



Committee on Finance and the Northampton City Council

*Councilor David A. Murphy, Chair
Councilor Maureen T. Carney
Councilor Marianne L. LaBarge
Councilor Gina-Louise Sciarra*

**City Council Chambers, 212 Main Street
Wallace J. Puchalski Municipal Building
Northampton, MA**

Meeting Date: March 27, 2018
Time: 4 p.m.

- 1. Meeting Called To Order:** At 4 p.m. Councilor Murphy called the meeting to order.
- 2. Roll Call:** Present were committee members Maureen Carney, David A. Murphy and Gina-Louise Sciarra. Also present were Auditor Thomas Scanlon and Jeff Gendron from Scanlon and Associates, LLC, Finance Director Susan Wright, Collector/Treasurer Kris Bissell, Principal Assessor Joan Sarafin, Auditor Joyce Karpinski, Mayor David Narkewicz and City Councilor Jim Nash. Councilor Marianne LaBarge arrived at 4:46 p.m.
- 3. Approve Minutes of March 1, 2018 Meeting:** Since the Administrative Assistant was not present, members tabled approval of the minutes to the next meeting.
- 4. FY2017 Year End Audit Review By Scanlon And Associates, LLC**
Mr. Scanlon reviewed the report entitled, "City of Northampton, Massachusetts, Report on the Examination of Basic Financial Statements for the Year Ended June 30, 2017." In general, there was no disagreement with management over the audit and no problems, and the process was very smooth, he reported. The financial reporting is in good shape and the accountability was very good. Auditors made no significant adjustments this year except a couple to clear up the water/sewer bearings.

On pages 3 and 4 of the document, the city received an unmodified opinion on the accuracy of its financial statements which bond agencies and grant-awarding agencies will look at, Mr. Scanlon said. He drew attention to government-wide financial statements presented on pages 16 and 17. In particular, on the city's 'Statement of Net Position Highlights,' he stressed the fact that there is a deficit of \$73,785,537 in the city's unrestricted net assets. "It's never good to have your net position in the negative," he observed. The two drivers of this deficit are the OPEB Obligation Payable of \$49.7 million and the Net Pension Liability of \$54 million, he advised. The OPEB obligation represents a real financial liability in that it represents promises made to retirees to pay their health insurance premiums. The city established an OPEB trust to address this liability which, as of June 30th, 2017, has approximately \$433,000. As he tells most of his clients, it's not

City Council Committee on Finance Meeting Minutes for February 15, 2018

possible to fund \$49 million within the regular budget, but the liability should be part of the thought process involved in budgeting and hiring. I.e. – when filling vacant positions through retirement, etc., the cost of future health benefits should be considered as part of the total cost and the city should consider making a contribution to the OPEB trust to meet this future liability. The only way OPEB costs go away is as people expire, he pointed out.

The city is on a payment schedule with the retirement system so that, at some point (2032, Susan Wright confirmed), the Net Pension Liability will be fully-funded.

In response to a comment from Councilor Murphy, Mr. Scanlon confirmed that these liabilities are typical of every municipality.

The city is paying retirees' health insurance as it goes, so it is fulfilling the promises made to retirees, but it hasn't set aside money for future payments, Ms. Wright clarified. The city is increasing the OPEB trust in the budget every year by over \$100,000, she added. The plan is that, once the pension obligation is fully funded in 2032, the city will shift the roughly \$6 million per year it contributes toward pensions to the health insurance liability. "We have a plan," she confirmed. "We have to take care of retirement first."

The theory behind OPEB is that one position can lead to liability for multiple health insurance premiums, Mr. Scanlon elaborated. When a police chief retires, the city has liability for the retired chief's health insurance and the health insurance for the new chief. If the new chief then retires and another is hired, the city can be paying three health insurance costs for one position.

In 2009, the Governmental Accounting Standards Board (GASB) began requiring municipalities to show this OPEB liability on their balance sheets, Mr. Scanlon recounted. If they look at retirees' health insurance costs in the budget, they have done nothing but go up, he noted.

Councilor Nash asked if the number of people in the retirement pool is growing, and Ms. Wright said she could answer that question by looking at the actuarial reports, which state the number of retirees. "There's more actives than retirees," she said. However, people are living longer, and public safety employees can retire early, so the city is more likely to have multiple costs for a public safety position than for other jobs.

Teachers are in the state retirement system for their pensions, but the city is responsible for their health insurance benefits, Ms. Wright confirmed. They are the largest group of retirees, she said.

In smaller communities, the retiree population is not growing significantly, but he would say the population is growing in Northampton, Mr. Scanlon said.

The projection of OPEB liability assumes that everybody eligible for health insurance takes it, but this is not the case, Ms. Wright pointed out.

Pages 18 and 19 present traditional financial statements (Balance Sheet – Governmental Funds and Statement of Revenue, Expenditures and Changes in Fund Balance – Governmental Funds), Mr. Scanlon continued. The 'Unassigned Fund Balance' (\$14 million) is made up of Free Cash, Stabilization and Overlay Accounts, he said. The city's Free Cash is \$4.1 million, the three Stabilization Funds are \$8.2 million

City Council Committee on Finance Meeting Minutes for February 15, 2018

and the Overlay balance is \$1.4 million, representing about 14% of the city's annual budget. Having 10% of the budget as reserves is considered good, Scanlon observed.

Mr. Scanlon drew attention to the 'Changes in Fund Balance' on page 19. The net change in fund balance for the General Fund is \$2,493,978, he presented. This tells him a lot in looking at the city's financial statements. It shows that the GF balance increased by \$2.4 million. The make-up of that is encumbrances from the previous fiscal year and the net increase in reserves. It is good to see and reflects sound financial policies, he indicated.

The city established a fiscal stabilization fund which hasn't been touched yet, he added. The original goal was to tap into it in FY2016 and FY2017, but the city didn't use it in those years, Ms. Wright confirmed. The city also didn't use it in FY2018 and it's uncertain if it will need to tap into it in FY2019, she said.

It's a lot easier for City Councils and Boards of Selectmen to make decisions to spend Free Cash and Stabilization when they are sitting on 10 to 15% of reserves and have the ability to put money back into reserves within a two-year period, Mr. Scanlon remarked. The city had negative Free Cash for one year, Councilor Murphy reminded. In 2010, the city started the year with no Free Cash and only \$4,000 in Stabilization, Ms. Wright confirmed.

City officials "should be congratulated" on their financial policies and financial decisions, Mr. Scanlon commented.

On page 18, accountants elected to show the Stormwater Fund as a governmental fund as opposed to an Enterprise Fund, he noted. It was a 50/50 call that could have gone either way. It's more 'user-friendly' than showing fixed assets with depreciation and full accrual, he suggested. The fund has a lot of public eyes on it, so he thought it would be easier to read. For Mass. General Law and budget purposes, it is an enterprise fund, but for generally accepted accounting principles (GAAP) purposes it is a governmental fund.

Non major governmental funds include grants, revolving funds and capital projects, he explained. The finance team has a quarterly policy to review those funds and see how they are being used, he advised.

Next, Scanlon drew attention to the statement of budgeted vs. actual expenses on page 22, which is the source of the city's free cash. The city took in \$2.2 million more in revenue than projected and spent \$2.1 less than budgeted, he pointed out. This represents a very good mix of how Free Cash is being generated; it's not all coming from one side, he observed. Projected revenue for excise and other taxes and Hotel and Meals taxes was conservative and came in higher than expected, he noted.

Finally, Mr. Scanlon reviewed pages 81 to 84, the Schedule of Real Estate, Personal Property and Rollback Taxes and Deferred Property Taxes. The last column is the detail in the Collector's office and the second to the last column is the General Ledger, he pointed out. Members can see there are no variances between the two figures, which is very good. The collection rate is 98.3%, which doesn't get much better. The schedule tells them as auditors and should tell readers that the Tax Collector is doing a good job and the tax accounts are balancing. The amount of tax liens is also not inordinately high (\$333,018). "You wouldn't want to see a balance here of like \$6 million." All of these schedules tell them that the collector is doing a good job. The whole point of the segregation of duties is that the Tax Collector is taking in cash and

City Council Committee on Finance Meeting Minutes for February 15, 2018

accounting for it in subaccounts and details and the City Auditor is maintaining the General Ledger. Those two accounts should be balanced; if there is a variance between them it means something is going on. There is minimal variance, he observed.

This is the 13th audit report he has sat in on and they just keep getting better and better, Councilor Murphy said.

The audit went very smoothly this year and Free Cash was certified early, Mr. Scanlon agreed. The city is very responsive to recommendations for adjustment, he indicated. Whenever an area of concern is identified in fieldwork, it is addressed immediately, he advised.

Mr. Scanlon reviewed the "City of Northampton, Massachusetts Management Letter for the Year Ended June 30, 2017." Page 4 contains informational items about the timeline for implementation of future GASB Statements.

The only new comment/recommendation is that departments turning over money to the Treasurer should indicate what portion of the deposit is cash and what portion is check. It just solidifies the audit trail of the cash. "Most everyone is doing that on their turnovers," Ms. Wright reported.

Mr. Scanlon briefly reviewed comments and recommendations from the prior audit year, noting how some of the issues have been resolved. Scanlon and financial officers discussed half a million dollars (\$497,355) in personal property taxes that are still outstanding for years prior to 2013. This is basically a matter of clearing these debts off the books and is something to work towards, Mr. Scanlon advised.

"We are working on this," Ms. Wright assured. She read about a town that did an amnesty program for back personal property taxes but it required special legislation, she related. In some cases the interest on the tax owed exceeds the original tax, and an amnesty program would allow owners to just pay the tax portion of the outstanding balance.

The third audit is a single audit that applies to cities and towns that spend over \$750,000 in federal money in a single year, Mr. Scanlon continued. (As a sanctuary city, there is a question about whether the federal government could withhold federal grants based on the city's sanctuary status, members noted.) The city received \$5.3 million in federal funds. As a result, auditors tested the Community Development Block Grant (CDBG) for compliance with laws and regulations applicable to the program.

Councilor LaBarge arrived.

Ms. Wright thanked the three financial officers for their work in carrying out financial operations. Over the 13 years he's been looking at these audit reports, the management letter is getting thinner and thinner and the suggestions are being dealt with, Councilor Murphy commented.

Councilor Carney moved to accept the FY2017 audit. Councilor Sciarra seconded. The motion passed unanimously 4:0.

He will report to the full council next week that the Finance Committee has reviewed the audit and thinks it's acceptable, Councilor Murphy said.

The Finance Committee took a five-minute recess. The committee reconvened at 5:01 p.m.

5. Public Hearing to Consider Proposed Water And Sewer Rates For FY2019

Councilor Murphy read the legal notice advertising the public hearing.

Councilor Sciarra moved to open the public hearing. Councilor LaBarge seconded. The motion passed unanimously 4:0.

As background, Mayor Narkewicz noted that this is now the fourth fiscal year of the new process for approving water and sewer rates prescribed by the Administrative Order reorganizing city government. Per the order, water rates are to be recommended by the Mayor and approved by the City Council. As members may remember, the rates were not changed for FY2015 and FY2016. The Mayor's office then went out and solicited public feedback and did a significant study resulting in the development of a new tiered rate system. The intent of the new system was to build more fairness into the rates for smaller vs. larger users and to build in incentives for water conservation. The two-tiered system has one rate for users with one-inch or smaller meters (small businesses and residential users) and another for users with one-inch or larger meters. There is a lower rate for the first 16 CCF of consumption to encourage water conservation.

Administrators based the sewer rate on 80% of metered water consumption as opposed to 100% as it was in the past. City officials went through a pretty extensive public process and also built in a provision for discounts for low-income residents.

The new rates were implemented in FY2017. In FY2018, administrators did not recommend an increase but maintained the same rates as in FY2017. This year, in consultation with Director LaScaleia about upcoming capital projects, the proposal is to make three changes to the rates:

For Tier 1 consumption, a 1% increase is proposed, from \$4.36 per CCF to \$4.40 per CCF

For Tier 2 consumption, a 2% increase is proposed, from \$5.82 to \$5.94 per CCF

For customers with meters larger than one-inch, a 2% increase is proposed, from \$5.72 to \$5.84.

The FY2019 sewer rate (based on 80% of metered water consumption) is going from \$7.52 per CCF to \$7.67, he concluded.

Mayor Narkewicz introduced Director LaScaleia to explain why the increase is needed to fund the capital improvement needs of the enterprise.

Director LaScaleia referred to her memo re: FY2019 Water and Sewer Rates dated March 16, 2018. DPW administrators did a thorough analysis of operations taking into consideration personnel and capital projects, including water line replacement, large capital expenditures and existing debt service. She put a price tag on some of the expenditures since FY2017 to show councilors the cost of the work that's been done. The DPW has done a significant amount of road reconstruction and, as part of that, utility work. In the memo, she listed some of the big-ticket construction projects that have been completed, such as Audubon Road, Hinckley Street and Day Avenue. She's tallied up what's been spent out of water enterprise for those
City Council Committee on Finance Meeting Minutes for February 15, 2018

projects, and it's pushing \$2 million. Just in the last 18 months, they've spent a significant amount of money on what she would call very basic infrastructure repairs to keep the system functioning. For this construction season, the DPW intends to continue routine maintenance with water line replacement on Chesterfield Road and Hampden Avenue. (This aggressive schedule is based on the Water Asset Management Plan produced for the DPW by a consultant several years ago, she noted.) In addition to routine maintenance, it is necessary to look at large infrastructure repairs that are needed. Director LaScaleia outlined four major projects included in the capital plan:

- ❖ Improvements to the Wastewater Treatment Plant. The city is looking at more than \$22 million in upgrades over the next five years, LaScaleia advised. \$22 million represents the first phase of upgrades based on the comprehensive Wastewater Management Plan. Additional upgrades are expected to cost another \$60 million on top of the \$22 million, she reported. In setting sewer rates, they need to take these anticipated costs into consideration.

Three projects related to the water enterprise:

- ❖ Rehabilitation of the Audubon tank
- ❖ Reservoir construction – the city has three active reservoirs that need \$8 million worth of work to address deficiencies
- ❖ Transmission main rehabilitation. 22,200 linear feet of transmission main provide water to the city from the water treatment plant. The main runs through a swamp, is largely inaccessible and is over 100 years old. DPW officials need to start the process of designing and constructing a new main.

In 2006, the city bonded over \$25 million for construction of the water treatment plant, Ms. LaScaleia reminded. The debt service on that bond still represents 29% of total revenue and does not fall off the books until FY2028. Even level-funding the budget for operations, the city cannot assume further debt with the current level of debt. The thought process is proposing a modest increase in rates with an eye toward the large pending infrastructure projects. The revenue will allow the city to assume more debt service to begin the process of permitting and design for some of these projects.

As far as the impact on residents, administrators have done some modeling to calculate the effect. The city presently has 8,681 water accounts, 7,271 of which are 5/8-inch meters, the standard size for a residential customer. The typical customer uses 15 CCF per quarter - a little over 11,000 gallons a quarter or 45,000 gallons per year. They did an analysis to show what the typical resident's bill would look like. The typical resident is looking at an increase of .60 per quarter or \$2.40 per year, she presented. The increase in the sewer rate represents about \$1.80 more per quarter or \$7.20 per year, for a total increase of \$9.60 a year.

The increase will give the DPW some flexibility in terms of debt service for some of these large capital projects, she concluded. There is plenty of permitting and design that has to go into these projects before they can actually launch. "This increased revenue will help to get us where we're going," she observed.

Members asked questions and offered comments.

Right now, a third of the water enterprise budget is debt, Ms. Wright advised. The city is paying about \$2 million a year in debt. Improvements to the sewage treatment plant will be funded with a combination of money from the Stabilization account and bonding, she added. The city will work with its financial advisors to come up with a plan for financing the work.

City Council Committee on Finance Meeting Minutes for February 15, 2018

Councilor Sciarra questioned whether the modest increase would be sufficient to cover the very large ticket items Director LaScaleia mentioned.

It's important as they go through this process to be deliberate and responsive to concern about stability and rates, Ms. LaScaleia responded. As they gradually phase these projects in, they will continue to have a conversation about what is appropriate as far as fee structure, she indicated.

Councilor Murphy said he didn't think they should assume that a 1% to 2 % annual increase would take care of the needed investments. The increase will probably increase incrementally until 2028 when the debt for the water treatment plant is paid off, he suggested.

It's important that everyone understand that there is a lot of infrastructure that can't be seen, Ms. LaScaleia asserted. When residents see the DPW digging up a water line, "that's just the tip of the proverbial iceberg," she commented, noting that reservoirs, the water treatment plant and equipment must be maintained and replaced.

Councilor LaBarge asked Director LaScaleia if she intends to do a presentation to inform the public of these pending projects.

"This is, in fact, a public hearing," Councilor Murphy reminded.

Councilor Murphy asked if there was any public comment.

"I think it's a reasonable increase based on all the stuff we've got to do," Councilor Nash commented.

There being no further public comment, Councilor LaBarge moved to close the public hearing. Councilor Carney seconded. The motion passed unanimously 4:0.

6. Financial Orders

A. **18.070 Order To Establish Water And Sewer Rates For FY 2019 - Referred By City Council 3/15/2018**

Councilor Carney moved to forward the order to the full council with a positive recommendation. Councilor LaBarge seconded. The motion passed unanimously 4:0.

7. New Business

-Reserved for topics that the Chair did not reasonably anticipate would be discussed.

Upon motion made and seconded, the meeting was adjourned at 5:41 p.m.

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