OFFICE OF SELECTMEN
MEMORANDUM

TO: B-SPACE Committee

FROM: Sean Cronin, Deputy Town Administrator

RE: School Renovations, New School & Financial Capacity

DATE: March 26, 2013

Board of Selectmen Chairwoman DeWitt and School Committee Chairman Morse asked that I undertake an analysis for the B-SPACE Committee of what capacity the Capital Improvement Program (CIP) has for additional School projects. The purpose of this memorandum is to report my findings to the Committee.

EXECUTIVE SUMMARY

The Town has a set of formal Fiscal Policies that guide financial planning. Chief among them are: (1) CIP Policies, (2) Use of Free Cash, and (3) Reserves. By following prudent policies over the past two decades, the Town has been able to recapture its Aaa bond rating and has established itself as a model to other municipalities of how to manage municipal finances. Available capacity within the CIP for additional school projects is limited by the parameters of these policies. In summary, there is approximately $8M of additional bonding capacity within the Town's "6% CIP Policy". However, it must be stated clearly that any additional debt results in the deferral of numerous cash-financed projects that impact many constituencies across town.

Various options have been discussed by the Committee and they all involve, in some way, the use of the Old Lincoln School and/or a new facility to house some segment of the School population. There is a direct relationship between the Old Lincoln School, a new facility, the Devotion School project, and the need for a Debt Exclusion Override and a General Override. As I previously explained to the Committee, the FY14 – FY19 CIP that is currently under review does not rely on a Debt Exclusion for any projects. However, once a conversation regarding a new school building is begun, the need for a Debt Exclusion must be at the forefront of the discussion, as the CIP cannot fund both 60% of a $90M Devotion School project and a new facility: as previously noted, approximately $8M of capacity exists within the 6% CIP Policy, an amount that is insufficient to construct a new facility.[1]

The timing of any potential General Override / Debt Exclusion Override votes depends greatly on the chosen plan and when the Old Lincoln School is put back into use as a school. As explained in the "Relationship Between the CIP & the Operating Budget" section on page 4, there is a scenario where there would be both a Debt Exclusion Override question and a General Override question on the ballot in May, 2014.

DETAILED ANALYSIS

Funding for the CIP comes from three primary sources:

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[1] I must note again that any additional debt results in the deferral of numerous cash-financed projects.

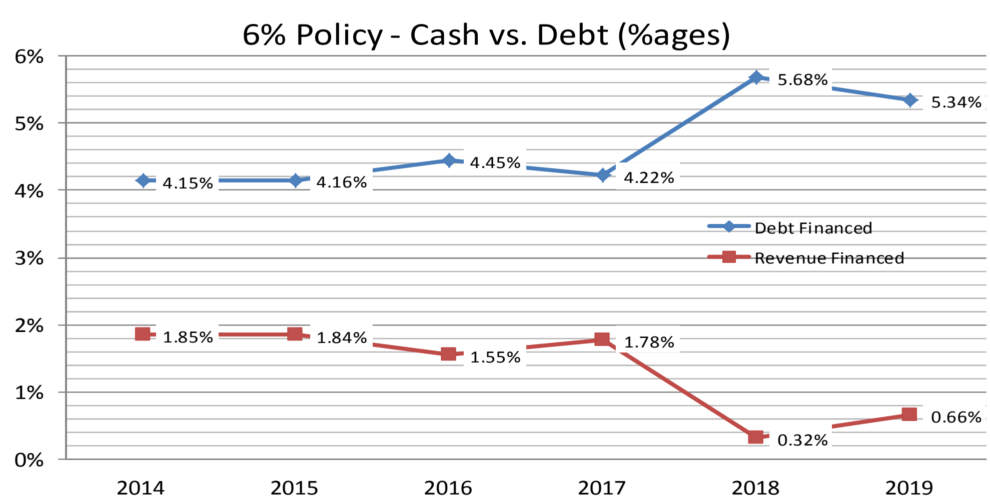
(1) *the "6% Policy"* – calls for 6% of the prior year's net revenue[2] to be dedicated to the CIP, with a split between debt and cash to finance projects. The goal is to have debt service be 4.5% and cash be 1.5%, totaling the 6%.
(2) *Free Cash* – the Policy calls for Free Cash to be used to bring total CIP funding up to 7.5%. This equates to using approximately $3.2M of Free Cash for the CIP.
(3) *Enterprise Funds* – the Water & Sewer Enterprise Fund and the Golf Course Enterprise Fund are both 100% cost recovery funds. Therefore, they each pay for 100% of their capital expenses.

The table below summarizes funding for the Proposed FY14 – FY19 CIP:

	2014	2015	2016	2017	2018	2019
6% Policy	$12.17	$12.74	$13.13	$13.54	$13.97	$14.44
Net-Debt *	$8.41	$8.83	$9.74	$9.53	$13.23	$12.86
% of Prior Yr Net Rev	4.15%	4.17%	4.47%	4.24%	5.70%	5.36%
Pay-as-you-Go	$3.76	$3.91	$3.39	$4.01	$0.74	$1.58
% of Prior Yr Net Rev	1.85%	1.84%	1.55%	1.78%	0.31%	0.65%
Free Cash	$4.82	$3.18	$3.28	$3.38	$3.49	$3.61
TOTAL	**$16.99**	**$15.92**	**$16.41**	**$16.93**	**$17.46**	**$18.04**
CIP as a % of Prior Yr Net Rev	8.4%	7.5%	7.5%	7.5%	7.5%	7.5%

* Defined as General Fund debt less debt supported by a debt exclusion.

It is crucial to understand how the 6% Policy works and the dynamic between debt and cash, as the core question I was asked was what additional capacity does the CIP have to fund additional School projects. The graph below shows how the 6% Policy works: as the portion of the 6% that is utilized for borrowing increases or decreases, the portion supported by the cash-financed monies moves in the opposite direction.



[2] Net Revenue is defined as Total General Fund revenue less the "Non-Appropriated" budget, Net Debt Exclusions, and Free Cash.

The split between debt and cash within the 6% Policy is driven by the use of debt for the financing of projects. The attached Debt Management Plan is at the core of the development of the CIP and results in the debt/cash splits shown in the table below:

(in millions)	2014	2015	2016	2017	2018	2019
Net Debt Financed [1]	$8.41	$8.83	$9.74	$9.53	$13.23	$12.86
Net Debt Financed as a % of Prior Yr Net Rev	4.15%	4.16%	4.45%	4.22%	5.68%	5.34%
Revenue Financed	$3.76	$3.91	$3.39	$4.01	$0.74	$1.58
Revenue Financed as a % of Prior Yr Net Rev	1.85%	1.84%	1.55%	1.78%	0.32%	0.66%
Total 6% Dedicated to CIP	**$12.17**	**$12.74**	**$13.13**	**$13.54**	**$13.97**	**$14.44**
	6.0%	**6.0%**	**6.0%**	**6.0%**	**6.0%**	**6.0%**

[1] As defined in the CIP Policies, "Net Debt" is total debt service exclusive of debt service related to a Debt Exclusion and debt service funded by enterprise fund revenues.

The amount of cash available for funding projects is driven by how much debt is used, so more debt means less cash. Since cash is normally used to fund smaller to mid-size projects, any additional debt would mean the deferral of those types of projects. This is shown clearly in FY18, when the full amount of debt service for the Devotion School project comes online: because of the $4.9M of new debt service for that project, there is less than $740K for cash-financed projects. This low-level of cash forced a reduction in the number of projects available for FY18 (and FY19).

Using an example for illustrative purposes, the table below shows the breakout of the 6% Policy when $8M of debt-financed work is assumed for the High School:

(in millions)	2014	2015	2016	2017	2018	2019
Net Debt Financed [1]	$8.41	$8.83	$9.74	$10.31	$13.97	$13.60
Net Debt Financed as a % of Prior Yr Net Rev	4.15%	4.16%	4.46%	4.57%	6.00%	5.66%
Revenue Financed	$3.76	$3.91	$3.39	$3.24	$0.00	$0.84
Revenue Financed as a % of Prior Yr Net Rev	1.85%	1.84%	1.54%	1.43%	0.00%	0.34%
Total 6% Dedicated to CIP	**$12.17**	**$12.74**	**$13.13**	**$13.54**	**$13.97**	**$14.44**
	6.0%	**6.0%**	**6.0%**	**6.0%**	**6.0%**	**6.0%**

[1] As defined in the CIP Policies, "Net Debt" is total debt service exclusive of debt service related to a Debt Exclusion and debt service funded by enterprise fund revenues.

This shows (a) the diminished amount of revenue-financed CIP available in FY's 17-19 and (b) how there is $0 revenue-financed CIP available in FY18 and just $840K in FY19. The 6% portion of the CIP becomes "tapped-out" at this point. The only cash-financed CIP available is the Free Cash portion (approximately $3.5M in FY18). It is Free Cash that would fund the "annual CIP items" such as streets, sidewalks, IT investment, energy conservation, and parks. Relying solely on Free Cash to fund these core CIP items is a situation the Town should avoid.

While this $8M for the High School is an example, it is a good one to use since the FY14 – FY19 CIP does not include any funding for the High School. Next year's FY15 – FY20 CIP would include the recommendations from the concept study currently being developed by HMFH.

As previously noted, taking on additional debt results in the deferral of numerous cash-financed projects. The table below is an example of what projects would be deferred because of an additional $8M of debt:

	FY						
	2014	2015	2016	2017	2018	2019	2020
ADJUSTMENTS							
Debt Service on $8M HS Project				780,000	761,000	742,000	723,000
Dean / Chestnut Hill Ave Signal - Delay by 1 Yr				(222,500)	222,500		
Fire Station Renovations - Station 1 MEP - Delay by 1 Yr				(320,000)	320,000		
Library Furnishings - Delay by 1 Yr				(105,000)	105,000		
Library Interior Painting / Facelift - Delay by 1 Yr				(100,000)	100,000		
Fire Station Renovations - Station 7 MEP - Delay by 1 Yr					(310,000)	310,000	
Fire Apparatus Rehab - Delay by 1 Yr					(500,000)	500,000	
Commercial Area Improvements - Eliminate 1 Yr of Funding					(60,000)		
Traffic Calming / Safety Improvements - Eliminate 1 Yr of Funding					(50,000)		
Town/School Ground Rehab. - Eliminate 1 Yr of Funding					(95,000)		
Parks/Playgrounds Rehab/Upgrade - Eliminate 1 Yr of Funding					(305,000)		
Town/School Energy Conservation Projects - Eliminate 1 Yr of Funding					(170,000)		
Fire Station Renovations - Station 7 MEP - Delay by another Yr						(310,000)	310,000
Brookline Reservoir Park - Delay by 1 Yr (debt svc impact)						(213,750)	6,375
Schick Playground Design - Delay by 1 Yr						(70,000)	70,000
Schick Playground Construction - Delay by 1 Yr							(700,000)
Town/School Bldg Envelope/Fenestration - Make Bond						(1,000,000)	(1,000,000)
Town/School Bldg Envelope/Fenestration - Make Bond (debt svc impact of 1st $1M)							142,500
High School - Quad - Delay by 1 Yr							(525,000)

One of the concepts discussed at the last Committee meeting was the construction of a new facility to house 8th and 9th grade students. Putting aside the important question of where would it be located, it raises interesting issues from a financing / timing perspective. As I understand the concept, Old Lincoln would be used as a "transition" space for a few years[3] while a new facility is constructed for an 8/9 School. Once a conversation regarding a new school building is begun, the need for a Debt Exclusion Override must be at the forefront of the discussion, as the CIP cannot fund both 60% of a $90M Devotion School project and a new facility.

A Debt Exclusion Override for the Devotion School project would free-up enough capacity for a new 8/9 School; in effect, you would be trading off debt associated with the Devotion School for the debt associated with a new 8/9 School. It would make sense to have a Debt Exclusion Override for the Devotion School rather than for a new school because funding for Devotion School will be before Town Meeting prior to any funding request for a new 8/9 School. (Funding for the Devotion School could be requested in May, 2014.) Under this scenario, a Debt Exclusion Override question for the Devotion School would be put on the ballot for the May, 2014 annual town election.

<u>RELATIONSHIP BETWEEN THE CIP & THE OPERATING BUDGET</u>

Various options have been discussed by the Committee and they all involve, in some way, the use of the Old Lincoln School and/or a new facility to house some segment of the School

[3] The $3M bond currently in the FY14 – FY19 CIP would be used to prepare Old Lincoln for use as a school again.

population. There is a direct relationship between the Old Lincoln School, a new facility, the Devotion School project, and the need for a Debt Exclusion Override and a General Override.

If the Old Lincoln School was put into place as a "transition" space for SY14-15 (FY15), operating monies would be required to run the school. In my opinion, absent any changes to educational policy and/or to employee contracts, a General Override would likely be required to generate those revenues. As I stated at the Committee's last meeting, an Override for operating the Old Lincoln School would lend itself to a discussion of seeking additional operating monies to relieve the budget pressures the Schools are under due primarily to the increased enrollment levels of the past few years. If an 8/9 School was ultimately constructed[4], the revenue from the General Override for operating the Old Lincoln School could be then be reallocated for the operating needs of the new school, once it is open.

Under such a scenario, there would be both a General Override question and a Debt Exclusion Override question on the ballot in May, 2014 (assuming the Town is ready to seek funding for the Devotion School project by then). If the Old Lincoln School is not opened until SY15-16 (FY16), then additional monies for operating the building would not be required, pushing off the need to seek a General Override for that purpose until May, 2015 (FY16). If this were to happen, that would mean a Debt Exclusion Override vote in May, 2014 for the Devotion School and a General Override vote one year later.

CONCLUSION

How the Town's CIP Financing Policy works, coupled with the interplay between the operating budget and CIP, is a complex and somewhat complicated subject that is of great importance in the Committee's discussion. I have attempted to explain how all the forces at play in the School space discussion come together and what the results of certain scenarios are. The simplest summary is that a Debt Exclusion Override will be necessary if there is a desire to both construct a new facility and undertake the Devotion School project. In addition, a General Override would likely be required to fund the operating costs of the Old Lincoln School and/or a new facility.

If there are any questions and/or you would like any additional information, please let me know.

cc Board of Selectmen
Melvin A. Kleckner, Town Administrator

[4] As explained on the previous page, a Debt Exclusion for the Devotion School project would be necessary in order to free-up capacity for a new 8/9 School.