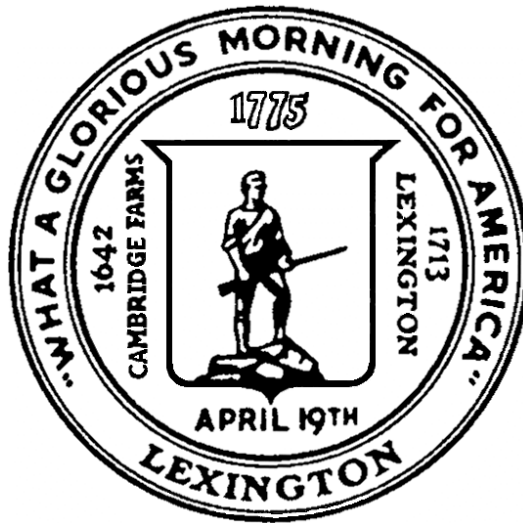


APPROPRIATION COMMITTEE

TOWN OF LEXINGTON



REPORT TO THE November 9, 2009 SPECIAL TOWN MEETING

Released November 9, 2009

Appropriation Committee Members—Fiscal Year 2010

Alan M. Levine, *Chair* • Glenn Parker, *Vice Chair*
John Bartenstein, *Vice Chair and Secretary* • Robert N. Addelson (*ex-officio; non-voting*)
Richard Eurich • Mollie Garberg • Pam Hoffman • Susan McLeish
Eric Michelson • Joe Pato

Summary of Warrant Article Recommendations

Abbreviations: GF = General Fund; EF = Enterprise Fund; RF = Revolving Fund

CPA = Community Preservation Act Fund; BAN = Bond Anticipation Note;

SF=Stabilization Fund; SSF=Specialized Stabilization Fund

An entry of "Indefinitely Postpone" in the right-hand column merely signifies our expectation.

Ar- ticle	Title	Funds Requested	Funding Source	Committee Recommendation
2	Zoning Bylaw – Amendment to PSDUP Lexington Technology Park	none	N/A	Approve (9-0)
3	Zoning Bylaw – Amendment to PSDUP Cubist Pharmaceuticals	none	N/A	Approve (9-0)
5	Authorize Munroe School Disposition	none	N/A	Pending
6	Approve Local Option Meals Excise	none	N/A	Approve (7-2)
7	Approve Local Option Room Occupancy Excise	none	N/A	Approve (7-2)
8	Contracts for Solar Energy	none	N/A	Approve (8-0)
9	Appropriate for Sister City Program	Unknown	GF	Pending
10	Appropriate to Traffic Mitigation Stabilization Fund	\$35,000	RF	Approve (9-0)
11	Appropriate to Stabilization Fund	approx. \$650,000	GF	Approve (8-0)
12	Appropriate for Waltham Street Pedestrian Crossing	\$25,000	SSF	Approve (9-0)
13	Amend FY2010 Operating Budget	none	N/A	Approve (8-0)
14	Amend FY2010 Enterprise Fund Budgets	none	EF	Approve (9-0)

Note: Some of the votes do not reflect the full membership of the Appropriation Committee because of unavoidable absences due to illness.

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Introduction

In this report, we present our recommendations on those articles with significant financial aspects to be acted upon at this Special Town Meeting.

The Town's most important component of available funds, known as the unreserved fund balance or "free cash," was recently certified as of July 1, 2009 by the Massachusetts Department of Revenue at \$6,159,509. This amount, which will be available for appropriation at the 2010 Annual Town Meeting to support the FY2011 budget, is substantially more than was projected in late spring and early summer by Town officials. One of the reasons that the figure is high is that the Assistant Town Manager for Finance and the staff of the Finance Department worked hard during the summer to close out open or pending purchase orders and similar items from the last three fiscal years. This effort yielded approximately \$1,700,000 for the unreserved fund balance, but it must be considered a one-time source of revenue.

The process of determining "new growth" (the increase in the tax base resulting from new construction) is far along and Town officials now expect the final figure for FY2010 to be at least \$2,450,000. This amount is a \$550,000 increase over the \$1,900,000 that was projected at the time of the 2009 Annual Town Meeting. This new growth estimate may be revised as analysis continues in order to use a solid value in connection with an appropriation to the Stabilization Fund proposed under Article 11.

The FY2010 State budget enacted after the close of the 2009 Annual Town Meeting includes a number of provisions intended to offset reductions in state aid to cities and towns. One such provision expressly subjects utility-owned poles and wires to local property taxation, effective at the start of FY2010. Historically these assets were considered exempt until the Appellate Tax Board (ATB) ruled in 2008 that they were taxable. Taxes on poles and wires that the Town collected during FY2009 remain in escrow pending appeal of the ATB decision. However, the legislative enactment resolves the issue going forward and this new tax is expected to generate almost \$700,000 in recurring revenue for the Town in FY2010 and subsequent years. The State budget also authorizes cities and towns to adopt as a "local option" increments to the meals and room taxes that could generate approximately \$500,000 in recurring revenue for the Town of Lexington (approximately \$210,000 for FY2010 since the earliest effective date would be January 1, 2010). These "local option" excise taxes will be taken up under Articles 6 and 7.

We were relieved to hear that Governor Patrick will not (yet) propose additional cuts in local aid for FY2010 as part of his plan to close the most recent gap between State revenues and expenses. Nonetheless, the Town Manager and staff are proposing to set aside \$231,000 of the projected revenue increase as a hedge against a potential reduction in State aid later this fiscal year. Under Article 11 Town Meeting will be asked to appropriate the balance of the net incremental FY2010 revenue, totaling approximately \$650,000, to the Stabilization Fund.

Additional explanation of changes to revenues and expenses will be reported by the Town Manager and staff as part of their presentation under Article 13 "Amend FY2010 Operating Budget".

For the articles involving appropriations, the possible sources of funds at this Special Town Meeting include the General Fund (which for this purpose generally includes the tax levy, other sources of funds such as state aid and local receipts), the Enterprise Fund, the Mitigation Fund, Free Cash, the Stabilization Funds, the Reserve Fund, the Traffic Mitigation Special Revenue Account, and Community Preservation Act (CPA) funds.

Warrant Article Analysis and Recommendations

CD Rezoning Financial Analysis

Articles 2 and 3 are requests from property owners for amendments to the Preliminary Site Development and Use Plans (PSDUP), documents previously negotiated by the Planning Board and passed by Town Meeting, which dictate the terms of the creation of unique Controlled Development (CD) zoning districts. In addition, a Memorandum of Understanding (MOU) has been negotiated by the Board of Selectmen for each project that details measures to be taken by the property owners and the Town, if the rezoning is approved, to address and mitigate the increased traffic these projects are expected to create.

Our committee's study and debate of these articles has centered primarily on the financial issues associated with the rezoning proposals and, in particular, the financial impact analyses that have been submitted by Connery Associates on behalf of the proponents. It should be noted that these analyses address only the direct "cash flow" impacts of the proposals, comparing the projected additional tax revenue from "new growth", permitting fees and traffic mitigation funds resulting from the rezoning proposals with the projected increase in the cost of providing town services such as police and fire services. They do not address more intangible impacts of the additional development – such as the aesthetic and "quality-of-life" considerations of increased density, congestion, visual impact and noise, or the availability of jobs closer to home and the potential for more local business activity. These are also valid factors for Town Meeting to consider but are inherently subjective and difficult to quantify.

The financial analyses of the rezoning proposals under both Articles 2 and 3 are based on identical or, at least, very similar premises. In this introduction, we address issues common to both. A more detailed look at the analyses of the individual projects follows in the separate write-ups on each article.

Incremental Cost of Town Services Related to Commercial Property

Estimating the "cost" of municipal services provided to a particular piece of property depends upon the property's use and the demands that it and similar properties of its type make on the various services provided by the Town. Generally, municipal service costs associated with commercial properties are significantly less than the costs attributed to residential properties. In particular, a commercial property makes no demand for public education services. Additionally, in many instances the Town does not provide other services such as lighting, trash collection and snow plowing to commercial properties. Thus, the addition of a new commercial property to the Town often imposes few new expenses or obligations on the Town in these areas.

Both commercial and residential properties often require assistance from public safety services, i.e., police and fire protection. The addition of new property may result in an increase in public safety costs as the Town must expand its human and equipment resources in those areas to accommodate the increased demand. Commercial property, as a whole, exerts a greater demand for police and fire services than does residential property. There are, however, gradations within the general category of commercial property, retail shopping centers and malls demanding far more public safety services than office parks or laboratory buildings.

In their analyses for both Lexington Technology Park and Cubist Pharmaceuticals, Connery Associates has assumed that the estimated public safety services costs attributable to non-retail businesses in Lexington may be fairly represented by approximately 35% of the Town's total police and fire budgets.

For FY2010, that total is approximately \$10,150,000. Thirty-five per cent of that figure is about \$3,550,000. To estimate the impact of each of the requested projects, the projected increase in square footage for each project was compared to the total existing square footage of existing commercial and industrial space in Lexington. This appears to be a plausible way to evaluate the expected increase in public safety costs to the Town should the projects be approved. We have no better method of performing such an evaluation.

The Town will face increased costs related to upgrading and maintaining its road and intersection infrastructure because of increasing levels of traffic, part of which will be due to increased levels of commercial development. These costs will be fully tangible. The proponents of the increased levels of development to be proposed under Articles 2 and 3 have signed memoranda of understanding (MoUs) with the Town regarding payments to help the Town mitigate the effects of increased levels of traffic. The terms of these MoUs are summarized below in our analyses of the two articles. We have not undertaken and therefore do not discuss below nor has Connery Associates presented in their financial impact analyses an analysis of whether those mitigation payments represent a fair contribution based on a quantitative traffic analysis of the costs the Town will face. Also, neither we nor Connery Associates present an estimate of traffic infrastructure long-term maintenance costs. Perhaps the pro-rated share of the long-term maintenance costs that are attributable to the proposed developments would not be a high dollar figure.

The incremental cost in Town services resulting from a proposed project, standing alone, does not permit a complete evaluation of a project or of its benefit to the Town. Similarly, considering in isolation the projected tax revenue predicted for a project will not present a balanced picture. We examine the ratio of these two numbers, estimated service costs divided by estimated tax revenue, to estimate the additional cost the Town will incur for each dollar of additional tax revenue it will receive. The calculation of this ratio is presented in the analyses of both the Lexington Technology Park and Cubist Pharmaceuticals proposals.

Commercial Property Tax Revenue

Predicting future property tax assessments, and thus the tax revenue that a property will generate, is a simpler task for residential property than for commercial property. There are two principal differences: (1) the method of valuing the property; and (2) the variability of assessed valuations.

Method – State laws and regulations determine the method the Town must employ to value real estate. The assessed value of a personal residence is determined by its retrospective sale value, what a hypothetical willing buyer would have paid to purchase the property, or a similar property, from a hypothetical willing seller. That determination, in turn, is based on factors such as size, style, location, and lot size, and how those factors have affected the selling price of similarly situated and comparable houses.

The assessed value for commercial property is determined by the retrospective potential income the property would have generated for its owner. Rents that a particular piece of property can be expected to generate are determined by the type of use (e.g., office, lab/office, retail) to which the property will be put. The property is placed into one of these general classifications, which then are further refined by the quality of the facilities, which affects the level of rent tenants are willing to pay (class A, B, C, etc). The income potential for a particular class and classification are determined by reducing the gross income by allowable expenses and then future offset to reflect the vacancy rates within each class and classification. Unlike residential assessments, the cost of construction and features of construction and other component features (such as parking structures) are only relevant if they contribute to a higher than average rent for the property.

Variability of Assessed Value – While both residential and commercial property values are affected by economic conditions, the way in which they are affected varies. In Lexington, the trend for residential property values has been slow and steady growth, with serious economic downturns causing a temporary cessation of growth or a slight devaluation. Commercial property values have also grown over time. However, the trend for their growth is less steady, with more frequent and more pronounced periods of devaluation and inflation. Standard economic factors that affect the business cycle will also adversely affect commercial rents, causing temporary and sometimes significant reductions in the assessed values for commercial properties. Lexington specifically, and Massachusetts and the nation generally, are currently confronting a number of these negative factors.

Connery Associates may fail to fully capture the impact of the current economic recession in their financial analysis. They use the latest assessed values and tax rates, but due to the limitations of the assessing system, these values reflect economic conditions as of January 1, 2008, prior to onset of the economic crisis. However, what truly matters is the value that is ultimately placed on the completed project, which will depend on economic conditions when the buildings are actually constructed and assessed. It is this value that will be counted as “new growth” and will increase the Town’s overall property valuation and overall maximum allowable property tax revenue as regulated by Proposition 2½.

Cost to Revenue Ratios

Just what will these properties yield in tax revenue? A firm knowledge of the anticipated classification of tenant and the use of the leased space is essential to establish a plausible range of future assessed values for a particular property. The proposal in Article 2 allows for a variety of future mixes between office and lab space, that increases the range of possible tax revenues in the estimate. The proposal in Article 3 is based on a definite plan regarding occupants and uses, and thereby should allow a less uncertain revenue prediction. However, as a rule the large variability in the assessed value of commercial property makes it inherently difficult to predict the future value of any commercial property, and therefore equally difficult to predict the tax revenue from that property.

It is important to understand the projected cost to revenue ratio. What is the magnitude of the costs of town services required by these projects, and how do they compare to the gross property tax revenue? The costs of town services required will inflate along a fairly predictable curve while future property valuations will be far less predictable. If the estimated cost to revenue ratio is very low, then the project will likely continue to generate a positive cash flow over a wide range of future valuations, so the risk of “losing money” by approving a project remains very low. If, on the other hand, the projected cost to revenue ratio for a proposed project is high (for example, 0.9 or greater), then the risk of “losing money” due to a slight downward variation in the property's future assessment is substantially higher.

Article 2: Zoning Bylaw – Amendment to PSDUP Lexington Technology Park	Funds Requested	Funding Source	Committee Recommendation
	none	N/A	Approve (9-0)

This article requests Town Meeting to amend the Preliminary Site Development and Use Plan for Lexington Technology Park which had earlier been approved by the 2004 Annual Town Meeting. For the present intents and purposes, the amendment requested in this Article is the same as that requested in Article 2 of the May 6, 2009 Special Town Meeting Warrant. At the request of Patriot Partners, Article 2 was indefinitely postponed at the May 6, 2009 Special Town Meeting. The Appropriation Committee’s Report to the May 6, 2009 Special Town Meeting contained a comprehensive background and review of

the Article submitted at that time. The reader is respectfully referred to that report for more detailed information.

The zoning change approved in 2004 permitted Patriot Partners, once it obtained a special permit from the Zoning Board of Appeals, to construct two new buildings on the property. In 2008, the Board of Appeals approved the Definitive Site Development and Use Plan submitted by Patriot Partners. The approval of the Zoning Board of Appeals authorized the construction of the two new buildings, increasing the maximum permissible gross floor area for the property to 696,600 square feet. A new building at 400 Patriot Way is up but is not yet occupied. It and the land on and immediately around it are owned by Shire Pharmaceuticals. We understand that ground breaking for the construction of a new building at 200 Patriot Way is expected to occur during the second quarter of 2010. It will be leased to Shire Pharmaceuticals.

Under this present Article, Patriot Partners, as it had done in the prior Article, seeks Special Town Meeting authorization to construct two more new buildings, and to increase the square footage on a building leased to Shire Pharmaceuticals, and occupied by its Human Genetic Therapies Division. This request, if approved by Town Meeting, will increase the maximum permissible gross floor area on the property by 380,000 square feet, approximately 55%, to 1,076,600 (the proposal actually anticipates a total of 1,586,600 square feet, of which 510,000 is assigned to parking garages and decks). The request anticipates that the increase in square footage will in part be accomplished by increasing the floor area ratio (the ratio of the building area divided by the overall lot area) from 0.15 FAR to 0.24 FAR. Additionally, whereas the current buildings on and at the property are restricted to a height of 45 feet (except for 400 Patriot Way, which has a permitted height of 54.5 feet), Patriot Partners is requesting that the two new buildings contemplated in this proposal be permitted a maximum height of 68 feet. The requested increase in maximum permissible gross floor area by 380,000 square feet is identical to the request in the prior Article 2.

Consistent with its original statements to 2004 Annual Town Meeting, Patriot Partners intends, to the maximum possible extent, to lease the proposed new buildings to businesses involved in research and development, laboratory work and biotechnology. If such "preferred" tenants are unavailable, it will lease portions of the contemplated buildings for general office use. However, the actual construction, and then leasing, of the two additional new buildings will not take place for a number of years. In addition to approval of this Article by Special Town Meeting, other reviews and approvals of this proposal must be obtained before construction can begin. Based on the projected timelines Patriot Partners has provided, it will take at least 18 months from the Special Town Meeting approval of this Article to the completion of all review, approval and permitting processes. Actual construction of the buildings will take another 18 to 24 months.

The Appropriation Committee met with representatives of Patriots Partners on October 28 to review the proposed project and its financial impact on the Town. We have also attended a number of other meetings and presentations regarding this project, including meetings of the Planning Board, meetings sponsored by Patriot Partners, and meetings sponsored by TMMA. Finally, we have reviewed materials and other information, including the Fiscal Impact Analysis, dated July 29, 2009, as well as its predecessor, the February, 2009 Fiscal Impact Analysis both prepared by Connery Associates.

As projected by Patriot Partners, the additional development contemplated by this proposal will generate revenue for the Town far in excess of the costs the Town will incur. Currently, existing buildings on the property – 125 Spring Street, 300 Patriot Way and 500 Patriot Way, together aggregating 292,683 square feet – have a combined assessed value of approximately \$44,300,000, approximately \$151 per square foot. When their construction is completed, the two new buildings are expected to have a higher square foot valuation. In its July 29, 2009 report, Connery Associates projects an average valuation for the new buildings at \$225 per square foot, \$50 higher than the projection of \$175 per square foot in its earlier

report. This average was calculated as a weighted combination of lab space and office space. Even buildings dedicated primarily to lab space will often contain around 25% basic office space.

The Town's valuations of commercial space qualifying as laboratory and research space typically run from \$175 to \$275 per square foot. Valuations of commercial space used solely or primarily as office space run from \$110 to \$150. In light of Patriot Partners' intent to lease the proposed new buildings to businesses involved in research and development, laboratory work and biotechnology, Connery Associates' estimated assessed value of \$225 appears to be a conservative and reasonable one. It is still markedly higher, or more optimistic, than the recent February estimate.

The 380,000 square feet of additional construction sought in this proposal thus produces, at the \$225 per square foot figure, an assessed valuation of \$85,550,000 (compare this to the \$66,500,000 figure in the February, 2009 Connery analysis). At the current commercial tax rate of \$25.27, the additional 380,000 square feet sought in this proposal, when completely constructed and built out, will generate new tax revenues approximating \$2,161,000 (the figure in the February Connery analysis was \$1,612,625). To some extent, this increase reflects the Town's differing commercial tax rates in effect at the time of the respective analyses (\$24.25 per \$1,000 for the analysis in February, \$25.27 for the one in July). It also reflects a higher attribution by Connery Associates of the projected tax the proposed buildings, upon completion, will generate.

In addition, the current Connery Associates analysis projects that the 789 structured parking spaces contemplated in the proposal will generate a tax value of about \$500 per space, producing a total tax value of \$394,000. The attribution of tax revenue to structured parking spaces does not conform to this Committee's understanding of how commercial tax assessments are done, and we remain skeptical of the validity of this portion of the tax revenue estimate. Nevertheless, the impact of discounting this portion of the analysis is not large enough to affect our recommendation.

Annual costs to the Town for the services it must provide on account of the additional buildings are estimated by Connery Associates at approximately \$337,000. This prediction is based upon the FY2010 average cost of police and fire departments services provided by the Town to its currently existing non-retail commercial taxpayers. It is comparable to and consistent with the \$308,000 in increased costs estimated in the February, 2009 analysis, which were predicated on the Town's FY2009 police and fire departments budget.

Connery Associates' projections mean that the proposed development will result in a net yearly gain to the Town of approximately \$2,218,000. If the projected tax revenue for the 789 structured parking spaces is not included in the calculation, the Town's net yearly gain is \$1,824,000. The net yearly gain to the Town, as projected in the February, 2009 Connery analysis, was \$1,305,000.

Based on Connery's figures, the cost to revenue ratio, the estimated increase in service costs to the estimated increase in tax revenue, is 0.13. In other words, for every dollar of tax revenue the Town receives from the proposed project upon its completion, the Town will incur 13 cents to provide municipal services. If the estimated tax revenue for the 789 structured parking spaces is removed from the calculation, the cost to revenue ratio increases to 0.15. In the February, 2009 Connery analysis, the cost to revenue ratio was 0.19. In practice, this cost to revenue ratio will fluctuate depending upon local, state and national economic conditions.

Various factors may reduce or delay the positive impacts predicted in the Connery Associates Fiscal Impact Analysis. It is likely that the buildings will not be fully tenanted immediately upon their completion or for the first year after the project is completed. Also the full impact of these new tax revenues will not be felt until the construction of the two buildings is completed. As noted earlier, that will not occur for some time. Patriot Partners has no current plans or schedule for the construction of the

two new buildings. Even with the most optimistic prediction, these two buildings are not likely to make an appearance for at least five years.

Nonetheless, the Appropriation Committee is satisfied that the figures on which the ultimate prediction is based are sound, and that – whether or not the projected generation of \$394,000 in additional tax revenue for the 789 structured parking spaces is counted or not – the tax revenue that will flow to the Town, whenever the buildings are constructed, will far exceed their costs.

In addition to the net fiscal benefit to the Town, the Town also expects to receive building permit fees associated with the construction of the two new buildings. It is estimated that those fees will be approximately \$1,500,000.

Patriot Partners has agreed to make a number of voluntary payments to or directly benefiting the Town, as reflected in the Amended and Restated Memorandum of Understanding between it and the Board of Selectmen. These payments are tied to the occurrence of various events:

(1) Within 30 days of the Attorney General's approval of its Amended PSDUP, Patriot Partners will contribute (a) \$65,000 to the Town's Traffic Mitigation Stabilization Fund, to enable the Town to prepare a traffic plan of the Spring Street and Hayden Avenue Corridors and (b) \$15,000 to the Town to assist in the study of Shade Street calming strategies.

(2) Prior to the issuance of a building permit for any new building that adds net square footage to the entire property in excess of the square footage approved in the original PSDUP (505,800 square feet), Patriot Partners will contribute a total of \$600,000 to fund traffic and transportation mitigation for the benefit of the Town and the contemplated project, \$500,000 of which shall be paid to the Town's Traffic Mitigation Stabilization Fund, and \$100,000 shall be paid to the Transportation Demand Management/Public Transportation Stabilization Fund.

(3) Prior to the issuance of a certificate of occupancy for the second new building, Patriot Partners will pay the Town an amount of money equal to the product of \$1,900 multiplied by the number of parking spaces exceeding 2,260 that are created on the entire property or for which the capacity has been created as of that time, the first \$100,000 to be contributed to the Transportation Demand Management/Public Transportation Stabilization Fund, and the entirety of the balance being contributed to the Traffic Mitigation Stabilization Fund.

(4) At any time after the issuance of a certificate of occupancy for the second new building, if any parking spaces are created or the capacity for any parking spaces is created on the property, Patriot Partners will pay the Town an additional sum equal to the product of \$1,900 multiplied by the number of those parking spaces as well as the capacity for those parking spaces.

The Amended and Restated Memorandum of Understanding also contains other agreements and undertakings by Patriot Partners. One of the more important agreements is that, as a precondition to the development of Building 100 on the property, that the Tax Increment Financing Agreement signed by the Town, Patriot Partners and Shire Human Genetic Therapies will be amended so that the value of Building 100 "shall be fully taxable and shall not be eligible for TIF exemptions from taxation by the Town." The Appropriation Committee also understands that the other agreements made by Patriot Partners in 2004 (as described in the discussion of Article 10 in our April 13, 2004 Report to Town Meeting) continue and remain intact.

The Committee unanimously (9-0) supports this request.

Article 3: Zoning Bylaw – Amendment to PSDUP Cubist Pharmaceuticals	Funds Requested	Funding Source	Committee Recommendation
	none	N/A	Approve (9-0)

This article requests approval of amendments to the Preliminary Site Development and Use Plan for the CD zone at 45, 55, and 65 Hayden Ave. which had earlier been approved by the November 1997 Special Town Meeting. The original PSDUP created a new zoning district that comprised two lots, then both owned by Spaulding & Slye Hayden Woods LLC. The 45 - 55 Hayden Avenue lot is now owned by Realty Associates Fund, and the lot at 65 Hayden Avenue is now owned by Cubist Pharmaceuticals. This article is sponsored by Cubist Pharmaceuticals and asks for permission for additional development at 65 Hayden Avenue. Any new obligations and liabilities would become the sole responsibility of Cubist Pharmaceuticals.

As the owners and occupiers of 65 Hayden Avenue and tenants of the space at 45–55 Hayden Avenue Cubist Pharmaceuticals occupies the entire CD district. Cubist has proposed adding approximately 104,000 sq ft of research and development space as an additional story onto the existing building at 65 Hayden Avenue and constructing a five story parking structure on the same parcel. They intend to occupy the new space for their own use and to begin construction as soon as possible.

The Appropriation Committee met with representatives of Cubist Pharmaceuticals on October 28 to review the proposed project and its financial impact on the Town. We have also attended a number of other meetings and presentations regarding this project, including meetings of the Planning Board, meetings sponsored by Cubist Pharmaceuticals, and meetings sponsored by TMMA. Finally, we have reviewed materials and other information, including the Fiscal Impact Analysis, dated July 14, 2009, prepared by Connery Associates and drafts of the Memorandum of Understanding between Cubist Pharmaceuticals, Inc. and the Town of Lexington.

The proposed development is for top quality lab/office space. This type of space is one of the highest value uses of commercial property. The Town's valuations of commercial space qualifying as laboratory and research space typically run from \$175 to \$275 per square foot. Currently the lab/office space at 65 Hayden Ave is valued at \$287/sq ft., putting it at the very top end of the range of valuations for such space in Lexington. The proponents' financial analysis assumes that the new space will be assessed at a value of \$225/sq ft. or about \$23,400,000 for 104,000 sq. ft. Based on current tax rates, a property with that assessed value would generate approximately \$591,000 in gross annual property taxes. They estimate that the development would lead to incremental public safety costs to the Town of \$92,000/year. The cost-to-revenue ratio would be about 0.16. The net revenue would be approximately \$499,000.

There are two reasons why the estimate of new tax revenue that this proposed development would generate may be subject to a much smaller margin of error than the corresponding estimate of the proposal submitted under Article 2. First, because the demand for the space exists now, the project will begin immediately. Secondly, there is no question as to the type of use, and therefore the level of the assessed value, which the property will generate. This is a high-end, high value project.

In addition to these net tax revenues, building and permitting fees are estimated at approximately \$300,000. These fees would be paid in increments over the estimated 18 months of construction.

In addition, Cubist Pharmaceuticals has agreed to make a number of voluntary payments to or directly benefiting the Town, as reflected in the Memorandum of Understanding between it and the Town. These payments are tied to the occurrence of various events:

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(1) Within 30 days of the Attorney General's approval of its Amended PSDUP, Cubist Pharmaceuticals will contribute (a) \$25,000 to the Town's Traffic Mitigation Stabilization Fund, to enable the Town to prepare a traffic plan of the Spring Street and Hayden Avenue Corridors and (b) \$50,000 as a first of four lump sum payments to satisfy obligations as set forth in Section 3.5 of Appendix E of the original PSDUP.

(2) Prior to the issuance of a building permit, Cubist Pharmaceuticals will make a First Payment (either to the Town's Traffic Mitigation Stabilization Fund or to the Transportation Demand Management/Public Transportation Stabilization Fund, as decided by the Town) of \$1,900/additional parking spaces created for up to the first 127 additional parking spaces to be created by the project. A minimum payment of \$216,300 is required and that payment rises \$1,900 for each additional space up to the maximum First Payment of \$229,900.

(3) On the first through the fifth anniversary of the First Payment, if Cubist creates the capacity for an additional 100 parking spaces, over and above the 121 additional spaces covered by the First Payment, a Second Payment of \$190,000 will be required. It will be paid by Cubist Pharmaceuticals, annual in 5 equal installments of \$38,000, due, to the Town. If the number of spaces striped exceeds the percentage of the Second Payment that has been made, payments will accelerate by \$1,900 per created space, and accordingly reduce future payments.

(4) Three years after the date of the Attorney General's approval of the Amended PSDUP, a CPI adjustment for inflation or deflation will occur to the \$1,900/space rate used in above sections 2 and 3.

(5) Either on the issuance of a certificate of occupation or 2 years after the payment made in section 1b, Cubist Pharmaceuticals will pay \$25,000 as the second of four lump sum payments to satisfy the original PSDUP.

(6) Two years after the payment made in section 5, Cubist Pharmaceuticals will pay \$25,000 as the third of four lump sum payments to satisfy the original PSDUP.

(7) Four years after the payment made in section 5, Cubist Pharmaceuticals will pay \$40,000 as the last of four lump sum payments to satisfy the original PSDUP.

The Memorandum of Understanding also contains other agreements that specify that while Cubist Pharmaceuticals and Realty Associates Fund have shared obligations resulting from the original PSDUP, Cubist Pharmaceuticals has assumed sole responsibility for the \$4,000 annual contribution to the LEXPRESS transportation provided in Section 3.5.4 of Exhibit E of the original PSDUP. The MoU replaces the responsibility for these annual payments with the four lump sum payments specified above as items 1(b), 5, 6 & 7.

The Committee unanimously (9-0) supports this request.

Article 5: Authorize Munroe School Disposition	Funds Requested	Funding Source	Committee Recommendation
	none	N/A	Pending

The Board of Selectmen has concluded that there is no foreseen municipal use for the Munroe School building. The building is in need of major maintenance and/or renovation work (heating/roof/electrical/windows) that would cost the Town roughly \$2,300,000. Additionally, the

building should be brought up to current Americans with Disabilities Act (which will require the installation of an elevator) and other code standards. As the owner, the Town is now responsible for much of this work and the associated expenses. However, a private non-profit organization, the Munroe Center for the Arts, has occupied the building for a number of years and is not paying rent or any other fee at a level sufficient to fund the work described above. In this current situation, the Town may face the need at any time to spend money on systems in the building, e.g., if a boiler were to fail, the Town, as landlord, would be liable for the purchase and installation of a new one.

These considerations motivated the Board of Selectmen to come up with a more satisfactory administrative arrangement for the Munroe School. The possibilities included a sale or long-term lease. The last municipal building sale was the Adams elementary school where the building was sold and the land was leased on a long-term basis. State laws have changed since that transaction was consummated and the maximum period for a land lease is now 10 years (General Laws of Massachusetts Chapter 40, Section 3) so it is no longer practical to sell a building and retain ownership of the land.

The Town evaluated the potential of leasing the facility and concluded that the necessary repairs would be substantially more expensive if done under the Town's ownership rather than by a private owner. Further, the priority of the Town is to maintain those properties currently used for municipal and school purposes and it has proven difficult to contend with emergency repairs of a property that is not used by the Town.

After reviewing the options, the Board of Selectmen decided to attempt a sale of the property (building and land). In order to encourage the presence of an arts education center in Lexington, the Selectmen would put a restriction on the deed to permit the building to be used only for certain purposes by certain categories of non-profit organizations. The Town would retain the right of first refusal to repurchase the property if the buyer decided to sell the property in the future. In anticipation that the sale to the buyer could be at a price below a fair market value, the repurchase terms would include a discount intended to recognize the discount of the original sale. Thus a request for proposals (RFP) for the purchase of the property (land and building) and a draft Purchase and Sale Agreement were developed in concert with these principles and issued this past summer.

One proposal was submitted in response to the RFP. That proposal was from the non-profit organization that runs the Munroe Center for the Arts, namely Lexington Friends of the Arts, Inc.

The Town Manager evaluated the non-price proposal with the help of two members of this Committee and others. Eight criteria were reviewed in the course of this evaluation. The Town Manager and staff summarized the evaluation results for each of the criteria as follows.

- 1) Plans for arts-education center use: *highly advantageous*;
- 2) Qualifications and experience of the bidder and its officers and employees: *between advantageous and highly advantageous*;
- 3) A use consistent with and enhancing the Building's historic importance to the residents of the town of Lexington: *between advantageous and highly advantageous*;
- 4) Plans to make renovations and/or capital improvements to the premises: *advantageous*;
- 5) Evidence of existing sources of financing or plans to obtain such financing sufficient to finance the proposed transaction: *between not advantageous and advantageous*;
- 6) Plans to permit Lexington residents or Lexington-based non-profit and community organizations to use the premises for social purposes or to allow Lexington civic, cultural, charitable, historical, municipal, educational, and arts-center groups to use the premises as a meeting place upon payment of a reasonable fee to the owner: *highly advantageous*;
- 7) Plans to provide additional community benefits: *highly advantageous*;
- 8) Agreement to terms of the Purchase and Sale Agreement: *unacceptable with the changes proposed by the MCA*.

In regard to criterion (5), the evaluation acknowledged that the organizations and people involved with the Munroe Center have a serious fundraising challenge before them, and they will be undertaking this challenge in a difficult economic environment. While the Munroe Center's board has made solid progress in obtaining pledges of support, they have no track record of meeting comparable fundraising goals.

In regard to criterion (8), the Munroe Center did not accept the terms proposed in the RFP for the discounted repurchase of the property and presented a counter-proposal. The latter was not acceptable to Town officials. As of press time, the repurchase terms as well as other less prominent aspects of the possible sale are still being negotiated.

The Town obtained two appraisals of the property reflecting the building's current condition and its location within both a residential zone and the Munroe Tavern Historic District (which effectively precludes demolition of the building, etc.). The appraisals differ in whether or not the deed is encumbered with a restriction that limits the use of the property to the operation of a non-profit arts organization. The appraised values are \$760,000 with the restriction and \$1,500,000 without it.

The Munroe Center team proposes to buy the property for \$1,000, and to pay the Town \$5,000 per year as a Payment In Lieu Of Taxes (PILOT), compounded at 2.5% annually.

We want to explicitly note that a decision by the Town to not sell the property free and clear of any new deed restrictions represents a financial sacrifice, since, according to the appraisals, the proposed deed restrictions reduce its market value by approximately \$740,000. If one accepts that the building is to be reserved for use by a non-profit organization, the market value is then the lower appraisal figure of \$760,000. A sale at below this market value can be interpreted as a town subsidy of the organization that buys the property and must be viewed as being in addition to the just-noted \$740,000 cost. In the case of the possible sale of the property to the Munroe Center for the Arts, the Town would in effect be providing an unbounded and interest-only loan of about \$760,000 to the Munroe Center. This is equivalent to a subsidy of roughly \$30,000 per year (4% per year of \$760,000). The total equivalent cost to the Town of selling the building for \$1,000, i.e., about \$1,500,000 less than an unrestricted market value, is then roughly \$60,000 per year.

For any course of action the financial analysis should account for long-term consequences as well as any immediate return such as the proceeds from a sale. If the Town does not sell the property the long-term consequences would involve maintenance and repair costs and/or rent or other payments. If the Town does sell the property, the long-term consequences could involve tax payments, payments in lieu of taxes, and municipal and education costs related to the property, e.g., the costs of educating children who might move into the building if it were converted to condominiums or other types of residences after an unrestricted sale in the open market. We have not attempted to think through the financial consequences of a wide range of scenarios because it is difficult to impossible to fairly include quality of life and other factors in determining bottom line values.

To summarize, selling the property would be advantageous to the Town since it would eliminate the Town's obligations to fund future repairs and maintenance of the property. The Town is not giving up a lucrative leasing opportunity nor is there a municipal or school use for the building at this time or in the foreseeable future. Furthermore, it appears that the sale of the property to the Munroe Center will strengthen that organization allowing them to increase their level of service to Lexington residents.

The proposed sale would be advantageous to the Munroe Center by giving them the authority to maintain and renovate the building as appropriate. The sale would also give them the wherewithal to borrow funds for work on the building and to conduct a capital fund-raising campaign. Such borrowing and fund-raising are effectively precluded without a long-term lease or ownership.

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The motion put forward asks for Town meeting to authorize the sale of the property and to allow the Board of Selectmen to agree to terms and conditions with the prospective buyer.

The Appropriation Committee is not prepared to take a position on this request until the Town and Lexington Friends of the Arts, Inc. have completed negotiations on the important provisions of a Purchase and Sale Agreement, at which time we expect the Town will provide a Letter of Intent to the Committee that describes the final terms.

Article 6: Approve Local Option Meals Excise	Funds Requested	Funding Source	Committee Recommendation
	none	N/A	Approve (7-2)

The Commonwealth of Massachusetts FY2010 budget included a provision to increase the sales and meals tax from 5% to 6.25% on August 1, 2009. It also provided for a local option tax of 0.75% on meals, with the funds collected to remain in the community that adopted the tax. This local excise takes effect on the first day of the calendar quarter following 30 days after acceptance by the Town or on the first day of a later calendar quarter as designated by the Town. If the Special Town Meeting accepts Article 6, it will go into effect on January 1, 2010. As of the writing of this report, 38 communities have adopted the local option meals tax.

Local sales tax receipts are remitted to the Towns on a quarterly basis. The Town estimates that it will collect approximately \$146,000 in FY2010 if the meals tax is adopted.

We are in an environment where the amount of state aid for FY 2010 and beyond is uncertain and it is likely that this year's estimate will be reduced as the State is experiencing revenue shortfalls. A mechanism has been provided whereby Towns can generate a modest amount of additional income by imposing this tax (impact – 23 cents on a meal costing \$30 – the average meal cost at a Lexington restaurant). While the restaurant sector has seen a decrease in sales due to the economic downturn, this tax is minimal and the impact on demand is expected to be minimal.

A minority of the Committee recommends that the Town not adopt the local option meals tax. Although that extra 0.75% by itself may appear modest, when added to the state sales tax it produces a total tax of 7%, a percentage likely to serve as a further disincentive, in an already depressed economic climate, to eating out. This could lead to a loss of customers, and therefore a decline in revenue, to Lexington's restaurants and other eating establishments. That loss of revenue would, in turn, result in lower additional tax revenue than was projected. Additionally, forgoing the 0.75% will make Lexington establishments more competitive with establishments in municipalities which have opted for the increase. Finally, the increased tax will primarily affect and be borne by Lexington residents, the individuals most likely to patronize Lexington establishments.

The Committee (7-2) supports this request.

Article 7: Approve Local Option Room Occupancy Excise	Funds Requested	Funding Source	Committee Recommendation
	none	N/A	Approve (7-2)

Effective February 1, 1986, Town Meeting adopted the provisions of M.G.L., c. 64G, sec. 3A, enabling the Town to collect a local option room occupancy excise tax of 4%. In reality, the Town itself does not collect this tax; rather, the Massachusetts Department of Revenue collects it, along with the Commonwealth's own 5.7% occupancy excise tax, from the entities subject to the tax. Under M.G. L., c. 64G, sec. 3, these entities include bed and breakfast establishments, hotels, lodging houses and motels. The Department of Revenue then distributes the monies collected to the Town on a quarterly basis, on September 30, December 31, March 30, and June 30.

In 2009, in recognition of the difficulties confronting municipalities caused by a combination of the severe and continuing downturn in the economy, the State's own financial difficulties, and the consequent and significant decrease in State aid, the Massachusetts legislature amended section 3A to increase the maximum permissible local option room occupancy excise tax from 4% up to 6%. For this increased rate to go into effect, Town Meeting must vote to increase the 4% rate it had previously adopted and also establish the effective date of the increase. If Town meeting so votes, the Town must then inform the Department of Revenue of the amount of the increase and the effective date of the rate change.

The Town's acceptance of an increase in the excise tax rate can become operative on the first day of the next calendar quarter after the Town Meeting vote, so long as at least 30 days separate the selected effective date and the vote. Thus, the earliest effective date Town Meeting can vote for the increase to take effect is January 1, 2010, although it can, if it wishes, choose a later date. If January 1 is the selected date, the Town would then begin to receive the increased revenues from the State on March 31, 2010, reflecting collections received during January, February and March.

Under the law, a vote by Town Meeting to amend the current 4% rate, whether up to the now permitted maximum of 6%, or down, binds the Town to that rate for the next 12 months. The Town can revoke its acceptance of the statute, or amend the rate it has previously voted, only once a year.

If Town Meeting votes to increase the rate by the maximum permitted, to 6%, the revenues from the excise tax are projected to increase by about \$150,000 over the entirety of a fiscal year. For FY 2010, the incremental revenue would be approximately \$62,000 (the Town would receive payments for 5 months in FY 2010).

As of October 21, 2009, the following communities adjacent or near to Lexington have elected to exercise the statutory option and have increased their local room occupancy excise tax to 6%: Bedford, Brookline, Burlington, Medford, Newton, Somerville and Woburn. The following communities, as does Lexington, currently have adopted a 4% occupancy excise tax: Acton, Arlington, Billerica, Needham, Natick, Stoneham, Sudbury, Wakefield, Waltham and Wellesley. Of these, Arlington, Natick, and Waltham are purportedly considering whether or not to exercise the option. Belmont, Carlisle, Concord, Lincoln, Wayland, Weston and Winchester have not adopted the provisions of M.G.L., c. 64G, sec. 3a, and thus do not have any local room occupancy excise tax.

A majority of the Committee recommends that the Town raise the excise tax to 6%. The arguments in favor are based on the largely undisputed observation that the Town's expenses to maintain the current level of services are generally rising faster than its revenues. This is especially true during this recession as State aid and local receipts such as building permit fees are down. To maintain the current level of

services over the next few years, the Town will likely need to find new sources of revenue. The room occupancy excise is one of the few ways that the Town can do this. Other ways are adoption of the increase in the meals tax (Article 6) or a Proposition 2 ½ override. In other words, adoption of the excise taxes will help limit the need for and/or the amount of an override. Also, the excise tax will effectively be paid by people living outside of Lexington. The majority does not accept the argument that the increase, being only 2% or \$4 on a \$200 hotel bill, will be a significant factor in the competitive position of the local hotels.

A minority of the Committee recommends that the Town leave the excise tax at 4%. These members note that an increase the room excise tax from 4% to 6% means that the total tax, inclusive of the state rate, will be 11.7%. On both national and local scales, the hospitality industry has experienced a significant decrease in business, as both corporate and personal travel has declined. Corporations and individuals are aggressively seeking to lower their costs. An increase in the excise tax may be passed on to the customer, or it may be absorbed by the hotels as a reduction in their lodging rates. Thus, a tax increase may mean a loss of business or a decrease in commercial revenue to hotels. In either eventuality, the adoption of the increase will add to the current difficulties of Lexington's hotels. Even with the increase, the amount of new excise tax revenue generated may be somewhat less than the projected \$150,000 per year due to a potential reduction in hotel business. If Town Meeting does not adopt an increase now, they may choose to do so at a later date. If economic conditions improve, Town Meeting can always reconsider the issue and decide if an increase in the local option room occupancy tax is merited.

The Committee (7-2) supports this request.

Article 8: Contracts for Solar Energy	Funds Requested	Funding Source	Committee Recommendation
	none	N/A	Approve (8-0)

The Town Manager is trying to identify the lowest cost option to acquire electricity for the Town, and would like to be able to consider electricity generated from solar panels installed on municipal buildings. The high cost of the panels required to generate solar-power electricity necessitates a long-term investment and pay-back period. This is regardless of whether the Town actually purchases the panels or they are owned by a third party and installed on municipal buildings. Therefore, solar-power-generated electricity can only become cost-effective if the Town can enter into a longer term contract than the five-year purchasing arrangement currently allowed by Town By-Laws (§ 32-4). This Article does not seek to change the By-Law; rather its passage would grant the Town Manager the authority to enter into purchase arrangements for solar-power-generated electricity for up to 20 years. Even with the authority granted to the Town Manager by this Article, the Board of Selectmen would need to approve this extended purchase arrangement.

The State and Federal governments are currently offering incentives to promote renewable energy. The Town Manager and staff have begun to investigate different options for acquiring solar-power-generated electricity. Based on their research they believe a 20 year purchasing agreement is required to obtain the lowest prices. If granted the ability to enter into a 20 year agreement, the Town Manager would issue an RFP for proposals from interested suppliers/installers, and then seek to enter into an agreement if the rates were considered to be favorable over the 20 year period.

We recognize the need to be able to enter into a longer term purchasing agreement than is currently allowed, and 20 years may be the appropriate length of time, but we feel more research is needed before a 20 year contract is signed.

While we applaud the efforts of the Town Manager and staff to take advantage of currently available financial incentives, we strongly encourage them to both broaden their research and include the Appropriation Committee and Capital Expenditures Committee in the process before any RFPs for solar-power-generated electricity are issued. Twenty years is a long time to be locked into rates without any recourse if electricity rates do fall. There may be other low cost options that allow a shorter contract.

The Committee unanimously (8-0) supports this request.

Article 9: Appropriate for Sister City Program	Funds Requested	Funding Source	Committee Recommendation
	Unknown	GF	Pending

Lexington has had a Sister City relationship with Antony, France stretching back about 20 years. Though the program has been in existence for some time, it has until now been funded largely through private contributions. This request made by the Lexington Tourism Committee is to facilitate a visit to Lexington of officials and residents from Antony, France on April 15 - 25, 2010.

Antony is a suburban city outside of Paris, with a population of approximately 60,000 and similar demographics to Lexington. This year a contingent of 42 traveled to Antony from Lexington, including Rep. Jay Kaufman and Town Manager Carl Valente. They were present at the dedication of a monument to Lexington, participated in public receptions and had the opportunity to discuss town operations.

The Lexington portion of the trip was funded in part by the individuals who attended, with some funds from the LASCA (Lexington Antony Sister City Association) and with the Selectmen's Gift Account paying for minor expenses. Each traveler covered their own travel expenses. The city of Antony has a Deputy Mayor for Sister Cities and a city budget which covered the Antony portion of the expenses such as the buses, excursions, and receptions.

The Town of Lexington has several Sister City relationships under the direction of the Board of Selectmen. The Board of Selectmen authorized the Tourism Committee to undertake a reunion and rededication of this relationship. The Lexington Tourism Committee would like to reciprocate the hospitality shown in Antony. The expectation is that approximately the same size contingent of Antony officials and residents would visit Lexington on Patriot's Day. This request would cover some portion of the expenses to host that visit.

Though the Appropriation Committee acknowledges the benefits of cultural exchange and tourism fostered by the Sister City program, members of the committee expressed general concern over the program being funded out of the tax levy at a time when economic conditions warrant especially conservative use of town funds. In addition, the timing of this request did not allow it to be prioritized with respect to other funding needs as normally occurs in the due course of budget development.

The Tourism Committee indicated that they will significantly revise the amount and nature of their request. At press time, this revised request was not available to this Committee. However, some members of the Committee indicated that they would support a modest request that was limited specifically to covering costs for the visitors, with the assumption that the remaining funds would be raised through private donations.

The Committee has not taken a position on this request.

Article 10: Appropriate to Traffic Mitigation Stabilization Fund	Funds Requested	Funding Source	Committee Recommendation
	\$35,000	Traffic Mitigation Special Revenue Account	Approve (9-0)

This article will transfer \$35,000 to the Traffic Mitigation Stabilization Fund, as required by Department of Revenue regulations.

This money comes from the first of several traffic mitigation payments by The Beal Companies as part of the CD rezoning agreement for Ledgement. That agreement stipulates that the town will use this money to pay for a traffic master plan for the Hayden and Spring Street Corridors.

The Committee unanimously (9-0) supports this article.

Article 11: Appropriate to Stabilization Fund	Funds Requested	Funding Source	Committee Recommendation
	approx. \$650,000	GF	Approve (8-0)

As discussed in the Introduction to this report, and will be further explained by the Town Manager and staff under Article 13 of this Special Town Meeting, the estimate of the revenues expected to be received during FY 2010 has increased since the budget was set last spring. This Article is a request to appropriate approximately \$650,000 (the exact figure is not available at press time) representing the net of the increase in the revenue and the changes in the operating budget from Article 13 to the Town's unrestricted Stabilization Fund. The current balance of the Stabilization Fund not including this proposed appropriation is \$6,805,815.66.

Appropriating money to a combination of stabilization funds, reserve funds, and continuing balance accounts, rather than building up Free Cash, is a policy recommendation made in March 2006 by the Selectmen's Ad Hoc Financial Policy Committee, and supported by the Town Manager. Since that time, Town Meeting has authorized the creation of, and/or appropriated money into, these various accounts. Town Meeting approves appropriations into and out of the Town's various stabilization funds by a two-thirds vote. This allows the Town to better allocate and track reserves set aside for specific purposes, and sets a higher bar (the required two-thirds vote) for the use of such funds.

Since the Ad Hoc Financial Policy Committee's report, Town Meeting has appropriated amounts to the unrestricted Stabilization Fund at the 2006, 2007, and 2008 Annual Town Meetings. An appropriation was not made to this Fund at the 2009 Annual Town Meeting in anticipation of needing funds to defray potential additional reductions in State Aid.

The Committee unanimously (8-0) supports this request.

Article 12: Appropriate for Waltham Street Pedestrian Crossing	Funds Requested	Funding Source	Committee Recommendation
	\$25,000	Traffic Mitigation Stabilization Fund	Approve (9-0)

This article will appropriate \$25,000 from the Traffic Mitigation Stabilization Fund.

This money comes from a traffic mitigation payment by Watertown Savings Bank as part of the rezoning agreement for their new branch office on Waltham Street. The town will use this money to pay for the study and design of a new pedestrian crossing on Waltham Street near Brookhaven. Our DPW expects that there will be some type of signalization warranted, but it is not known at this time whether it will be a full vehicle/pedestrian signal or just a pedestrian signal.

The Committee unanimously (9-0) supports this request.

Article 13: Amend FY2010 Operating Budget	Funds Requested	Funding Source	Committee Recommendation
	none	N/A	Approve (8-0)

The warrant for the Annual Town Meeting generally includes an article to allow Town Meeting to amend the current fiscal year operating budget. This is necessary when unforeseen expenses must be funded, or it is determined that an account can or must be adjusted downwards if circumstances have changed, and the originally budgeted amount is no longer necessary or even fundable. There is enough information to change several accounts now to more accurately reflect the Town's spending, rather than waiting until the Annual Town Meeting in the spring.

This article seeks to amend five accounts in the FY2010 Operating Budget that was approved at the 2009 Annual Town Meeting. Three accounts will be subject to an increase to be financed by the tax levy: Shared Expenses, the Finance Department, and the Town Clerk. The DPW account will add an expense that is covered by a payment from the developer Patriot Partners. The Human Services account will be decreased due to the elimination of the Adult Supportive Day Care program effective July 1, 2009. The result is a net decrease to the FY 2010 appropriated operating budget of \$8,274.

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Budget Line Item		Dollar Amount	Reason for change
2150	Shared Expenses	\$50,000	Additional funding for Worker's Compensation
8400	Finance Dept.	\$41,000	Routine investment fees formerly covered by interest payments
8500	Town Clerk	\$50,000	Special Election
3120	DPW	\$15,000	Traffic mitigation study for Shade Street (paid for by Patriot Partners)
6130	Human Services	(\$164,274)	Elimination of the Adult Supportive Day Care program
Total Recommended Supplemental Appropriations		(\$8,274)	

The Committee unanimously (8-0) supports this request.

Article 14: Amend FY2010 Enterprise Fund Budgets	Funds Requested	Funding Source	Committee Recommendation
	none	EF	Approve (9-0)

This article proposes minor housekeeping adjustments to the appropriations made for the water and sewer enterprise funds at the Annual Town Meeting last spring.

Adjustments to Reflect Final MWRA Charges

In January or February of each calendar year, the Massachusetts Water Resources Authority (MWRA) provides its member towns with a preliminary estimate of their water and sewer assessments for the upcoming fiscal year. The Town uses these preliminary estimates to establish the MWRA component of the water and sewer enterprise fund appropriations at the annual town meeting. In June of each year, the MWRA completes its budget process and issues final assessments to its member towns. The final assessments are typically less than the preliminary estimates.

Water and sewer rate-setting for each fiscal year takes place during the late summer or early fall following the annual town meeting. Since at this point the final MWRA charges have been determined, the Town's practice has been to set rates in an amount projected to be sufficient to cover the actual, final MWRA assessments, as well as the other direct and indirect costs of the water and sewer enterprises appropriated at the Annual Town Meeting. The Town, therefore, usually raises in the rates and pays to the MWRA each year an amount somewhat smaller than the amount originally appropriated at the annual town meeting.

At the Annual Town Meeting this past spring, the Town Meeting was asked to appropriate amounts for the FY2010 water and sewer budgets that included projected MWRA assessments exceeding even the preliminary assessments issued by the MWRA on February 10, 2009. This conservative approach apparently was based on a concern that, given the state fiscal crisis, state subsidies that have traditionally supported the MWRA might be reduced or eliminated. In fact, that concern did not materialize and the final MWRA assessments for both water and sewer came in below the preliminary estimates, as set forth in the chart below.

	MWRA Prelim.	Appropriated	MWRA Final	Adjustment
Water	\$4,483,223	\$4,600,000	\$4,482,551	(\$117,449)
Sewer	\$6,337,141	\$6,500,000	\$6,245,946	(\$254,054)

The adjustments addressed in this article will reduce the original appropriations made for the FY2009 water and sewer enterprise budgets at last spring's Annual Town Meeting to reflect the actual, final MWRA assessments.

FY2010 Rate-Setting, Use of Water and Sewer Retained Earnings

At previous special town meetings held in the fall of 2007 and 2008, appropriations were requested and made from the water and sewer reserves known as "retained earnings," to reflect and ratify decisions that had been made by the Board of Selectmen during the fall rate setting proceedings to use a portion of the funds' retained earnings to mitigate rate increases. (Under the state statute governing enterprise funds, G.L. c. 44, § 53F1/2, accumulated surpluses resulting from the operations of an enterprise fund may be used either "for capital expenditures of the enterprise, subject to appropriation, or to reduce user charges." Operating deficits must be funded with existing reserves or, in the absence of such reserves, made up in the following year's rates.) The FY2010 water and sewer rates will again be subsidized from retained earnings. Appropriations for this subsidy are not necessary at this fall's Special Town Meeting, however, because they were already included in the budgets adopted at the Annual Town Meeting. A brief review of recent rate-setting decisions, the results of operations for FY2009, and the status of the water and sewer enterprise fund retained earnings is set forth below.

FY2009 Rates and Operating Results. At last year's FY2009 rate-setting, in the fall of 2008, projected costs for the water and sewer funds were up by 10% and 3.3% respectively, due primarily to increases in MWRA charges and increases in debt service costs attributable to the Water and Sewer Enterprise Funds' share (17% and 7% respectively) of the debt service costs for the construction of the new DPW facility. To meet those increased costs, the Town Manager recommended, and the Board of Selectmen adopted: (1) a 9.5% increase in water rates, projecting a draw of \$463,050 on water fund reserves to mitigate the rate increase; and (2) a 0% increase in sewer rates, projected to generate a small surplus of about \$40,000. The actual results of operations in FY2008 came in close to what had been anticipated. The water fund generated a surplus of approximately \$222,000 including the subsidy (meaning the actual draw on the water reserves was \$222,000 less than the planned draw of \$463,500, or about \$241,000), and the sewer fund ended the year with an operating deficit of approximately \$167,000 (meaning that amount was effectively drawn from the sewer reserves).

Changes in Retained Earnings. The changes in the reported retained earnings of the water and sewer funds (equivalent to certified free cash in the General Fund) are set forth in the table below.

Enterprise Fund Retained Earnings

	6/30/06	6/30/07	6/30/08	6/30/09	Change FY08-FY09
Water	\$2,090,334	\$2,496,655	\$2,537,249	\$2,113,729	\$(423,520)
Sewer	\$ 447,441	\$2,137,540	\$2,763,179	\$1,831,967	\$(931,212)
Total	\$2,537,775	\$4,634,195	\$5,300,428	\$3,945,696	\$(1,354,732)

Reductions in the retained earnings for both the water and sewer funds are significantly greater than what one would expect given the relatively favorable FY2009 operating results described above. The reason is that Town Meeting for the first time made advance appropriation at this year's Annual Town Meeting from retained earnings to mitigate anticipated FY2010 rate increases. Although the amounts appropriated – \$525,000 to subsidize water fund rates and \$625,000 to subsidize sewer rates – did not actually reduce

the amount of cash in the funds as of 6/30/09, under applicable municipal accounting principles, these amounts must be treated as liabilities and deducted from the retained earnings figure. In effect, this recognizes a reduction in the reserves due to a planned FY2010 subsidy a year in advance.

FY2010 Rate-Setting. At this fall's water and sewer rate-setting, the Town Manager advised that projected costs for the water and sewer funds for FY2010 were up by 0.73% and 5.0% respectively, for a combined *increase* of 2.94%. Nevertheless, the Town Manager recommended, and the Board of Selectmen voted to adopt, a reduction of both the water and sewer rates by 1.8% and 3.8% respectively, for a combined *decrease* of 3.8%. The rate reduction will occur because the Board of Selectmen decided to use the full amount appropriated from retained earnings at the Annual Town Meeting last spring to subsidize the FY2010 rates even though costs, particularly the MWRA costs, have not increased as much as originally anticipated and the amounts appropriated last spring were more than necessary to avoid rate increases.

General Comments. While amounts have been appropriated for several years now from retained earnings to subsidize the water and sewer rates, the full amounts of those planned subsidies have not always been required due to more favorable operating results than anticipated. As a consequence, the reserves in the water and sewer funds still remain quite substantial, ranging from about 20% (in the case of the sewer reserves) to 30% (in the case of the water reserves) of the total annual budget. However, the subsidization of rates from reserves cannot continue forever, and at some point, when there are no longer adequate reserves for this purpose, there will likely be a need for significant rate increases as has occurred in the past. The Committee continues to urge the adoption of a policy addressing the appropriate amounts and uses of water and sewer reserves. In the development of such a policy, consideration should be given to the possibility of applying some portion of the reserves to water and sewer fund capital projects, which by lowering future debt service costs would help to provide long-term rate stability instead of merely short-term rate relief.

The Committee unanimously (9-0) supports this request.