

BUDGET SUMMARY AND OVERVIEW

To: The Honorable Members of the Falmouth Town Council

From: Nathan Poore, Town Manager

Date: March 28, 2008

Re: 2008-09 Budget Transmittal Letter

I hereby present to you the proposed fiscal year 2009 municipal budget. This budget was reviewed extensively by finance department staff, my office, and the rest of the department head/management team. I am pleased to report that this budget will not have any impact on the municipal portion of the mil rate net of the November 2008 referendum approval for open space acquisition. This has been accomplished while adding substantive expenses associated with previously approved programs such as the new public safety building. All of the changes to the budget are explained in detail throughout the budget document.

The proposed General Operating Budget for the Town is \$ 10,843,880, which represents an increase of \$ 660,783 over the current year's appropriation. This translates into a 6.5% increase. Without the open space funding, the proposed General Operating Budget for the Town is \$10,343,880, representing an increase of \$160,783 over the current year's appropriation. This results in nearly flat funding at a 1.6% increase. Despite significant changes in various funding levels, this budget is consistent with the long tradition of financial stability for the town. I believe that former Councils made excellent decisions supporting budgets that adequately funded capital needs and the tradition needs to be carried forward.

Expenditures

A major driving force to this budget is the Capital Improvement Plan (CIP) which increased from FY08 approved appropriations. New expense for the funding of the open space land acquisition reserve is the reason for this increase. The remaining CIP was re-evaluated with replacement schedules examined and updated for life expectancy and increased costs. This process allowed us to have sustainable reductions in funding of some reserves, while maintaining confidence that we are not under funding future capital expenditures. It is worth noting that the CIP would have had a net decrease without the new open space funding.

We were able to cut numerous line items in all departments by looking at historical spending patterns. Department heads/managers assisted with this process and were given opportunities to offer alternatives to the suggested cutbacks. By the end of the process, this document received support from all department heads/managers. Some of the more significant cuts include but are not limited to: lower than historical increase for salaries, health insurance, retirement contributions, elimination of two positions, printing, legal, waste disposal, and overlay.

Salaries and benefits represent the largest share of all expenditure categories. The typical pay increase will be around 3% for personnel. We were able to realize some savings in health insurance (non-union personnel) by changing the benefit level without major impacts to most employees. The change of many individual retirement plans, from ICMA-RC to the Maine

Public Employment Retirement System (MPERS), has resulted in savings compared with last year's budget. The FY09 budget also has staff reductions in departments of the Town Clerk and Parks and Public Works, but there are increases in the Community Development Department and building maintenance.

The opening of the new Police Station and expansion of Central Fire Station have increased the operating expenses of the Town. An additional custodian was hired to accommodate all the added facility space. A fiber optic connection was installed between the new Police Station and Town Hall to create a secure and dedicated connection between the two facilities. We have also expanded our computer network in order to accommodate employees that have moved outside of Town Hall. Finally, the utility costs of the added facilities have increased our expenses.

Revenues

We balanced the new expenditures with a combination of fund balance (one-time use), new property valuation growth, and fee adjustments in several departments. Unfortunately, the collective total of all non-property tax revenues is decreasing. Overall, revenues are up \$68,725 from last year's budget. Decreasing non-property tax revenues was one of the greatest challenges in the development of this budget. The budget to budget increase is 1.4%

Projected Future Needs and Budget Impacts

There are some items that were discussed during budget development meetings and included in department budget requests that are not funded in this budget. Most of our discussions focused on staffing needs.

- Consolidation of the front-end services including vehicle registration, Town Clerk, and Assessing will continue to warrant detailed study and time to discover the potential cost savings.
- We are working on an update to both TIF plans. There are potential impacts to street improvement and maintenance costs.
- We will monitor the reduction of one position in the Parks and Public Works Department and the elimination of the Deputy Clerk position to determine if these are long-term sustainable commitments.
- We are continuing our efforts to analyze the condition of infrastructure and developing plans to manage the system. Planning will include a process for developing policy and a strategy for new infrastructure and replacement/ reconstruction.
- I look forward to working with the Council as we work toward meeting the needs of Falmouth citizens. I need to acknowledge and thank everyone who participated in the development of the proposed budget including all department heads/managers and their staff. Special appreciation and acknowledgement is also owed to Randy Davis and John McNaughton.

Budget Analysis

This section of the budget document, identified as the Budget Analysis, provides an overview of spending at multiple levels. The information in this section will illustrate budget impacts, explain changes and new programs, and compare resource allocation.

Tax Rate Calculation

This tax rate calculation table utilizes an added valuation projection of \$30 million in new construction and lot formation.

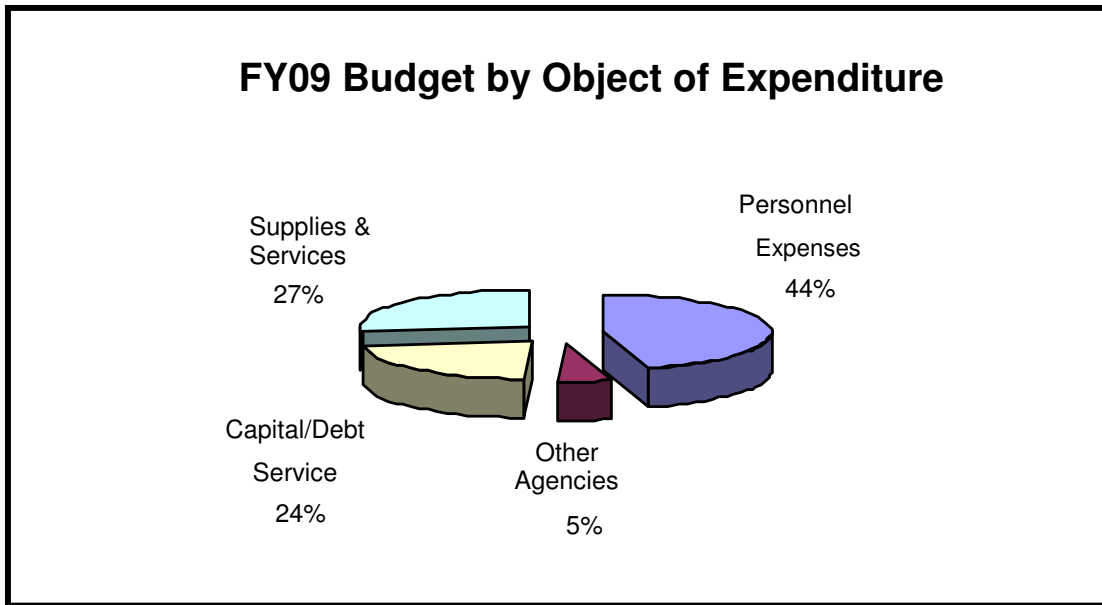
Property Tax Rate Calculation 2008-09 Town Budget	
Expenditures	10,843,880
Non-tax revenues	(4,968,300)
Net from property taxes	5,875,580
2008-09 projected valuation	1,695,646,000
2008-09 projected tax rate	3.47
2007-08 rate	3.20
Tax rate increase (decrease)	0.27

*\$500,000 for open space acquisition is equivalent to 0.30.

Expenditures (By Object of Expenditure)

This table and following chart demonstrates how funds are allocated amongst four major categories. We are primarily a service providing organization so it is not surprising to see that a significant amount of our budget is associated with personnel costs.

Personnel	Supplies & Services	Capital / Debt Service	Other Agencies
\$ 4,765,535	2,938,258	2,634,880	505,207



Expenditures (Personnel)

The total cost of personnel services (wages and benefits) in the FY09 budget is **\$ 4,765,535** representing a 1.6 % increase over FY08. Offsetting factors have kept this category relatively flat.

- The new Police Station and expanded Central Fire Station facilities will utilize a new full-time building maintenance professional to meet cleaning and maintenance expectations.
- The full impact of the new Director of Long Range Planning is part of this budget. This is partially offset by the ability to do planning projects in house as opposed to hiring consultants.
- The pay increase will be 3.0% for personnel.
- We have changed the health insurance benefit levels for all non-union personnel to match the plan now provided to one of the unions. This results in a premium savings for the Town and employees.
- Many employees switched their retirement plans from ICMA to MPERS, lowering employer contributions. Since MPERS also includes long-term disability coverage to its members, the Town also shows a decrease in our Long Term Disability premiums.
- Because of poor claims experience in prior years, the Town will see an increase in Worker's Compensation expense.

Expenditures (Supplies and Services)

The proposed budget includes \$ **2,938,258** for supplies and services, which represents a 7.7% increase over the FY08 budget. The more notable increases in this category include:

- With the Police and Fire staff moving out of Town Hall to their own facilities, there was a need for updated and expanded computer network and phone services. The increased costs include a fiber optic connection to insure security and reliability, as well as increased professional and contractual services to maintain the larger systems. We identified the need to upgrade most systems regardless of the building projects so much of the increase was inevitable but could have been deferred one or two years.
- We reduced the silver bullet collection cost in FY08. We anticipated less recyclable material but flow has not changed since the start of curb side collection. Therefore, the FY07 spending level needs to be restored, resulting in a significant increase when compared to FY08.
- Utility costs have increased due to new facilities and an anticipated unit cost increase.

Expenditures (Capital Outlay / Debt Service)

Funding levels in this particular category are the backbone to ongoing fiscal stability. We will continue to fund capital needs from annual revenues; special reserve funds, and the issuance of debt. A successful capital improvement program (CIP) will not show mil rate impact fluctuations with substantial peaks and valleys. This budget and the remaining CIP are structured to accommodate the goal of steady funding without significant changes in the mil rate. The proposed budget includes funds for implementing the FY09 portion of CIP. Capital Outlays / Debt Service costs next year will total \$ **2,634,880**, which reflects a 18.3% increase from the current budget. This increase is due entirely to the new open space acquisition reserve fund. Without this new fund, there would have been an actual reduction in the requested appropriation.

The CIP was evaluated and the capital replacement schedules were updated for life expectancy and inflation. This evaluation allowed us to reduce funding to some reserves while remaining confident that these reserves will not be underfunded for future capital expenses.

The Town's strategy of making prudent investments in its capital equipment/facilities and infrastructure should be continued. Continuing this strategy will sustain the condition of our infrastructure and minimize long-term maintenance costs.

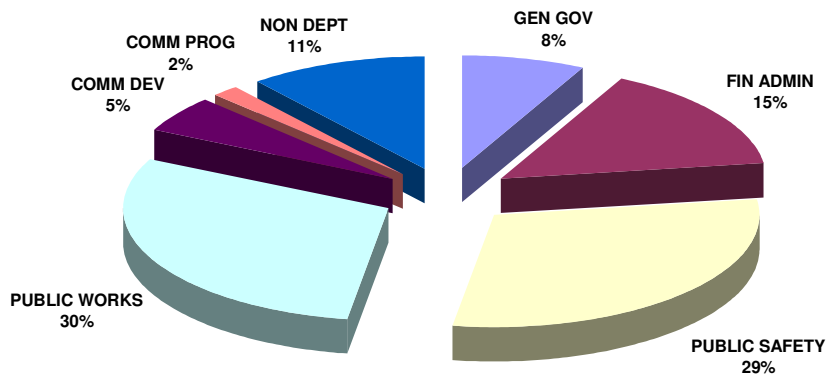
Expenditures (Contributions)

Contributions to outside agencies include the Library, Metro Bus, Highland Lake Watershed Study and Conservation, and overlay. The request is down 6.2% when comparing to the FY08 budget. Funding levels, based on outside agency recommendations and requests total **\$505,207** in FY 09. The proposed budget includes a contribution toward the operations of the Library in the amount of \$374,000, which represents a 3.5 % increase. Metro Bus (including Regional Transportation Program) expenses will increase by \$41,000. These increases are offset by a significant decrease in overlay.

Expenditures (Budget Summary by Department)

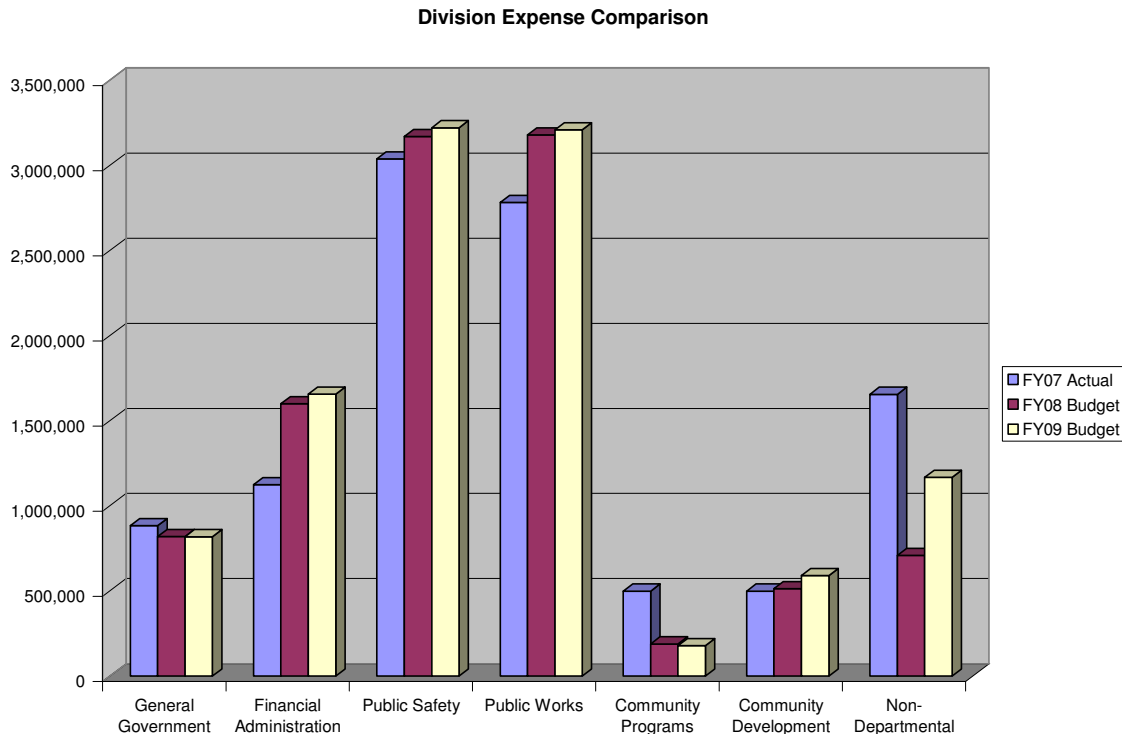
This pie chart illustrates how the proposed budget allocates resources by Department. It is clear that the majority of our spending goes toward the delivery of actual services such as Community Programs, Public Safety, Parks and Public Works. Administration expenses are much smaller pieces of the pie which is desirable so that more resources can be used for the actual delivery of services.

Town of Falmouth FY09 Budget



Budget Allocation by Department

The bar graph shown below presents a budget comparison by department. The explanation for variations are different depending on many factors including but not limited to the shift in CIP funding (added a \$500,000/year reserve fund for open space acquisition), varying levels of inflation (depending on the types of expenditures made within each department), reductions in some areas, and program changes.



Changes in department budgets include a number of explanations such as:

- **General Government:** There is a decrease in legal fees, printing (eliminating town report mailing and relying on website access), and other miscellaneous decreases.
- **Finance:** Higher network systems costs associated with the new website, connectivity to the new Public Safety buildings, and overall IT upgrades. The most significant difference when compared to lower levels in FY07 is due to the Public Safety building debt service which started in FY08.
- **Public Safety:** The increase in this category is attributed to contracted salary increases, higher cost for vehicle maintenance, and building operations (new police station).
- **Public Works:** We will be allocating larger portions of the Public Works Director and Deputy Director to the TIFs. The rationale is that a significant amount of their

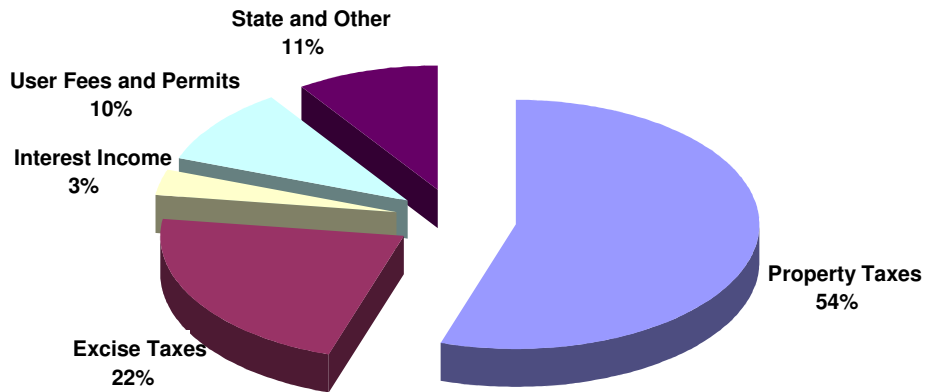
time and capital investments are concentrated with the TIF districts. We are also eliminating one full-time position and adding one part-time position resulting in a net decrease. There are also decreases in funding for the Parks Equipment and Park Renovation reserves. Many of these decreases are offset by increases in solid waste contractual and recycling services, such as the need to fund silver bullet hauling at the FY07 level rather than the reduced FY08 budget.

- **Community Programs:** We have lowered the funding to the Recreation and Adult Education programs. The management of these programs has been very efficient over the past few years. The accounts associated with this department have a surplus that will allow a sustainable decrease in funding.
- **Community Development:** Salaries for the Director of Long Range Planning and the Peer Review and Site Inspector are responsible for the increase in this department. The function of the Peer Review and Site Inspector has resulted in a significant decrease in contractual services. Revenues are collected for inspection work that was previously expensed out to consultants.
- **Non Departmental and Other Agencies:** The primary reason for an increase in this area is due to new funding for open space land acquisition and increased funding for the Metro and RTP bus programs. Decreases in overlay and contingency accounts offset some of the increase. The apparent spike in FY07 is due to supplemental appropriations for the settlement of retirement benefits with staff and unanticipated land purchases.

Revenues

Municipal services are supported by a number of revenue sources including property taxes which account for 54% of all revenue sources for municipal (non-education) services. Property taxes are used exclusively to fund the Cumberland County assessment and 75% of the funding required to support education comes from property tax revenues. The following pie chart shows where all our revenues come from and demonstrates how much we rely on property taxes (chart only applies to municipal services).

Town of Falmouth Sources of Revenue

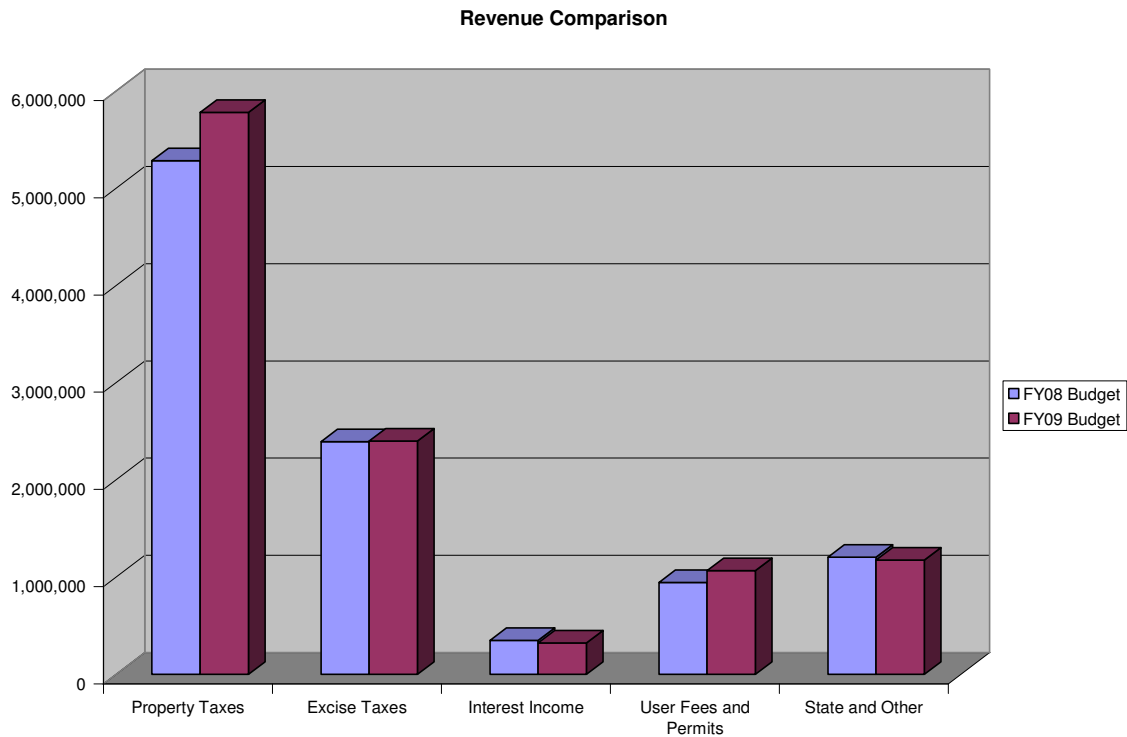


Non-property tax revenues can fluctuate beyond the control of local officials which is typically why some level of conservative estimating is necessary. The estimated revenues in FY09 are not conservative and leave very little room for unanticipated adjustments. The projected revenue estimates are similar to revised FY08 estimates. Projected FY09 revenues are lower than the original FY08 budget which was one of the greatest challenges in the development of this budget. The budget to budget increase is 1.4% with the following revenue sources providing the most significant impacts:

- Planning Board Fees (25,000)
- Investment Income (25,000)
- State Revenue Sharing (57,000)
- Authorized Use of Fund Balance 30,000
- Ambulance Charges 30,000
- Mooring Fees 28,000

The decrease in non-property taxes revenues created significant challenges to the development of this budget. Normally, we can depend on an increase in these revenues (average increase over the last five years was approximately \$164,000) to combine with added property valuation growth. For the past few years, this formula has worked well in Falmouth but the drop in non-property tax revenues created an immediate hurdle resulting in a need to consider significant cuts and adjustments on the expense side of the budget.

The following bar graph compares FY08 and FY09 revenue projections.



Financial Condition

One of the primary strengths of this organization has been and continues to be its stable financial condition. This part of the report demonstrates financial condition through analyzing several characteristics and practices. Collectively, these snapshots of our organization show that the Town is in an enviable position.

Financial analysts use several financial indicators to measure a municipality's financial condition. This report identifies, similar to previous reports, the following information/indicators: property tax burden; ratio of bonded debt to assessed valuation; direct debt per capita; tax collection rate; and the Town's undesignated, unreserved fund balance.

Property Tax Burden

The State Bureau of Taxation publishes full value tax rates for all Maine communities each year. Full value tax rates are used so that fair comparisons can be made between communities. The rate is calculated by using the State determined valuations and the locally determined property tax commitments. State valuations are always behind two years which is the reason why data is not available for 2006 and 2007.

This table compares Falmouth's full value rate with other greater Portland Communities. Since 2000, Falmouth has had a rate below the average in each year with the exception of 2003. This table relies on State derived data and revised data is not yet available.

Greater Portland Communities	2005	2004	2003	2002	2001	2000
Cape Elizabeth	11.71	12.48	12.72	13.91	15.07	15.88
Cumberland	12.54	13.70	14.22	15.67	16.74	17.41
Falmouth	12.44	14.38	15.28	15.48	16.38	17.15
Gorham	12.69	14.37	15.22	16.11	16.61	17.74
Portland	14.91	15.96	17.59	19.03	19.57	20.91
Scarborough	11.23	12.52	12.86	13.93	15.11	16.27
South Portland	13.23	14.09	14.91	16.40	18.53	18.57
Westbrook	15.27	17.97	17.30	18.44	19.30	19.35
Windham	11.72	14.11	13.91	14.33	14.78	15.45
Yarmouth	15.22	16.63	18.00	19.33	18.46	18.56
Average Full Value Rate	13.09	14.62	15.20	16.26	17.05	17.73
Falmouth	12.44	14.38	15.28	15.48	16.38	17.15
Variance from Average	0.66	0.24	(0.08)	0.79	0.67	0.58

Debt Ratios

The Maine Municipal Bond Bank has found the average debt/valuation ratio for Maine municipalities to be 2.1%. Municipalities have a legal debt limit of 15%; however, bond analysts consider anything under a 3 % debt/valuation ratio to be acceptable. As of June 30, 2008, Falmouth's gross debt/valuation ratio will be 1.05%. When the state subsidy for the 2000 high school bond issue is factored in, the effective debt/valuation ratio drops to 0.71%. It should be noted that the bonded indebtedness of the Town's sewer utility is paid for through sewer user charges, and not through property tax dollars, and therefore is not shown in this table.

Fiscal Year End June 30	Pop.	Assessed Valuation (x 1,000)	Total Direct Debt* (x 1,000)	Debt as % of Assessed Value	Direct Debt per Capita
2008	11,900	1,752,772	18,414	1.05%	1,547.39
2007	11,760	1,705,815	19,998	1.17%	1,884.23
2006	11,460	1,658,290	17,486	1.05%	1,525.83
2005	11,320	1,643,281	18,925	1.15%	1,671.82
2004	11,205	1,534,080	20,863	1.36%	1,861.94
2003	11,021	1,135,149	22,022	1.94%	2,013.53
2002	10,802	1,099,391	23,570	2.14%	2,182.00
2001	10,556	1,027,758	23,845	2.32%	2,270.95
2000	10,310	889,126	18,703	2.10%	1,814.06
1999	9,859	838,717	5,160	0.62%	523.38
*Reflects School Debt and does not reflect state subsidy for high school bond issue.					

Assessed Valuation

Over the past 20 years, Falmouth's valuation has increased between 1-4% per year as a result of new construction. The Town Assessor has projected that new construction will add \$30 million, or 1.8% to the Town's assessed valuation for 2009 for a total valuation of \$1,695,634,400 (exclusive of TIF valuation). This equates to over \$140,000 per capita, which is generally considered a very good valuation ratio for a community with limited commercial tax base.

SPECIAL NOTE: The tax rate calculation process for FY 2009 is complicated by the fact that the Assessor is conducting a revaluation of all residential and commercial properties to approximately 100% of market value, effective with April 1, 2008 valuations. Thus, the actual tax rate for FY 09 will be lower than FY 08, because of the higher valuation base denominator used in the tax rate calculation. The only way to achieve an "apples-to-apples" comparison between the two tax years will be to factor in only the new valuation.

Tax Collection Rates

A municipality's tax collection rate is another indicator of financial stability. Falmouth has had an excellent collection rate exceeding 98% in each of the past five years. Unfortunately, with the declining economy, we may see a decline in the collection rate in the next few years, which may have a negative impact on the Town's fund balance.

Undesignated Fund Balance

Falmouth's unreserved, undesignated fund balance as of June 30, 2007 was \$10,319,158. The fund balance should not be looked at as "cash on hand" or as simply surplus funds. There are a number of encumbrances against the fund balance such as reserves for receivables (unpaid taxes). For example, as noted above, if the tax collection rate were to decline to 91%, as it did during the recession in the early 90's, the amount that would need to be reserved for tax receivables would increase substantially. Fortunately, the current fund balance exceeds the minimum standards set by the Council's adopted fund balance policy, providing the Town with a healthy "available" fund balance. A copy of the fund balance policy is attached as Appendix D.

The fund balance provides the Town with adequate coverage for various liabilities, accounts receivable, unforeseen expenses or shortfalls in revenues. It also has enabled the Town to meet most of its cash flow needs despite the timing of property tax collections, which are well into the fiscal year.

Analysis of Fund Balance	
Unreserved, undesignated Fund Balance (6/30/07)	\$10,319,158
Net Receivables	(461,631)
Tax-acquired property	(6,647)
Other non-cash assets	(58,305)
Unencumbered Fund Balance	9,792,575
Council's Minimum Fund Balance Reserve* * 16.7% of total 2007-08 expenditure budget	(5,931,099)
Supplemental Appropriations	(153,000)
Projected "Available" Fund Balance	\$3,708,476

The “available” fund balance should not be relied upon for regular tax relief. In accordance with Council fund balance policy, this available balance is to be used only for what is commonly called “one-time” expenses. This budget includes use of \$100,000 of available fund balance to flatten the impact of the CIP. We expect FY09 to be the last year of fund balance use to balance the CIP. Regular reliance on fund balance will artificially reduce the tax rate but when fund balance is no longer available, the tax rate will increase dramatically. “Available” fund balance is essential for the Town’s ability to respond to unforeseen circumstance. These unforeseen circumstances can include natural disasters, premature infrastructure failure, and economic influences uncontrollable at the local level.

LD1 Compliance

In 2004, the Maine legislature passed the municipal “expenditure cap” statute known as “LD1”. Under this statute, the annual percent increase in the municipal (non-school and non-county) property tax levy is subject to a maximum cap based on both a statistical income growth limit percentage established each year by the state, as well as a property growth limit calculated by the Town’s Assessor. The estimated LD1 limit for 2008-09 is calculated as follows:

Actual 2007-08 municipal tax levy limit	\$6,172,014
Plus estimated 5.04% 2008-09 growth limit	<u>311,070</u>
Projected 2008-09 tax levy limit	\$6,483,084
Projected 2008-09 municipal tax levy	<u>5,933,580</u>
Amount under tax levy limit	\$549,504
Percent. Under tax levy limit	8.5%