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City Manager

CITY OF WORCESTER

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TO THE WORCESTER CITY COUNCIL

COUNCILORS:

In January, I presented to City Council a projected \$8 million budget deficit for Fiscal Year 2013 after analysis of the Governor's FY 2013 Budget and its corresponding Unrestricted Local Aid recommendation for the City. This original projection was derived from a similar set of circumstances as in past years—growth of fixed costs; required reserve-building deposits; formula-based increases to fund our public schools; debt service for completed public school capital improvements; and nominal wage increases for employees (net 2.5% after two successive fiscal years with 0% wage increases).

Much has transpired since January 2012. As you know, our Five Point Financial Plan projections are derived from trends, forecasts and the marketplace (futures, etc.). These projections become more definitive the further we move into the budget recommendation process and into the current Fiscal Year. After additional detailed review and analysis, I am pleased to inform you that positive adjustments, as detailed below, will reduce the January 2012 projected deficit of \$8 million by \$4.8 million. I must be very clear that these adjustments are due to two primary factors – positive revenue trends reflecting marginal improvements to the local economy and continued cost reductions/ cost containment for employee health care due to the sweeping reform implemented last fiscal year.

Our collective work to address runaway cost centers, re-organize City government and bring our expenditures in line with our revenue realities has put us in a far better financial position than in previous fiscal years at this time. As you know, we have had to tackle deficits as high as \$32 million in this economic downturn prior to my submission of a balanced budget recommendation to your Honorable Body.

The following summary details the projected FY2013 deficit, as of this writing, and the adjustments made to narrow the gap:



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**FY 2013 Budget Projections – as of March 7, 2012**

**January 2012 Deficit Projection Per Five Point Financial Plan** **(\$8,000,000)**

**Revised Revenue Collections** **\$1,000,000**

We have been very conservative on budgeted revenues in certain categories in this economic downturn. We adjusted these estimates downward for three consecutive fiscal years accordingly and rightfully so. I am please to state that local revenue categories such as motor vehicle excise and building permits consistently exceed or have exceeded those conservative budgets due to marginal improvements to the local economy. Therefore, it is reasonable for the City to increase these budgeted revenues to reflect these consistent year-to-year improvements in these categories. This situation repeats itself in the new real estate revenues associated with new construction growth. Combined, this will allow us to increase budgeted revenues by an additional \$1 million for FY2013 (from our January 2012 projections).

**Overlay Reserve** **\$500,000**

It is expected that the very thorough DOR revaluation process underway will allow for a reduction in the FY2013 appropriation to the overlay reserve account from \$3.5 million to \$3 million. This will “free up” approximately \$500,000 for other appropriation purposes for Fiscal Year 2013.

**Health Care Reform Savings** **\$3,300,000**

The hard work accomplished to negotiate and implement new “GIC-like” health insurance plans for our employees has resulted in lower growth than anticipated in premium costs. Preliminary discussions with our health insurance carriers and review of our claims experience to date have resulted in a much lower than expected premium increase from the anticipated average of 8% to approximately 4%. In addition, the final migration of all subscribers to the new lower cost “GIC-like” health plans and the anticipated lower premiums associated with this transition will combine with the premium decreases to redirect \$3.3 million from employee health care costs to direct City services. It is important to note that separate and distinct from the City’s savings the Worcester Public Schools estimate that they will save approximately \$2.7 million due to these factors to help address their budget needs for FY2013. These redirected funds can be re-programmed to classroom services but will never show as an increase over the State’s minimum contribution formula. Reforms and more efficient/ effective use of redirected “reform” dollars to the classroom do not count within the outdated formulas.

**Total Revised FY 2013 Deficit Projection** **(\$3,200,000)**

As reported in January 2012, the Governor’s budget includes the potential for additional Unrestricted Local Aid to cities and towns if State revenue benchmarks are achieved. This “one-time” allocation will not be included within my FY2013 budget recommendation since these funds are not definitive. However, in the event that this appropriation is released, I intend to identify services and/or capital investments that can be funded with these one-time, non-recurring dollars, similar to Fiscal Year 2012. This will provide the flexibility to maintain important services, such as stump removal or crosswalk painting, without the risk of having to re-structure or reduce departments or divisions in future fiscal years.

Our current financial position moving into Fiscal Year 2013 is very promising, but even as we plan for some level of stability in the short-term, we must not lose sight of the long-term liabilities (pension and OPEB). We will continue to face these challenges to balance budgets in future fiscal years. These are bona fide City obligations that require our attention. The current pension funding schedule calls for 4% increases in the City's assessment each year, which is higher than our annual rate of revenue growth. As of the last valuation the retirement system was 71% funded, leaving an unfunded liability of \$300 million.

Similarly, we continue to carry forward our liability to fund retiree health care benefits (OPEB) now and in the future. The future costs of these benefits have reached a staggering \$765 million as of the last valuation. Unlike the pension system, there is **no funding source** in place and we continue to pay as we go—another unsustainable model. For the first time, the City is funding health insurance for more retired employees and spouses than active employees; and this trend will only continue. Combined, these unfunded liabilities total approximately \$1 billion owed by the City. If we do not move to contain or begin to fund these costs centers, they will continue to absorb a greater percentage of our operating funds and limit our ability to provide services in the future.

My Administration and I will continue our work to address the remaining deficit of \$3.2 million prior to the submission of my FY2013 Budget Recommendation by late April of this year. I will continue to keep you updated on all our actions in this regard.