Town of Hopkinton
Fiscal Year 2024 Budget
Initial Discussion Paper
September 29, 2022

This paper provides background to support the launch of the fiscal year 2024 (FY24) budget process for the Town of Hopkinton. There is a level of uncertainty at the beginning of every budget process, and the high inflation, volatile energy prices, and supply chain disruptions that characterize the preparations for the FY24 budget are no exception to that general rule. Town practice is to complete a review of available funding and a bottom-up budget review of the cost and value of services delivered each year.

Projected FY24 Revenues

The following table summarizes current initial estimates of FY24 General Fund sources of funding compared to budgeted funding estimates for FY23 under a 2.5% tax impact scenario:

	Table 1: Sources of Funds	**FY23 Budgeted Sources of Funds**	**FY24 Projected Sources of Funds**	**% Chg. FY23 - FY24**	**FY23 Tax Impact**
1	Levy Base	$78,088,438	$82,603,149	5.78%	2.32%
2	New Growth	$2,500,000	$1,500,000	-40.00%	1.73%
3	Debt Exclusions	$6,191,346	$6,317,172	2.03%	0.14%
4	Less - Provision for abatements	-$2,500,000	-$2,500,000	0.00%	
5	Estimated Net Property Tax Revenue	$84,279,784	$87,920,321	4.32%	
6	State Aid	$10,172,326	$10,680,942	5.00%	
7	Less - Regional & State Program Charges	-$483,315	-$507,481	5.00%	
8	Estimated Net State Aid	$9,689,011	$10,173,462	5.00%	
9	Excise Tax, Licenses, other Local Receipts	$4,900,026	$5,145,027	5.00%	
10	Cost Share from Enterprise Funds	$757,355	$780,076	3.00%	
11	Ambulance, Misc. Sources	$845,584	$658,643	-22.11%	
	Total Recurring Sources	$100,471,760	$104,677,529	4.19%	
12	Non-Recurring Sources: Cert. Free Cash	$3,348,753	$4,150,000	23.93%	
	Total Sources of Funds:	**$103,820,513**	**$108,827,529**	**4.82%**	

Almost all of the Town’s revenue comes from a few sources, all of which have very good prospects over the next budget cycle. As discussed at length in the 2022 Appropriation Committee Report, residential property tax is the Town’s dominant revenue source. While the general real estate market is cooling somewhat due to recent-record interest rates which limit

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affordability for buyers; that cooling is likely to have little or no impact on the Town's collection of levied property tax. Restated, tax collection is not dependent on a continuous rise in property values and is very stable. The Town's second largest revenue stream is from Local Aid from the Commonwealth, and the state's coffers are so overflowing that an arcane law is poised to trigger a multi-billion dollar tax rebate; suggesting Local Aid should continue to be reliable in the near term. Eversource Energy's aggressive tax strategy continues to pose a bounded challenge to the Town which will be discussed below.

On Table 1 row 1, the Tax Levy Base is projected to rise through a 2.5% statutorily allowed increase in the tax levy ($2,014,711). Since this source contributes 76% to total expected net revenue, it is vastly dominant in importance; and because it is based on firm, known data, and because collections are secured by the Town's right to lien; this existing estimate of this dominant source of funding is rock solid. The levy base could rise later in the budget process, if actual New Growth for FY 2023 comes in above the $2,500,000 budgeted last cycle. The actual New Growth number will be computed in six to eight weeks. As of now, residential construction is tracking about $10 million above last year's estimates ($170K in potential tax revenue); however, two-thirds of new growth is expected to come from commercial taxes and there is insufficient information available at this point in the work cycle to adjust the Tax Levy Base estimate, irrespective of the positive trend in residential construction. The municipal financial regulatory framework requires cautious budgeting of revenue, and there is no basis to increase this revenue estimate at this time.

On Table 1 row 2, the significant reduction in projected New Growth in the tax levy reflects a tail-off in construction at the Eversource LNG Facility renewal project. New Growth is expected to contribute under 2% of available resources, but nearly half of new recurring funding. Hopkinton recognized $70M in new valuation at the Eversource LNG site in FY22 and has budgeted for another $70M in new valuation for FY23. The Town's expectation was that the project would be complete with the work taxed in the FY23 cycle, but it appears there may be some additional taxable value to capture in FY24 or beyond. There is insufficient information available at this point in the work cycle to adjust the estimated revenue further.

On Table 1 rows 6 and 7, estimates a 5% increase in local aid from the Commonwealth and a corresponding 5% increase in charges for state and regional programs administered through the Commonwealth. Net Local Aid is an important source of funds, contributing 9.3% of expected net revenue. This estimate reflects a cautious budgeting approach based on the multi-year average: FY19, 7.4%; FY20, 1.3%; FY21, 6.3%; FY22, 10.6%. The actual level of local aid could be higher or lower based on the actions of the new Governor and the Legislature, and will be tracked through the budget process. The municipal financial regulatory framework requires caution budgeting of revenue, and there is an insufficient basis for projecting growth of this source above 5% at this time.

On Table 1 row 9, local receipts (including motor vehicle excise tax) are projected to rise by 5%. This is a noteworthy source of funds, contributing 4.7% of expected net revenue. This source is dominated by Motor Vehicle Excise Tax. Because the valuation basis for Motor Vehicle Excise taxation drops rapidly from 90% of MSRP in the year of manufacture to 10% of MSRP in the fifth year of life, consistency in revenue is dependent on some steadiness in the replacement cycle timing and value of vehicles that Hopkinton residents decide to purchase. Restated, if many people elect to buy new, expensive cars more rapidly than usual, Motor Vehicle Excise Tax will go up; and if many people elect to hold on to their older cars for several consecutive years, Motor Vehicle Excise Tax will go down. The Town will have virtually no information on FY23's experience before February, 2023. This estimate for FY24 is extremely preliminary and is based on the assumption that vehicle purchase trends from 2020-2022 will continue with no significant deviation. Although this preliminary forecast is subject to appropriate re-evaluation and revision as additional information comes to the Town from the Registry of Motor Vehicles, the municipal financial regulatory framework requires cautious budgeting of revenue, and there is not a basis for projected growth above 5% in this category at this time.

On Table 1 row 11, the apparent reduction of $187K involves the end of a multi-year FEMA grant for the Fire Department that was previously shown on this line, as well as the drop off of a one-time re-appropriation of funds (Fire Truck repair funds that were not needed because the truck was lost in an industrial accident.) The estimate shown is a return to the baseline level expected without grant or other special case activity. A large majority of this estimated revenue (84%) is connected to insurance and other reimbursements for emergency medical ambulance service, and this line is budgeted cautiously based largely on past ambulance receipts, consistent with the municipal regulatory framework.

On Table 1 row 12, Certified Free Cash is one-time funding available to support priorities in the coming year. A higher than typical amount is available, in part, because Eversource Energy paid $2,073,303 in bills that were unpaid in connection with business personal property tax appeals pending before the Appellate Tax Board. Because Eversource paid those bills on pending personal property tax appeals, a special reserve requirement that the Massachusetts Department of Revenue imposes was dropped and free cash that had been tied up as a reserve is now available. The Town is now in a free cash certification cycle and expects that an additional $2.9 million in certified free cash could be available to the Town. Town past practice is to hold at least $550,000 of that certified free cash back to cover snow and ice costs and other end of year expenses that are authorized to be paid out of certified free cash.

Projected FY24 Expenditures

On a strategic level, the Town Manager's priorities in initiating the FY24 budget process are to advance accomplishment of the Town's vision and mission, including the priority to advance diversity, equity, inclusion, and belonging in the Town of Hopkinton. This effort is informed in part by the Strategic Planning initiative undertaken in 2022, which will continue as part of this budget process. On an operational level, the budget process pursues those aims with a focus on change and improvement in three areas:

- Sustaining and improving Town service delivery operations through a rigorous budget process that prioritizes finding efficiencies and focusing spending to support key service outcomes and impacts; with a priority on diversity, equity, inclusion, and belonging
- Sustaining and improving the Town's capital infrastructure through judicious recapitalization and investment practices
- Ensuring long term fiscal stability by allocating resources to support adequate reserves, steady funding of long-term liabilities, and adherence to best practices in Hopkinton Financial Policies

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Table 2 below shows a possible distribution of FY24 expenditures if revenue is limited to the current estimates of revenue shown in Table 1, and if Financial Policy is strictly adhered to:

	Table 2: Uses of Funds	FY23 Budgeted Uses of Funds	FY24 Projected Uses of Funds	% Chg. FY23 - FY24
13	Tax Lien Administration Costs	$50,000	$50,000	0.0%
14	State Funded Library Spending	$28,736	$28,335	-1.4%
15	Repayment of Debt Principal & Interest	$7,194,987	$7,238,634	0.6%
15a	*Repayment of Existing Debt P&I, Excluded*	*$6,232,360*	*$6,317,172*	*1.4%*
15b	*Repayment of Existing Debt P&I, In Levy*	*$962,627*	*$921,462*	*-4.3%*
15c	*Est. Repayment of New FY24 Debt P&I, Excluded*		*TBD*	
15d	*Est. Repayment of New FY24 Debt P&I, In Levy*		*TBD*	
16	Deficits & Judgments	$0	$0	0.0%
17	Snow and Ice Surge Costs	$0	$0	0.0%
18a	*Hopkinton Public Schools*	*$55,522,404*		
18b	*Special Education Stabilization Fund*	*$1,094,024*		
18c	*Regional Schools*	*$565,876*		
18	Education	$57,182,304	$81,911,041	2.7%
19	General Government	$5,358,535		
20	Public Safety	$7,674,460		
21	Public Works	$6,549,584		
22	Health & Human Services	$1,327,435		
23	Culture & Recreation	$1,053,435		
24	Employee Benefits & Insurance	$14,852,647	$16,040,859	8.0%
	Sub-Total Departmental Expenses	$93,998,400	$97,360,560	3.6%
	Total Recurring Uses of Funds	**$101,272,123**	**$104,677,529**	**3.4%**
25	Transfer to OPEB (post-retirement health care)	$420,250	$832,850	98.2%
26	Transfer to Stabilization	$0	$700,000	
27	Town Meeting Capital Articles from Free Cash	$2,128,140	$2,617,150	23.0%
	Total Non-Recurring Uses of Funds	**$2,548,390**	**$4,150,000**	62.8%
	Total Uses of Funds:	**$103,820,513**	**$108,827,529**	**4.8%**

The projected initial sources and uses of funds for FY24 shows an approach that is consistent with the Town's Financial Management Policy. That Financial Management Policy aims to have (but does not require) recurring costs paid out of recurring funding; that non-recurring funding (e.g., certified free cash and other one-time sources) be used to support non-recurring needs; that long-term liabilities be addressed; and that stabilization reserves be adjusted as budgets adjust. Those priorities are reflected in Table 3, with the balance of projected funding shown for Departmental operating expenses:

Table 3: Recurring and 1-Time Sources & Uses of Funds	FY23 Budgeted	FY24 Projected	% Chg. FY23 - FY24
Recurring Sources of Funds	$100,471,760	$104,677,529	4.2%
Recurring Uses of Funds	$101,272,123	$104,677,529	3.4%
Net Recurring Funds	-$800,363	$0	
Non-Recurring Sources of Funds	$3,348,753	$4,150,000	23.9%
Non-Recurring Uses of Funds	$2,548,390	$4,150,000	62.8%
Net Non-Recurring Funds	$800,363	$0	

There are particular economic factors that create higher-than-usual uncertainty with respect to FY24 spending to sustain FY23 service levels. Inflation and economic volatility have been at the highest levels in decades, and that impacts the Town in several specific ways:

- Wage inflation - Wages represent about 70% of Town operating spending, and are therefore the most material factor in considering inflation overall. Restated, a 1.4% increase in wages results in a 1% increase in the overall budget. While several collective bargaining agreements have been settled with near term impacts that are manageable in terms of wage inflation, one significant contract is still pending, and the Town should be mindful that wage inflation may be looming as a factor in FY25 or beyond.

- Energy Cost Escalation - Although energy is a central factor in many industries, Hopkinton spends approximately 1% of its budget on fuel for vehicles and energy for buildings. Additionally, the Town holds some advantageous contracts for the purchase of energy over the FY24 budget cycle, and the Town's solar installations help buffer energy cost volatility and help dampen the FY24 impact of energy volatility. Energy saving measures through LEED engineering in modern facilities have also improved energy efficiency. For example, Marathon Elementary is 38,480 square feet larger than Center School but uses 877 fewer MMBTUs of energy per year.

- Project Costs - Over the past two years there has been an increasing trend of rapid capital project price escalation that outpaces the lengthy Town budget cycle. Those outcomes have been driven by well-documented national supply chain challenges related to both the COVID-19 Public Health Emergency and the energy crisis sparked by Russia's destabilizing invasion of Ukraine. Because of this price volatility, and because of the Town's long lead time for adjusting budget requests through Town Meeting action, the Town plans to budget capital projects with much higher than usual contingency amounts; entrusting the Select Board with monitoring execution, with “proceed or pause” authority with respect to contingency funds. Budgeting in this way would put additional pressure on FY24 sources of funds, but would support timely and perhaps more cost-efficient completion of critical capital projects.

- Economic volatility - The Town is over seven months from a May 2023 Town Meeting vote on the FY24 budget. In economically stable times, moderate change could be expected over that period. Given the supply chain challenges still in place and the significant uncertainty about how military events in Eastern Europe will affect global stability, and specifically world-market energy price stability, the cone of uncertainty extending to May, 2023 is wider in terms of potential outcomes than the Town has seen in decades. Moderate portions of the FY24 operating budget are sensitive to that volatility, and budgeting to address that volatility will be covered in CFO budget submission directions . As discussed, project costs funded through operating and capital budgets are more sensitive and direction in CFO budget submission directions will instruct Departments to submit capital requests with increased contingency amounts to minimize delay and re-approvals of critical initiatives.

Revisiting the three operational priorities in the budget process in the context of resources available:

- Sustaining and improving Town service delivery operations through a rigorous budget process that prioritizes finding efficiencies and focusing spending to support key service outcomes and impacts: The constrained spending position in Table 2 above suggests that the amount initially estimated to be available for Departmental increases, 2.7%, will be insufficient to satisfy contractual, inflationary, and service growth costs (including diversity, equity, inclusion and belonging) for Hopkinton Operating Departments (Table 2 rows 18 - 24), including the Hopkinton Public Schools. This insufficiency, and options for addressing it, are discussed below.

- Sustaining and improving the Town’s capital infrastructure through judicious recapitalization and investment practices: The constrained spending position in Table 2 above allocates $2.6M in one-time funding (certified free cash) for pay-as-you-go capital projects (Table 2 row 27.) The estimates make no provision for funding additional debt within the tax levy, expecting that any large dollar value capital needs will be proposed as “excluded debt” under the Proposition 2 ½ budgeting framework; with due consideration to be given to Community Equity with respect to any additional tax impact from new excluded debt. Adjustments will be made later in the budget process for any new debt to be funded within the tax levy limits.

- Ensuring long term fiscal stability by allocating resources to support adequate reserves, steady funding of long-term liabilities, and adherence to best practices in Hopkinton Financial Policies: The constrained spending position in Table 2 above sets aside $832,850 (Table 2 row 25) toward the long-term OPEB liability. In a May 13, 2022 memo to the Select Board, the Hopkinton Chief Financial Officer reported about a significant rise in the computed OPEB liability, from $28.1 million to $40.0 million. In that memo, several possible measured actions for addressing that rise in the projected liability were identified. One approach was to raise the base amount to be contributed to the Town's OPEB Liability Trust Fund by a step increase, and continue escalating annual contributions from that new baseline funding amount at 2.5% annually. This paper foresees following that approach. The constrained spending position in Table 2 above also sets aside $700,000 to bolster the Town's General Stabilization Trust Fund (Table 2 row 26.) Town Financial Management Policy calls for a Stabilization reserve level of 5% of the Operating Budget. As the size of the Operating Budget grows, the recommended reserve rises. Based on the preliminary forecasts, the projected FY24 Stabilization Trust Fund Target would be $5.3M. The June 30, 2022 Stabilization Trust Fund level was $3.9M. The $700,000 addition to the General Stabilization Trust Fund identified in Table 2 would close half the gap.

Overall, the constrained spending position in Table 2 above shows recurring costs fully funded by recurring revenue, consistent with Town Financial Policy recommendations, as shown in Table 3. In that sense, the spending levels shown in Table 2, while insufficient to sustain services with an increase in Departmental budgets of 2.7%, are compliant with Town Financial Policies.

Even at the constrained level shown in Table 2, the Town's commitment to Community Equity warrants a review of how tax impact affects Hopkinton's most vulnerable residents. While many in the community may desire more services and may be willing to pay associated costs, low income seniors struggling to stay in their long-time homes, families who struggled to buy into or rent in Hopkinton, or others, may be particularly sensitive to the tax impact of additional spending. There is always a desire to balance service improvement and growth with sensitivity to our citizens in financial need. While mechanisms exist to support higher levels of spending, they should be considered with the impact on citizens at every economic strata. The allowable 2.5% increase in the tax levy will have about a 2.33% tax impact on existing homeowners and businesses. That impact could be higher if the Annual Town Meeting sends capital items to the voters for consideration as "excluded debt", and if the voters approve any capital items considered. A 2.33% tax impact would raise the tax bill of the average home in Hopkinton with a value of $681,100 and a tax bill of $11,599 by $270. To consider Community Equity, a Hopkinton home in the 5% percentile of value (having 95% of Hopkinton homes with a higher value) is assessed at $391,100, with a current tax bill of $6,659. For that home, a 2.33% tax impact budget for FY24 would add $155 to the tax bill for the owners of that home. While a $270 tax increase may have a moderate impact on the owner of Hopkinton's median priced home, a $155 tax increase may have a significant impact on the owner of a home at the 5th value percentile.

The challenge at this earliest phase of the budget process is that projected sources of funds are insufficient to both support continuation of FY23 service levels into FY24, with funds available for Departmental increases limited to +2.7%; and to meet all the aspirations contained in Town Financial Policy. However, it would be possible to sustain service levels into FY24 with

Departmental increases in excess of 2.7% if policy objectives were partially sacrificed, or if revenue estimates improve; or some combination of the two.

- Management of the Overlay for Tax Appeals - Because Eversource Energy has continued its hostile strategy of malicious, cost-inducing property tax appeals, Table 1 (row 4) again shows a very high contribution of $2,500,000 to the tax overlay account. This use of funds is in place solely and exclusively as a contingency fund in case Hopkinton's taxation of Eversource Energy is overturned on appeal. The Town has high confidence in the careful, fair, and highly professional tax amounts levied on Eversource. Tax appeals adjudicated in the past several years have completely sustained the Town's position of confidence. However, the Town's financial regulator, the Massachusetts Department of Revenue, has promulgated rules for Town fiscal administration that do not foresee blatant abuse of the tax system by large taxpayers; and the Town is required to maintain reserves vaguely prescribed as "adequate" in the Overlay account. The $2,500,000 earmarked in this document for expected future malicious Eversource Energy appeals, by itself, serves to squeeze out service growth and tax relief. As one option, the Town could assume a somewhat higher level of risk and contribute a somewhat lesser amount to the Overlay account, freeing up resources to support service delivery and/or for tax impact control.

- Use of Certified Free Cash for Ongoing Operations - Town Financial Policy contains an objective of paying for recurring expenses with recurring funding. The initial projected Sources and Uses of Funds presented in this document comport with that objective. The Town could assume a level of risk and apply some amount of one-time funding from certified free cash to support recurring operations; which would support service delivery or mitigate tax impact in the short run. Likewise, the Federal Government has expanded Town authority in using $5.3 million in available American Recovery Plan Act (ARPA) funds, and those one-time funds could be used to support service delivery in FY24; again, contrary to Town Financial Policy objectives of funding recurring needs with recurring revenue.

- Revenue Estimates - While the cautious projection of revenue is the cornerstone of municipal budgeting, these estimates are typically refined between September and January. The Board of Assessors may find that New Growth in the tax base is higher than expected in FY23, which would add to the levy for FY24. Data from the Registry of Motor Vehicles may support higher estimates of excise tax revenue. A new Governor may signal a stronger position on Local Aid. Legitimate, cautious improvement in revenue estimates (especially in categories that do not affect residential tax impact) may provide some opportunities for sustaining services into FY24.

- Restrict Growth In or Diminish Service Delivery - Beyond the annual search for efficiencies in the budget process, the FY24 budget could be managed by declining or delaying the expansion of services, or by reducing existing services.

Based on the cautiously developed source of funds shown in Table 1 above, $108.8 million would be available to support operations in FY24, allowing for a 2.7% rise in Departmental spending. A spending plan modified to provide for a 5.1% rise in Departmental spending, would require $110.6M.

Table 4: Gap to Sustain FY23 Service Levels into FY24

Uses of Funds from Table 1, Departments +2.7%	$108,827,529
Uses of Funds, Adjusted with Departments +5.1%	$110,652,259
Amount Required to Adjust Departments to +5.1%	$1,824,730

Considering both community equity issues involving tax impact, and the recent willingness of Hopkinton residents to support the sustainment of excellent public services, and the judicious, targeted increases in service levels; the recommendation is to initiate the FY24 budget process with a target for Departmental spending at not more than +5.1%.

Achieving a balanced budget at that level will eventually require some level of net favorable outcome on revenue estimates, and some level of compromise on the Town's Financial Policy priorities. Absent sufficient progress in those two areas, adjustments to spending will be required during the budget process.

To summarize opportunities for developing an additional $1.8 million in Departmental spending, allowing for a 5.1% increase in spending:

- Risk could be assumed on Eversource Energy Property Tax appeals, and an amount less than $2.5 million could be added to the Overlay reserve for pending tax litigation
- One-time funding from certified free cash or from available federal ARPA awards could be used to support operations, even though this would require using one-time sources of funding to support recurring needs
- Revenue estimates, particularly Local Aid from the Commonwealth or New Growth could improve as time passes and more detailed information is know
- Spending could be constrained below the target 5.1%, with possible service delays or reductions

While not optimal, this recommended approach provides a path forward for initiating a difficult FY24 budget cycle; with a focus on balancing service objectives with risks and opportunity as the process unfolds.

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