Town of Andover

Revenue and Expenditure Task Force

<u>Budget Commentary</u>

January 2020

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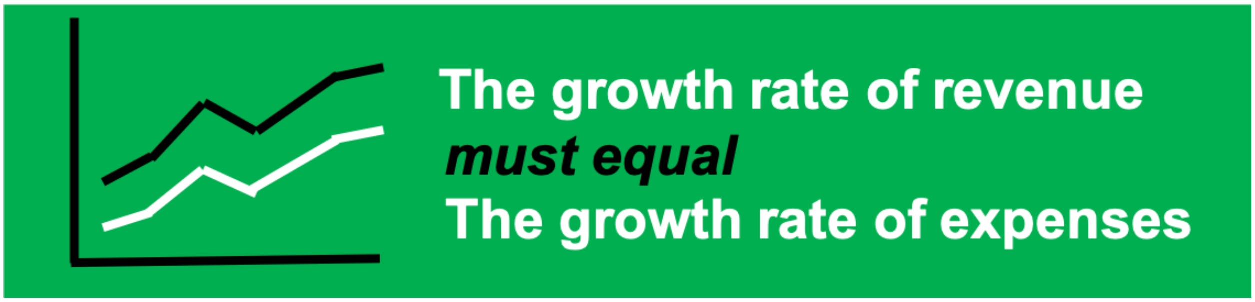
I. INTRODUCTION

The Town of Andover faces a long-term financial challenge of enormous consequences. Even with revenues rising, running the Town is becoming more expensive. The Town's expense growth is higher than its revenue growth. If not addressed, at stake are the tenets of what makes Andover the best place to work and live in Massachusetts, including its schools and basic municipal services.

Late in 2018, Town Management appointed the Revenue and Expenditure Task Force to look critically at the Town's budget assumptions, both short and long-term. The Task Force was to determine the highest threats and opportunities, and where possible, make recommendations to the Town of actions that might be considered in the years ahead.

It is not the purpose of this Task Force to present a "third party viewpoint" on the line items in the Town budget; the Town is fortunate to have a highly active and deeply involved Finance Committee to help shepherd that process. Instead, it is to work in collaboration with the Town Manager and his staff to shape realistic expectations over the long term for proposals and assumptions for future Operating Budgets to address the structural deficit.

The Task Force's work is driven by one overarching theme: To review and assess the Town's long-range plan with the underlying premise that:



For the Town to sustain its operations, the slope of these two lines must be parallel or be diverging with the revenue line on top. Execution of such a goal is challenging as the underlying cost structure carries annual demands for additional resources that are hard to deliver from the existing business model. Widespread understanding of the basic premise that the slopes of the Town's revenue and expense trajectories must match or favor the revenue side, is an important starting point for all financial management strategies and tactics that follow. Any movement toward a sustainable financial structure requires action on both the revenue and expense sides, supported by realistic modeling.

The Task Force's decision-making process must examine possible or likely outcomes, including sensitivity analyses of the major assumptions to varying conditions. The Task Force must also discuss how the Town will protect itself from the unexpected, along with at least an outline of possible contingency steps, including, but not limited to, a Proposition 2 ½ override. The Task Force decided in this first year of its existence that it would focus on some of the biggest and most difficult budget categories for analysis and recommendation. Other budget areas will be addressed in the future.

It should be noted that the Task Force fully believes that the current Town Administration has approached the Town's financial challenges with creativity and determination, including establishing a long-range financial plan, providing predictable and meaningful capital improvement programs, and developing concrete strategies to address unfunded liabilities. The Task Force is grateful for the Town's capable leadership as stewards for the taxpayers of Andover.

The balance of this document is composed of:

- Goals and Objectives
  - Which states the purpose and plan of the Task Force.
- Executive Summary
  - Which summarizes the findings of the Task Force in the areas of Revenue, Retirement, OPEB, Health Insurance and Other.
- Report Findings
  - Which provides detail on the Task Force's findings in the aforementioned categories.

The Revenue and Expenditure Task Force consists of members who were appointed by the Town Management team. The Appointed Members include:

- Kevin Connors
- Melissa Danisch
- Daniel Esdale
- Joseph Guilmartin
- Paul MacKay
- Donald Robb (In Memoriam Oct 2019)
- Gregory Eliasen
- Thomas Hartwell, Vice Chairman
- Timothy Vaill, Chairman

Representing the Town Management team area:

- Andrew P. Flanagan - Town Manager
- Donna M. Walsh - Finance and Budget Director
- Patrick J. Lawlor - Director of Administrative Services

In addition, various other Town Committees sent representatives to the Task Force meetings.

This unique collaboration between dedicated citizen volunteers and our highly competent Town Management Team is providing thoughtful and spirited discussion of critical financial matters during this important period in the Town's fiscal history.

Timothy L. Vaill, Chairman

II. GOALS AND OBJECTIVES

The Charge

The Revenue and Expenditure Task Force has been established to review the Town's long-range financial plan and the Town Manager's recommendations for addressing the structural deficit.

What is a Structural Deficit?

A deficit can be defined in two ways, ongoing or temporary.

1) A structural deficit is an ***ongoing*** deficit that occurs when recurring expenses exceed recurring revenue, regardless of the economic cycle.

2) A non-structural deficit is a ***temporary*** condition caused by revenue shortfall, such as local receipts, or lower-than-expected state revenues and it is usually attributed to economic cycles.

States, cities and towns reserve resources for the specific purpose of addressing temporary conditions, as does Andover. Long-range financial forecasts portray the risks associated with costs that are clearly not temporary. To weather inevitable economic downturns and to minimize cyclical cuts in services and employees, the Town needs to perfect its capacity to create financial plans and budgets that address the ongoing aspect of structural deficit.

The Revenue and Expenditure Task Force has been charged with achieving the following goals:

- Become well-versed about the Town's revenues, expenditures and related tax impacts.
- Analyze the Town Manager's five- and ten-year revenue and expenditure forecasts identifying any structural deficits that may occur.
- Review the Town Manager's recommendations for reducing the structural deficit throughout the life of the long-range financial plan.
- Generate and vet revenue and expenditure ideas that could mitigate the structural deficit.
- Recommend to the Town Manager a package of short- and long-range options that will contribute to the reduction of the structural deficit as appropriate.
- As appropriate, communicate findings to interested groups.

III. EXECUTIVE SUMMARY

The Task Force convened in December 2018. The Task Force met fourteen times from December 2018 to November 2019. It is estimated that the work of the Task Force will continue into the next budget cycle as well. Its Charge (or "Mission") is outlined in the previous section.

It is the consensus of the Task Force that, based upon the information provided to it, the Town of Andover has an ongoing structural budget deficit (as defined above). It is the view of the Task Force that the structural deficit is both an immediate and a long-term threat to the fiscal sustainability of the Town.

The Town's 6/30/17 and 6/30/18 audited government-wide financial statements showed losses of ($13.5 million) and ($12.3 million), respectively and a negative net worth of ($65 million) at 6/30/18.

The problem is not unique to the Town of Andover. Many cities and towns around the state face a similar problem. However, many of the towns to which Andover compares itself have positive net worth and better funded retirement pension plans. The Town cannot sustain its level of services, the quality of life for residents, or an ability to retain existing and attract new businesses, unless this challenge of future structural deficits is resolved. There is no silver bullet, no obvious quick fix. The Town will have to examine its service levels, as well as the means by which these services are provided and funded.

The path ahead will likely be very difficult. Actions must be carefully considered in order to keep the Town an attractive community for both businesses and residents. This discussion offers several recommendations, focused on key drivers responsible for the imbalance between revenues and expenditures.

The Task Force's recommendations are around efficiencies and ways to reduce the growth of expenditures. A summary of the recommendations follows:

Component	Recommendation
Revenue	1. Having just come through a robust economy, the Town should maintain its conservative revenue forecasting posture, in anticipation of a projected economic downturn. 2. The Town might consider FY2021 Local Receipts being less than the budgeted amount for FY2020 and the actual amount for FY2019. 3. The Town should conduct a thorough investigation of potential additional revenue sources in the form of fees and taxes, including a Proposition 2 ½ override.
Retirement	1. The Town's discount rate (6.25%) should be used to determine the Town's annual contribution for pensions for FY2021. 2. The Town and Andover Retirement Board (ARB) should agree on using the same discount rate.

	3.	The Town and ARB should consider having actuarial valuations prepared annually
	4.	The Town should consider applying excess free cash towards pension debt.
OPEB	1.	The Town should consider raising its annual contribution to the OPEB Trust fund and establish a funding schedule on when the plan will be fully funded.
	2.	The Town should document its control policies, processes and procedures regarding pension and OPEB participation and reporting.
	3.	The Town might consider creating an OPEB Trust Advisory Board.
Health Insurance	1.	The Town should continue to work with the Insurance Advisory Committee to review plan design changes.
	2.	The Town should explore offering high-deductible health plans and health savings accounts.
Other	1.	The Town should consider including differences between the annual budget and its audited financial statements in appropriate financial documents.

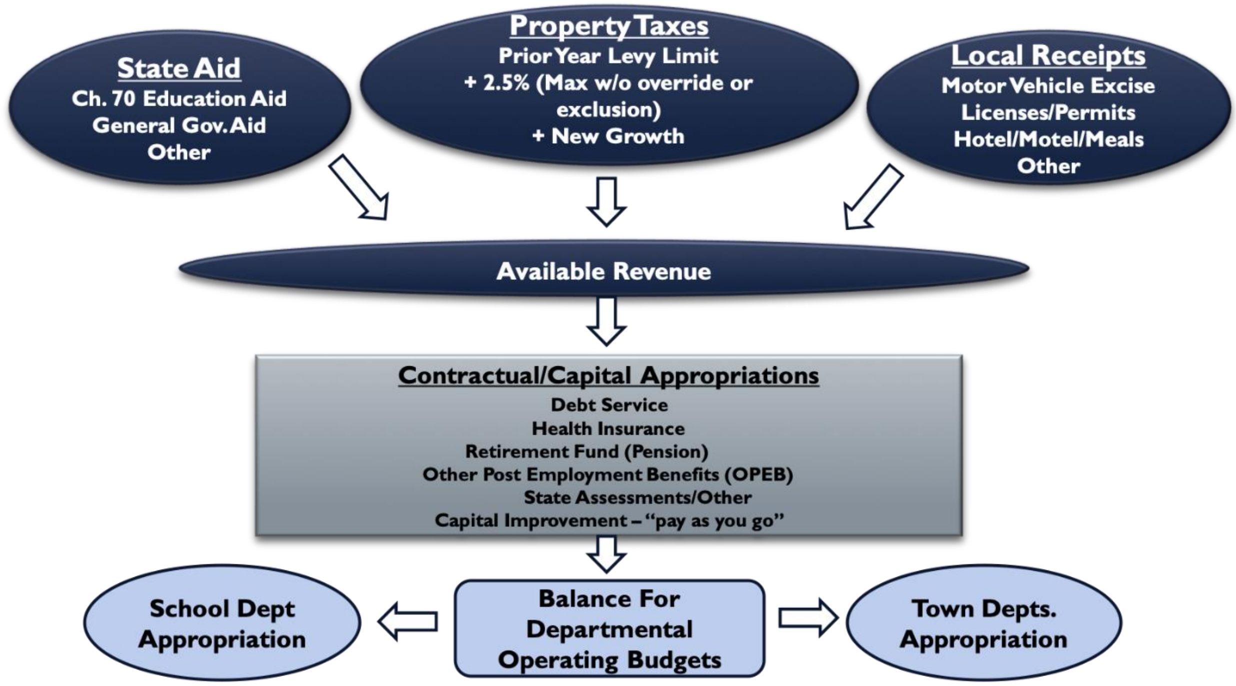
The Task Force looks forward to meeting with the Town Manager to discuss its findings in order to track the Town's response to its recommendations and to meet with the entire Select Board early in FY2021 budget deliberations.

IV. REPORT FINDINGS

Section 1: Revenue

<u>Introduction</u>

Town Budget Model



Three categories factor into the projection of revenues. They are:

- State Aid
- Property Taxes
- Local Receipts

The forecast for each category is composed of a number of things. The Task Force examined each category and the elements of which it is constructed, and tested the underlying assumptions.

Property Taxes

The estimated property taxes for the coming fiscal year are = (the prior year's levy limit + 2.5% + New Growth).

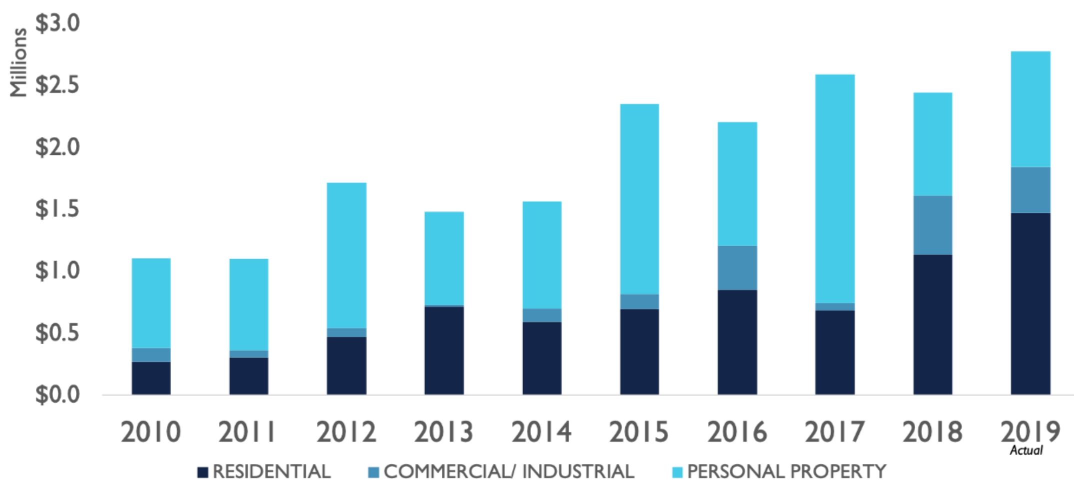
New Growth is the value of new property that has been acquired or built which increases the assessed property value. There are three classes of New Growth:

1. Residential (home additions, home renovations, new homes)
2. Commercial/Industrial (new office buildings, renovated business space)
3. Personal Property (merchandise, furniture, equipment)

The current assumption for New Growth is the five (5) year average. *As of October 31, 2019, the assumption for New Growth is the ten (10) year average.

New Growth History

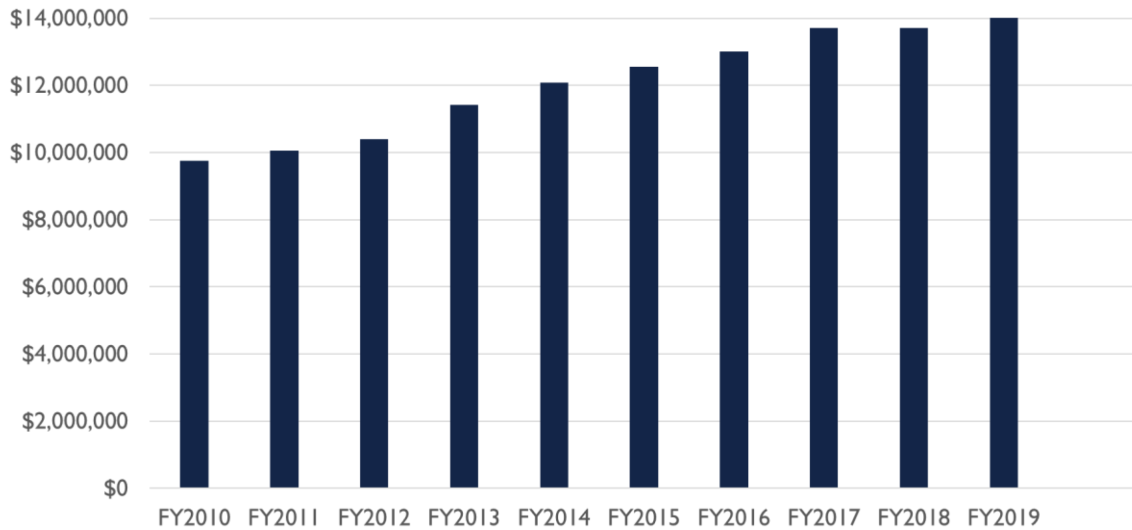
New Growth Averages*		*Projection vs. Actual FY2019*	*Projection vs. Actual % of budget*
Three year average	**$2,600,574**	*$172,355*	*0.09%*
Five year average	**$2,471,589**	*$301,340*	*0.17%*
Ten year average	**$1,931,422**	*$841,507*	*0.47%*



Local Receipts

Local Receipts include meals tax, hotel room tax, motor vehicle excise tax, licenses, and permits. There are a total of 23 categories of local receipts allowed by the Massachusetts Department of Revenue. The current assumption by the Town for Local Receipts is based on the five (5) year average. *As of October 31, 2019, the average is no longer used, but rather figures based on actual performance and trend analysis for each individual category of local receipts.

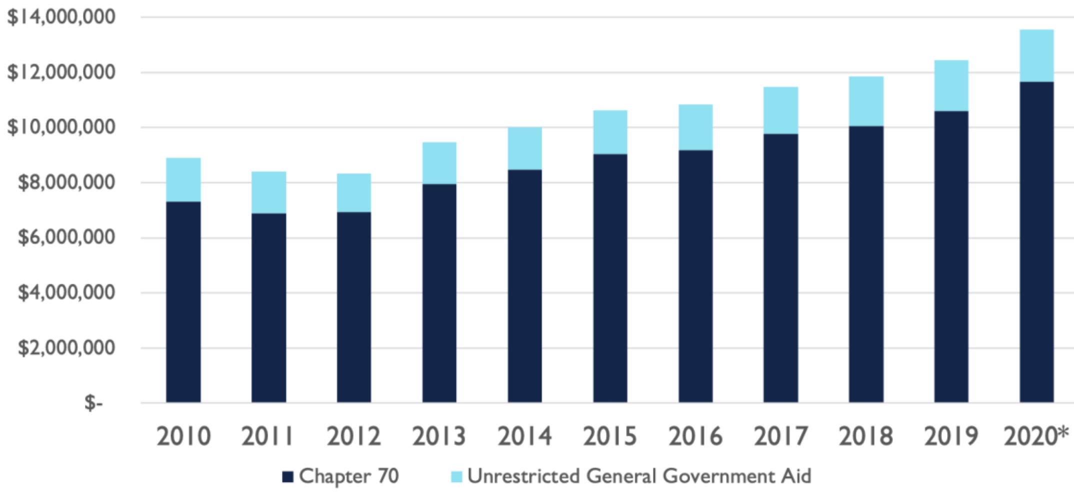
Local Receipts History



State Aid

State Aid is financial assistance from the Commonwealth of Massachusetts to municipalities. There are two major sources of funds: Chapter 70 (Education) and Unrestricted General Government Aid. The current assumption by the Town for State Aid is a 2% annual increase for Chapter 70 and UGGA. *As of October 31, 2019, an assumption of 4% annual increase is used for Chapter 70 and 2% for UGGA.

State Aid History



Recommendations

1. Having just come through a robust economy, the Town should maintain its conservative revenue forecasting posture, in anticipation of a projected economic downturn.

License and Permit collections are a possible predictor of future New Growth. While the Town has experienced record New Growth since 2014, the value of License and Permits issued dropped significantly, 18.5%, in FY2019 from the prior year, and is at its lowest level since FY2014. Notably, FY 2019 License and Permit collections also were under FY2019 budget by 12%.

The Town should adopt the ten (10) year average for Licenses and Permits projection for FY2021 because the 5 year average is based on short term economic gains and is not a conservative measurement.

2. The Town should consider FY2021 Local Receipts being less than the budgeted amount for FY2020 and the actual amount for FY2019.

The increase in Hotel/Motel Excise receipts, which increased 18.3% in FY2019 over FY2018, may not be sustainable as they likely reflect the effects on occupancy rates due to the 2018 gas crisis.

3. The Town should conduct a thorough investigation of potential new revenue sources in the form of fees and taxes, including a Proposition 2 ½ override.

Towns across the country facing similar challenges are exploring revenue strategies that would provide significant new revenue which are legal and practical to implement and likely to be accepted by their communities. Any new revenue sources must be measured against current fees collected.

Section 2: Retirement

Introduction

The Andover Contributory Retirement System, an independent entity, is managed by the ARB. ARB has the fiduciary responsibility to manage retirement funds for active and retired Town employees, and certain school employees. Teachers are members of a separate system, the Massachusetts Teachers Retirement System (MTRS), to which the Town is not required to contribute

The Andover Contributory Retirement System provides qualified members with a defined benefit plan (Pension). Employees hired after July 1, 1996 contribute 9% of gross pay, plus an additional 2% on compensation over $30,000. Note: Municipal employees neither pay into nor receive Social Security benefits. All members hired after January 1, 1979 contribute 2% on compensation over $30,000.

The most recent pension reform instituted by the State occurred in 2012, which among other changes, increased the earliest retirement age from 50 to 60 for employees hired after April 2, 2012. Employees hired prior to April 2, 2012 are eligible to retire at age 55, with at least 10 years of service, or 20 years of service at any age. Employees hired after April 2, 2012 are eligible to retire at 60 with at least 10 years of service. Public Safety employees are classified in a separate group with different eligibility standards.

Pensions are calculated by factoring the age of the retiree and years of service and can range from 14.50% of the average salary of the employee's highest three years of compensation to 80% of the average salary of the employee's highest three years of compensation.

The Town's pension benefit payments exceed employer/employee contributions. The ratio of active to retired has been decreasing each year. History suggests that about 30-40% of active employees will retire over the next 10-15 years, the ratio of active to retired will be close to 1:1 within a decade.

The Task Force believes obligations already incurred should be fulfilled. ARB is currently considering a change of eligibility for new employees in the retirement plan from part-time employees (20 hours) to fulltime employees. The financial impact of such a policy change would be positive on both future pension obligations and OPEB. The potential impact of this eligibility change upon staff recruitment should be studied and taken into consideration.

Recommendations

The Town's unfunded liabilities are the most significant financial threat to the Town's long-term wellbeing. In 2001, the Town's pension plan was 82% funded. By 2007, funding levels had shrunk to 65%. Today, the Town's pension plan is 43% funded, despite an 11 year bull market in stocks. As unfunded liabilities rise, the potential for the deterioration of the Town's credit rating increases. Investors may require higher interest costs to compensate for higher risks driven by unfunded liabilities, thus threatening the Town's affordable access to the capital markets. While the Town has for many years successfully maintained its AAA bond rating (the highest rating given) Standard & Poor's (S&P) noted in its 2019 report that Andover's large pension and OPEB obligation, "…without a plan in place to sufficiently address the obligation in the short-to-medium term, is a credit weakness."

As of June 30, 2019, the Net Pension Liability (Retirement) was $180.9 million, and the Net OPEB liability was $127.8 million, totaling $309.7 million. Using the US Census Bureau estimate as of July 1, 2018 of 12,369 households in Andover, unfunded liabilities debt per household is $25,038, or 2.51 years of property taxes at the average FY2019 single family tax bill of $9,973. In short, the unfunded Pension and OPEB liabilities are the Town's version of the global warming crisis; though the Town and ARB have taken steps to address this growing debt, this is an increasing threat looming on the medium-term horizon that becomes more difficult to solve with each successive year.

It is the opinion of the Task Force that it should be a top priority of the Town to deal more aggressively with the unfunded liability debt in a way that doesn't threaten the Town's ability to provide essential services or require taxation levels that reduce economic growth.

Specifically, the Task Force recommends:

1. The Town's discount rate (6.25%) should be used to determine the Town's annual contribution for pensions for FY2021.

Though the above statement may seem rather innocuous, it is not. The Town is currently making annual contributions using the 7% discount rate (see current schedule below) as required by ARB. The Town does have the option to contribute more than what ARB is requesting.

Fiscal Year	Current Schedule	Schedule at 6.25%	Difference
2021	$12,025,710	$12,478,716	$452,907
2022	$12,891,561	$13,626,649	$735,088
2023	$13,819,754	$14,880,301	$1,060,547
2024	$14,814,776	$16,249,289	$1,434,513
2025	$15,881,440	$17,744,223	$1,862,783
2026	$17,024,904	$19,376,692	$2,351,788
2027	$18,250,697	$21,159,348	$2,908,651
2028	$19,564,747	$23,106,008	$3,541,261
2029	$20,973,409	$25,231,760	$4,258,351
2030	$22,483,494	$27,553.082	$5,069,588
2031	$24,102,306	$30,087,966	$5,985,660
2032	$25,837,672	$32,856,059	$7,018,387
2033	$27,697,984	$35,878,816	$8,180,832
2034	$29,692,239	$39,179,667	$9,487,428
2035	$31,291,402	$42,082,798	$10,791,396
Total	**$306,352,095**	**$371,491,275**	**$65,139,180**

While such a change would be an additional $452,907 in the Town's FY2021 contribution, over the course of the 15-year funding schedule if the 6.25% discount is used, the difference is dramatic and harbors significant implications to the Town and its residents. A reduced discount rate of 6.25% will result in the Town having to contribute $65 million more than the current plan schedule. That approaches almost four times the total Public Safety budget in FY 2019.

The discount rate is the long-term expected rate of return on investments. ARB has used overly optimistic discount rates over the last 20 years (8% average over last 20 years) while the investment portfolio earned only 4.39% for this period. Since Town contributions are calculated in part on the assumed investment returns, this is the principal reason for the Town's significant growth in unfunded pension liability. The practice of using discount rates that are too high has impacted plan-funded levels in two ways:

- Actual asset levels have not increased as fast as the assumptions because the assumptions are too aggressive; and
- The Town is not contributing as much as it should because the higher discount rate keeps the Town's contribution amount artificially lower.

Over 75% of annual pension expense paid by the Town today is for services rendered by employees/retirees from prior years. It is the opinion of the Task Force that taxpayers should fully pay for the compensation of employees, including their pension benefits, at the time taxpayers receive services from the employees.

The Task Force recognizes the contribution schedule using 6.25% will be challenging to accommodate and will require significant changes to either services or taxes or both.

The Town needs to continue to demonstrate to the rating agencies that a viable plan is in place to reach full funding by 2035. The impact of a bond rating downgrade by S&P would be extremely detrimental as it would result in the costs of borrowing potentially increasing significantly, and a reduction in confidence by outside experts in the Town's fiscal practices. Using the national averages for Municipal Bonds as of 10/23/19 the difference in a 30-year AAA versus AA and A bond yields are 0.2%, and 0.35% respectively, implying the cost to the issuer is 9.5% more in the first case and 16.7% in the latter.

Such an increase in bond yields would affect the cost of capital projects, such as school construction, dramatically.

2. The Town and ARB should agree on using the same discount rate.

The Task Force encourages the Town and ARB to agree on using the same discount rate in valuing pension liabilities and setting the annual Town's contribution schedule. ARB will be deciding on a new discount rate in the first quarter of 2020 and should consider the Town's basis for using 6.25%. It is solely in the authority of the ARB to set its own discount rate (with PERAC approval).

3. The Town and ARB should consider having actuarial valuations prepared annually.

Actuarial reports provide key information needed to prepare the Town's audited financial statements. They are also the key source documents for information regarding actuarially determined required contributions as well as the funded status of both pensions and OPEB. Actuarial reports for pensions and OPEB are currently prepared every two years. The actuary provides financial data for the second year financial reporting based on one year old data. Demographic information, long term investment return assumptions, payroll growth, etc., may change the second year and contribution schedules could be affected. The Town, working with the ARB, should consider having these reports prepared annually.

Advantages in having valuations prepared annually include:

- More accurate financial reports.
  Given the size and growth of these unfunded liabilities, it is important to have as current financial information as possible to make informed financial decisions.

- Making required contributions
  A key purpose of an actuarial valuation is to inform the Town and ARB of the contribution amount needed each year to adequately fund benefits. Receiving this information every two years runs the risk of the second year funding being incorrect if underlying assumptions, such as investment returns, are not achieved.

4. The Town should consider applying excess free cash towards pension debt.

Future debt rarely generates the urgency of more immediate problems. The Town's pension debt constitutes an emergency by any reasonable standard. The consequences of not addressing it soon will be real and painful, potentially including increased future tax burdens, damaged property values and essential service cutbacks.

State regulators require the Town to have its pension debt fully funded by 2035. The contribution schedule on page 13 shows the Town will have to make payments totaling $371.5 million (using the 6.25% discount rate) over the next 15 years to reach that date. This represents a 417% increase in pension payments compared to the $89 million paid the previous 15 years. A large portion of the payments are paid at the back end of the funding schedule. $150 million, or 40%, of the $371.5 million in payments are expected to be paid the last 4 years of the funding schedule. It is unlikely the Town would be able to pay these annual contributions without significant increases in taxes and/or reduction in services.

One possible solution to address the growing pension debt and meet the full funding schedule of 2035 is to pay down the debt sooner than accomplished through the annual required contribution. Contributing more in the early part of the 15 year schedule is akin to paying down a mortgage earlier. Just like making minimum payments on a credit card may not ever pay off the balance, the Town needs to move aggressively to full funding to avoid future problems with pension debt. The sooner that debt is paid off, the sooner costs go down. This would reduce interest payments on the unfunded pension liability balance and, depending on the supplemental payments made, could save the Town millions over the 15 year period.

The primary advantages of additional contributions are:

- Savings in interest and lowering the overall cost of the pension program
- A reduction to unfunded pension liability for financial statement purposes
- A reduction in pension expense for financial reporting purposes
- Lower risk of low funded status in the future
- Lower risk of higher contributions in the future
- Meeting the fully funded date of 2035 as required by the regulators

Section 3: OPEB

Introduction

OPEB relates to post-employment benefits other than pensions. This is mostly retiree health insurance. Retiree health insurance costs include enrollment in traditional health insurance plans and Medicare supplement plans. Retirees pay a percentage of their health insurance premiums. State statues require the Town to pay a minimum of 50% of retiree and employee healthcare.

OPEB is governed by Governmental Accounting Standards Board (GASB) Statements 74 & 75. Beginning in 2018, GASB 75 required the total OPEB liability be recorded on the Town's financial statements. GASB requires an actuarial valuation be performed at least every two years.

The unfunded OPEB liability as of June 30, 2015 was $184 million. In April, 2016, the Select Board voted to incrementally increase retiree contribution rates. This significantly reduced OPEB liability to $128 million. As of June 30, 2019, the OPEB liability was $127 million.

Recommendations

OPEB faces different challenges than the Town's pension plan. Unlike the pension plan, employees do not contribute to the OPEB fund. State statutes require pension plans to be fully funded by 2040 (our regulators are requiring an earlier date of 2035) whereas there is no full funding requirement for OPEB. In the absence of a required funding schedule, Andover has, as many cities and towns, not adequately set aside assets to fund this debt.

Another problem, and perhaps the most significant, is the growth rate of healthcare cost which is, at present, greater than the rate of inflation. To make OPEB liability calculations, actuaries typically project the current growth rate of healthcare cost forward 50 years or more. Projecting even a small percentage growth forward over half a century produces a tremendous sum, and the resulting liabilities are enormous.

1. The Town should consider increasing its annual contribution to OPEB and establish a funding schedule for fully funding OPEB.

The chart below shows cash contributions over the next 10 years to the OPEB trust fund from the Town's scheduled annual contributions combined with estimated savings from 2016 OPEB reform. The "Required cash contributions" column is from the 6/30/19 actuary's valuation report on OPEB. This column shows cash contributions required by the Town to fully fund OPEB in 29 years. 10 years was used below to illustrate the additional contribution required to meet the 29 year period.

	Town annual contributions (1)	Savings from OPEB Reform (2)	Expected cash contributions (1+2)	Required cash contributions	Additional contribution required
FY 2020	$1,064,940	$906,194	$1,971,134	$4,792,767	$2,821,633
FY 2021	$1,083,812	$978,690	$2,062,502	$4,799,122	$2,736,620
FY 2022	$1,107,530	$1,056,985	$2,164,515	$4,848,221	$2,683,706
FY 2023	$1,135,218	$1,109,834	$2,210,798	$4,372,547	$2,161,749
FY 2024	$1,163,599	$1,165,326	$2,328,925	$4,376,502	$2,047,577
FY 2025	$1,192,689	$1,223,592	$2,416,281	$4,309,381	$1,893,100
FY 2026	$1,222,506	$1,284,772	$2,507,278	$4,309,253	$1,801,975
FY 2027	$1,253,069	$1,349,010	$2,602,079	$4,357,834	$1,755,755
FY 2028	$1,284,395	$1,416,461	$2,700,856	$4,579,378	$1,878,522
FY 2029	$1,316,505	$1,487,284	$2,803,789	$4,651,214	$1,847,425

Source: FY2019 GASB Statements, Stone Consulting

As the above chart shows, the Town’s scheduled annual contributions are insufficient to fully fund OPEB in 29 years. The actuary did not provide a schedule on when the Town will be fully funded under the current contribution schedule. The Town should consider increasing its annual OPEB contributions. The Town should request the actuary to prepare a funding schedule showing what the Town would need to contribute with a 35 year and 40 year full funding date.

2. The Town should document its control policies, processes and procedures regarding pension and OPEB participation and reporting.

It is important that the Town has controls suitably designed and implemented to achieve proper participation in the Town's pension and OPEB Plans and reliability of data reported to the actuary.

3. The Town should consider creating an OPEB Trust Advisory Board.

Members should have investment management, accounting, actuarial and risk management skills. Advisory Board responsibilities would include, but not be limited to, recommending investment policy and asset allocation strategy, review and recommendation of rates and assumptions used in actuarial reports and continually advising on potential improvements.

Section 4: Health Insurance

Introduction

Governed by Massachusetts General Law Chapter 32B, Andover has been self-insured since FY2016. Andover's carrier is Blue Cross/Blue Shield. Two plans are offered:

- HMO and PPO options for active employees and retirees under age 65
- Medex for retirees 65 and older

Active Employee Enrollees		
Department	**Number of Enrollees**	**Percentage of Plan**
Town	282	29.04%
School	689	70.96%

Active Employee Contributions Share		
Department	**Amount**	**Percentage**
Town	$3,948,316	28.95%
School	$9,689,848	71.05%

Total Contributions	
Town	$17,160,591
Active Employees	$4,070,577
Retirees	$2,226,676
Total	***$23,457,742***

Active/Retirees Breakdown
Total Premiums Actives
$17,708,742
Total Premiums Retirees
$5,749,102

Andover has purchased re-insurance (stop loss) for individual claims over $175,000. Andover works with a consultant to monitor claims and set rates (annually in the March/April timeframe). The Town has taken substantial steps to reform its healthcare offerings. Some changes that have been instituted include:

- 2012: the Select Board accepted Chapter 32B, sections 21 through 23 which allowed the Town to make plan design changes in the HMO and PPO plans in accordance with the most enrolled plan in the GIC (Group Insurance Commission). The effect was savings of $1.1M for FY2013-FY2015.
- 2013: the Town began to offer a Health Insurance Opt-Out program. To date, 40 employees have enrolled in the program, with savings over $775,000.
- 2015: the Town moved retired teachers from the GIC to Town plans.
- 2016: the Town moved from a premium based plan with a third-party administrator, to self-insured.
- 2017: Town officials elected to change plan design under Chapter 32B sections 21-23, saving approximately $900,000 in FY2018.

- 2017: employees hired after July 1, 2017 pay 30% of premiums for HMO plans, up from 18.9% for individual plans and 23.1% for family plans, saving approximately $382,000 in FY20.

The FY2020 total appropriation of $22,074,808 includes $21,680,625 for General Fund, $318,966 for Water Department, and $75,217 for Sewer Department. The Long Range Financial Plan projects an average annual increase of 7.27% over the next four years.

Health Insurance Budget History	
FY2020	$21,340,842
FY2019	$20,662,075
FY2018	$19,257,000
FY2017	$17,905,037
FY2016	$17,052,416

The rate increase for FY2020 is 4.29%. However, the Town's health insurance appropriation increased 6.84% due to the addition of new employees and retirees. Even if there is no net increase of full-time employees, when an employee retires and a replacement is hired to replace them, the result is that there are two people on health insurance.

Recommendations

1. **The Town should continue to work with the Insurance Advisory Committee to review plan design changes.**

2. **The Town should explore high offering deductible health plans and health savings accounts.**

Section 5: Other

Recommendations

1. The Town should consider including differences between the annual budget and its audited financial statements in appropriate financial documents.

The Town prepares its annual balanced budget in accordance with State statutes. However, the balanced budget process is not inclusive of all expenses accrued that year, such as OPEB and pension unfunded expenses. The citizens of the Town may view the Town budget as representing that current year revenues are sufficient to pay for services provided that year. This is not always the case. The Town's budget process, though it serves well as a vehicle for planning, control and accountability, does not reflect the Town's complete financial results.

To illustrate, the Town reported balanced budgets for FY2018 and FY2017 but the Town's published audited financial statements report losses of ($12.3 million) for 6/30/18 and ($13.5 million) for 6/30/17. These losses were principally due to higher pension and OPEB expenses recorded in the Town's financials than that budgeted for Pension and OPEB expense. The differences between budgetary and accrual basis of accounting should be disclosed by the Town in a manner that is clearly understandable for those who don't have expertise in accounting

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