the second week of meetings. Town staff have now accelerated the process, and this would have allowed financial articles to be considered as soon as the first night of meetings. The Committee's goal was to publish its report a week before the planned start of the 2020 Annual Town Meeting, but we did not meet this target date.

The initial release of this report was on March 25, 2020. This update was released on May 11, 2020, three weeks in advance of the first night of the 2020 Annual Town Meeting, which is now set for June 1, 2020.

Reserve Fund

As of publication, the Committee has not been asked to approve any Reserve Fund transfers during FY2020, and the balance in the Fund remains at $900,000. The appropriation to the Reserve Fund for FY2021 will be reduced to $750,000.

The Town Manager notified the Committee that a transfer from the Reserve Fund may be requested in FY2020 to cover unanticipated expenses for the Town's response to the COVID-19 outbreak.

Developments Since Adoption of the FY2020 Budget

A Special Town Meeting was held in November 2019. Under Article 3 of that meeting, appropriations were made into the Capital Stabilization Fund, the Traffic Mitigation Stabilization Fund, and the Transportation Demand Management Stabilization Fund. Under Article 4, minor adjustments were made to the FY2020 operating budget to accommodate half a year's salary and benefits for a Sustainability Director, and to the Water and Wastewater Enterprise Fund budgets due to changes in the MWRA assessments. Under Article 8, $1,500,000 was appropriated for a study of traffic in the Hartwell Ave. area to be funded by $1,250,000 in borrowing and $250,000 from the Traffic Mitigation Stabilization Fund. Under Article 9, funds were appropriated for the conversion of most streetlights to LED fixtures.

FY2021 Revenue and Budget

The main body of this report contains the Committee's analysis of all the appropriation requests that make up the next fiscal year's budget. Here we discuss some of the overarching trends in Town finance.

The Town Manager's report at the start of the Brown Book provides a comprehensive overview of the FY2021 estimated revenue and proposed budget, which are summarized in the following two tables.

Revenue Source	FY2020 Tax Recap	FY2021 Projected	$ Change	% Change	% of Total Revenue
Property Tax	$184,821,513	$192,311,761	$7,490,249	4.1%	80.9%
State Aid	$16,283,199	$16,517,703	$234,504	1.4%	7.0%
Total Local Receipts	$14,082,119	$14,280,713	$198,594	1.4%	6.0%
Available Funds	$14,314,142	$14,942,168	$628,026	4.4%	6.3%
Other Available Funds: Use of Capital Stabilization Fund	–	–	–	0.0%	–
Revenue Offsets	($1,860,652)	($2,181,086)	($320,434)	17.2%	(0.9%)
Enterprise Receipts	$1,696,348	$1,749,435	$53,087	3.1%	0.7%
Gross General Fund Revenues	$229,336,668	**$237,620,694**	**$8,284,025**	**3.6%**	**100.0%**
Less – Revenue Set-Aside for Designated Expenses	$12,495,310	$11,641,422	($853,888)	(6.8)%	4.9%
Net General Fund Revenues	$216,841,358	**$225,979,271**	**$9,137,913**	**4.2%**	**95.1%**

Gross revenue was initially projected to increase 3.6% in FY2021, which would be similar to last year, and suggested a declining trend away from the average of 5% growth we have seen in the recent past. State Aid was estimated to grow by only 1.4% this year, but that number is now uncertain.

When the Town's "new growth" tax revenue is certified in the fall, the revenue from property tax may be increased, resulting in higher gross revenue.

Budget Program	FY2020 Appropriated	FY2021 Recommended	$ Change	% Change
Education 1000	$116,023,888	$121,220,803	$5,196,915	4.5%
Shared Expenses 2000	$60,541,457	$62,727,317	$2,185,860	3.6%
Municipal Departments 3000-8000	$40,276,016	$41,582,360	$1,306,344	3.2%
Subtotal–Operating Budget	*$216,841,361*	***$225,530,480***	***$8,689,119***	***4.0%***
Cash Capital	$8,137,274	$7,743,515	($393,759)	(4.8%)
Other *(Approp. to reserves, misc.)*	$4,358,036	$1,388,151	($2,969,885)	(68.0%)
Total General Fund	$229,336,671	**$234,662,146**	**$5,325,475**	**2.3%**

It is far too soon to offer any detailed projections for the impact of COVID-19 on Town revenue for FY2021, but it is assumed that state and local revenues will fall below initial projections. Lower state revenue could lead to reduced state aid for all municipalities across the Commonwealth. Local revenue from sources such as hotel and restaurant excise tax, automobile excise tax, and building permits are expected to underperform, reducing the recurring revenues that sustains the Town's operating budget. At the same time, a subset of operating expenses will be reduced while some Town services are suspended, such as the Community Center and the Town pool. This will help offset some of the lost revenue.

The proposed budget has a significant surplus. It will provide the consistent and reliable level of service that is expected by residents during the coming fiscal year. The surplus results from recent changes that reduced appropriations to the PEIL Fund (OPEB) and the Capital Stabilization Fund (CSF). These changes could have a noticeable impact on future costs to the Town. We anticipate that Town Meeting will consider how to deploy these funds at a special town meeting later in the year, giving the Town some flexibility as we navigate through a period of uncertainty. These surplus funds could be used to cover revenue shortfalls or new expenses, or they could eventually be appropriated following the original budget intent.

Fiscal Policy Guidelines

The following description is taken from the Brown Book Overview, p. iii:

> *In May and October of 2019, the Select Board, School Committee, Appropriation Committee and Capital Expenditures Committee reviewed and reaffirmed the Town's fiscal guidelines. The FY2021 annual operating budget adheres to the following principles in order to preserve the Town's long-term financial condition:*
>
> 1. *Continue to set aside funds to transfer into the Capital Stabilization Fund as part of the comprehensive long-term strategy for funding future school and municipal projects.*
> 2. *Core services currently provided through the operating and capital budgets should be maintained, recognizing that changes in service demands may require that additional resources be provided in certain areas.*
> 3. *Recurring revenues, not reserves or one-time revenues, should support operating expenses.*
> 4. *Debt will not be used to fund current operating expenditures.*
> 5. *Adequate reserves and contingency funds will be budgeted, as appropriate, consistent with the original recommendations of the Ad Hoc Financial Policy Committee (2006) and reaffirmed in 2019.*
> 6. *Sufficient funds for building maintenance will be budgeted to properly maintain facilities and equipment as well as foster energy conservation.*
> 7. *Use of one-time revenues should be limited to funding one-time expenses (e.g., capital projects) or used to fund reserve accounts.*
> 8. *Continue to provide funding for the Other Post-Employment Benefits (OPEB) liability.*
> 9. *New targeted revenue sources should be considered to fund specific projects.*

These renewed and updated policies influenced the development of the FY2021 budget in several specific ways listed below:

- Continue the five-year program to phase out the use of Free Cash for the operating budget,
- Continue the recently doubled budget for ongoing annual water system improvements (based on a 100-year replacement cycle),
- Commence a multi-year program to phase out the use of debt for ongoing annual improvements in both the Water and Wastewater Enterprise budgets,
- Prioritize and narrow the list of capital projects in the master plan within a five-year window,
- Favor the use of cash capital rather than debt when feasible.

As the Town transitions away from using Free Cash in the operating budget, there will be a period of adjustment. In addition, water and wastewater rates will reflect the cost of additional maintenance work and the shift away from debt funding.

5-Year Forecast

This year the report brings a new approach to the 5-year budget projection in Appendix A. For the past several years, the Town Finance Department has prepared a detailed 5-year forecast, and the Committee no longer sees a need to develop a forecast independently. This year Appendix A summarizes the Finance Department's projections and discusses the implications for future Town budgets. We appreciate the challenge of producing a projection that provides useful insights five years in the future, and we look forward to working with the Finance Department on refinements to these projections.

Short-Term Outlook

We note that growth of the Education budget (a combination of Lexington Public Schools and Minuteman Regional High School) has outpaced growth in gross revenue. This is cause for concern given the relative size of Education in the operating budget. This created pressure on the FY2021 budget, resulting in a more limited set of program improvements for LPS, and a reduction to reserves and revenue set-asides in order to balance the budget. These decisions will reduce the Town's free cash balance in the subsequent year and increase pressure on future budgets.

The overwhelming concern for the Town, and the nation, at this time is the COVID-19 pandemic, and we stand at a point of great uncertainty. We could be facing a prolonged recession, which would reduce revenues from several sources. Although it seems less likely, the impact could be short-lived with more modest reductions in revenue, but the outlook in the short term is generally poor.

Property tax revenue from commercial and industrial owners is far more volatile than residential property tax revenue. A global economic recession would hurt local businesses, impacting global, regional, and local revenue. Lower employment at the local level would lead to lower retail activity and fewer new business opportunities. In recent years, a steady 20% of the Town's property tax revenue has come from commercial, industrial and personal (CIP) property taxes. A drop in CIP tax revenue would put pressure on residential tax rates, but this would likely come with a lower rate of inflation that would dampen the need for operating overrides.

A significant decline in state income tax revenue would lead to cuts in almost every form of state aid, with few alternatives to make up the loss other than our stabilization fund.

We note that in past economic downturns, the direct impact on Town finances has been delayed by a year. Despite the immediate impact to our residents and businesses, much of the current year's revenue is "baked in", and the impact of recent economic trends will take another year to show up in the Town's balance sheet. Now is the time to prepare for challenging conditions.

Updates

Update 1: This report was updated on May 11, 2020 in response to changes in the proposed FY2021 budget reflected in revised motions for Article 17 and Article 19, and a significant change in the MWRA assessments (see Article 5). Change bars in the margins indicate areas of this report that have been revised since the first version.

This report presents the official positions of the Committee as of the date of publication. The Committee will continue to meet as necessary prior to and during Town Meeting and it may revise its official positions based on new or updated information. In a typical year, the Committee also reports orally to Town Meeting on each article. The oral report summarizes the Committee's current position, which may have been updated following publication of this report.

This year may require changes in our usual practice, but we will endeavor to satisfy our responsibility to provide financial advice to Town Meeting.

Warrant Article Analysis and Recommendations

Article 4
Appropriate FY2021 Operating Budget

Funds Requested	Funding Source	Committee Recommendation
See below	*See below*	**Approve (8-0)**

The discussion of the operating budget is divided into three sections for the major components of the budget: Education, Shared Expenses, and Municipal.

Education (1000)

Program 1000 Education	**FY2020 Budget**	**FY2021 Recommended**	**% of Education**	**$ Change**	**% Change**
1100 Lexington Public Schools	$113,553,757	$118,357,656	97.64%	$4,803,899	4.2%
1200 Regional High School	$2,470,131	$2,863,147	2.36%	$393,016	15.9%
1000 Total Education	$116,023,888	**$121,220,803**	**100%**	**$5,196,915**	**4.5%**

Lexington Public Schools (1100)

The School Committee has voted to recommend an appropriation of $118,357,656 for the Lexington Public Schools (LPS) operating budget for FY2021. This amount does not include:

- The school portion of Shared Expenses (2000), see below, including public facilities, employee & retiree benefits, pension, debt service, liability insurance, and reserve funds.
- Revenue from federal, state, local, and private grants, or revolving and donation fund activity, none of which are subject to appropriation by Town Meeting.

The request represents an increase of 4.2% over the FY2020 appropriation.

The new Lexington Children's Place (LCP; preschool) building opened in September 2019, and the new Maria Hastings Elementary School was occupied in February 2020. These moves had minor effects on the FY2020 operating budget, i.e., the addition of two custodial positions, that carry forward into this budget.

Further information about the budget request may be found in the "Education" section of the Brown Book and in the LPS Budget Book.

A breakdown of this operating budget into salaries and wages, and expenses is shown below.

Appropriation	**FY2020 Budget (adjusted)**	**FY2021 Recommended**	**Dollar Increase**	**Percent Increase**
Salary and Wages	$95,442,183	**$98,932,332**	$3,490,149	3.7%
Expenses	$18,111,574	**$19,425,324**	$1,313,750	7.3%
1100 Lexington Public Schools	$113,553,757	**$118,357,656**	$4,803,899	4.2%

Source: Lexington Public Schools FY2021 Recommended Budget, January 7, 2020

Salaries and Wages

Salary and wage changes result from changes in the number of employees, step increases, cost of living adjustments (COLA), and position reclassifications. The budget takes both anticipated bargaining unit settlements and increases for non-union positions into account. The effective dates of the most recent collective bargaining agreements may be found in the LPS Budget Book on page "Budget Overview – 10".

Salaries and wages make up 84% of the FY2021 request. The increase over FY2020 comprises both salary increases for existing staff and the net addition to the staff of 3.2 full-time equivalent (FTE) employees (including unallocated positions). This net increase is the sum of a decrease of 9.32 FTEs from currently authorized positions ("base changes") mostly resulting from an analysis of how special education services are delivered, and increases of 5.70 FTEs to satisfy legal mandates, 3.57 FTEs driven by enrollment increases, and 3.25 FTEs to effect program improvements.

See the Brown Book or the LPS Budget Book for a detailed list of the positions that will be consolidated, eliminated, or created. The cost of the benefits associated with the new positions, $49,739, is included under Shared Expenses.

Expenses

Expenses make up 16% of the FY2021 request. The increase in out-of-district tuition of $909,522 is the largest for any single line in the detailed expense budget (see the "Expenses" section of the LPS Budget Book). There are also sizable increases for transportation costs for regular education students ($271,210) and special education students ($230,262). The budget for LPS legal expenses has been reduced by about $84,000 based on lower utilization during the two most recent school years. There are also modest reductions because one-time expenditures from the FY2020 budget for the move into the new Hastings School and the strategic planning initiative are not part of the FY2021 budget.

School Enrollments

The student population that the district serves includes the following categories:

- PreK in-district including special education and tuition-paying general education students;
- K-12 in-district general education and special education (including METCO);
- PreK-22 out-of-district placement.

This table shows student enrollments for the past three years and the enrollment projected for the fall of 2020. Decreases in enrollment at the elementary level from October 1, 2017, to October 1, 2018, and further to October 1, 2019, are the first declines in over ten years. Our experience has been that enrollment figures are somewhat volatile, and trends are difficult to spot, so a generous level of flexibility is warranted. The budget includes 7.5 unallocated FTEs to cover potential increases in regular education or special education staff in case the enrollment increases go beyond the projections listed in the table below (but not beyond estimated 90% confidence upper limits on the enrollment increases). If the increases do not materialize, the positions will not be filled and the corresponding amounts will not be spent, unless other unexpected critical needs for the funds arise within the school system.

	Oct. 1, 2017 Enrollment	**Oct. 1, 2018 Enrollment**	**Oct. 1, 2019 Enrollment**	**Projected FY2021 Enrollment**
Early Childhood	73	69	68	74
Elementary	3,150	3,094	3,019	3,011
Middle School	1,813	1,833	1,828	1,874
High School	2,212	2,263	2,275	2,295
Total	**7,248**	**7,259**	**7,190**	**7,254**

The FY2020 LPS METCO program includes a total of 223 students. The METCO enrollment has been as high as 240 students. The target FY2021 enrollment is approximately 230 students.

In the current school year (FY2020), a total of 1,072 students are on IEPs. Of these, 950 are in-district and 122 students are out-of-district placements. The overall proportion of K-12 students on IEPs is roughly 15%, which is similar to the ratio in comparable communities.

Special Education Costs Including Out-of-District Tuitions

For at least the past five years, special education costs have tended to rise at a higher rate than other parts of the LPS operating budget. SPED expenses amounted to 32.67% of the actual expenditures in FY2019, are 33.77% of the budget for FY2020, and represent 33.37% of the request for FY2021.

The FY2021 request for out-of-district tuition, $8,229,139 represents a 12.4% increase over the corresponding FY2020 amount. The requested amount will be supplemented by three non-appropriated sources of funds (pre-paid tuitions/LABBB credit, IDEA grant, and state Circuit Breaker reimbursements).

Funding Sources Not Subject to Appropriation

The annual appropriation from the Town supports the majority of the school budget. However, the complete school budget includes additional funds from state, federal and other sources that are not subject to appropriation by Town Meeting and are therefore not included in this request. The amounts of these funds vary year to year. Brief discussions of some of these funds follow:

- **Federal Grants** – For FY2021, the School Department projects that it will receive $2,188,702 in federal grants, unchanged from the FY2020 budget projection.
- **State Grants** – As noted above, the School Department projects that it will receive $1,609,326 in FY2021 from the state METCO program. Based on an enrollment of 230 students, the projected state aid averages to $6,997 per METCO student. Cherry-sheet local aid for education is treated as General Fund revenue and is not included in state grants.
- **"Circuit Breaker" Reimbursements** – Reimbursements are received from the state when the costs of special education services for an individual student, whether in-district or out-of-district, exceed a multiple of four times the statewide foundation budget. In the past, reimbursement rates have varied between 35% and 75% of the tuition cost. Circuit breaker reimbursement funds are paid to the district quarterly based on the prior year's approved claims. Funds received go into the Circuit Breaker Revolving Account, do not require further appropriation, and must be expended by June 30 of the following fiscal year. The Lexington Public Schools current practice is to apply the funds received in a given fiscal year (based on SPED expenses in the prior fiscal year) as a revenue offset in the following fiscal year. For example, LPS will receive (or has received) a reimbursement in FY2020 based on FY2019 SPED expenses and will use that reimbursement to offset SPED costs in FY2021.

  The District projects that $4,070,391 received in FY2020 will be available for expenditure in FY2021. With a projected reimbursement rate of 70%, the Circuit Breaker reimbursement in FY2021 is projected to be $3,991,255.

Fee Programs

Fees for participants in certain programs, such as preschool, athletics, and transportation, support those programs in whole or in part. Detailed information about the fees and proposed fee changes may be found in the "Revenue Offsets" section of the LPS Budget Book.

Regional High School (1200)

Lexington's FY2021 projected assessment for the Minuteman Regional High School (MRHS) of $2,863,147 represents an increase of $393,016, or 15.9%, over FY2020. It follows on the prior year's increase of 16.2% and an increase of 27.3% from FY2018 to FY2019. The current increase primarily reflects three factors: (1) Lexington's enrollment growing from 52 to 62 students, (2) Belmont withdrawing from the district causing an increase in Lexington's assessment of $251,653 (64% of the total increase) and (3) sharply increased debt service costs for the recent completed new school building, of which Lexington's share is $645,643.

The District's Budget

The Minuteman Regional High School (MRHS) Committee has approved a FY2021 budget of $25,502,946, a $2,734,117 increase (+12%) over FY2020. The increase is the net effect of a 6.56% increase in the cost of operations and a $1,477,552 increase in debt costs attributable to construction of the new MRHS building.

This budget funds the second year of operations in the new school building, designed for an enrollment of up to 628 students. Current high school enrollment is 602 students, of which 395 students come from the 10 member towns of the school district, and 207 students from out-of-district communities.

District Developments

The new school building was opened on schedule in September 2019 and was completed within budget. The cost of this project was offset by almost $44 million from the Massachusetts School Building Authority (MSBA). The remaining balance was financed with bonded debt. The debt service is funded via the assessments to district members, and by a new state-authorized facilities fee for capital costs charged to non-member towns that enroll students at the school. This fee is set by the Department of Elementary and Secondary Education (DESE) and towns are classified by whether they offer at least 5 Chapter 74 (vocational-technical) programs. In FY2020 $904,023 was collected and will be applied to the FY2021 budget. The per-student charge in FY2021 for towns lacking access to vocational-technical education will be $7,775 and $5,831 for towns that have programs.

The district currently has ten member towns. Following a negative vote by the residents of the Town of Belmont in a special district-wide referendum election held in 2016 to approve the construction of the new MRHS facility, and with the consent of the remaining member towns, Belmont is scheduled to withdraw from the district effective July 1, 2020. The net result of Belmont's withdrawal is the loss of $1,508,256 of assessment revenue from the FY2021 budget, and this increases Lexington's FY2021 assessment by over $250,000.

While it was anticipated that the new school building would drive increased applications, the success has exceeded expectations. Applications for FY2021 from in-district towns are up 33%, with 230 applications received by January 30, 2020. In-district students are given priority, and for the first time in decades it is likely that the incoming freshman class will be 100% in-district. If this enrollment trend continues, by FY2024 the school enrollment could consist primarily of in-district students.

Enrollment	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20*	FY21†
In-district	445	430	409	437	410	391	347	337	354	395	482
Out-of-district	309	255	340	356	332	277	271	231	162	207	156
Total	754	685	749	793	742	668	618	568	516	602	638

** New school occupied.* *† Based on applications received.*

MRHS continues to have by far the highest average per-pupil costs of any regional vocational district. According to FY2018 state data, while still in the old building and with an enrollment of only 564 students, the per-student average cost was $35,111, compared to a statewide median of $21,996. The second-highest district, South Middlesex Regional Vocational Technical, had a per-pupil average cost of $26,846. MRHS has a significantly lower student-teacher ratio when compared to similar districts, due in part to its 46.5% enrollment in special education. This is the highest level of any public school in the state (the average is 18%). This level is similar for students coming from both in-district and out-of-district communities.

Towns sending out-of-district students are responsible for providing transportation to their students and are subject to additional fees beyond the base tuition. These towns are assessed a "capital fee" which represents a share of the debt service for new building. This capital fee revenue is applied to the following year's debt service, reducing assessments for member towns. For out-of-district students that receive SPED services, their sending towns are assessed for supplemental SPED tuition. The district will be recommending an increase in the out-of-district per-student SPED tuition from $6,200 to $7,400, in order to cover actual costs.

Despite these fees, out-of-district students are effectively subsidized by member towns. DESE set the base out-of-district tuition rate at $17,965 per student in FY2019 (expected to increase 2.5% to $18,414 for FY2020). This does not cover the full cost of district education, nor is the state Chapter 70 aid for out-of-district students sent to MRHS. If the school was fully enrolled with only in-district students, our calculations suggest that per-student assessment costs would fall by up to 30%, bringing them in line with the state average.

District Budget Overview

This is the first budget built since occupying the new school and is a transitional step towards an accurate base budget. It addresses the needs of increased enrollment and maintenance of the new building, grounds, and equipment.

With the anticipated enrollment for the FY2021 freshman class the school will be above its 628-student capacity. This follows an even larger enrollment increase from FY2019 to FY2020. As of October 1, 2019, 602 full-time students (high school and post-graduate) were enrolled. Roughly 66% of high school students were from the ten in-district towns. Total full-time enrollment increased from October 2018, by 86 students, with in-district enrollment increasing 41 students and out-of-district enrollment increasing 45 students.

Staffing changes include a net increase in academic, vocational, administrative, and support staff of 2.5 FTEs. This enrollment-driven increase follows a cumulative reduction in staff of 19.5 FTE since FY2015, after enrollment peaked in FY2014. Salaries for FY2021, which make up 60% of the operating budget, will increase by a total of $583,000 after factoring in contractual obligations. Funding for technology, allowing each student to have a computer, will increase by $108,583.

The total health insurance budget is increasing by $317,548 (8%) based on insurance experience and increased staffing. Debt service payments for FY2021 rise to $5,092,385 (+41%) as debt service for the new building ramps up. A $60,000 (+20%) payment will be made toward the funding of the District's $22,945,000 Other Post-Employment Benefits (OPEB) unfunded liability. The OPEB liability will be recalculated in June 2020.

Roughly 32% of the revenue in the MRHS FY2021 budget comes from a combination of state aid, reserves, and fees shown in the table below. In total, this non-assessment revenue increased by $1,253,604 in FY2021, due in large part to the new out-of-district capital fee. Chapter 70 funds and transportation aid are estimates based on the Governor's H-2 budget, which proposes modest increases in Chapter 70 aid and transportation aid statewide compared with FY2020. MRHS's share of Chapter 70 aid increases slightly and Transportation Aid increases 17.39%. Both are based on October 2019 enrollments.

Non-Assessment Revenue Sources	FY2020	FY2021	Change $
Chapter 70	$2,092,403	$2,095,633	$3,230
Transportation Aid	$832,392	$977,179	$144,787
Prior Year Tuition	$3,047,131	$3,048,695	$1,564
Current Year Tuition	$400,000	$600,000	$200,000
Excess and Deficiency (E&D) Funds	$540,000	$540,000	–
Out-of-district Capital Fee		$904,023	$904,023
Total	**$6,911,926**	**$8,165,530**	**$1,253,604**

Lexington's Assessment

The remainder of the revenue is raised through assessments on member towns and tuition for out-of-district students. Member towns are assessed a share of the District's total costs for the upcoming year, net of the District's non-assessment revenue, based on four factors:

1. The State-Required Minimum (SRM) per-student tuition cost set annually by the DESE,
2. An additional charge for operating costs in excess of the SRM that is allocated based on the four-year average student enrollment,
3. Transportation costs,
4. Debt service costs from capital projects.

One percent of the debt service cost is assessed equally to all member towns and the remainder is apportioned based on the most recent four-year rolling average of student enrollment and a "combined effort" factor as determined by the Chapter 70 formula.

A breakdown of the Town's FY2020 and FY2021 MRHS assessments is shown below. The projected assessment for FY2021 is $2,863,147, an increase of $393,016 (15.9%) over the final FY2020 assessment.

Projected Lexington Assessment – Based on Unapproved House-2 Budget Bill

	Enrollment Basis		Assessment Components		Per-Student
	FY2020	**FY2021**	**FY2020**	**FY2021**	**FY2021**
State-Required Minimum	53	65	$799,005	$1,057,954	$16,276
Regular Day Students*	52.25	55.13	$962,102	$1,011,769	$18,352
Transportation	53	65	$86,714	$83,516	$1,285
Total Operating Costs*			*$1,847,821*	***$2,153,239***	
Capital*	49.63	55.13	$618, 510	$709, 908	$12,877
Post-Graduate Programs	1	0	$3,800	–	–
TOTAL ASSESSMENT			$2,470,131	**$2,863,147**	
Annual % increase (decrease)			*16.2%*	*15.9%*	

* *Starred rows in this table use average enrollment over the prior 4 years, while non-starred rows use current enrollment. The respective per-student amounts cannot be combined arithmetically.*

The FY2021 operating cost per student works out to $33,126 (assuming 65 regular day students). Due to the assessment formula, the per-student amount lags behind short-term enrollment trends. A rising enrollment (as we expect this year) will tend to lower per-student costs (and vice versa) until the 4-year average stabilizes. Enrollment in other member towns can also affect this figure, particularly if it leads to higher out-of-district enrollment.

We anticipate further changes to the projected revenues and budgeted expenses in the MRHS budget following publication of this report. It is likely that the assessment will be adjusted prior to being presented to Town Meeting.

Shared Expenses (2000)

The Shared Expenses section of the budget covers appropriations for various activities that are managed centrally rather than by the Lexington Public Schools (LPS) or individual municipal departments. Although these expenditures do not appear in the budgets of LPS or individual departments, they are driven primarily by decisions by LPS and those departments.

As shown in the table below, over 60% of shared expenses fund employee benefits, which are administered by municipal staff, but which are driven by current and past staffing decisions made by LPS and the municipal departments. The second largest line item (19.0%) is to support facilities used by LPS and municipal activities that are managed by the Public Facilities Department. The third largest line item (16.8%) is for debt service, which is administered by the Finance Department. Debt service is driven by current and past capital expenditures and financing decisions.

Program 2000 Shared Expenses	**FY2020 Restated**	**FY2021 Budget**	**% of Shared Expenses**	**Change $**	**Change %**
2100 Employee Benefits & Insurance	$36,512,823	$37,964,483	60.5%	$1,451,660	4.0%
2200 Property & Liability Insurance	$1,132,304	$1,095,000	1.7%	($37,304)	(3.3%)
2310 Solar Producer Payments	$410,000	$410,000	0.7%	$0	0.0%
2400 Within-Levy Debt Service	$9,853,984	$10,517,445	16.8%	$663,461	6.7%
2510 Reserve Fund	$900,000	$750,000	1.2%	($150,000)	(16.7%)
2600 Facilities	$11,732,346	$11,990,390	19.0%	$258,044	2.2%
TOTAL	**$60,541,457**	**$62,727,317**	100.0%	$2,185,860	3.6%

The recommended total Shared Expenses budget for FY2020 is $62,727,317, which represents an increase of $2,185,860 or 3.6% over the restated amount for FY2020.

Employee Benefits & Insurance (2100)

As shown in the table below, Line 2100 includes costs for retirement; health, dental, and life insurance; workers' compensation, unemployment insurance, and the Medicare tax. The total request for Employee Benefits and Insurance is $37,964,483, which represents a $1,451,660 or a 4.0% increase over the FY2020 appropriation.

The table below provides a breakdown of the benefits budget by category. Retirement accounts for almost 18% of the total, with virtually all of it going into the contributory retirement (pension) fund. The Town is following a schedule of payments based on the 2018 actuarial study projected to eliminate unfunded pension liabilities by 2024. Once that goal is reached, and assuming the Town can maintain its fully funded pension status, the annual cost for contributory retirement will be significantly lowered by reducing or eliminating payments toward any unfunded pension liability (but see also the Post-Employment Insurance Liability Fund in Article 17).

Benefits Category	**Amount**	**Percentage**
Health Insurance	$27,026,973	71.4%
Dental insurance	$1,139,837	3.0%
Life insurance	$25,000	0.1%
Retirement	$6,701,444	17.7%
Medicare	$1,996,229	5.3%
Unemployment	$200,000	0.5%
Workers' Compensation	$875,000	2.3%
TOTAL	**$37,964,483**	**100.0%**

Health insurance cost is by far the single largest item in the Employee Benefits budget, accounting for 71% of the total. The FY2021 request for health insurance is $27,026,973, which represents a 4.1% increase over the estimate for FY2020. The Town remains a member of the State's Group Insurance Commission (GIC) health insurance program, which has helped hold down the rate of increase, but health care costs (nationally as well as for the Town) continue to outpace general inflation. As it has been since FY2016, the FY2021 split of healthcare premiums between employer and subscribers is 82/18 or 75/25 depending on the health plan chosen by the employee (the town pays a larger share for employees who choose a lower cost plan). The Brown Book, p. IV-6, contains a discussion of health-benefit costs, including changes in the numbers of subscribers since FY2016. The projected number of subscribers used for the FY 2021 budget represents an increase by 0.5% compared to FY2020 and 10.4% compared to FY2016.

Solar Producer Payments (2300)

This line item reflects payments for the installation and operating costs of the solar array at the Hartwell Ave compost facility. Against the annual cost of $410,000, which covers both the initial capital cost and maintenance costs, staff estimates that the array will generate $600,000 in payments from Eversource (the electric utility serving the Town), so the array is projected to generate a net contribution to the General Fund of $190,000. The recommended FY2021 budget is the same as the FY2020 budget. For FY2022, staff will review three full years of results to reassess funding levels.

Note this budget item does not include the Town's rooftop solar arrays and payments in lieu of taxes for the solar operations, which are recorded under personal property taxes per the Massachusetts Department of Revenue. The Brown Book includes a table on p. IV-13 showing more complete estimates for the Town's solar installations, with projected net revenues of over $400,000 in FY2021.

Debt Service (2400)

The Debt Service amount covers annual payments for within-levy debt service. Gross within-levy debt service is projected to rise 6.7% as indicated in the above table. When the set aside for land purchases and certain cemetery revenues are removed from the gross debt service totals, the net amount is projected to rise by 4.4%, which is below the Town's target ceiling of 5.0%, so there is no recommendation to use the Capital Stabilization Fund as a funding source here.

The Town also makes annual payments for exempt debt service, but the funds for these payments do not need to be appropriated by Town Meeting. Every project funded with exempt debt must be approved by a majority of voters in a town-wide referendum, after which the Select Board sets the tax levy to provide sufficient funding. The portion of the tax levy raised for exempt debt service is *exempt* from the limits imposed by Proposition 2½. See p. IV-11 in the Brown Book for a detailed schedule of exempt debt.

Staff estimates that the combined debt service for exempt and non-exempt debt will rise only 1.7% in FY2021. For more details on debt service, see the Debt Service section in the Brown Book.

Reserve Fund (2500)

The Reserve Fund provides a critical source of funding for extraordinary and unforeseen expenses during the fiscal year that can be tapped without the need for appropriation by Town Meeting. Requests for transfers from this fund are generally initiated by the Select Board and/or Town staff and require formal approval by the Appropriation Committee. The FY2021 requested appropriation for the Reserve Fund is $750,000, a reduction from the $900,000 that was appropriated from FY2014 to FY2020. During those years the fund has seen limited use. In FY2018, $106,000 was transferred from the fund, and in FY2019 the fund remained unused. At the end of the fiscal year any unused amount flows to Free Cash.

Facilities (2600)

The Department of Public Facilities manages the operation, maintenance, and custodial service of Lexington's municipal and school buildings. This Department also supports the School Master Planning process; manages recurring maintenance of roofs, building envelopes, and HVAC systems; and implements other priority projects. The FY2021 projected total Public Facilities operating budget is $11,900,390 which represents a 1.4% increase over FY2020.

Municipal (3000-8000)

The municipal operating budget comprises all line items from 3000 to 8999. As shown in the table below, the FY2021 Recommended Budget of $41.6 million represents a $1.3 million or 3.24% increase. The largest components of the municipal budget are those for Public Safety, the DPW, and General Government.

Municipal Budgets	FY2020 Appropriated	FY2021 Budget	Change $	Change %
3000 Public Works	$10,482,790	$10,805,637	$322,847	3.08%
4000 Public Safety	$14,623,802	$15,536,792	$912,990	6.24%
5000 Culture & Recreation	$2,848,949	$2,959,426	$110,477	3.88%
6000 Human Services	$1,458,936	$1,486,822	$27,886	1.91%
7000 Land Use, Health & Development	$2,579,144	$2,624,761	$45,617	1.77%
8000 General Government	$8,282,395	$8,168,922 $	($113,473)	(1.37%)
TOTAL	$40,276,016	**$41,582,360**	**$1,306,344**	**3.24%**

Public Works (3000)

The recommended appropriation for Public Works of $10,805,637 represents a 3.08% increase over FY2020. Of the total, 91.3% is covered by the tax levy, 5.8% is covered by payments from the enterprise funds for services rendered, and 2.9% comes from other sources, primarily fees and the Cemetery Trust Fund. About 40% of the recommended budget is for compensation, i.e., salaries and wages, while the remaining 60% is for Expenses.

The net increase in compensation of $91,765 (2.16%) from FY2020, includes the conversion of a Staff Engineer to a Senior Engineer (annual cost of $9,426 plus an additional $137 in Shared Expenses). An additional point to note is that the contract for AFSCME Local 1703 Public Works is currently being negotiated and the estimated cost of the additional compensation under a new contract is budgeted in the Salary Adjustment account.

The net increase in expenses of $231,082 (3.70%) from FY2020 is largely for contractual services and supplies. Two Program Improvement Requests totaling $22,000 are recommended. The first is a real time monitoring system contract for $12,000 that will monitor pavement conditions during a snowstorm and enable better utilization of resources. The second is an appropriation of $10,000 towards regular maintenance of the Town's playgrounds.

Some noteworthy points in the budget are:

- The initial savings from conversion of the Town's streetlights to LEDs that was funded at the fall 2019 STM is rather conservatively estimated at $28,550. If no serious maintenance problems develop and projected reductions in electricity use are realized, further savings are likely. Future budgets will reflect the experience of the first year after the conversion project has been completed.
- There is a net increase of $98,123 for refuse collection, disposal, and recycling which is due to the unsettled recycling market.

Public Safety (4000)

Public Safety covers Law Enforcement (4100) and Fire and Rescue (4200). Of the total recommended appropriation of $15,536,792, about 52% is for Law Enforcement and 48% for Fire and Rescue.

The recommended FY2021 appropriation for Law Enforcement is $8,038,558 which is a 6.23% increase over the FY2020 budget. About 88% of the budget is for compensation and approximately 12% is for expenses. The net increase in compensation of $421,087 (6.32%) is driven by contractual cost of living adjustments and absorbing a seventeenth crossing guard into the operating budget. A Lead Dispatcher position has been created without impact to the compensation budget by using a State 911 grant. However, the additional benefit costs of $15,836 for this position are reflected in Shared Expenses. An increase in the regional gasoline contract, the replacement of portable radios, and professional development of the dispatch staff are included in the budget for expenses which has increased by $50,441 (5.55%).

The recommended FY2021 appropriation for Fire and Rescue is $7,498,234, which is a 6.26% increase over the FY2020 budget. About 91% of the budget is for compensation while approximately 9% is for expenses. The net increase in compensation of $399,137 (6.24%) is driven by contractual cost of living adjustments. The budget for expenses has increased by $42,325 (6.46%) primarily due to the addition of a command vehicle and the projected increase in diesel costs.

Culture and Recreation (5000)

Culture and Recreation covers Cary Memorial Library and Recreation and Community Programs. The recommended appropriation of $2,959,426 represents a 3.88% increase over the FY2020 budget. Note that the budget to be appropriated under this article is only for the Cary Memorial Library. The Recreation and Community Programs budget is funded under Article 5 by the Recreation Enterprise Fund and, to a lesser extent, by the tax levy. About 80% of the recommended budget is for compensation while the remaining 20% is for expenses.

The net increase in compensation of $34,865 (1.49%) is driven by contractual cost of living adjustments and by increasing working hours for one library technician in Adult Services from 25 hours/week to 37 hours/week. Note that the contract with the Cary Memorial Library Staff Association expires in June 2020 and prospective increases are budgeted in the Salary Adjustment account.

The net increase in expenses of $75,612 (14.79%) is primarily driven by increases for supplies and materials and contractual services. This includes a $46,000 Program Improvement Request to fully fund a gap in the materials budget which is required to retain certification by the Massachusetts Board of Library Commissioners.

Human Services (6000)

The recommended appropriation for Human Services of $1,486,822 represents a 1.91% increase over the FY2020 budget. About 44% of the recommended budget is for compensation while the remaining 56% is for Expenses.

The net decrease in compensation of $20,579 (-3.02%) is driven by contractual cost of living adjustments, a Program Improvement Request to increase the Transportation Manager position from 0.8 to 1.0 FTE, which are more than offset by Bedford and Carlisle absorbing a higher percentage of the Veterans District Director salary.

The net increase in expenses of $48,465 (6.23%) includes a $50,000 Program Improvement Request for a number of transportation pilot programs partly offset by reductions due to declining veterans' services caseload. Funding for the William James Interface Mental Health Referral Service for FY2021 will be shared between the municipal and school budgets.

In addition to the General Fund appropriation requested here, Human Services will also be funded by $197,498 from revolving funds (Article 9) and grants.

Land Use, Health, & Development (7000)

Land Use, Health, & Development covers six different budgeting units. The recommended appropriation of $2,624,761 represents a 1.77% increase over the FY2020 budget. About 80% of the recommended budget is for compensation while the remaining 20% is for expenses.

The net increase in compensation of $103,077 (5.13%) is driven by contractual cost of living adjustments, staff turnover, reduction in consultant usage, and the addition of a second Health Agent to conduct inspections.

The net decrease in expenses of $57,460 (-10.11%) reflects the termination of the Bike Share program and temporary Visitor Center operations.

In addition to the General Fund appropriation requested here, Land Use, Health, & Development will also be funded by $490,899 of revolving funds (Article 9).

General Government (8000)

General Government covers six different budgeting units. The recommended appropriation of $8,168,922 represents a 1.37% *decrease* from the FY2020 restated budget.

Program 8000 General Government	FY2020 Restated	FY2021 Budget	Change $	Change %
8100 Select Board	$1,274,896	$1,294,876	$19,980	1.57%
8200 Town Manager	$1,934,800	$1,524,432	($410,368)	(21.21%)
8300 Town Committees	$62,411	$64,100	$1,689	2.7%
8400 Finance	$1,844,028	$1,902,345	$58,317	3.16%
8500 Town Clerk	$514,620	$590,452	$75,832	14.74%
8600 Information Technology	$2,651,640	$2,792,717	$141,077	5.32%
TOTAL	$8,282,395	**$8,168,922**	**($113,473)**	**(1.37%)**

Of the total net decrease of $ 113,473, the primary driver is a substantial reduction in the Salary Adjustment account under the Town Manager's budget (8200) which reflects the finalization of several collective bargaining agreements in the past year. A part-time Municipal Assistant to support the Human Resources department as well as a full year of salary for the Sustainability Director are included here. The Town Clerk budget (8500) has been increased due to the upcoming elections. Two thirds of the total increase in the IT budget (8600) of $141,077, is driven by increases in support contracts and the professional development/training budget. The remaining one-third is driven by contractual cost of living adjustments.

The Committee recommends approval by a vote of (8-0).

Article 5
Appropriate FY2021 Enterprise Funds Budgets

Funds Requested	Funding Source	Committee Recommendation
$10,616,030	**Water EF**	
$10,447,390	**Wastewater EF**	**Approve (8-0)**
$3,015,408	**Recreation EF**	

This article addresses the appropriation of funds for the operation of the Town's three enterprise funds: the Water Enterprise Fund, the Wastewater Enterprise Fund, and the Recreation and Community Programs Enterprise Fund. For an overview of the legal framework and accounting concepts that apply to the operation of an enterprise fund, please refer to Appendix B.

The appropriations addressed in this article cover the complete operating costs of the respective enterprises with two exceptions. Indirect costs paid over to the general fund are appropriated under Article 4.

Contributions to the Post-Employment Insurance Liability (PEIL) Fund by the water and sewer funds (but not by the recreation fund) for retirement health benefits are appropriated under Article 17. All appropriations under this article are funded by enterprise rates or fees with one exception: In the case of the recreation fund, $218,916 of the enterprise's total appropriation is made from the tax levy, in accordance with a policy established when the Community Center was completed in 2015, to support Community Center operations that are generally available to all residents and are not fee-supported.

The following discussion focuses on the anticipated operating expenses and revenues of the enterprise funds for FY2021 and issues they raise. Capital appropriations are addressed in Articles 11 (Recreation Capital), 12 (Municipal Capital), 13 (Water System Improvements) and 14 (Wastewater System Improvements).

Water and Wastewater Enterprise Funds

A breakdown of the funding request for the Water and Wastewater Enterprise Funds, and the percentage changes from the prior fiscal year, are shown in the following tables. *See* Brown Book, pp. V-27, V-31.

Water Enterprise Fund	FY2020 Appropriated	FY2021 Requested	$ Change	% Change
Compensation	$785,010	$804,234	$19,224	2.45%
Expenses	$508,875	$502,925	($5,950)	(1.17%)
Debt Service	$1,277,412	$1,278,770	$1,358	0.11%
MWRA Assessment	$7,413,364	$8,030,101	$616,737	8.32%
Total Requested in Article 5	**$9,984,661**	**$10,616,030**	**$831,369**	**8.33%**
Indirect Expenses (Article 4)	$894,573	$930,001	$35,428	3.96%
Cash Capital (Article 13)	–	$200,000	$200,000	–
OPEB Contribution (Article 17)	$2,761	$2,761	–	–
Total Water Enterprise	**$10,881,995**	**$11,748,792**	**$866,797**	**7.97%**

Wastewater Enterprise Fund	FY2020 Appropriated	FY2021 Requested	$ Change	% Change
Compensation	$355,614	$366,568	$10,954	3.08%
Expenses	$432,950	$444,150	$11,200	2.59%
Debt Service	$1,278,322	$1,388,579	$110,257	8.63%
MWRA Assessment	$7,851,947	$8,248,093	$396,146	5.05%
Total Requested in Article 5	**$9,918,284**	**$10,447,390**	**$628,557**	**6.34%**
Indirect Expenses (Article 4)	$532,094	$541,663	$9,569	1.80%
Cash Capital (Article 14)	–	$100,000	$100,000	–
OPEB Contribution (Article 17)	$3,004	$3,004	–	–
Total Wastewater Enterprise	**$10,453,931**	**$11,092,057**	**$638,126**	**6.10%**

Note that these tables differ from those contained in the warrant in three respects: (1) the MWRA assessments for water and wastewater reflect the MWRA's preliminary assessments, which are lower than the

10% increase "placeholders" assumed in the Warrant[1]; (2) indirect expenses to be charged to the enterprise funds, although appropriated separately under Article 4, have been included for completeness as they must be taken into account when water and wastewater rates are set in the fall; and (3) the charges to the Water and Wastewater Enterprise Funds to help fund liabilities for Other Post-retirement Employment Benefits ("OPEB"), although appropriated separately under Article 17, have also been added for completeness. The principal operating costs of the water and wastewater enterprise funds and issues pertinent to this year's budget are addressed briefly below.

Operating Costs

MWRA Assessments. The largest components of both the water and wastewater fund budgets are the assessments charged by the Massachusetts Water Resources Authority (MWRA), which now represent approximately 70% of the total budget for each fund. The Town will be assessed a share of the MWRA's total FY2021 water and sewer budgets based on the Town's proportionate usage in the most recent full calendar year, CY2019, relative to other towns in the MWRA community. Based on the MWRA's preliminary assessments, Lexington's water assessment for FY2021 will increase by 8.32% and its wastewater assessment by 5.05%, for a combined increase of 6.64%. This percentage increase, higher than it has been in recent years, is the main driver of this year's significant water and wastewater fund budget increases.

Update 1: On May 20, 2020 the MWRA issued final assessments which were (on a combined basis) materially lower than their preliminary assessments, "…to provide financial relief and flexibility to MWRA's member communities". Lexington's combined assessment increase was reduced from 6.6% to 4.4%. The related appropriations in the FY2021 budget will not be adjusted for this Annual Town Meeting, but the new lower assessments will be used when setting water and wastewater rates in the fall.

Direct Town Costs. In addition to the MWRA assessments, the expenses of the water and wastewater fund budgets include direct costs incurred by the Town, primarily for: (1) the wages and salaries of the employees in the DPW's Water and Sewer Divisions, (2) the expenses of water and sewer maintenance activities and equipment, and (3) debt service on prior borrowings for water and sewer capital improvements. These costs are increasing more modestly, consistent with prior years.

Indirect Town Costs. The Water and Sewer Enterprise Fund budgets also include indirect costs for services provided by other Town departments to support water and sewer operations, such as insurance costs (health and liability), retirement funding, engineering costs, and the cost of services provided by the Comptroller, the Management Information Systems (MIS) Department, and the Revenue Department. The Town reviews the appropriate level of indirect costs each year and adjusts the charges to the enterprise funds accordingly.

Debt Service. Debt service costs represent the payoff of principal and interest on debt incurred for water and sewer fund capital projects in prior years, typically funded by 10-year bonds. Debt service costs are increasing minimally this year for the water fund (.11%) but more substantially for the wastewater fund (8.63%). It should be noted that debt service costs for both funds are projected to increase substantially in FY2022. *See* Brown Book, pp. XI-8-9 and discussion of Articles 13 and 14 below.

Cash Capital. In a break from past practice, it is proposed this year to begin transitioning the funding of recurring, regular capital investments made for the maintenance and upgrade of the Town's water and wastewater systems ($2,200,000 annually for the water system and $1,000,000 annually for the wastewater system) from borrowing to cash capital. To minimize the impact of this changeover on rates, the transition would be phased in gradually: in the case of the water fund, at the rate of $200,000 per year for eleven years; and in the case of the wastewater fund, $100,000 per year for ten years. *See* Brown Book, pp. V-26-27 and V-30-31.

[1] The preliminary assessments are issued in February. Final MWRA assessments issued in June, typically a bit smaller than the preliminary assessments, are used to set water and sewer rates during the Town's annual rate-setting process in the fall. If a special town meeting is held in the fall, appropriations for MWRA expenses are normally adjusted to reflect the final assessments.

As this Committee has advocated in past reports, the use of cash capital instead of borrowing makes sense in the case of regular, recurring capital investments as it will improve transparency during rate-setting and avoid interest costs. Because debt service for debt incurred in prior years will wind down only gradually, this changeover will result in somewhat higher water and sewer rate increases than would otherwise be required during the early years of the transition. However, as the old debt is retired, debt service costs will moderate and eventually the overall costs of the annual capital investment program will be lower as interest costs are eliminated. For a more detailed treatment of the impact of the changeover, *see* discussion of Articles 13 (Water System Improvements) and 14 (Wastewater System Improvements) below.

Rate-Setting Issues

Because changes in the operating budgets of the water and wastewater enterprises approved at the annual town meeting ultimately translate into changes in the water and wastewater rates when set later in the year, a brief comment on those rates and the impact of this year's budget is in order.

By and large, rate increases have been relatively modest for more than a decade. From FY2006 through FY2020, they fluctuated between -1.9% and 6.6% for an average annual rate increase of 2.7%. However, with a combined water and wastewater increase in the FY2021 budget of 7.05% (compared with a combined increase last year of just 2.93%) and the introduction of cash capital and other looming pressures on the rates, rate increases are likely to be higher for FY2021 and years beyond, at least for some period of time.

One of those other factors is an apparent new trend of declining usage as plumbing fixtures are modernized to waste less water and residents pay more attention to water conservation. Since most of the water and wastewater funds' costs are fixed, not variable, the "sale" of fewer units of water necessarily results in a higher per-unit cost. Largely for this reason, at the rate-setting for FY2020 last fall, water and wastewater rates had to be increased on a combined basis of 7.3% even though the combined water and sewer budgets increased by only 2.93%. If the trend of decreasing usage continues, this year's combined budget increase of 7.05% could translate into an FY2021 water and wastewater increase next fall that is even higher. The "silver lining" in this cloud, of course, is that residents whose usage reflects the town-wide decline will see their bills increase less than the rates.

Another factor putting pressure on the rates going forward, as discussed under Articles 13 and 14 below, is a projected increase in debt service over the next few years resulting, in the case of the water fund, from an increase last year in the annual capital maintenance program investment from $1,000,000 to $2,200,000; and in the case of both the water and wastewater funds, the extraordinary appropriation last year of nearly $5 million in debt (split equally between the two funds) for the automated meter reading project.

An unknown is whether and how much MWRA assessments will increase in future years. If Lexington's share of the overall MWRA usage continues to increase in future years, as it did this year relative to other communities (Lexington had a combined assessment increase of 6.6% compared with a 3.6% increase system-wide), this could be yet another factor imposing upward pressure on rates. On the other hand, an extended period of drought, by increasing irrigation usage and water fund revenue, could help to offset a required water rate increase (at least for those Lexington residents who do not use extensive irrigation).

Retained Earnings

As discussed in Appendix B, the State statute governing enterprise funds, G.L. c. 44, § 53F½, requires that accumulated surpluses resulting from the operations of an enterprise fund, referred to as retained earnings, remain with the fund as a reserve, and that they be used only for capital expenditures of the enterprise, subject to appropriation, or to reduce user charges. Deficits must be funded with existing reserves or, in the absence of such reserves, made up in the following year's rates. The Town's policy is to maintain a balance of approximately $1 million of retained earnings in each fund as a buffer against revenue shortfalls resulting from unexpected reductions in usage or an unanticipated need for extraordinary expenditures. The table below shows how the balance of retained earnings has been deployed over the past several years and their proposed appropriation at this ATM for FY2021.

Retained Earnings: Appropriations and Year-End Balances

Fiscal Year	FY2016	FY2017	FY2018	FY2019	FY2020	FY2021
Water						
Starting Balance [1]	$2,119,458	$1,786,659	$1,800,533	$531,683	$1,612,998	**$1,346,448**
Approp. for Rate Relief [2]	–	–	–	–	–	–
Bedford, Burlington Mitig [3]	$275,000	$131,000	$190,900	–	–	–
Approp. for Capital [4]	$1,015,500	$620,500	$1,095,000	$105,000	$775,000	**$130,000**
Projected End Balance [5]	$903,958	$1,035,159	$514,633	$426,863	$837,998	**$1,216,448**
Wastewater						
Starting Balance [1]	$2,027,941	$1,032,942	$2,270,848	$576,523	$1,521,373	**$998,736**
Approp. for Rate Relief [2]	–	–	–	–	–	–
Approp. for Capital [4]	$1,390,500	$177,500	$1,290,000	–	$700,000	–
Projected End Balance [5]	$637,441	$855,422	$980,848	$576,523	$821,373	**$998,736**

[1] Certified retained earnings as of the end of the prior fiscal year (as of 6/30/2019 for this year's ATM). The anomalous figures for 2018 resulted from an under-certification of retained earnings at the end of FY2017 that was made up the following year.

[2] Appropriations from retained earnings to subsidize the next fiscal year's operating budget.

[3] Several years ago, Lexington supplied unusually large quantities of water to Bedford as Bedford worked to correct issues with its alternative supplies. The retained earnings resulting from these extraordinary sales were "earmarked" and applied to mitigate the rate impact in subsequent years.

[4] Proposed appropriations for capital projects for the next fiscal year (FY2021 at this ATM).

[5] Note that appropriations from retained earnings at the annual town meeting must be deducted as a liability from the projected retained earnings to be certified as of the end of the current fiscal year, even though the funds will not be applied until the following fiscal year. The projection of anticipated retained earnings assumes break-even operational results during the current fiscal year. A higher (lower) starting balance available for appropriation the following year indicates that the current year's operating results were higher (lower) than were projected at rate-setting, resulting in an operating surplus (deficit).

From roughly 2009 to 2014, accumulated retained earnings in excess of the desired buffer ("excess retained earnings") were appropriated on a regular basis to mitigate water and sewer rate increases. This practice was discontinued, however, as it simply pushed required rate increases down the road a year. Since that time, as shown in the table above and consistent with recommendations made by this Committee, excess retained earnings have been used primarily to offset the need for borrowing for capital investments of the enterprises, thereby lowering debt service costs and required future rate increases over a more extended period of time, as well as saving interest cost.

Particularly where applied to regular, recurring capital investments, this use of retained earnings is similar to the now-proposed use of cash capital; however, being deployed a year in arrears, it leaves a substantial amount of funds idle for a year; and not being part of the annual operating budget, its use to fund regular capital investment needs is less transparent during the rate-setting process. Ideally, rates would be set such that the water and sewer funds are on a break-even basis and do not generate substantial retained earnings in excess of the targeted reserves; however, given the difficulty of predicting usage and the need for conservatism in setting the rates, surpluses can be expected to continue. The best use of the extra funds is for non-recurring expenses or capital projects, such as the $500,000 in retained earnings appropriated last year from each of the water and sewer funds toward the automated meter reading project.

Consistent with this observation, a limited amount of retained earnings is proposed for appropriation from the water fund at this annual town meeting to fund, or help fund, two smaller capital projects: $55,000 to replace a 6" trash pump, *see* Brown Book, p. XI-6; and a contribution of $75,000 to the hydrant replacement program, *see* Brown Book, p. XI-18, both to be appropriated under Article 12 (Municipal Capital Projects and Equipment). No retained earnings are requested for appropriation from the wastewater fund.

Recreation Enterprise Fund

In 2015, following the inauguration of the Lexington Community Center (LCC), the Recreation Department was reorganized to include LCC operations and renamed the Department of Recreation and Community Programs (DRCP). This change resulted in increased costs for the Recreation Enterprise Fund as the FY2016 LCC budget included $383,073 to fund 5.5 full time and seasonal staff to plan, manage and deliver community programs along with the supplies needed. That level of staffing has continued through the present. See the Brown Book, p. VII-9. The proposed appropriations for FY2021, and changes from the prior fiscal year, are shown in the table below.

Recreation Enterprise Fund	FY2020 Appropriated	FY2021 Requested	Dollar Increase	% Change
Compensation	$1,471,683	$1,535,363	$63,680	4.33%
Expenses	$1,481,895	$1,480,045	($1,850)	(0.12%)
Debt Service				
Total Requested in Article 5	**$2,953,578**	**$3,015,408**	**$61,830**	**2.09%**
Indirect Expenses (transfer to General Fund)	$269,681	$277,771	$8,090	3.00%
Total	**$3,223,259**	**$3,293,179**	**$69,920**	**2.17%**

The operational costs of programs offered by the DRCP are generally designed to be revenue neutral, with charges to users matching the program's operating costs. However, to support LCC operations that are generally available to all residents and are not fee-supported, a portion of LCC costs are now supported by the tax levy. Accordingly, the motion includes a transfer of $218,916 in tax levy funds into the Recreation Enterprise Fund, to be appropriated under this article.

In addition to the subsidy from the tax levy, sources of revenue include $375,000 from the Recreation Enterprise Fund retained earnings, $1,448,963 from user fees for recreation, $465,300 from registration fees for Community Center programs, and $775,000 from greens fees at Pine Meadows Golf Course. The budgeted revenue from fees is based on projections. The Director of Recreation and Community Programs, through the Recreation Committee, sets fees for use of the Town's playing fields, gyms, and other recreational facilities with the approval of the Select Board.

The Recreation Enterprise Fund has in the past contributed to the debt service on some recreation capital projects, in particular the renovation of Lincoln Field some years ago. However, all recreation capital costs are now covered using the General Fund through a combination of free cash, within-levy debt, excluded debt (though not recently), and Community Preservation Act (CPA) funding.

The balance of retained earnings in the Recreation Enterprise Fund at the close of FY2019 was $669,744, of which $555,000 is proposed to be appropriated at this annual town meeting. An appropriation from retained earnings of $375,000 is requested under this article for application to the operating budget. An additional $180,000 of retained earnings is requested for appropriation under Article 15, of which $100,000 would fund a design for the renovation of the clubhouse at the Pine Meadows Golf Course and $80,000 would be used to purchase equipment at the Pine Meadows Golf Course.

The Committee recommends approval by a vote of (8-0).

Article 6
Establish Qualifications for Tax Deferrals

Funds Requested	Funding Source	Committee Recommendation
None	**N/A**	**Approve (8-0)**

This article proposes to raise the income limit for participation in the Town's tax deferral program under G.L. c. 59, § 5, Cl. 41A from $75,000 to $90,000. Under the deferral program, qualifying residents age 65 or older can postpone payment of some or all of their property taxes, in an amount up to half the value of their home, until the property is sold or otherwise disposed of. For general background on Clause 41A and other programs offering property tax relief to seniors, please see Appendix D to this report.[2]

The 41A Program and the Home Rule Petition

Under generally applicable state law, the highest income limit a Town may adopt for participation in the Clause 41A program is that established by the Department of Revenue each year under the state's "Circuit Breaker" income tax relief program for a single person who is not a head of household, currently $60,000. In 2008, in response to a home rule petition, the state legislature enacted a special law (Chapter 190 of the Acts of 2008) allowing Lexington to expand eligibility beyond that permitted under the general laws. Among other things, Chapter 190 permits the Town, by vote of Town Meeting and with the approval of the Select Board, to set a higher income limit for deferrals.[3] Town Meeting most recently raised that limit from $70,000 to $75,000 in 2019.

The Proposed Increase

This year, the Tax Deferral and Exemption Study Committee (TDESC) has recommended that the Town increase the deferral income limit by an additional $15,000 to $90,000, and the Select Board has voted to approve such an increase. The change is intended to help ensure that all persons who have been participating in the program can continue to do so, and to allow more residents to participate.

The proposed new limit is based on the state Circuit Breaker's current limit for married couples filing jointly, which is considerably more generous than the single-filer maximum limit referenced in Clause 41A. While a $90,000 limit is higher than that in most other communities, it is not unique. Last year, the Town of Arlington established a limit of $88,000, the then-applicable Circuit Breaker limit for married couples. The TDESC considered proposing that Lexington's limit be pegged automatically to the higher Circuit Breaker limit, effectively indexing it for inflation, but elected to defer such a proposal until the impact of this year's substantial increase on the number and magnitude of deferrals can be evaluated.

Committee Recommendation

With a history of low utilization, and a participation rate that has not materially changed after the most recent increases in the income limit (see chart below), it is unlikely that this year's proposed change will significantly increase the number of deferrals or produce a material impact on the Town's finances. The cumulative balance of all deferrals outstanding increased from about $1 million in FY2015 to about $1.8 million in FY2019, but it has been relatively stable for the past three years as the dollar amount of old deferrals paid off roughly offsets the dollar amount of new deferrals taken out.

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[2] A brochure prepared by the Tax Deferral and Exemption Study Committee entitled *Property Tax Relief Programs* is available on the Town web site `http://www.lexingtonma.gov/taxrelief`. The site also has detailed information about who qualifies for Clause 41A deferrals and the application process.

[3] The special law also permits the Town to adopt a lower age of eligibility than 65, or to condition eligibility on objective criteria of disability or other hardship for persons who would not otherwise qualify based on their age, but the Town has never done so.

Lexington Property Tax Deferral History

Fiscal Year	Interest Rate[4]	Number of Deferrals	Income Threshold	Average Deferral	Total Deferred
2005	8.00%	16	$40,000	$4,688	$75,000
2006	8.00%	16	$40,000	$4,625	$74,000
2007	4.77%	15	$40,000	$4,905	$73,578
2008	4.92%	20	$40,000	$5,092	$101,832
2009	1.66%	26	$40,000	$5,938	$154,380
2010	0.68%	28	$50,000	$6,287	$176,034
2011	0.34%	28	$51,000	$6,335	$177,391
2012	0.26%	29	$60,000	$6,601	$191,457
2013	0.18%	29	$60,000	$6,898	$200,051
2014	0.15%	29	$65,000	$7,637	$221,479
2015	0.12%	28	$65.000	$8,089	$226,501
2016	0.25%	43	$65,000	$8,524	$366,553
2017	0.66%	41	$70,000	$9,094	$372,859
2018	0.82%	42	$70,000	$9,569	$401,897
2019	1.96%	40	$70,000	$10,046	$401,850
2020	2.55%	*TBD*	$75,000	*TBD*	*TBD*

The Committee believes that an increase of the tax deferral income limit to $90,000 will offer needed property tax relief to some moderate-income senior homeowners who cannot currently take advantage of the deferral program. The Committee also believes that the state Circuit Breaker limit for married couples is a reasonable measure of financial need, particularly in view of Lexington's relative high property tax. Given the nature of the program, which essentially involves well-secured temporary loans by the Town, the burden on and financial risk to the Town are minimal.

The Committee recommends approval by a vote of (8-0).

Article 7
Petition General Court to Amend Legislation Regarding Tax Deferrals

Funds Requested	Funding Source	Committee Recommendation
None	**N/A**	**Approve (8-0)**

This article requests that the Select Board be authorized to seek special legislation which would allow Lexington to delay, for one year, the requirement of Chapter 59, §5, Clause 41A of the General Laws that the interest rate for deferred property taxes increase to 16% upon the death of a person whose taxes have

[4] The general law originally provided for an interest rate of 8% but was subsequently amended to allow a town, by vote of its legislative body, to establish a lesser rate. Effective in 2007, Town Meeting adopted a variable rate intended to match what the Town would otherwise earn on these funds for the year in question. See Appendix D. Historical interest rates are set forth in the table below. *See also* Brown Book p. xii. The interest rate for FY2021 will be 1.41%.

been deferred. The Clause 41A deferral program, as noted in the discussion of Article 6 above, allows qualified residents age 65 or older to postpone the payment of some or all of their property taxes, in an amount (including interest) up to half the value of their home, until the property is sold or otherwise disposed of.

Deferral Interest Rate

Clause 41A originally provided for a deferral interest rate of 8% but now permits a town, by vote of its town meeting, to establish its own deferral interest rate anywhere from 0% to 8%. That rate continues in effect for each year's deferral until the property is sold or conveyed or the person whose taxes have been deferred dies. The deferred taxes, plus accrued interest, are due and payable when the property is sold or conveyed, whether that occurs before or after death.

At the 2006 Annual Town Meeting, Lexington adopted a variable interest rate for deferrals intended to match the return the Town would otherwise earn on the funds deferred: the monthly one-year Constant Maturity Treasury (CMT) rate as published by the Federal Reserve for the first week in March before each applicable fiscal year, not to exceed 8%. That rate, which tends to be roughly 3 percentage points less than the prime rate, was 1.96% for deferrals granted in FY2019; 2.55% for deferrals granted in FY2020; and will be 1.41% for deferrals granted in FY2021.

Escalated Rate

While Clause 41A gives towns the flexibility to establish a reasonable interest rate for deferrals during the life of the person whose taxes are deferred, but it does not allow the same flexibility once that person (or a surviving spouse who has assumed the deferral obligations) dies. Rather, it mandates an immediate escalation of the deferral interest rate, upon "the conveyance of the property or the death of the person whose taxes have been deferred," to the rate of 16%.[5]

This high interest rate may be justified in the case of deferrals that are not promptly repaid, as required, when the property is sold or conveyed. However, in a case where a person whose taxes have been deferred has died, but the property has not yet been sold or conveyed, its immediate imposition upon death has proved, in many cases, to result in hardship.

Although the Town certainly has an interest in having low-interest tax deferrals paid back promptly, it generally takes some time for an estate to arrange for the sale or conveyance of a decedent's property necessary to enable the deferrals to be repaid, particularly if the home has to be put on the market for sale to a third party. If the estate must be probated, even the most agile executor may need months to complete the judicial process required to convey the property, especially if the homeowner died intestate. Under these circumstances, a high interest rate is hard to justify as an incentive to assure prompt payment.

Given that such delays are common, and often unavoidable, the imposition of a 16% interest rate immediately upon the death of a low or moderate-income homeowner can result in a significant financial hardship for that person's heirs. If substantial taxes have been deferred, the higher interest rate, applied over the first twelve months, can easily add up to the equivalent of an additional year of property tax (e.g., $80,000 in deferred taxes at a 16% rate would generate an interest charge of $12,800). If the property is sold to a third party, that higher interest must be deducted from the proceeds of sale. If the property is conveyed directly to an heir, the estate (or the recipient of the property) must generate sufficient cash not only to repay the deferred taxes but also to pay a higher interest bill.

[5] Specifically, Clause 41A provides that interest shall accrue at the rate provided in Chapter 60, § 62 of the General Laws. Section 62 allows a homeowner whose property has been taken or sold for nonpayment of taxes to redeem the property upon payment of all taxes in arrears, plus interest at the rate of 16%.

Proposed Legislation

The special legislation proposed in the motion under this article[6] would not eliminate the 16% interest rate but would mitigate its impact by delaying its imposition for one year after the death of a person whose taxes have been deferred if the property has not yet been sold or conveyed. During that one-year delay, interest would not be waived altogether but would continue to accrue for each year's deferral at the original CMT rate applied to that deferral.

If the property is sold or conveyed, either before or after the death of the person whose taxes have been deferred, but the full amount of the deferrals plus accrued interest is not immediately paid, then the 16% interest rate would take effect.

Committee Recommendation

The goal of the 41A deferral program is to alleviate the property tax burden on low- to moderate-income homeowners, and the low interest rate system adopted by the Town in 2006 is an integral component of that program. This Committee believes it is sensible and appropriate to delay any increase in interest rates on deferred taxes for up to a year after death if the property has not yet been sold or conveyed. This delay would allow a reasonable time for the estate to arrange a sale or conveyance. The income that would otherwise be generated with a higher interest rate is not a significant revenue source for the Town, and its delay for one year would have no material impact on the Town's finances.

The Committee recommends approval by a vote of (8-0).

Article 8
Short Term Rental Impact Fee

Funds Requested	Funding Source	Committee Recommendation
None	**N/A**	**Approve (7-0-1)**

This article proposes that the Town accept the entirety of Massachusetts General Laws Chapter 64G, Sections 3A & 3D. In combination with new zoning legislation proposed under Article 36, this would regulate the types of units that can be used for short term rentals in Lexington and impose a 3% community impact fee for such rentals. Our report focuses on the financial implications of these proposed legislative changes.

Town Meeting voted to accept M.G.L. c. 64G, §3A at a special town meeting in November 2009. If Town Meeting accepts both M.G.L. c. 64G, § 3D(a) and § 3D(b), which requires a separate vote for each subsection, then a 3% community impact fee will be imposed on short term rentals of any unit in a two-family or three-family dwelling in Lexington. The zoning bylaw change proposed under Article 36 would further limit short term rentals to units in owner-occupied dwellings only.

The state-wide room occupancy excise tax rate is 5.7%. Beginning July 1, 2010, per the local adoption of c. 64G, §3A, Lexington imposed a 6% local option room occupancy tax, which is paid in addition to the state tax, for a total room occupancy tax of 11.7%. This tax applies to room rentals of 90 days or less in

[6] The proposed legislation would amend the special act previously obtained by Lexington, Chapter 190 of the Acts of 2008, which allowed Lexington to vary the eligibility provisions of Clause 41A. For a description of the 2008 Act, see the discussion of Article 6 above. The language in the motion differs somewhat from the language contained in the Warrant but has the same objective. A similar amendment of Clause 41A that would apply generally to all municipalities was proposed last year by our State Representative but did not advance out of committee, hence the need for special legislation.

hotels, motels, bed and breakfast establishments, and lodging houses. Beginning July 1, 2019, the room occupancy tax also applies to short term rentals of property for 31 days or less.

The room occupancy tax is collected by the Department of Revenue and the portion attributable to local option taxes and community impact fees is distributed quarterly to municipalities.

The table below shows the history of the Town's excise tax revenue since FY2015 along with 3- and 5-year averages. Revenue in the current fiscal year is estimated at $970,000, an increase of 2.4% from FY2019.

Excise Tax Category	Other	Room Occupancy	Jet Fuel	Meals
FY2015 Actual	$1,698,096	$880,026	$346,731	$471,339
FY2016 Actual	$1,727,554	$951,942	$278,337	$497,276
FY2017 Actual	$1,616,713	$1,056,493	$78,074	$482,146
FY2018 Actual	$1,562,971	$902,617	$203,854	$456,499
FY2019 Actual	$1,659,673	$947,681	$240,085	$471,907
Average 2017–2019	*$1,613,119*	*$968,930*	*$174,004*	*$470,184*
Average 2015–2019	*$1,653,001*	*$947,752*	*$229,416*	*$475,833*
FY2020 Estimated	**$1,648,000**	**$970,000**	**$200,000**	**$478,000**

Revenue Impact

The community impact fee of 3% on short term rentals would be in addition to the current local option 6% tax and the state 5.7% tax, resulting in a 14.7% tax on short term rental units in Lexington. Hotels, motels, bed and breakfast establishments and lodging houses would not be subject to the community impact fee.

At least 35% of the community impact fees must be dedicated to affordable housing or local infrastructure projects. By a vote of the Select Board, this 35% portion could be deposited directly into the Affordable Housing Stabilization Fund, bypassing appropriation by Town Meeting. The remaining 65% would flow to the General Fund.

The Committee does not have sufficient information to provide a detailed analysis of the revenue impact that would follow approval of this article. An estimate of revenue from the community impact fee would be based on the number of short term rental units and on the average annual revenue from such units. At the moment, we have neither figure.

All operators are legally required to register their properties with the Department of Local Services. Lexington currently has 42 properties registered, of which 36 are for short term rentals. If Article 36 is approved, some of these units may no longer be allowed to be used for short term rentals. It is also likely that a significant number of unregistered properties are being used for short term rentals in Lexington. This makes it difficult to estimate in advance the number of units that will be subject to the community impact fee.

Since short term rentals have been subject to the room occupancy tax for less than a full year, we have insufficient data with which to calculate an average annual revenue.

Based on regional estimates of short term rental activity, the Committee assumes that community impact fee revenue will be under 5% of the current 5-year historical average for room occupancy tax (which is currently derived mostly from large commercial hotels), and possibly much lower. If that assumption is correct, the revenue would be under $50,000. New regulations on short term rentals may also generate new expenses for enforcement, which will offset this new revenue. The net revenue impact may be quite limited, but we will need to re-evaluate the impact once we have more data.

The Committee recommends approval by a vote of (7-0-1).

Article 9
Establish and Continue Departmental Revolving Funds

Funds Requested	Funding Source	Committee Recommendation
See below	**RF**	**Approve (8-0)**

This article seeks reauthorization of all existing revolving funds, plus the creation of a new revolving fund for Lab Animal Permits in FY2021, as shown in the table below. Information regarding the nature and purpose of revolving funds can be found in Appendix C of this report.

The spending limit proposed for each of the funds is based on a reasonable estimate of the fees and charges likely to be received, as well as of the expenditures likely to be required. A summary of the historical receipts, expenditures, and balances for each fund during FY2019 and the first half of FY2020 can be found in Appendix C of the Brown Book.

Program or Purpose	Authorized Representative or Board	Departmental Receipts	FY2020 Request	FY2021 Request
School Bus Transportation	School Committee	School Bus Fees	$1,150,000	**$1,150,000**
Building Rental Revolving Fund	Public Facilities Dir.	Building Rental Fees	$544,916	**$560,000**
DPW Burial Containers	Public Works Dir.	Sales	$50,000	**$50,000**
Lexington Trees Fund		Gifts and Fees	$45,000	**$45,000**
DPW Compost Operations		Sales and Permits	$773,710	**$790,000**
Minuteman Household Hazardous Waste Program		Fees from Consortium Towns	$220,000	**$250,000**
Regional Cache—Hartwell Avenue		Participating Municipality Fees	$20,000	**$20,000**
Senior Services Programs	Human Services Dir.	Program Fees and Gifts	$75,000	**$75,000**
Health Programs	Health Director	Medicare Reimbursements	$45,000	**$45,000**
Tourism/Liberty Ride	Economic Development Dir.	Liberty Ride Receipts	$210,000	**$200,000**
Visitors Center		Sales, Program Fees and Donations	$101,253	**$205,000**
Residential Engineering Review	Engineering Dir.	Fees Paid by Developers	$57,600	**$57,600**
Lab Animal Permits	Public Health Dir.	Lab Animal Permit Fees	–	**$40,000**

The change in the Visitors Center budget reflects the expected return to a more typical revenue pattern following the transition from the Temporary Visitors Center into the newly completed building. Note that the Visitors Center FY2020 budget included an appropriation from the General Fund that will not be in the FY2021 budget.

For FY2021 a new Lab Animal Permits Revolving Fund is proposed with an initial appropriation of $40,000 to fund inspections for a growing number of lab animals in commercial and industrial properties.

The Committee recommends approval by a vote of (8-0).

Article 10
Appropriate the FY2021 Community Preservation Committee Operating Budget and CPA Projects

Funds Requested	Funding Source	Committee Recommendation
$5,400,225	**CPA**	**10(a-c,e-o) Approve (8-0)** **10(d) IP**

Funds Requested:

	Project	**Appropriation**
a	Archives & Records Management / Records Conservation & Preservation	$20,000
b	Restoration of Margaret, Lady Lexington, Painting	$9,000
c	Battle Green Master Plan—Phase 3	$317,044
d	Conservation Land Acquisition	–
e	Daisy Wilson Meadow Preservation	$22,425
f	Wright Farm Site Access Planning and Design	$69,000
g	Athletic Facility Lighting	$450,000
h	Park Improvements—Hard Court Resurfacing—Valley Tennis Courts	$100,000
i	Park and Playground Improvements—Sutherland Park	$95,000
j	Park Improvements—Athletic Fields—Harrington, Bowman, and Franklin Field	$370,000
k	Parker Meadow Accessible Trail Construction	$551,026
l	Lexington Housing Authority—Greeley Village Community Center Preservation	$130,000
m	LexHAB—116 Vine Street Design Funds	$100,000
n	CPA Debt Service	$3,016,730
o	Administrative Budget	$150,000
	TOTAL	**$5,400,225**

10(a) Archives & Records Management/Records Conservation & Preservation

This $20,000 request is for the conservation and preservation of historic municipal documents and records. The ongoing project will fund the conservation and preservation of older documents and make them available in the Town's digital archives. Documents to be conserved under this funding request include Colonial Tax Warrants, an 1873 Tax Book, Police Department Journals from 1874–1909, and Valuation Books from 1916–1918.

10(b) Restoration of *Margaret, Lady Lexington*, Painting

This $9,000 request is to hire a conservator to restore the historic painting, *Margaret, Lady Lexington*, which is owned by the Town and displayed in the lobby of the Cary Memorial Building. The painting's aesthetic and structural condition is fair to poor, with paint loss, tears, and a weakening canvas and frame. Restoration would include being transported in a climate-controlled vehicle to the conservator studio, where appropriate work would be completed. Work would begin in January 2021 and take 4-6 months to complete.

10(c) Battle Green Master Plan - Phase 3

Implementation of the 2010 Battle Green Master Plan was divided into three phases. Phases 1 and 2 were fully funded in FY2012 and FY2013 and have been completed. Due to CPA funding constraints in FY2020, the requested appropriation of $570,438 for Phase 3 was reduced to $253,394 (leaving $317,044 unfunded). Work on Phase 3 using the partial funding approved in FY2020 will begin this spring.

This year's request for $317,044 will fund the remaining items in Phase 3, which include wear-tolerant surfaces around the monuments, pathway lighting, and landscaping. Once the Phase 3 work is completed during the 2021 construction season, the Battle Green Master Plan will be almost fully implemented. The exceptions are parking and traffic related work, which are anticipated to be funded at the 2023 Annual Town Meeting.

10(d): Conservation Land Acquisition

This item will be indefinitely postponed.

10(e): Daisy Wilson Meadow Preservation

This request for $22,425 will bring Lexington's ongoing multiyear Conservation Meadow Preservation Program to the 5-acre Daisy Wilson Meadow. Hennessey Field and Joyce Miller's Meadow were restored under this program in 2015–16: Meadows at the Wright Farm were restored in 2018–19. The goals of the project are to remove trees, shrubs, and vines which have grown over meadow land, restore views of historic stone walls, remove invasive plants, and provide an annual mowing and maintenance regime to preserve meadow habitat.

10(f): Wright Farm Site Access Planning and Design

This request for $69,000 is to engage a consultant to create a site access and design plan with cost estimates for conservation land access, parking, and trail access, taking into account proposed uses for the barn and property. A second phase of the project will request funds for permitting, bid documents, and construction; there is no date set for this second phase.

Article 10(g) Athletic Facility Lighting

This request is to complete the Athletic Facility Lighting project at the Gallagher Tennis Courts, Center basketball courts, and Town Pool Complex. Funding for this project of $975,000 was approved at the 2018 Annual Town Meeting and the scope called for the upgrades to be completed at these locations, as well as the Center #1 baseball field and Center #2 softball field. Repairs and improvements were completed at Center #1 and Center #2 in May 2019. However, the upgrades were not completed at other facilities as the bid for these components came in over-budget.

The total cost for this project is now $1,425,000, almost 46% over the original budget. This committee would have preferred that the proponents returned to Town Meeting to gain approval for the additional funding prior to commencement of the project. We strongly recommend that a more robust approval process be adopted by the Town in order to avoid similar overruns on other current and future projects and reluctantly recommends approval of this article.

Article 10(h) Park Improvements - Hard Court Resurfacing

This ongoing program provides funding for resurfacing, painting and striping the hard court surfaces (basketball and tennis courts) at Recreation facilities. The FY2021 funding request will resurface, paint and restripe the Valley tennis courts, install a new bike rack and pave the parking area and stone dust path. The tennis courts were last resurfaced in 2008. These repairs of hard court surfaces will increase their quality and safety. Note that the budget appropriation has increased from a similar prior year project due to an increased estimate from the architect as well as the current construction climate.

Article 10(i) Park and Playground Improvements

This request will update and replace playground equipment and install a bike rack at Sutherland Park. The proposed improvements will renovate and rehabilitate existing safety surfacing and equipment so that the site will be in compliance with the standards of the Consumer Product Safety Commission (CPSC), the American Society for Testing and Materials (ASTM) and the American with Disabilities Act (ADA). Additionally, at the recommendation of the ADA Compliance Study that was completed in 2017, the surfacing tiles at the entrance of the playground will be reset, an accessible route to the dugouts at the baseball field will be created, and an accessible path will be extended from the existing asphalt path to the water fountain near the entrance of the park. The equipment at Sutherland Park was last replaced in 2000.

Article 10(j) Park Improvements - Athletic Fields

This ongoing multi-year capital program is to address safety and playability concerns as well as provide adequate and safe field conditions. This program funds improvements to athletic fields, including renovations to natural turf, drainage, new irrigation systems, and site amenities including benches and backstops. The FY2021 funds will be used for such improvements to the Harrington Elementary School Field. Based on recommendations from a 2017 ADA Compliance Study, the gravel driveway from Lowell Street will be paved to provide more accessible parking and a formal entrance, an accessible route will be created from the school drive to the team areas, and the team areas will be renovated to provide more appropriate wheelchair space. In addition, new in-ground irrigation systems will be installed at the Bowman and Franklin School fields. If approved, renovations will begin in the Fall of 2020.

Article 10(k) Parker Meadow Accessible Trail Construction

This request will fund construction of a universal accessible passive recreation trail system at Parker Meadow Conservation Area, a 17-acre parcel located near Lexington Center with access off the Minuteman Bikeway. This is a collaborative project involving private citizens, land stewards, Conservation Commission, Recreation Committee, and the Commission on Disability. Design funds were approved at the 2014 Annual Town Meeting and bid ready construction documents are expected in February 2020. If approved, the project would be ready for construction at the beginning of FY2021.

10(l): LHA Greeley Village Community Center Preservation

This article requests $130,000 to repair and thereby preserve the Community Center building at Greeley Village, a 100-unit affordable housing development managed by the Lexington Housing Authority. The project will replace rotting wood on a second floor balcony, rotting wood and rusting metal supports for the ground floor ramp deck, and deteriorating windows and exterior doors. The total cost for this project is $205,000; $75,000 of the project will be funded by the Commonwealth of Massachusetts Department of Housing and Community Development.

10(m): LexHAB- 116 Vine Street Design Funds

This article requests $75,000 for the first phase of a three-phase project to develop six affordable housing units on a 30,000 square foot lot on Vine Street that was reserved for affordable housing when the 14.2 acre Leary Farm site was purchased by the Town with CPA funds in 2009. These funds will support selecting a design team, holding meetings with neighbors and stakeholders, and developing the design scope, budget, and schedule. The full project cost, including this initial funding, is estimated to be $3.5 million, with $3.425 million to be requested in FY2022 or FY2023.

10(n): CPA Debt Service

Projected debt service on the CPA projects is outlined in the following table. Two different types of debt instruments are used: bond anticipation notes (BANs), and multi-year municipal bonds. BANs provide interest-only borrowing for a term of up to one year. They are issued for individual projects prior to bundling the debt from several projects to create a single multi-year bond.

Project TM Approval Final Payment	Total Appropriation	Total Debt Financing	FY2021 Debt Service
Wright Farm Purchase ATM 2012 FY2024	$3,072,000	$2,950,000	**$351,050**
Community Center Acquisition STM 3/2013 FY2024	$10,950,000	$7,390,000	**$880,100**
Cary Memorial Building Upgrades STM 3/2014 FY2025	$8,677,400	$8,241,350	**$786,000**
Center Track and Field Renovation ATM 2018 FY2022	$3,340,000	$2,829,000	**$1,951,444**
TOTAL	**$26,039,400**	**$20,550,350**	**$3,968,594**

The debt service for the Wright Farm purchase will be paid from the Open Space Reserve, $560,000 of the Community Center Acquisition debt service will be paid from the Historic Resource Reserve, and the remaining debt service payments will be paid from the Unallocated Reserve.

The practice of the Town, based on recommendations from the Appropriation Committee and Capital Expenditures Committee, is to limit the size and duration of debt funded by the CPA to the practical minimum, usually below the maximum that would be allowed by statute. This reduces the potential for long-term financial commitments that would linger should the residents vote to rescind the CPA surcharge in the future. That said, this practice should not be allowed to consign too much of the CPA annual revenue for debt service, which would stifle the ability of the CPC to fund new projects directly with cash.

10(o): Administrative Budget

The Community Preservation Act permits up to 5% of annual CPA funds to be spent on the operating and administrative costs of the CPC. The CPC may pay for staff salaries, mailings, public notices, overhead, legal fees, membership dues, and other miscellaneous expenses related to CPA projects. As in past years, the CPC is requesting an appropriation of $150,000, which is well below the 5% cap. This money will be used to fund the Committee's part-time administrative assistant, membership dues to the non-profit Community Preservation Coalition, administrative expenses, legal and miscellaneous expenses, and land planning, appraisals, and legal fees for open space proposed to be acquired using CPA funds. Funds appropriated for administrative expenses but not spent in a given fiscal year revert to the CPA Undesignated Fund Balance at year's end.

The Committee recommends approval of 10(a-c,e-o) by a vote of (8-0).
The Committee supports indefinite postponement of 10(d).

Article 11
Appropriate for Recreation Capital Projects

Funds Requested	Funding Source	Committee Recommendation
$180,000	**Recreation EF Retained Earnings**	**Approve (8-0)**

Recreation Capital Projects

Description	Funding Request	Funding Source	Brown Book reference
11(a) Pine Meadows Clubhouse	**$100,000**	Recreation EF RE	p. XI-15
11(b) Pine Meadows Equipment	**$80,000**	Recreation EF RE	p. XI-16

This article requests $180,000 from the Recreation Enterprise Fund retained earnings to be used for design and engineering costs required for renovating the clubhouse at the Pine Meadows Golf Course and the purchase of new equipment to maintain the course. These capital investments are described in Section XI of the Brown book, items 17 and 22, respectively. The Recreation Enterprise Fund is funded by user fees. Information on the available balance for this and other enterprise funds may be found in the discussion of Article 5.

The design and engineering costs associated with renovation of the clubhouse at Pine Meadows Golf Club are estimated to be $100,000. The clubhouse was constructed prior to the Town's acquisition of the course in 1988 and needs a complete renovation. Work is anticipated to include renovating the main concourse area and the bathrooms, including plumbing and fixtures, replacing the roof, and making the building ADA-compliant. An additional $80,000 is requested to purchase a new fairway mower and a top dresser machine to replace existing equipment acquired in 2001 and 2012. Life expectancies are 10 years for a fairway mower and 15 years for a top dresser. The new equipment will ensure proper maintenance of the turf, improved pace of play, and superior playing conditions.

The Committee recommends approval by a vote of (8-0).

Article 12
Appropriate for Municipal Capital Projects and Equipment

Funds Requested	Funding Source	Committee Recommendation
$6,758,526	*See below*	**Approve (8-0)**

The aggregate amounts for each funding source are summarized in the following table.

Request	Funding Source	Section
$2,634,022	Tax Levy	(h)
$1,963,000	GF debt	(e), (f), (g)
$1,740,000	Free Cash	(a), (b), (c), (d), (i), (j), (k), (l), (m)
$275,000	Compost Revolving Fund debt	(f)
$130,000	Water EF Retained Earnings	(c), (f)

Request	Funding Source	Section
$16,504	Trans. Network Co. Special Revolving Fund	(j)

The requested appropriations are listed below together with funding breakdown and the Committee's recommendations. For a discussion of the items in this request, please see the Brown Book (relevant pages are listed). The Capital Expenditures Committee Report to the 2020 Annual Town Meeting contains further discussion of these capital requests.

Description	Amount	Funding Source	Brown Book p.	Committee Recommendation
12(a) Ambulance Replacement	**$325,000**	Free Cash	XI-15	Approve (8-0)
12(b) Athletic Fields Feasibility Study	**$100,000**	Free Cash	XI-16	Approve (8-0)
12(c) Hydrant Replacement Program	$75,000 $75,000 **$150,000**	Free Cash Water EF RE	XI-18	Approve (8-0)
12(d) Storm Drainage Improvements and NPDES compliance	**$385,000**	Free Cash	XI-18	Approve (8-0)
12(e) Sidewalk Improvements	**$800,000**	GF debt	XI-6	Approve (8-0)
12(f) Equipment Replacement	$1,038,000 $55,000 $275,000 **$1,368,000**	GF debt Water EF RE Compost RF debt	XI-6	Approve (8-0)
12(g) Townwide Signalization Improvements	$125,000	GF debt	XI-18	Approve (8-0)
12(h) Street Improvements	**$2,634,022**	Tax Levy	XI-17	Approve (8-0)
12(i) New Sidewalk Installations	**$280,000**	Free Cash	XI-17	Approve (8-0)
12(j) Transportation Safety Group	**$16,504**	Trans. Network Co. Special RF	XI-15	Approve (8-0)
12(k) Municipal Technology Improvement Program	**$100,000**	Free Cash	XI-18	Approve (8-0)
12(l) Application Implementation	**$325,000**	Free Cash	XI-19	Approve (8-0)
12(m) Phone Systems & Unified Communications	**$150,000**	Free Cash	XI-19	Approve (8-0)

Street Improvements in item 12(h) will also use $1,072,681 from Chapter 90 state aid which is not subject to appropriation by Town Meeting.

The Committee recommends approval by a vote of (8-0).

Article 13
Appropriate for Water System Improvements

Funds Requested	Funding Source	Committee Recommendation
$2,000,000	**Water EF Debt**	**Approve (8-0)**
$200,000	**Water EF Rates**	
$2,200,000		

This article addresses proposed capital expenditures to be made during FY2021 as part of a continuing program to upgrade and maintain the assets of the Water Enterprise Fund. For general background on the enterprise funds and the relationship between the budget process and the water rate setting process, please see Appendix B and the discussion under Article 5.

Work to Be Done and Funding

A total of $2,200,000 is requested this year to replace unlined or inadequate water mains and deteriorated service connections and to eliminate dead ends in water mains. The details of the projects can be found in the Brown Book, p. XI-8. Capital appropriations for similar purposes have been made in most years over the last decade (except for FY2006 and FY2012, when engineering studies were not ready). The goal is to assure dependable service with high water quality, pressure, and volume for domestic needs, commercial needs, and fire protection, as well as to minimize water main breaks.

Traditionally, the amount requested under this article each year was $1,000,000. Beginning last year, that amount was increased to $2,200,000, and this higher level of capital investment is expected to continue indefinitely. The justification for the substantial increase is an asset management study recently completed by a consultant, the Wright-Pierce environmental engineering firm, which recommended an ongoing annual expenditure of this magnitude to keep Lexington's water system safe and reliable. The asset management plan identifies areas of vulnerability, aging pipe, and areas with low volumes and pressures; and it recommends the replacement of 1% of the Town's water mains on an annual basis (based on an estimated system useful life of 100 years).

In a break from recent practice, it is proposed that this year's maintenance and upgrade work be funded not exclusively with debt, but with a combination of debt ($2,000,000) and cash capital raised in the rates ($200,000). The goal is gradually to completely transition funding of the maintenance program to a cash capital basis. To mitigate pressure on water rates in the short term, the changeover would be phased in over eleven years. See discussion of Article 5 above and Brown Book, p. XI-8.

Rate Implications

This Committee supports the principle of routine capital investment to assure the continued safety, soundness and longevity of the Town's water and wastewater infrastructure. It has also advocated for funding the cost of these long-term maintenance operations—essentially the annual operating expense of the enterprise funds—with cash capital raised directly in the rates charged to users. The current practice of revolving debt financing incurs significant interest expense, which is ultimately passed on to ratepayers. See, e.g., AC Report to 2019 Annual Town Meeting, p. 37: "A sustainable funding strategy would rely on cash capital, funded directly by rate revenue, for the most predictable components of the program."

However, Town Meeting should be aware that the combination of the recent substantial increase in the planned annual expenditure and the changeover in funding to cash capital will have a noticeable impact on water and wastewater rates, both this year and for a number of years going forward. Going forward, the impact on rates should be offset increasingly by lower debt costs and a reduced risk of unscheduled repairs of aging pipes.

Before FY2006, as this Committee has noted in previous reports, capital expenditures for water distribution and related improvements were funded by a combination of enterprise fund cash capital, which was raised in the rates, and borrowing. Subsequently, there was a transition to funding these ongoing improvements exclusively with debt. While that change mitigated rate increases early on, it effectively pushed much of the burden of the program off to future ratepayers, steadily increasing the annual debt service costs of the Water Enterprise Fund, both in dollar and percentage terms.

The proposal now to transition from exclusive debt funding back to cash capital will, conversely, increase the burden on current ratepayers, at least in the short run. This is because, until that transition has been completed, the rates will have to support not only continuing and increasing debt service for past expenditures, but also the cash capital portion of current expenditures. Because the level of annual expenditures for the capital maintenance program recently doubled, the debt service component of the rates will continue to grow, gradually tapering off over the next eleven years as borrowing for that program is reduced. See Brown Book, p. XI-8 (table of projected debt service for the water enterprise fund).

The table in the Brown Book on p. V-27 projects an 8.17% increase in rates for FY2021. We estimate that approximately 2% of this increase is attributable to the new $200,000 in FY2021 cash capital financing.

For the next fiscal year, FY2022, water enterprise debt service is projected to increase by approximately $600,000 (some of which is attributable to other projects).[7] See Brown Book, p. XI-8. This debt service increase, if all authorized debt is issued, would add about 5% to any FY2022 budget increase. The appropriation of an additional $200,000 in cash capital in FY2022, as planned, would add another 1.5% or so for a total increment to the rate increase otherwise required of approximately 6.5%.

Thereafter, the impact on the rates of the increased annual maintenance expenditures and the transition to cash capital should diminish. Since the portion of the maintenance program funded by borrowing will steadily be reduced over the next eleven years, debt service increases for that program should begin to level off and eventually drop. The transition to cash capital, until it is completed, would continue to add each year an increment of $200,000 to the budget, but the percentage impact of that increase on the rates would gradually decline as the total budget grows (unless the annual expenditure level and cash capital component is increased, see Brown Book, p. XI-21). Once the transition has been completed, the continuous funding requirements of the water system maintenance program should be stable, with no impact on rate increases.

Committee Recommendation

Cognizant of these rate pressures, the Committee recommends approval of both the appropriation amount and the funding method requested in this article. Although the recent doubling of the level of annual maintenance and upgrade expenditures was unanticipated, the need for it is well-documented. The changeover to cash capital funding is desirable as it will more transparently and directly reflect the true current cost of system upgrades and maintenance when rates are set, as well as saving interest costs. Finally, the plan to phase the changeover in over an eleven-year period is a reasonable way to avoid the “sticker shock” of the changeover which, if done all at once, would add a one-time increment to the rates of about 20%.

The Committee recommends approval by a vote of (8-0).

[7] In particular, a significant part of the FY2022 projected debt service increase presumably results from the appropriation at last year’s annual town meeting of $2,740,000 in debt for the water enterprise fund’s share of the $5,940,000 automated meter reading project. See FY2020 Brown Book, p. XI-13.

Article 14
Appropriate for Wastewater System Improvements

Funds Requested	Funding Source	Committee Recommendation
$1,301,200	**Wastewater EF Debt**	**Approve (8-0)**
$100,000	**Wastewater EF Rates**	
$1,401,200		

This article addresses proposed capital expenditures to be made during FY2021 as part of a continuing program to upgrade and keep current the assets of the Wastewater Enterprise Fund, including both sewer mains and pumping stations. For general background on the enterprise funds, and the relationship between the budget process and the water rate-setting process, please see Appendix B and the discussion under Article 5.

Work to Be Done and Funding

A total of $1,401,420 is requested this year. $1,000,000 is requested as part of an ongoing, multi-year plan, to investigate the condition of and rehabilitate sanitary sewer infrastructure in order to improve the system's operation, reduce backups and potential overflows, prevent malfunctions, and reduce infiltration, thereby lowering measured flows through the MWRA meter. Another $401,420 is requested as part of an ongoing program to upgrade Lexington's ten sewer pumping stations. The details of both programs, including the expected work sites can be found in the Brown Book, p. XI-9. Capital appropriations for similar purposes have been made in most years (except for FY2006, when engineering studies were not ready, and FY2011, when only pump station upgrades were performed).

In a break from recent practice, as in the case of the Water Enterprise Fund, it is proposed that this year's maintenance and upgrade work be funded not exclusively with debt, but with a combination of debt ($900,000) and cash capital raised in the rates ($100,000). Given that this work is expected to continue at essentially the same level indefinitely, the goal is gradually to transition the funding of this program to a cash capital basis, thereby avoiding interest costs. To mitigate pressure on wastewater rates in the short term, the changeover would be phased in over ten years. *See* Brown Book, p. XI-9. The pump station upgrade program, whose projects occur more sporadically (*see* 5-year capital plan, Brown Book, p. XI-21), would continue to be funded with debt.

Rate implications

The history of funding practices for the wastewater fund is similar to that for the water fund. *See* discussion of Article 13 above. Prior to FY2006, capital expenditures for wastewater distribution system improvements were funded primarily by enterprise fund cash capital, which was raised in the rates. Subsequently, there was a transition to funding these ongoing improvements primarily with debt. While that change mitigated the need for rate increases early on, it effectively pushed much of the burden of the program off to future ratepayers, steadily increasing the annual debt-service costs of the wastewater fund, both in dollar and percentage terms.

The proposal now to transition from exclusive debt funding back to cash capital will, conversely, increase the burden on current ratepayers somewhat, at least in the short run. This is because, until that transition has been completed, the rates will have to support not only continuing debt service for past expenditures, but also the cash capital portion of current expenditures. However, because the level of annual expenditures for wastewater system maintenance is relatively small – less than half that for water system maintenance – and has been level-funded over many years, there should be little or no rate impact from growing debt service for this program, and the phase-in of cash capital at only $100,000 per year would have a less dramatic impact on rates.[8]

Committee Recommendation

The Committee recommends approval of both the appropriation amount and funding method requested in this article. It supports the principle of making, on a regular basis, the capital investment necessary to assure the continued safety, soundness and longevity of the Town's water and wastewater distribution infrastructure. The changeover to cash capital funding is desirable as it will more transparently and directly reflect the true current cost of system maintenance and preservation when rates are set, as well as saving interest costs. Finally, the plan to phase the changeover in over a ten-year period is a reasonable way to avoid the "sticker shock" of the changeover which, if done all at once would add a one-time increment to the rates of about 10%.

The Committee recommends approval by a vote of (8-0).

Article 15
Appropriate for School Capital Projects and Equipment

Funds Requested	Funding Source	Committee Recommendation
$1,299,246	**Free Cash**	**Approve (8-0)**

The requested funds will be used to purchase equipment to aid Lexington Public Schools staff in teaching and administration, to provide devices to be assigned to students to allow for innovative learning methods that integrate supportive technologies, problem-based approaches and higher order thinking skills, and to maintain and upgrade LPS information technology infrastructure.

We note that the funding strategy for annual school technology requests is transitioning from debt to cash capital, which is reasonable given the relatively limited lifetimes of the hardware. For a more detailed list and description of the items in this request, please see the Capital Expenditures Committee Report to the 2020 Annual Town Meeting and the Brown Book page XI-13.

The Committee recommends approval by a vote of (8-0).

Article 16
Appropriate for Public Facilities Capital Projects

Funds Requested	Funding Source	Committee Recommendation
$1,736,285	**Free Cash**	
$5,300,152	**GF Debt**	**Approve (8-0)**
$208,962	**Tax Levy**	
$7,245,399		

This article requests the appropriation of funds for the facilities projects summarized below. For further discussion of items, please see the report of the Capital Expenditures Committee and the Brown Book (page

[8] However, increasing debt service from other previously approved capital projects – in particular that resulting from the appropriation at least year's annual town meeting of $2,470,000 in debt for the wastewater fund's share of the $5,940,000 automatic meter reading project – could have a material impact on this and future years' wastewater rates. *See* Brown Book, p. XI-9, Table III.

numbers provided for reference). This Committee concurs with the rationale advanced by the Capital Expenditures Committee in its report for approving the appropriations listed below.

Project Description	Funds Requested	Funding Source	Brown Book	Committee Recommendation
16(a) Police Outdoor/Indoor Firing Range – Hartwell Avenue	$125,000	Free Cash	XI-13	Approve (8-0)
16(b) Center Recreation Complex Bathrooms & Maintenance Building Renovation	$100,000	Free Cash	XI-14	Approve (8-0)
16(c) Public Facilities Master Plan	$100,000	Free Cash	XI-13	Approve (8-0)
16(d) LHS Science Classroom Space Mining	$150,000	Free Cash	XI-14	Approve (8-0)
16(e) Townwide Roofing Program	$2,010,152	GF Debt	XI-5	Approve (8-0)
16(f) School Building Envelopes and Systems	$239,285	Free Cash	XI-14	Approve (8-0)
16(g) Municipal Building Envelopes and Systems	$208,962	Tax Levy	XI-14	Approve (8-0)
16(h) Facility and Site Improvements Building Floor Program School Paving & Sidewalks Program	 $125,000 $125,000	 Free Cash Free Cash	 XI-14 XI-14	Approve (8-0)
16(i) Public Facilities Bid Documents	$100,000	Free Cash	XI-14	Approve (8-0)
16(j) Public Facilities Mechanical/Electrical System Replacement	$672,000	Free Cash	XI-11	Approve (8-0)
16(k) Westview Cemetery Building Construction	$3,290,000	GF Debt	XI-7	Approve (8-0)

Article 16(k)

The funding source for this article is General Fund Debt, however the Town intends to fund the debt service primarily with fees from the sale of cemetery lots. Staff projections indicate that some additional funding beyond the fee revenue will be necessary, which will be appropriated from the General Fund.

One member of this committee has expressed concern that the nationally declining trend of traditional burials in favor of cremation could lead to decreased fee revenues before the debt is fully paid off. This would require General Fund appropriations larger than the original projections to cover the debt service in later years.

The Committee recommends approval by a vote of (8-0).

Article 17
Appropriate to Post-Employment Insurance Liability Fund

Funds Requested	Funding Source	Committee Recommendation
$750,000	**Tax Levy**	**Approve (8-0)**

Update 1: The size of the appropriation was reduced from $1,935,486 to $750,000. The funding from Free Cash and the enterprise funds was removed from this request and will remain unallocated to provide additional budget flexibility at a later special town meeting. The Committee agrees with the Town Manager that this is a prudent change to the original budget. The Committee's recommendation has not changed.

The PEIL Fund holds funds that will be used in the future to pay for health care benefits for retirees. These benefits make up most of the "other post-employment benefits" (OPEB) that the Town provides as part of the total compensation for its employees. For a detailed discussion of OPEB, the present status of the PEIL Fund, and related issues, please see Appendix F.

The Town of Lexington's future OPEB liabilities are not fully funded. The unfunded liability is the sum of the actuarially determined obligations incurred during current and prior fiscal years that have not been funded (via contributions to the PEIL Fund). Every year, the unfunded liability grows by the present value of future benefits earned during the current year[9], less the value of benefits provided to retirees during the current year through the operating budget, and less any contribution to the PEIL Fund for future liabilities.

If a discount rate of 7.5% is assumed, the requested amount is consistent with the policy previously articulated by the Selectmen for the annual appropriation into the PEIL Fund of 35–100% of the normal cost (see Appendix F), which for FY2021 is projected at $4.8 million.

If approved, this appropriation would increase the balance in the PEIL Fund from the current balance of $19,115,349 as of December 31, 2019, to approximately $19,865,349.

The funding for the request is based on the use of $750,000 from the remaining balance of the Health Insurance Claims Trust Fund[10] to help cover the Town's annual health insurance costs[11]. This use frees up a matching amount in the General Fund for this request or other potential uses.

The original proposed budget requested an additional $1,129,721 from Free Cash, $186,232 of which reflected the amount the Town received in Medicare Part D reimbursements in FY2019 from the federal government. The Town does not anticipate receiving any further Medicare Part D reimbursements since all of the Town's retirees are now on Medicare plans through the Group Insurance Commission (GIC). In addition, the original request included contributions from the Water Enterprise Fund and Wastewater Enterprise Fund to fund the liabilities for benefits of the employees of the respective departments.

The Committee recommends approval by a vote of (8-0).

Article 18
Rescind Prior Borrowing Authorizations

Funds Requested	Funding Source	Committee Recommendation
None	**N/A**	**IP**

State law requires that Town Meeting vote to rescind the unissued portions of borrowing authorizations (appropriations funded by debt) that are no longer required for the purpose stated in the authorization. Rescinding these authorizations is the final bookkeeping task for all debt-based appropriations.

As of press time, staff has presented no prior borrowing authorizations requiring rescission to the Committee. If rescissions are requested at Town Meeting, the Committee will revise its recommendation.

The Committee supports indefinite postponement of this article.

[9] The present value of the expected post-retirement benefit obligations attributable to employee service during the fiscal year is referred to as the "normal cost" or "service cost".

[10] The Health Insurance Claims Trust Fund is a reserve fund the Town was required to maintain when it self-insured for health benefits. When the Town joined the fully insured Group Insurance Commission (GIC), it was agreed that the fund would gradually be spent down for employee health benefit costs.

[11] The Health Insurance Claims Trust Fund had a remaining balance of $3,147,322 on December 31, 2018.

Article 19
Establish, Dissolve and Appropriate To and From Specified Stabilization Funds

Funds Requested	Funding Source	Committee Recommendation
See below	*See below*	**19(a,b) Approve (8-0)** **19(c) Approve (6-2)**

Update 1: Article 19(a) to appropriate $1,773,062 into the Capital Stabilization Fund ($164,987 from the Tax Levy and $1,608,075 from the General Fund) was deleted, and subsequent items were renumbered. These funds will remain unallocated to provide additional budget flexibility at a later special town meeting. The Committee agrees with the Town Manager that this is a prudent change to the original budget. The Committee's recommendation on the remaining items has not changed.

State law authorizes towns to create and maintain stabilization funds for both general (the Stabilization Fund) and specified purposes (e.g., the Capital Stabilization Fund). Funds created for specified purposes may only be used to fund those purposes. The Town currently has eight such funds. Appendix E summarizes the laws governing specified stabilization funds and provides a brief history and description of each of the Town's funds, along with the most recent fund balances available.

Town Meeting may create a specified stabilization fund, alter a fund's specified purpose, approve appropriations into a fund, or appropriate money from a fund. Appropriations into specified stabilization funds do not authorize expenditures, but rather are transfers of funds into accounts for specified future uses. Additions or withdrawals not addressed by other specific warrant articles are appropriated in this general article.

As of this update to the report, the motion contains three items:

(a) That $3,500,000 be withdrawn from the Capital Stabilization Fund to mitigate debt service for projects exempt from Proposition 2½.
(b) That $111,922, the first payment received from Brookhaven under an MOU, be appropriated into the Affordable Housing Capital Stabilization Fund. Note that the Fund currently has a zero balance.
(c) That $111,000 be appropriated from the Affordable Housing Capital Stabilization Fund for renovations and capital improvements at properties managed by the Lexington Housing Assistance Board, Inc. (LexHAB).

The proposed $3.5 million withdrawal is to address higher exempt debt service cost associated with the New Hastings Elementary School, construction of the Lexington Children's Place School, and the new Fire Headquarters.

Item 19(b) will appropriate funds received under an MOU from Brookhaven at Lexington into the Affordable Housing Capital Stabilization Fund, which has a zero balance. When Brookhaven at Lexington secured approval in 2017 for an addition to its facility, it signed an agreement with the Town under which it would make payments over 15 years to the Town to be used by LexHAB for "affordable housing purposes," with the payments to start when a unit in the new addition first received a Certificate of Occupancy.

In the future, we expect these payments from Brookhaven at Lexington will be transferred into the Affordable Housing Capital Stabilization Fund without appropriation.

The Committee unanimously supports items 19(a) and 19(b).

Item 19(c) would appropriate $111,000 of the money deposited under item 19(b) to fund renovations and capital improvements in affordable units managed by LexHAB. This request is supported by a majority of the Committee, who believe that renovation of existing units is a legitimate use of the funds. Town Counsel has also opined that the proposed uses are permissible under both the MOU and the specified stabilization fund's statement of purpose. The Select Board originally suggested, and unanimously supports, this use of funds.

Members in opposition believe that the spirit of the agreement with Brookhaven, under which payments were determined using the estimated cost of creating 5.5 affordable units, requires that these funds be devoted to constructing new units, rather than renovations or improvements on existing units.

The table below summarizes the requested appropriations along with recent fund balances. The third column shows requested additions or withdrawals (parenthesized). The last three rows of the table list, for information purposes, withdrawals from three other stabilization funds requested under Article 4 and Article 20.

Stabilization Fund	Fund Balance 3/12/2020	Deposit (Withdrawal)	Source/Destination	Committee Recommendation
Capital	$25,158,929	**($3,500,000)**	Exempt debt payments (Article 4)	**Approve (8-0)**
Affordable Housing Capital	$0	**$111,922**	Payment from Brookhaven MOU	**Approve (8-0)**
		($111,000)	LexHAB affordable housing	**Approve (6-2)**
Debt Service	$437,058	($124,057)	Offset debt payments for 2003 school projects	*See Article 20*
Visitors Center Capital	$215,549	($200,000)	Debt service for new Visitors Center	*See Article 4*
Transportation Demand /Public Transportation	$376,127	($141,000)	Lexpress and contribution to REV shuttle	*See Article 4*

Any additional payments received prior to the vote on this article will be deposited into special revenue accounts. If necessary, the motion will be updated to include additional transfers into the specified stabilization funds.

The Committee recommends approval of 19 (a) and (b) by a vote of (8-0).
The Committee recommends approval of 19 (c) by a vote of (6-2).

Article 20
Appropriate From Debt Service Stabilization Fund

Funds Requested	Funding Source	Committee Recommendation
$124,057	**DSSF**	**Approve (8-0)**

In August 2006, the Town received a lump-sum reimbursement of approximately $14 million from the Massachusetts School Building Authority (MSBA) to cover its remaining obligation for construction projects previously completed at Clarke and Diamond Middle Schools and Lexington High School. The Massachusetts Department of Revenue (DOR) required the Town to set aside the excess funds from this upfront reimbursement for these school construction projects, and to apportion those funds over the life of the bonds related to the projects to help fund the debt service.

The 2009 Annual Town Meeting voted to establish a specified stabilization fund under G.L. c. 40 Section 5B called the Debt Service Stabilization Fund (DSSF). The $1,739,894 remaining from the FY2007 set-aside was then appropriated into the DSSF. This fund allows the Town to invest the set-aside funds beyond the one-year arbitrage limit that would otherwise apply. The current balance in the DSSF is $548,390. The bonds for the subject school construction projects mature in 2023, which will also be the final year for the required annual appropriations from the DSSF.

The Committee recommends approval by a vote of (8-0).

Article 21
Appropriate for Prior Years' Unpaid Bills

Funds Requested	Funding Source	Committee Recommendation
None	**N/A**	**IP**

As of publication, no action is anticipated under this article.

The Committee supports indefinite postponement for this article.

Article 22
Amend FY2020 Operating, Enterprise, and CPA Budgets

Funds Requested	Funding Source	Committee Recommendation
$658,950	**State CPA matching funds**	**Approve (8-0)**

As of press time there is one change proposed for the FY2020 CPA budget. It is possible that additional changes will be requested in the motion presented to Town Meeting, at which time the Committee will update its recommendation if needed.

When the 2019 Annual Town meeting passed CPA Article 14, the state match was estimated at $561,000. A year-end surplus in the state budget allowed for legislation to increase the amount of money distributed to municipalities under the CPA. As a result, Lexington's state match increased by $658,950, more than doubling the original estimate. Typically, the state would have disbursed our CPA matching funds in October of last year and the Town would have revised the FY2020 CPA budget during the fall Special Town Meeting, but delays in settling the state budget pushed off distribution of this money until January 2020.

The original FY2020 budget projected $5,686,000 in annual revenue from the CPA surcharge and state matching funds. The additional state matching funds raised the FY2020 CPA revenue to $6,344,950. Following CPA requirements, the Town appropriates 10% of the annual CPA revenue into each of the funds designated for Open Space Reserve, Historic Resources, and Community Housing, with the remaining 70% appropriated into the Unbudgeted Reserve.

To reflect the updated revenue, the appropriations into each of the reserves will be amended such that 10% of the final total revenue ($634,495) is appropriated into each of the three dedicated funds, and the remaining 70% ($4,441,465) is appropriated into the Unbudgeted Reserve.

The Committee recommends approval by a vote of (8-0).

Article 23
Appropriate for Authorized Capital Improvements

Funds Requested	Funding Source	Committee Recommendation
None	**N/A**	**IP**

As of publication, no action is anticipated under this article.

The Committee supports indefinite postponement for this article.

Article 24
Reduce Legal Expenses (Citizen Petition)

Funds Requested	Funding Source	Committee Recommendation
See below	*See below*	**Disapprove (2-6)**

This citizen's petition is premised on the proposition that the Town could achieve cost savings by hiring in-house counsel to perform much of the Town's legal work in lieu of relying exclusively on outside counsel. It seeks to achieve this result by making certain adjustments to the operating budget that is the subject of Article 4.

Specifically, the article asks Town Meeting to reduce the expense line item in the municipal budget for legal services (which funds outside counsel) by $300,000, and to increase the line item which supports the Town Manager's staff (which could be used to hire in-house counsel) by $100,000, for a net budget reduction of $200,000. The underlying assumptions are that $100,000 would be sufficient to hire an in-house lawyer and that outside legal costs would thereby be reduced by 73%, from the budgeted $410,000 to $110,000. The article does not specify what should be done with the resulting surplus from these proposed budget adjustments.[12] It also does not seek any adjustments to the budget of the school department.

Some other municipalities, primarily larger cities and towns such as Boston, Cambridge, Brookline and Newton, employ one or more in-house counsel, and there are some advantages to this arrangement. Given the current economics of the legal profession, in particular the large number of unemployed or under-employed lawyers, it is fair to say that the hourly cost of an in-house lawyer, after accounting for wages and benefits, is substantially less than the hourly cost of outside counsel.[13] It is also likely that a dedicated in-house lawyer would have greater familiarity with Town personnel and practices and be more accessible to Town staff on a day-to-day basis.

There are also some disadvantages. Because in-house counsel deal with the affairs of only a single municipality, rather than a variety of municipalities, they are not likely to have the same breadth of experience as outside counsel. Law firms concentrating in municipal law, having specialists with particular skills and experience in certain areas such as real estate transactions, environmental concerns, or courtroom litigation, can add substantial value to the services provided. It is not clear whether a community the size of Lexington

[12] Among other things, the net $200,000 reduction in the "legal" budget could be used: to increase other line items in the operating budget; to increase the appropriation to the Capital Stabilization Fund currently proposed under Article 19; or to lower the tax rate. Alternatively, it could simply remain unallocated and, if not appropriated at a special town meeting in the fall, flow to Free Cash at the end of the fiscal year.

[13] The proponent has brought to this Committee's attention on numerous occasions classified advertisements placed in the *Massachusetts Lawyers Weekly* by municipalities seeking to hire in-house counsel at a very modest salary level, and these positions presumably do not go unfilled.

would have enough “routine” legal work to occupy an in-house lawyer full-time. And if the work of a particular outside law firm, or a lawyer within a firm, should be found wanting, it would be far easier and less disruptive to replace that firm or lawyer than it would be to discharge a Town employee and find a suitable replacement. The choice between the two approaches is, at best, a judgment call.

The Town’s governing statute, the Selectmen-Town Manager Act, confers the responsibility for engaging counsel not on Town Meeting but on the Select Board and the Town Manager. Section 2(b) of that Act provides that “[the Select Board] shall appoint… a town counsel.” Section 9(h) provides that “[t]he town manager shall… have the authority… to employ special counsel with the approval of the [Select Board] to assist the town counsel whenever in his judgment it may be necessary.”

Given this statutory mandate, a majority of this Committee believes it is the prerogative of the Select Board and the Town Manager, acting as the “executive branch” responsible for managing the day-to-day affairs of the Town, to determine how best to meet the Town’s needs for legal representation.[14] While it might be reasonable for Town Meeting to adopt a non-binding a resolution urging a different approach, the majority believes it is neither appropriate, nor in the best interests of the Town, as long as the Select Board’s judgment is reasonable, for Town Meeting to try to force a change in this hiring policy through changes in the budget.

A minority supports this request on the grounds that (1) a substantial portion of the town’s legal services are of a routine nature (i.e. not specialized as in bond or labor counsel), (2) the amount spent on routine legal services is substantial enough that use of in-house counsel would yield a savings, (3) a significant pool of qualified candidates exists from which to hire in-house counsel, (4) free external resources exist to support in-house counsel in their dealings with routine legal services, and (5) outside counsel could still be maintained for litigation or complex legal problems.

The Committee recommends disapproval by a vote of (2-6).

Article 25
Purchase of Land/Eminent Domain

Funds Requested	Funding Source	Committee Recommendation
$177,000	**Parking Meter Fund**	**Approve (8-0)**

This article seeks $177,000 to purchase from the Lexington Historical Society (LHS) a portion of land adjacent to their headquarters and in the Center Business District. The town has had 16 2-hour parking meters on this land for decades, and now as part of the Grain Mill Alley improvement project wants to install an alternative transportation node on a small portion of the property.

This small triangular parcel is 3,791 sq. ft., and is bounded by the Minuteman Commuter Bikeway, Edison Way, the entrance to the Depot Square Attended Parking Lot, and the Grain Mill Alley path across the Bikeway.

[14] In fulfillment of that responsibility, the Select Board has periodically convened special committees to examine the issue and make recommendations. Those committees, while recognizing that there may be reasonable alternatives, have consistently recommended continuation of the current arrangements.

Source: `https://lexingtonma.mapgeo.io/`

In 1959 the B&M Railroad discontinued use of the Lexington Depot building and sold it and its land, along with this parcel to Depositors Trust Company. In 1999 Depositors closed this branch and sold their holdings to the LHS.

The Town enjoyed public use and access of this property while the Trust Co. occupied the building. With permission of the landowner, the Town installed parking meters during Central Business District Improvements in the mid 1960's. The town has maintained the parking spaces and adjacent landscaping, cleared the snow, and collected meter revenue. The LHS continued to allow public access and for this use to continue.

At the 2015 Annual Town Meeting, Article 8(o) appropriated CPA funds to design improvements to either end of Grain Mill Alley. At the 2016 Annual Town Meeting, Article 8(o) appropriated CPA funds to implement the design, including building an alternative transportation node adjacent to the Bikeway, on both town land and also a small portion of this land owned by the LHS. This node would include bike racks, a bike repair station, and seating. The Town's efforts to gain permission from the LHS to build the node on their property culminated in negotiations for sale of the entire parcel to the Town. The selling price was reached by averaging two independent appraisals done by LHS and the Town.

The Committee recommends approval by a vote of (8-0).

Article 34
Authorize Special Legislation—Development Surcharge for Community Housing (Citizen Petition)

Funds Requested	Funding Source	Committee Recommendation
None	N/A	**Pending**

This article proposes special legislation that attempts to mitigate the loss of moderate-income housing in Lexington by establishing a targeted and measured surcharge on specific residential development activities. This surcharge would fund the creation of community housing to address identified housing gaps, such as the need for housing attainable by Lexington municipal and school employees.

The residential housing market in Lexington has been strong for the past ten years due to the abundance of high-paying jobs in greater Boston area, proximity to cultural and historical attractions, high-performing Lexington public schools, and a high level of municipal services. With a declining number of buildable lots and an increasing rate of teardowns for existing old homes, residential houses for sale have tended to become bigger and more expensive, putting them out of reach for most low- and moderate-income buyers in the area.

To mitigate the loss of moderate-incoming housing resulting from the high demand for buildable parcels of land, this article would establish a residential linkage fee, "the community housing surcharge," to be added to building permit fees for all new single- and two-family residential construction where an existing single- or two-family dwelling had been demolished.

The Select Board would determine the amount of the community housing surcharge. That charge would vary depending on the certified total gross floor area of the structure or structure permitted by a building permit, and/or the specific type of real estate transaction. The Select Board would evaluate and adjust the rate of the community housing surcharge for inflation annually. The Select Board would be authorized to adopt additional requirements, exemptions, and regulations to implement or enforce the community housing surcharge.

The Committee notes that the article does not specify a limit on the magnitude of the surcharge, but this could be amended by the Select Board.

The building commissioner of the Town of Lexington would not issue a certificate of occupancy for a building until the applicable community housing surcharge required was paid in full. Alternatively, an applicant intending to reside in the home could opt to have the amount of the surcharge added to the real estate taxes on the property, in which case it would not be due and payable until a sale of the home to a third party. If such an election were made, 20% of the surcharge would be abated each year for five years until fully abated. The goal would be to limit the application of the charge to those building on spec.

The article contemplates that all received surcharges would be deposited into the Affordable Housing Capital Stabilization Fund (AHCS) for future use. A two-thirds vote of Town Meeting would be required to dedicate such a revenue stream, once established, to the ACHS on an ongoing basis; and a two-thirds vote would be required to remove funds from the ACHS for a particular use or otherwise change the fund.

This article requests authorization for the Select Board to petition the Massachusetts General Court to enact special legislation enabling the surcharge described above. The Select Board would be authorized to approve amendments to the requested legislation, before its enactment by the General Court, as long as such amendments were within the scope of the general objectives of the motion.

The Committee has not taken a position on this article as of press time.

Appendix A: 5-Year Budget Projections

For the past two decades, the Appropriation Committee has prepared budget projections that were presented in appendices to the Committee's annual ATM reports. At the time those projections started, Town staff did not publish any comparable projections. More recently, however, the Town's Finance Department has begun to prepare its own forecasts for use in the Budget Summit process in preparation for the next fiscal year's proposed budget. Projections for FY2021were presented at the first budget summit held on October 30, 2019. Subsequently, the department made modest revisions to reflect the proposed budget for FY2021 presented in the Brown Book.

Rather than prepare separate projections for Town Meeting, this year we summarize the Finance Department's projections and discuss their implications in planning for future Town budgets.

Budget figures in the tables in this appendix are given in thousands of dollars.

Summary of Projections

Table A-1 summarizes total revenues and expenses, showing actual results for FY2018-19, revised budgeted figures for FY2020 (still underway), the proposed budget for FY2021 presented in the Brown Book, and projected figures for FY2022-FY2025. The bottom line shows the net surplus(deficit). For FY2018 and FY2019, the Town ran substantial overall surpluses, about 4% of expenses in FY2018 and almost 5% in FY2019. These surpluses were then available for the Town in the next year in the form of free cash. For FY2020, currently underway, the revised budget shows income and expenses in balance, as required under state law. However, it is likely that the fiscal year will end with a surplus because Town budgets are generally conservative in the sense that they strive not to overestimate revenues or underestimate expenses to ensure that the Town does not run a deficit (which is forbidden under state law). Similarly, the recommended budget for FY2021 is balanced, and it seems likely that the final actual figures will result in a surplus as a result of the Town's conservative approach to budgeting.

Table A-1. Actual and Projected Revenues and Expenses

	FY2018 Actual	FY2019 Actual	FY2020 Revised	FY2021 Proposed	FY2022 Projection	FY2023 Projection	FY2024 Projection	FY2025 Projection
Total Revenues	$ 216,614	$ 224,456	$ 229,337	$ 237,621	$ 243,178	$ 249,870	$ 258,298	$ 266,032
Total Expenses	$ 208,347	$ 214,002	$ 229,337	$ 237,621	$ 249,716	$ 258,980	$ 269,554	$ 276,650
Revenue-Expenses	$ 8,267	$ 10,454	$ (0)	$ (0)	$ (6,538)	$ (9,110)	$ (11,257)	$ (10,618)
As percent of expenses	4.0%	4.9%	0.0%	0.0%	-2.6%	-3.5%	-4.2%	-3.8%

The projections beyond the FY2021 budget under consideration show projected expenses exceeding projected revenues, yielding deficits ranging from 2.9% of expenses in FY2022 to 4.4% in FY2024. However, any projection of revenues or expenses is subject to considerable uncertainty, as we discuss in greater detail below. When the time comes to prepare a budget for one of those years, if the projection still indicates a deficit, changes will have to be made to bring budgeted expenses and revenues into line with one another. We note that the projections originally presented at the first budget summit in October 2019 for FY2021 showed a deficit of just under $2 million, but a combination of adjustments, including limited program improvements and reduced contributions to some reserve accounts, brought that budget into balance.

Projections, particularly those several years out, are subject to substantial uncertainties, however the projected deficits suggest a modest revenue increase and the need to control costs. We present the projections in more detail below.

Projected Revenues

Table A-2a shows projections of various revenue categories and provides notes on the assumptions behind those projections. Property taxes dominate revenues, accounting for 78% of total revenues in FY2018 (actuals) rising to 84% in the projection for FY2025. As a result, the assumptions concerning property tax revenues are critical to the projections.

Table A-2a. Projected Revenues by Category

	Revenue Category	FY2018 Actual	FY2019 Actual	FY2020 Revised	FY2021 Proposed	FY2022 Projection	FY2023 Projection	FY2024 Projection	FY2025 Projection
1	Property Tax Levy	$ 169,332	$ 176,841	$ 184,822	$ 192,312	$ 199,870	$ 207,616	$ 215,557	$ 223,696
2	State Aid	$ 15,737	$ 16,013	$ 16,283	$ 16,518	$ 16,733	$ 16,952	$ 17,171	$ 17,392
3	Local Receipts	$ 16,739	$ 16,969	$ 14,082	$ 14,281	$ 14,498	$ 14,694	$ 14,930	$ 15,174
4	Available Funds	$ 15,159	$ 15,059	$ 14,314	$ 14,942	$ 12,493	$ 11,007	$ 11,021	$ 10,285
5	Revenue Offsets	$ (2,027)	$ (2,074)	$ (1,861)	$ (2,181)	$ (2,217)	$ (2,255)	$ (2,293)	$ (2,483)
6	Other Revenues	$ 1,674	$ 1,647	$ 1,696	$ 1,749	$ 1,802	$ 1,856	$ 1,912	$ 1,969
7	**Total Revenues**	**$ 216,614**	**$ 224,456**	**$ 229,337**	**$ 237,621**	**$ 243,178**	**$ 249,870**	**$ 258,298**	**$ 266,032**

Notes on assumptions

1	Property Tax Levy	Reflects statutory allowable growth of 2.5% and assumed new growth of $2.75 million annually.
2	State Aid	Assumes FY2020 Chapter 70 aid increasing at $25 per pupil Minimum Aid in FY2022-25.
3	Local Receipts	Assumes modest growth in local receipts based on evaluation of historical averages.
4	Available Funds	Free Cash estimate of $10,500,000 available for FY2022 and $9,000,000 for FY2023-2025. Annual contributions of $141,000 from TDM Stabilization Fund to support Lexpress and the Alewife Shuttle, $385,000 from Parking Fund to support Traffic Bureau and snow removal; and $50,000 from Cemetery Fund to support Cemetery Division. In FY2021-2023, $750,000 annually from balance of Health Claims Trust Fund to be used to fund health insurance, resulting in an equal amount in the tax levy becoming available to fund contributions to OPEB Trust per BOS policy. Includes in FY2021-FY2025 use of Capital Projects Stabilization Fund to offset within-levy debt service, as detailed in Line 14.
5	Revenue Offsets	$750K for overlay (property tax abatement and exemptions) in FY2021-25. $400K set-aside for snow & ice deficit
6	Other Revenues	Assumes FY2021 Water, Sewer and Recreation Indirects increasing by 3% annually.

Source: Lexington Finance Department

Table A-2b shows the projected year-to-year percentage increases in the various revenue categories. Note that Property Tax Levy and State Aid grow more slowly from FY2022–FY2025 than in the earlier years. In both cases, the differences appear to reflect conservative assumptions, which we discuss in more detail below for property tax revenues. The other notable change is in Available Funds, which shrink in several of the projected years due to lower levels of free cash. This is due to some of the more aggressive changes noted above to close the shortfall in the FY2021 proposed budget, which will lower free cash for the next fiscal year.

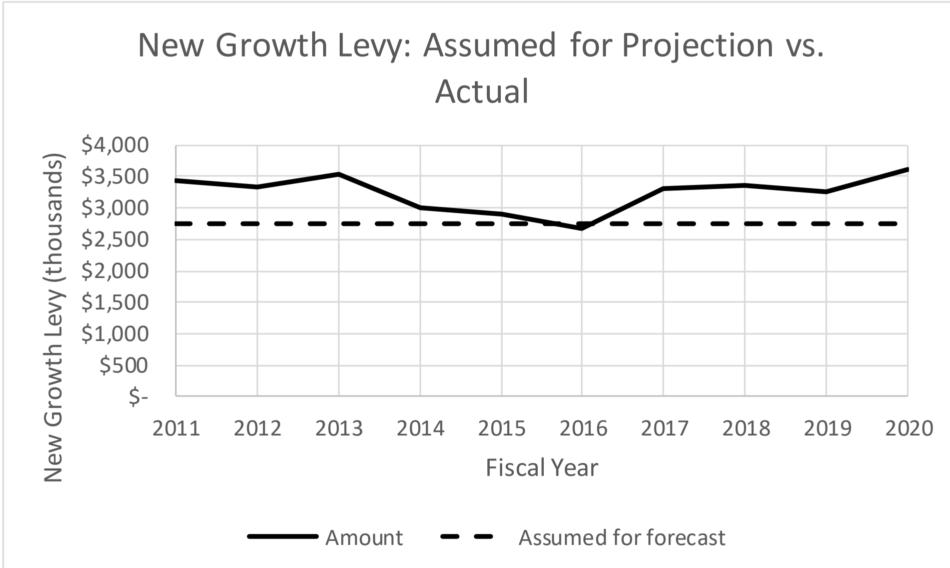
Table A-2b. Annual Rates of Increase in Revenues

	Revenue Category	FY2019 Actual	FY2020 Revised	FY2021 Proposed	FY2022 Projection	FY2023 Projection	FY2024 Projection	FY2025 Projection
1	Property Tax Levy	4.4%	4.5%	4.1%	3.9%	3.9%	3.8%	3.8%
2	State Aid	1.8%	1.7%	1.4%	1.3%	1.3%	1.3%	1.3%
3	Local Receipts	1.4%	-17.0%	1.4%	1.5%	1.4%	1.6%	1.6%
4	Available Funds	-0.7%	-4.9%	4.4%	-16.4%	-11.9%	0.1%	-6.7%
5	Revenue Offsets	2.3%	-10.3%	17.2%	1.7%	1.7%	1.7%	8.3%
6	Other Revenues	-1.6%	3.0%	3.1%	3.0%	3.0%	3.0%	3.0%
7	**Total Revenues**	**3.6%**	**2.2%**	**3.6%**	**2.3%**	**2.8%**	**3.4%**	**3.0%**

Note: Each entry shows the percentage change from the previous year, calculated from Table A-2a.

Proposition 2½ limits growth in the property tax levy to 2.5% each year plus an allowance for growth in the tax base resulting from capital investment, e.g., construction and renovation, commonly called "New Growth." The limit on the tax levy may be temporarily exceeded to cover debt service on projects that are deemed exempt from Proposition 2½ as the result of a town-wide referendum. In addition, a successful operating override referendum can permanently increase the tax levy limit.

Leaving aside exempt debt service and operating overrides, New Growth is the key determinant of increases in property tax revenues. The Finance Department's projections assume that New Growth will be $2.75 million per year, up slightly from the $2.5 million assumed in recent prior years. As shown in the figure below, this assumption is conservative in the sense that it is lower than the actual new growth in nine of the last ten fiscal years.



The average for New Growth over the last ten years was $3.24 million. If we use this average rather than the assumed $2.75 million, this results in an additional $490,000 per year in projected revenue, which is further compounded by the 2.5% annual increase in the tax levy.

The Finance Department's projection assumes that the conservative figure assigned for New Growth in the budget can be used as a valid projection, but in the long run this will underestimate future tax revenue. The budget for New Growth is intentionally set well below the expected value as a safeguard against a budget shortfall, which could result if actual New Growth fell below the budgeted amount. The projection should instead be based on measurable trends, including, but not limited to, the long-term average for New Growth[15]. Table A-3 shows the cumulative increase in projected revenues over five years, which grows to $2,576,000 by FY2025. This represents roughly 25% of the projected revenue gap shown in Table A-1.

Table A-3. Impact of Using Historical Average of New Growth Levy
Rather than Assuming $2.75 million per Year.

	2021	2022	2023	2024	2025
Annual increment	$490	$490	$490	$490	$490
Cumulative impact	$490	$992	$1,507	$2,035	$2,576

Notes:
Amounts shown in thousands of dollars.
Annual increment = difference between historical average and value assumed in projection
Cumulative impact = prior balance x 1.025 + annual increment

It is more difficult to evaluate the assumptions regarding the projections of other revenue categories, but we note that past forecasts for those other categories have not been consistently low or high.

However, for total revenues, in the last three completed fiscal years (FY2017–FY2019), actual revenues have been higher than projected, especially for projections made several years in advance. For example, projections for FY2019 made in 2015 were 11% below actuals and those for FY2018 made in 2014 were 4.2% lower than the actual.

[15] Sadly, the COVID-19 outbreak may herald a sharp and prolonged divergence from recent trends in commercial activity, new growth, and state aid. We have *not* attempted to incorporate such changes into this year's projections.

Projected Expenses

Table A-4a shows the Finance Department's expense projections by category.

Table A-4a. Projections of Expenses

	Expense Category	FY2018 Actual	FY2019 Actual	FY2020 Revised	FY2021 Proposed	FY2022 Projection	FY2023 Projection	FY2024 Projection	FY2025 Projection
	Education	*$103,922*	*$108,677*	*$116,024*	*$121,221*	*$128,812*	*$133,965*	*$139,297*	*$145,570*
8	LPS Wages	$85,176	$90,272	$95,442	$98,932	$104,135	$107,421	$109,762	$113,808
9	LPS Expenses	$17,076	$16,280	$18,112	$19,425	$21,528	$23,080	$25,724	$27,570
10	Minuteman	$1,670	$2,126	$2,470	$2,863	$3,149	$3,464	$3,811	$4,192
	Municipal	*$46,452*	*$48,216*	*$52,217*	*$53,792*	*$55,732*	*$57,484*	*$59,293*	*$61,071*
11	Municipal Wages	$30,493	$30,964	$32,511	$33,520	$34,776	$35,785	$36,782	$37,669
12	Municipal Expenses	$15,959	$17,252	$19,706	$20,271	$20,956	$21,700	$22,512	$23,402
	Shared Expenses	*$57,973*	*$57,109*	*$61,096*	*$62,608*	*$65,172*	*$67,531*	*$70,964*	*$70,010*
13	Debt Service	$6,712	$7,228	$7,619	$8,114	$8,261	$8,674	$9,107	$9,563
14	Mitigated Within Levy	$325	$574	$0	$0	$0	$0	$0	$0
15	Land Purchase Note	$2,351	$3,050	$2,235	$2,403	$2,320	$0	$0	$0
16	OPEB	$1,830	$1,830	$1,880	$1,930	$1,980	$2,030	$2,080	$2,130
17	Retirement	$5,713	$5,955	$6,421	$6,701	$7,122	$7,472	$6,473	$1,680
18	*Benefits*	*$24,651*	*$25,404*	*$29,005*	*$30,188*	*$31,685*	*$33,256*	*$34,905*	*$36,636*
18a	Medicare	$1,677	$1,759	$1,911	$1,996	$2,096	$2,201	$2,311	$2,426
18b	Health Insurance	$21,950	$22,586	$25,952	$27,027	$28,378	$29,797	$31,287	$32,851
18c	Dental	$1,003	$1,038	$1,117	$1,140	$1,185	$1,233	$1,282	$1,333
18d	Life	$21	$20	$25	$25	$25	$25	$25	$25
19	Reserve Fund	$0	$0	$900	$750	$750	$750	$750	$750
20	Workers' Comp.	$613	$554	$887	$875	$901	$928	$956	$985
21	Unemployment	$182	$138	$200	$200	$200	$200	$200	$200
22	Property & Lib. Ins.	$713	$733	$882	$845	$887	$932	$978	$1,027
23	Uninsured Losses	$107	$112	$250	$250	$250	$250	$250	$250
24	Solar Production	$355	$352	$410	$410	$410	$410	$410	$410
25	Capital	$6,422	$7,549	$8,137	$7,744	$8,466	$9,190	$9,914	$9,939
26	Other	$311	$70	$0	$200	$215	$215	$215	$215
27	Approp. to Capital Stab.	$7,690	$3,560	$2,269	$1,773	$1,500	$3,000	$4,500	$6,000
28	Unallocated Revenue	$0	$0	$0	$225	$225	$225	$225	$225
29	**Total Expenditures**	**$208,347**	**$214,002**	**$229,337**	**$237,621**	**$249,716**	**$258,980**	**$269,554**	**$276,650**

Table A-4b provides the department's notes on the assumptions underpinning the projections.

Table A-4b. Notes on Projected Expenses

Expense Category	Notes on Assumptions
Education	
8 LPS Wages	Illustrates a level-services budget and does not include program improvements. Includes a 2.5% increase on base budget for step increases and ($750,000) for annual staff turnover savings. Assumes anticipated funding for unsettled contracts in FY2021-25. Includes additional staffing due to projected enrollment increases in FY2021-25 based on preliminary FY2020 Enrollment projections from Oct. 1 data. Recurring additional staff-related costs are inclusive of benefits, workers comp., and Medicare.
9 LPS Expenses	Program budget per pupil rates are adjusted by 2.2% Consumer Price Index (CPI) in FY2021 and 2.40% in FY2022-25; applied against preliminary projected enrollment levels. All other lines adjusted by 2.2% in FY2021 and 2.4% in FY2022-25. Special Education Out-of-District Tuition and Transportation lines are projected based on program trends. Approximately 81-85% of total expense line increases are driven by these budget lines (FY2021-25).
10 Minuteman	FY2022-25 projections increase by 10%.
Municipal	
11 Municipal Wages	Projections based on step increases for current staff, settled collective bargaining contracts, and anticipated contract settlements for out-years.
12 Municipal Expenses	Level-service budget using CPI of 7% for electricity, 5.5% for natural gas, 20% for IT software expenses as the Town transitions to the Cloud, and 1.8% for all other expenses.
Shared Expenses	
13 Debt Service	Within levy debt service is projected to grow by 5% annually. Amounts above that will be mitigated by use of the Capital Stabilization Fund.
14 Mitigated Within Levy Debt Service	Within levy debt service mitigated by use of the Capital Stabilization Fund. FY22-25 left as $0 to not dilute the rest of the projections.
15 Land Purchase Note Retirement	Use of Free Cash to pay down short-term notes issued to pay for the land purchases at 173 Bedford St. and Pelham Rd.
16 OPEB	Continued funding of OPEB - increasing by $50,000 per year
17 Retirement	Contributory Retirement assessment (based on 2024 amortization of unfunded liability and 7.50% interest rate assumption) plus Non-Contributory payments
18 Benefits	
18a Medicare	5% increase in Medicare, reflecting an increase in the number of eligible employees and increases in wages.
18b Health Insurance	FY2021, growing at 5% annually.
18c Dental	FY2021, growing at 4% annually.
18d Life	Level Funding
19 Reserve Fund	Level Funding
20 Workers' Comp.	FY2021 base growing at 3% annually. As a continuing balance account, full appropriation is effectively spent each year; "actual" values reflect current year spending. Balance as of 6/30/19 = $1.5M.
21 Unemployment	Level Funding
22 Property & Lib. Ins.	Reflects additional expenses for new buildings (LCP, Fire Station, Hastings), with 5% growth in out-years
23 Uninsured Losses	Level Funding. As a continuing balance account, full appropriation is effectively spent each year; "actual" values reflect current year spending. Balance as of 6/30/19 = $1.06M.
24 Solar Production	Payments to Syncarpha for construction costs of Hartwell Ave. solar arrays.
25 Capital	Includes $4.9M for cash capital in FY2021; $5.6M in FY2022, $6.3M in FY2023 and $7.0M in FY2024-25 from
26 Other	Reflects various warrant articles such as Senior Tax Work-Off and $200K in unanticipated needs in FY2021-25.
27 Approp. to Capital Stab. Fund	Reflects past and projected transfers to continue funding the Capital Stabilization Fund to cover the high school project.
28 Unallocated Revenue	Proposed allocation set-aside for yet to be determined priorities.

Source: Lexington Department of Finance

To simplify the discussion of the expense projections, Table A-5a aggregates the expense categories from Table A-4a. The three major groupings are Education, Municipal, and Shared Expenses. For Education, we show LPS and Minuteman separately. We provide a further breakdown for shared expenses, breaking out appropriations for capital projects and to the Capital Stabilization Fund and OPEB, all three of which are determined by explicit policy decisions, some of which are made after the Town knows actual new growth and the amount by which actual expenses are less than budgeted. The "other" shared expenses are dominated by employee benefits, the largest component of which is Health Insurance costs.

Table A-5a. Expense Projections Aggregated

Expense Category	FY2018 Actual	FY2019 Actual	FY2020 Revised	FY2021 Proposed	FY2022 Projection	FY2023 Projection	FY2024 Projection	FY2025 Projection
Education	*$103,922*	*$108,677*	*$116,024*	*$121,221*	*$128,812*	*$133,965*	*$139,297*	*$145,570*
LPS	$102,252	$106,551	$113,554	$118,358	$125,662	$130,500	$135,486	$141,378
Minuteman	$1,670	$2,126	$2,470	$2,863	$3,149	$3,464	$3,811	$4,192
Municipal	$46,452	$48,216	$52,217	$53,792	$55,732	$57,484	$59,293	$61,071
Shared Expenses	*$57,973*	*$57,109*	*$61,096*	*$62,608*	*$65,172*	*$67,531*	*$70,964*	*$70,010*
OPEB	$1,830	$1,830	$1,880	$1,930	$1,980	$2,030	$2,080	$2,130
Capital	$6,422	$7,549	$8,137	$7,744	$8,466	$9,190	$9,914	$9,939
Capital Stabilization Fund	$7,690	$3,560	$2,269	$1,773	$1,500	$3,000	$4,500	$6,000
Other	$42,032	$44,169	$48,809	$51,162	$53,226	$53,312	$54,470	$51,941
Grand total	**$208,347**	**$214,002**	**$229,337**	**$237,621**	**$249,716**	**$258,980**	**$269,554**	**$276,650**

Amounts in *italics* are subtotals and are not included in total
Source: Aggregation of values in Table 4a.

Table A-5b shows the year-to-year percentage increases in the various aggregated categories. Education expenses are projected to grow more rapidly than municipal expenses. Within education, the Town's contribution to Minuteman is projected to rise substantially more rapidly than the budgets for LPS. The Town plans to increase OPEB contributions at $50,000 per year, a modest annual rate of about 2.5%.

Table A-5b. Annual Rates of Increase in Expenses

Expense Category	FY2019 Actual	FY2020 Revised	FY2021 Budget	FY2022 Projection	FY2023 Projection	FY2024 Projection	FY2025 Projection
Education	4.6%	6.8%	4.5%	6.3%	4.0%	4.0%	4.5%
LPS	4.2%	6.6%	4.2%	6.2%	3.9%	3.8%	4.3%
Minuteman	27.3%	16.2%	15.9%	10.0%	10.0%	10.0%	10.0%
Municipal	3.8%	8.3%	3.0%	3.6%	3.1%	3.1%	3.0%
Shared Expenses	3.8%	8.3%	3.0%	3.6%	3.1%	3.1%	3.0%
OPEB	0.0%	2.7%	2.7%	2.6%	2.5%	2.5%	2.4%
Capital	17.6%	7.8%	-4.8%	9.3%	8.5%	7.9%	0.2%
Capital Stabilization Fund	-53.7%	-36.3%	-21.9%	-15.4%	100.0%	50.0%	33.3%
Other	5.1%	10.5%	4.8%	4.0%	0.2%	2.2%	-4.6%
Grand total	2.7%	7.2%	3.6%	5.1%	3.7%	4.1%	2.6%

Note: Each entry shows the percentage change from the previous year, calculated from Table A-5.

Planned contributions to the Capital Stabilization Fund to reduce the future impacts on taxes of the High School project show the greatest volatility, continuing to fall through FY2022 and then rising for the remaining three years. Even in FY2025, however, the planned contribution is lower than the actual in FY2018 (and the actuals in FY2016-18, not shown in the tables). Other shared expenses are projected to rise at relatively low rates and to actually decline in FY2025, reflecting primarily two factors: (1) the land-purchase notes are expected to be fully retired in FY2022, dropping projected payments to zero in FY2023–FY2025, and (2) the Town expects to complete the retirement of its unfunded liability for pension funds in FY2024, allowing contributions to fall to the level needed to cover liabilities incurred from each additional year of employment starting in FY2025.

Concluding Remarks

The Finance Department's projections appear to suggest that over the next half-decade, the Town will have to find ways to reduce expenses or increase revenues to maintain a balanced budget as required by state law. However, our review suggests that the problems may be less severe than they appear because the Town follows a fairly conservative approach in forecasting revenues.

To address the financial strains suggested by the projections, some combination of actions may be needed to meet balanced budget requirements, such as:

1. Improving efficiency so that the same services can be provided with fewer resources. Such opportunities may well prove elusive.

2. Creating additional sources of revenue. There may be opportunities to increase some fees or add new ones, but it is not clear that there are opportunities for significant increases.
3. Reducing service levels.
4. Relaxing of some of the goals embodied in the Town's fiscal policies, e.g., curtailing contributions to the Capital Stabilization Fund or other reserves.
5. Passing Proposition 2½ operating override(s) to permanently boost annual property tax revenue.

Each of these alternatives involves important tradeoffs that we will not discuss here.

It is also important to note that actions to reduce operating expenses or increase recurring annual revenues in one year will generally carry forward to reduce future deficits. For example, reductions in service levels, if not restored, will reduce future deficits without additional action in later years.

However, actions to eliminate a projected deficit in one year that affect only budgeted revenues or expenses and not actuals generally will not carry forward because they will reduce the end-of-year budgetary surplus and thereby lower the carryover of funds that would then be available for expenditure the next year.

Appendix B: Enterprise Funds

The Town of Lexington has maintained Water, Wastewater (Sewer), and Recreation Enterprise Funds since the state legislature enacted legislation authorizing such funds, G.L. c. 44, § 53F ½, in the late 1980's. An enterprise fund "establishes a separate accounting and financial reporting mechanism for municipal services for which a fee is charged in exchange for goods or services. Revenues and expenses of the service are segregated into a fund with financial statements separate from all other governmental activities" and are accounted for on an accrual basis. *DOR Enterprise Funds Manual (April 2008)*. An enterprise fund provides management and taxpayers with information to measure performance, analyze the impact of financial decisions, and determine the cost of providing a service. Enterprise funds may be operated on a stand-alone basis, *i.e.,* supported by fees, or subsidized by the General Fund.

The Water and Wastewater Enterprise Funds operate on a completely stand-alone basis. These funds do not rely on any tax-levy revenues but cover their complete operating and capital needs with user charges and fees. The Recreation Enterprise Fund is only partially stand-alone. It covers its operating costs with user charges and fees and contributes to the debt service on certain recreation capital projects (most recently, the Lincoln Field restoration project for which the debt has now been fully repaid). Most recreation capital costs are subsidized by the General Fund through a combination of within-levy borrowing, Community Preservation Act (CPA) funding, and debt exclusion funding.

Establishing the Enterprise Fund Budgets

At the Annual Town Meeting each year, Town Meeting appropriates an operating budget and authorizes capital expenditures for each of the three enterprise funds for the upcoming fiscal year. Later in the year (in the early fall in the case of the Water and Wastewater Enterprise Funds), user charges are set that are designed, based on projections of usage for the fiscal year, to be sufficient to cover the appropriations made by Town Meeting to run the enterprises.

Depending on the accuracy of the usage projections, the actual revenue realized by the enterprise during the year may exceed or fall short of the appropriated amount. Any operating surplus must be retained in reserve in the enterprise fund. The funds accumulated in that reserve (referred to as "retained earnings") may be applied only to meet the capital needs of the enterprise or to reduce user charges. Any operating loss (after applying any accumulated reserves in the fund), must be made up in the succeeding fiscal year's appropriation.

Since FY2007, the Annual Town Meeting Warrant has contained a separate Article for the appropriation of the enterprise fund operating budgets (previously, appropriations for the enterprise funds were commingled with those for the General Fund). This presentation makes it easier to understand the operating budgets of the enterprise funds. However, it should be noted that certain indirect costs that are charged by the General Fund to the enterprise funds are still appropriated as part of the municipal operating budget, this year in Article 4. For the complete operating costs of the enterprise funds, including indirect costs, see the Brown Book sections on Water, Wastewater, Recreation.

To present a more meaningful picture of the complete enterprise fund operating budgets, the tables included in the write-up of this article have been expanded from those presented in the Warrant to show the indirect as well as the direct costs of the funds. Debt service costs for previously approved capital expenditures are shown in the enterprise fund operating budgets. However, it should be noted that appropriations for capital needs of the enterprises, whether funded by cash or borrowing, are addressed in separate capital Warrant articles.

Appendix C: Revolving Funds

Ordinarily, revenue received by any municipal department must be deposited in the General Fund and cannot be expended for any purpose without further appropriation by Town Meeting. A revolving fund allows Town Meeting to dedicate in advance a specific source of anticipated revenue from fees and charges, on an ongoing basis and without the need for further appropriation, to pay expenses for rendering the services for which those fees and charges are collected.

Revolving funds managed by municipal departments are generally governed by G.L. c. 44, § 53E1/2. (There are also a number of revolving funds managed by the School Department, such as the School Lunch Fund, which are governed by other statutes and are not within the control of Town Meeting.) Under Section 53E1/2, a municipal revolving fund can be established only by vote of Town Meeting.

That authorization must be renewed prior to each succeeding fiscal year. The authorization must specify:

- the purpose(s) for which monies deposited in the fund may be used
- the source(s) of funds to be deposited
- the board, department or officer authorized to expend monies from the fund
- a limit on the total amount that may be expended from the fund in the ensuing fiscal year

Expenditures may not be made, nor liabilities incurred, in excess of the balance of the fund. If a revolving fund is reauthorized, any balance in the fund may be carried over to the next fiscal year. If a revolving fund is not reauthorized, or if the purposes for which the money in the fund may be spent are changed, the balance in the fund reverts to the General Fund at the end of the fiscal year unless Town Meeting votes to transfer the funds to another duly established revolving fund.

Appendix D: Tax Relief Programs

In early 2004, the Board of Selectmen created an ad hoc Tax Deferral and Exemption Study Committee to explore ways in which the property tax relief available to low and moderate-income senior citizens and other needy residents could be enhanced and made more accessible. Since then, with the guidance of this committee, Town Meeting has taken a succession of steps to expand such relief, for the most part maximizing the options that the Town is allowed to adopt under existing state law and, in some cases, using home rule petitions to further increase opportunities for tax relief.

The principal programs for tax relief now available to Lexington homeowners are:

- A state income tax *"Circuit Breaker"* program providing a state tax credit for low and moderate-income homeowners and renters age 65 and over (at no cost to the Town).
- A *tax deferral* program under which low-to-moderate-income homeowners age 65 or over may defer any or all of their property tax, after applying any available exemptions, up to half the value of their house. The deferral need not be repaid until the house is sold or transferred. The interest rate applied to each year's deferral is a variable rate designed to match the Town's earnings on its funds. *See generally* G.L. c. 59, §5, clause 41A.
- A *tax exemption* program under which homeowners age 65 or over with limited income and limited assets other than the value of their home may deduct $2,000 from their annual property tax. *See generally* G.L. c. 59, § 5, clause 41C.
- A locally-controlled *Senior Service* program adopted by Town Meeting in 2006.
- A Community Preservation Act *surcharge exemption* program.

<u>State Income Tax "Circuit Breaker"</u>

Low- and moderate-income homeowners age 65 and over whose homes have an assessed valuation not greater than an annually adjusted ceiling may obtain a tax credit on their state tax returns (see table below). Low and moderate-income renters are also eligible for a tax credit. Qualified owners or renters are entitled to a refundable dollar-for-dollar credit on their state income tax, up to an annually established limit, to the extent that real estate taxes and one half of water and sewer bills (in the case of homeowners) or rent (in the case of renters) exceeds 10% of the applicant's income. This program is administered by the Massachusetts Department of Revenue and has no direct impact on Town finances.

<u>The "41A" Deferral Program</u>

This program is authorized by G.L. c. 59, § 5, Clause 41A. Although not widely used, it is an important tool because it offers immediate and substantial property tax relief to seniors with significant equity tied up in a residence. Those who qualify may defer any part or all of their property tax for a given year, up to a cumulative total of half the assessed valuation of the property. All deferred taxes are eventually paid when the property is sold or transferred, whether before or after the resident's death. Towns are permitted to set their own interest rates for this program at any rate up to 8%. Lexington's rate is based on a floating Treasury rate equivalent to the Town's return on its funds in the year of deferral (recently less than 1%). The rate set for each year remains in effect for the life of deferrals granted in that year.

In 2008, in response to a home rule petition, the state legislature enacted a special law (Chapter 190 of the Acts of 2008) allowing Lexington to establish a more generous income eligibility limit than that permitted under state law generally.[16] Town Meeting most recently raised the income limit from $70,000 to $75,000 in 2019.

[16] The special law also permits the Town to adopt a lower age of eligibility than 65, or to condition eligibility on objective criteria of disability or other hardship for persons who would not otherwise qualify based on their age, but the Town has never done so.

The 41A deferral program is an attractive form of tax relief from the Town's point of view because it is essentially revenue-neutral. While a significant increase in the number of participants could potentially affect the Town's cash flow, there is little risk of loss since the Town is in effect making well-secured loans. The Town anticipates repayment of all deferred taxes with interest, and over time an equilibrium should be reached under which as many deferral agreements are repaid as are entered into.

The total amount of deferred taxes now carried by the Town as accounts receivable is shown below.

The "41C" Exemption Program

For many years, the Town has made available to qualifying seniors a property tax exemption under Clause 41 of G.L. c. 59, §5, and its successor, Clause 41C. Under the "41C" Program, the Town receives partial reimbursement from the State for exemptions defined under the program, subject to appropriation. The portions of the exemptions that are not reimbursed are funded from the Town's overlay account.

Prior to 2004, the amount of the credit was limited to $500 per year and eligibility criteria were quite restrictive. Since then, the Town has taken a number of steps to expand both eligibility and the credit amount. Taking advantage of new local options made available by the legislature in 2002, Town Meeting voted in 2004 to:

- Increase the amount of the exemption to $750.
- Lower the age of eligibility from 70 to the minimum allowed age of 65.
- Increase the income threshold from $13,000 (single) / $15,000 (married) to the maximum allowed amount of $20,000 (single) / $30,000 (married).
- Increase the threshold for personal assets, not including the home, from $28,000 (single) / $30,000 (married) to the maximum allowed amount of $40,000 (single) / $55,000 (married).

In 2005, Town Meeting voted to adopt the provisions of G.L. c. 59, § 5, Clause 41D, which automatically adjusts the income and asset limits for Clause 41C (but not the exemption amount) by a COLA established annually by the state Department of Revenue. The current income and asset limits are detailed in the table below.

In 2006, Town Meeting voted to increase the exemption to the maximum allowable amount of $1,000, and in 2018 voted to double it to $2,000 under the provisions of G.L. c. 59, §5, Clause C½.

The Senior Service Program

Low-income seniors may perform volunteer work for the Town in exchange for a reduction in their property tax, currently up to a maximum credit of $1,540 (see table below). The Senior Service program, formerly funded from the overlay account, is now funded as part of the Town's annual budget and is subject to appropriation.

In 2006, Town Meeting voted to rescind its acceptance of the statewide senior property tax work-off program under G.L. c. 59, § 5K, and to establish a locally controlled program instead[17]. This gave the Town the flexibility, through its Board of Selectmen, to:

- Allow participation by persons under age 60, such as the disabled and handicapped, who might be able to benefit from the program.

[17] In 1999, the state legislature authorized cities and towns, by accepting G.L. c. 59, § 5K, to offer seniors the opportunity to reduce their property-tax obligation by up to $500 in exchange for community service. Lexington, which had earlier maintained its own program, accepted this statute shortly after it was enacted. The statute allows towns to set their own rules and procedures for implementation, but limits participation to persons age 60 or over and also limits the hourly credit to the state's minimum wage. In 2002, the maximum amount of the Section 5K credit was increased to $750. In 2009 it was increased to $1,000, and in 2016 it was increased to $1,500. The 2010 Municipal Relief Act added a provision allowing towns to adopt a local option to set the maximum instead at 125 hours of service at the prevailing minimum wage (with a minimum wage of $12 per hour, the maximum credit is now $1,500, but that maximum would automatically increase if the minimum wage increases).

- Pay a wage in excess of the minimum wage.
- Allow a higher amount to be credited against a participant's property tax bill than permitted under state law.

Although the Board of Selectmen has the authority to expand eligibility to persons under age 60 who are disabled or handicapped, it has not yet done so, nor has it adopted a wage in excess of the state's minimum wage. The current eligibility qualifications and benefit limits are detailed in the table below.

CPA Surcharge Exemption

Low-to-moderate income homeowners age 60 or over, and low-income homeowners under age 60, may obtain a 100% exemption from the CPA surcharge on their property tax. These exemptions directly reduce the amount of CPA revenue that the Town receives.

Tax Relief Programs – Limits and Qualifications as of December 2019

State Income Tax Circuit Breaker		
Maximum assessed valuation		$808,000
Income limits		
• Single individual		$60,000
• Head of household		$75,000
• Married, filing jointly		$90,000
Maximum tax credit		$1,130
41A Property Tax Deferral		
Income limit (single or married)		$75,000
Interest rate for FY2020		2.55%
Total amount deferred in FY2019		$401,850
Cumulative deferred as of 6/30/2019		$1,797,948
41C Property Tax Exemption	**Single**	**Married**
Income limit	$27,830	$41,747
Assets limit	$55,665	$76,537

Senior Service Program	
Income eligibility	$70,000
Maximum benefit per household	(140 hours) $1,540
Hourly Rate	$11.00

Complete details on all of the tax and utility relief programs available to Lexington residents are set forth in a brochure entitled *Property Tax Relief Programs, Fiscal Year 2020,* available on the Town web site at `http://www.lexingtonma.gov/taxrelief`.

Appendix E: Specified Stabilization Funds

The state statute authorizing towns to create and maintain a stabilization fund, G.L. c. 40, section 5B, was amended in 2003 to permit the creation of multiple, separate stabilization funds for specified purposes. It was further amended by the Municipal Modernization Act in 2016. The creation of such funds, the specification of their purpose, any alteration of their purpose, and any appropriation out of the funds, must be approved by a two-thirds vote of Town Meeting. Appropriations into a fund may be approved by a majority vote of Town Meeting; and the dedication of a recurring revenue stream to a fund, which continues for a minimum of three years until revoked, may be made by a two-thirds vote of Town Meeting. To supplement its general Stabilization Fund, Lexington has created a number of specified stabilization funds, which are described below.

At the 2007 Annual Town Meeting, four specified stabilization funds were established to replace certain pre-existing special revenue accounts. Monies in the special revenue accounts, funded by negotiated payments from developers, had previously been spent without specific appropriation. In order to comply with Massachusetts Department of Revenue guidelines, and to make the existence and use of the funds more transparent, monies accumulated during the year in the special revenue accounts are now transferred periodically by vote at an annual or special town meeting to the following specified stabilization funds, where their appropriation is now subject to review by Town Meeting:

Transportation Demand Management/Public Transportation (TDM/PT) S.F.: Contains payments negotiated with developers to support the operations of transportation services. It was initially created to support the Lexpress bus service and the 2016 Annual Town Meeting extended the purpose of this fund to "supporting the planning and operations of transportation services to serve the needs of town residents and businesses."

Traffic Mitigation (TM) S.F.: Contains payments negotiated with developers to support traffic mitigation projects, such as improvements to signals and pedestrian access at intersections, including funds previously contained in the Avalon Bay TDM special revenue account.

School Bus Transportation S.F.: Supports daily school bus operations and was originally funded with $200,000 contained in the Avalon Bay School Bus Transportation special revenue account. This fund was dissolved at the 2018 ATM.

Section 135 Zoning Bylaw S.F.: Created to finance public improvements using monies contributed by developers pursuant to Section 135 of the Code of Lexington.

At the 2008 Annual Town Meeting, the *Special Education Stabilization Fund* was created to set aside reserves to help cover unexpected out-of-district special education expenses that exceed budget. A related goal was to enhance transparency around the out-of-district special education budget component by segregating this expense item and bringing budget overruns to Town Meeting for its approval. This fund was created in FY2009 with an initial appropriation of $350,000 and another $350,000 was appropriated to the fund at the spring 2009 Annual Town meeting. The current target level for this fund is $1,000,000.

At the 2009 Annual Town Meeting the *Center Improvement District Stabilization Fund* was created and was funded by a $100,000 payment received from the developer of Lexington Place in FY2010. The funds may be used for projects such as tree planting, sidewalk improvements to the abutting connector between the parking lot and the sidewalk. In each year from FY2018–2020, $27,000 was appropriated for the bike share program in Lexington Center.

At the 2011 Annual Town Meeting two more funds were created:

Avalon Bay School Enrollment Mitigation Fund: funded with a $418,900 payment received from Avalon Bay pursuant to an Education and Trust Fund Escrow Agreement dated May 31, 2006. The terms of that agreement called for the establishment of an escrow fund in the amount of $750,000 with disbursements made to the Town annually if the number of students residing at the development (Avalon at Lexington Hills) exceeded 111. The amount payable per student in excess of 111 was $7,100. The fund was dissolved at the 2018 ATM.

Transportation Management Overlay District Fund (TMOD): funded by payments from those developers who choose to pay a transportation mitigation fee rather than taking responsibility for improving all the intersections in the area to a certain level as provided in Section 135-43.C of the Zoning Bylaw. Per Section 135-43.C(5)(c) "any transportation mitigation fees paid to the Town are intended to be used to fund infrastructure improvements that are necessitated by the proposed development of the applicant."

At the 2012 Special Town Meeting, the *Capital Stabilization Fund* was created to set aside funds for future capital projects, including but not limited to building renewal projects, and/or to mitigate the impact on taxpayers of debt service, both excluded and non-excluded, related to capital projects.

Current Town policy has a goal of keeping debt service at approximately 5% of total revenue. When the Town must issue a particularly large bond, such as was needed for the new Estabrook School construction combined with the Bridge and Bowman school renovations, the Town's debt service rises sharply. This rise is typically followed by a period of lower growth in debt service while the Town pays down its existing debt, and limits additional borrowing, until debt service converges back on the goal of 5% of total revenue.

Rather than adding the higher debt service directly into the tax levy, this fund allows the Town to smooth the impact of sudden increases in debt service on property tax bills. Town Meeting can set aside funds in periods when the Town has a surplus, and in later years these funds can be appropriated to directly reduce annual debt service, which in turn reduces the amount that must be raised in the tax levy.

At the 2018 Annual Town Meeting, three new funds were created with dedicated revenue streams. The *Visitor's Center Capital Stabilization Fund* was established to serve as a repository for grants, gifts, or special fees related to the Visitor's Center building capital project. The *Water System Capital Stabilization Fund* was established for the specific purpose of reserving monthly payments received from the Town of Bedford per an agreement for the sale of water (water from the MWRA goes to Bedford through Lexington's system). The agreement with Bedford has two components, 1) the cost of water used, and 2) a flat annual fee or "demand charge" that is split into monthly payments. The annual fee is set so as to cover costs of future infrastructure improvements related to the Lexington-to-Bedford water connection. It is envisioned that the monthly payments would be put into this stabilization fund for future capital projects instead of being applied annually for rate reductions. The annual fee for FY2018 was $62,175 and it will increase each year by a CPI factor. The *Affordable Housing Capital Stabilization Fund* was established to reserve payments from Brookhaven for affordable housing, commencing in FY2020 per an agreement in regard to the rezoning article for Brookhaven's expansion at the 2017 Annual Town Meeting.

The table below shows the balances in stabilization funds as of March 12, 2020.

Stabilization Fund	Balance
Transportation Demand Management	$376,127
Traffic Mitigation	$643,443
Special Education	$1,148,715
Capital	$25,158,929
Center Improvement	$10,328
TMOD	$98,143
Debt Service	$437,058
Visitors Center	$215,549
Affordable Housing Capital	$0
Water System Capital	$71,702

Appendix F: Other Post Employment Benefits

The OPEB Liability

The Town of Lexington is required by State law to provide health benefits to retired employees that are comparable to those provided for active employees. These and other retirement benefits that are distinct from pension benefits are known as "other post-employment benefits" or OPEB for short. Health care benefits are by far the largest component of OPEB. Currently, all of the Town's retirees are eligible for Medicare and receive Medicare supplement coverage from the Town.

Because the Town is obligated to provide these benefits in the future, the anticipated costs extending over the lifetimes of current vested employees and retirees represent a financial liability. The size of the liability depends on the number of employees, each employee's number of years of service, the time intervals over which the retirees are expected to receive retirement benefits, the expected cost of providing those benefits in those future years, and the present value of those future benefits.

In a hypothetical world where the number of retirees remains constant and annual per-capita medical costs inflate at a rate close to a general inflation index, the size of the OPEB liability in terms of inflation-adjusted dollars would be relatively stable, because the increases and decreases would tend to balance out. In practice, however, the inflation-adjusted value of the OPEB liability most often increases each year, because of increases in the inflation-adjusted per-capita costs of health care, growth in the number of retirees receiving benefits, and an upward trend in longevity.

The Post Employment Insurance Liability (PEIL) Fund

The Post-Employment Insurance Liability Fund or PEIL Fund was created pursuant to authority granted to the Town through a special act of the Massachusetts legislature in 2002 (MGL Chapter 317). The Fund was created to allow the Town, at the discretion of Town Meeting, to set aside funds to pay for future retiree health benefits. Once money has been appropriated into the PEIL Fund, Town Meeting may only appropriate money out of it to pay for health care costs of retirees.

The Retirement Board is responsible for the management of the PEIL Fund as well as the Retirement Fund, which supports the Town pension system. The rules governing the management of these two funds are similar and, unlike most other Town monies, the balance in each of these funds can be invested in equities to yield a risk/return ratio suitable for long-term growth.

GASB standards and the choice of a discount rate

Government Accounting Standards Board statement 45 (GASB 45) requires the determination of the actuarial value of the Town's OPEB liability every two years and the inclusion of a summary of the results in the Town's financial statements. Bond rating agencies consistently ask about the actuarial report, suggesting that the size of the OPEB liability, and its current funding level, factor into the Town's bond rating.

Estimating the present value of a complicated long-term liability like OPEB involves many actuarial assumptions, and the final results are very sensitive to some of these factors, especially the *discount rate* (the investment rate of return assumed for the actuarial evaluation), the predicted *rate of inflation of per-capita medical costs*, and the *number of active and retired employees*, An understanding of the actuarial results in a proper context requires consideration of the underlying assumptions, and judgment of how well they mirror real-world expectations.

The Town engages an actuarial consultant who must follow procedures and reporting templates established by GASB standards to produce the actuarial report. The primary purpose of this report is to inform potential investors about one specific aspect of the financial health of the Town, and to enable uniform financial comparisons across multiple municipalities. However, the required report only provides guidance to a municipality, and the municipality may use its own modeling if seeking to control or reduce its OPEB liability.

Based on the requirements of GASB 45, for the most recent report received in January 2018, the actuary determined that a “blended” discount rate of 5.0% is appropriate for financial reporting purposes. The “blended rate” is well below the discount rate typically used for long-term investments, and this magnifies the estimate of the OPEB liability. The future liability is closely tied to the discount rate, in the sense that a lower discount rate, i.e., lower expected investment returns, results in a higher estimate of the present value of the liability. At the request of the Town, the actuary also analyzed the OPEB unfunded liability using a 7.5% discount rate.

While it is undoubtedly true that certain future annual appropriations for OPEB expenses will need to be higher if the normal cost (see below) is not annually appropriated to the PEIL Fund in the year of accrual or if the Town does not appropriate funds to cover previously incurred liabilities, the relevance to policy makers as opposed to potential bond purchasers of using a blended discount rate to gauge the liability is questionable. The reason is that a statement of a liability is a statement of value at the present time. Unfunded liabilities will not be paid using funds available at the present time, but with funds that will be raised in the future. Therefore, the most relevant information would be obtained by comparing projected annual expense schedules for the different funding policies under consideration. In short, OPEB liabilities computed on the basis of low discount rates do not necessarily serve as useful guides to target levels of appropriations into the PEIL Fund.

In 2011, the Town’s OPEB report used a blended discount rate of 2.5% yielding a liability of $302 million. In 2013, with the consent of the Town’s actuarial consultant, a higher blended discount rate of 4.5% was used, yielding a liability of $130 million. This large drop in the official estimate of the liability is mostly due to the use of a higher discount rate. At the Town’s request, the FY2013 actuarial analysis was revised to include an auxiliary schedule using a discount rate of 7.75%. This yielded a liability of approximately $90 million as of June 30, 2013. The actuarial analysis done as of the end of FY2015 estimated the liability at $129 million assuming a discount rate of 8%. The latest actuarial report was received in January 2018. It reported the then-current unfunded liability at approximately $200 million using 5% for the discount rate and at about $138 million using 7.5% as a discount rate.

GASB 74 and 75

Two GASB statements, nos. 74 and 75, have recently superseded GASB 45. The impact will mainly be noticeable for financial reporting purposes, and in the reporting of the results of the actuarial analyses done for the Town every two years in two separate documents.

Pre-Funding OPEB

There are two approaches to handling the OPEB liability. The first is a *pay-as-you-go* model where annual OPEB expenses are paid entirely through appropriation from the tax levy. This model uses current dollars to pay for current expenses related to benefits earned in previous years. The Town’s pay-as-you-go OPEB cost for FY2018 was approximately $6.8 million and the projected cost for FY2020 is approximately $7.5 million not including small amounts for the Town’s shares of retiree dental and life insurance.

The other approach is a *pre-funded* model in which, after full funding is achieved, an amount equal to the present value of future benefits earned during the current year is appropriated into the PEIL Fund, and that appropriated amount plus the investment returns from the Fund on that amount are used to pay for benefits that come due. This model, that uses current dollars to pay for future expenses, is also the way the Retirement Fund (pensions) will operate when it is fully funded.

Under the pre-funded model, after previously incurred liabilities are fully funded, the amount that needs to be appropriated into the trust fund each year is referred to in the actuarial analysis as the “normal cost” or “service cost”. The normal cost is an actuarially determined annual contribution that would fund the Town’s share of future retiree benefits earned by active employees in the current fiscal year.

The most recent report done as of the end of FY2017 projects the normal cost for FY2021 will be about $4.8 million assuming a 7.5% discount rate.

Currently, the intention is to transition to the pre-funded approach; hence, there have been appropriations into the PEIL Fund at each annual town meeting since 2008. Until the Town fully funds its OPEB liability, moving toward the pre-funded model will require the Town to continue paying for a number of years for annual pay-as-you-go OPEB expenses, while also appropriating funds into the PEIL Fund. Both types of payments reduce the unfunded OPEB liability, and the fund's ongoing investment earnings further decrease the unfunded liability. This combination of appropriations could be continued until the PEIL Fund is fully funded.

The PEIL Fund will be fully funded when the cost of all benefits earned in previous years may be reasonably expected to be fully covered by the Fund balance and investment returns. At that point the Town's annual OPEB appropriation would be limited to covering the normal cost for the given year and would therefore be lower than the pay-as-you-go cost.

The pay-as-you-go and pre-funded model each have advantages and disadvantages. The pay-as-you-go model is simpler to administer, but there is no benefit from long-term investment earnings, and no hedge against the higher inflation of health care costs. In the pre-funding model, once a sufficient trust fund balance is achieved, the investment earnings pay for a substantial portion of the costs. Building up the trust fund results in higher expenses during the decades-long transition period, but eventually results in lower annual appropriations from the tax levy.

Under pay-as-you-go, there is a large gap between the time when services are rendered and the time when funds must be raised to pay the benefits associated with those services. This gap can complicate long-term financial planning. With pre-funding, the projected fully-loaded cost of services is accounted and paid for in the current year.

Even partial pre-funding has some benefits. Any monies in the PEIL Fund provide assurance that the Town will be able to satisfy at least some portion of its future liability, and the Fund could also be used as a reserve, e.g., to fund a portion of retiree health costs in particularly challenging fiscal years.

On the other hand, appropriating money into the PEIL Fund reduces the funds available to spend on other items or to be put aside for other purposes. One should consider whether funding the PEIL Fund takes priority over other liabilities, such as the costs of maintaining or replacing roads and buildings in a timely manner. In some circumstances, choosing the latter might generate significant future savings.

On March 10, 2014, based on a recommendation from the OPEB Working Group, the Board of Selectmen endorsed a formal policy for making annual appropriations to the Post Employment Insurance Liability (PEIL) Fund:

> It is the policy of the Board of Selectmen to recommend to Town Meeting each year a budget contribution to the OPEB Trust Fund in an amount that ranges from 35 to 100 percent of the full Normal Cost, with the General and Enterprise Funds bearing their respective shares of those contributions. This approach will mitigate growth in the Unfunded Actuarial Accrued Liability, reducing the amount the Town will need to budget for health insurance by approximately one-third, as the assets of the OPEB Trust Fund will be used to underwrite the annual cost of retiree benefits.
>
> Further, it is recognized that there are competing claims for limited Town funds, which are considered as part of the annual budget process. Consequently, the annual recommendation for OPEB funding shall be made in the context of other capital and operating budget needs, such that recommended OPEB funding shall not have a material, detrimental impact on service delivery or the maintenance of Town capital assets and infrastructure.

The Committee supports this policy.

History of appropriations into the PEIL Fund

The history of appropriations into the PEIL Fund is given in the following table. Since the monies in the Fund are invested, the Fund balance does not precisely track the sum of past appropriations into, and in the future, out of the Fund.

The balance in the PEIL Fund was $19,115,349 as of December 31, 2019.

Venue of Appropriation	**Amount**
2008 Annual Town Meeting	$400,000
2009 Annual Town Meeting	$440,690
2010 Annual Town Meeting	$479,399
2011 Annual Town Meeting	$500,000
2012 Annual Town Meeting	$500,000
2013 Annual Town Meeting	$775,000
2014 Annual Town Meeting	$1,119,000
2015 Annual Town Meeting	$1,200,000
2016 Annual Town Meeting	$1,512,318
2017 Annual Town Meeting	$1,842,895
2018 Annual Town Meeting	$1,842,895
2019 Annual Town Meeting	$1,885,486