TOWN OF HOLLISTON
FINANCIAL POLICIES

I. INTRODUCTION

The following financial policies are established by the Town of Holliston through its Board of Selectmen and Finance Committee in order to set forth the broad framework for management of the Town's finances and to inform the annual budgeting process. The intent of these financial policies is that they serve as a guide for policy makers, administrators, department heads and advisors, recognizing that Town Meeting retains full right to appropriate funds and incur debt as it deems appropriate, subject to statutory constraints.

II. RESERVE FUND

Policy: Set aside a minimum of $200,000 and not more than .5% of the Omnibus Budget each year to provide for extraordinary or unforeseen expenditures not anticipated before Town Meeting, and/or to allow immediate expenditures of funds in the event of an emergency.

Practice: The Reserve Fund is authorized by section 6 of Chapter 40 of the General Laws (see Appendix C) and has been utilized by the Town for more than seventy-five years. The unexpended balance, if any, at fiscal year's end is closed out to the General Fund and becomes part of the Free Cash calculation.

Plan: Maintain the existing Reserve Fund level.

Progress: The Reserve Fund has been $212,675 for the last three fiscal years and is projected at that level through FY20.

III. STABILIZATION FUND

Policy: Maintain a minimum balance equal to 8.1% of General Fund expenditures with a target goal of 10% and a maximum goal of reaching 15% of General Fund expenditures.

Practice: Stabilization Funds are authorized by section 5B of Chapter 40 of the General Laws. The Stabilization Fund provides financial flexibility in times of economic stress (rainy day fund) and has been utilized by the Town for more than fifty years. It should be used only for extreme events, such as natural disasters, emergency conditions, sudden economic stress or as a bridge for a short term financial event. A plan to replenish the fund, preferably within one year but not more than three years, should be developed when the fund is used. The minimum balance is set to enable the Town of Holliston to reach and maintain a "strong" budgetary flexibility rating from Standard & Poor's based on the Stabilization Fund alone, without reference to the variable and volatile Free Cash balances. The Town will endeavor to reach the target balance, so that the fund can be used without impacting the credit rating.

Plan: Build the Stabilization Fund through transfers from Free Cash and other available funds (unexpended special articles, "excess" revolving fund balances, etc.) and appropriations of unanticipated and/or one time revenues.

Progress: The Stabilization Fund balance ($2,587,590) was at 4.59% of FY13 General Fund expenditures ($56,342,250) as of July 1, 2014.

IV. CAPITAL OUTLAY

Policy: The "cash" Capital Outlay policy seeks to ensure that the Town of Holliston maintains, preserves and replaces the equipment, vehicles, technology, infrastructure and buildings needed to efficiently and effectively support the Town's programs and operations. Regularly scheduled updates and refreshes to capital assets are required to prevent larger costs or loss of services that could result from deferral or inadequate funding.

- The minimum or target annual "cash" capital outlay/expenditure should be set to 2% of the Omnibus Budget (or an amount derived from annual depreciation figure; or an amount derived from capital inventory replacement cost and lifespan analysis).
- The annual "cash" capital outlay/expenditure will be funded through a combination of budgeted capital, allocations from Free Cash, and allocations from the Capital Expenditure Fund (CEF).
- The minimum balance in the CEF should be maintained at not less than 2% of the Omnibus Budget.
- If the annual capital outlay amount is not needed for capital expenditures in a given year, the "excess" above the amount needed should be appropriated into the CEF.

Practice: A capital expenditure funded under the "cash" Capital Outlay policy will have a useful economic life of more than five years and cost more than $10,000 and not exceed $1 million – or be otherwise classified as fixed assets on the Town's financial statements. Bulk purchase of similar items such as technology and furniture should be aggregated and the total considered a capital item. Larger capital investments involving the replacement of Town buildings, major facilities and the construction of new facilities to expand or upgrade Town programs, or capital needs exceeding $1 million will typically be funded through borrowing and/or overrides, and are addressed within the broader Capital Improvement Plan (CIP) policy. Smaller and routine annual asset maintenance is to be managed within the departmental operating budgets.

The CEF was created by Chapter 46 of the Acts of 1993 and exists to support the annual "Cash" Capital Outlay when budgeted capital and free cash allocated to capital are insufficient, and as a place to hold funds intended for capital investments. The CEF can be used to sustain the annual capital outlay, to offset debt service in times of economic stress, or to avoid borrowing for a capital acquisition. Not more than one-third of the balance in the CEF should be drawn down in any one year period. If the fund drops below the recommended minimum balance, a plan to replenish the fund, preferably within one year but not more than three years, should be developed. Maintaining the stated minimum balance in the CEF contributes to a "strong" liquidity rating from Standard & Poor's.

Plan: The town will work toward a goal of budgeting 2% of the Omnibus Budget (or an amount derived from the annual depreciation figure; or an amount derived from capital inventory replacement cost and lifespan analysis) for the purpose of maintaining, preserving and replacing "cash" capital assets. Gradually increase the annual capital set aside until it reaches 2% of the

Omnibus Budget. Complete the comprehensive asset inventory in 2015, so that the minimum annual "cash" Capital Outlay can be validated against an objective benchmark.

Progress: The capital set-aside for budgeting purposes has been increased to $625,000 (1.2% of the Omnibus Budget) in FY15 and the revenue/budget projection calls for an increase to $650,000 from FY16 through FY18; the Capital Expenditure Fund balance of $1,394,003 as of November 1, 2014, is 2.66% of the FY15 Omnibus Budget.

(Note: The Town of Holliston is in the process of developing a comprehensive CIP policy. The "cash" Capital Outlay policy will sit within the broader CIP policy framework.)

V.   FREE CASH

Policy: To be used to increase reserves, to fund capital or other one-time expenditures, to reduce debt, or to reduce the tax levy, and not to support or supplement the Omnibus Budget.

Practice: Eliminate reliance on Free Cash for operating revenue due to its variability and volatility. Annually transfer the balance of Free Cash, or a substantial portion thereof, to the Stabilization Fund, with the remainder of the balance, if any, going to one-time expenses, for capital or to reduce the tax levy.

Plan: Reduce the amount of Free Cash used to support the Omnibus Budget to $0 by FY18.

Progress: The amount of Free Cash used to support the Omnibus Budget has been reduced to $375,000 in FY15 and the five year revenue/budget plan reduces the support in increments of $125,000 per year to $0 in FY18.

VI.   DEBT SERVICE

Policy: Debt should be reserved for the purchase of large, non-recurring capital items of $1 million or more and which have a life of ten years or more, and the term of the debt should not exceed the life of the asset. The Town will endeavor to maintain a strong to very strong S&P rating in this category by keeping the General Fund debt service to expenditures ratio below 8% and by keeping the net direct debt to General Fund revenue ratio between 30% and 60%.

Practice: When considering the use of debt, the Town will take into account:

- The debt exclusion option – a temporary tax increase used to raise additional taxes to fund capital projects for which the community may borrow.   The additional amount is added to the levy limit only during the life of the debt.
- The capital outlay expenditure exclusion option is a temporary tax increase used for the year in which the capital item is acquired.
- The annual fixed-cost that additional debt will add to the debt service portion of the Omnibus Budget. (Note that S&P considers total governmental fund debt service as a percentage of total governmental funds expenditure lower than 8% to be "very strong".)
- The additional burden that additional debt will place on the Town's revenue position. (Note that S&P considers net direct debt as a percentage of total governmental funds revenues at between 30 to 60% to be "strong".)

Plan: Minimize long term debt through more robust annual capital spending and through short term financing. Minimize the term of any bond issue so that at least two-thirds or outstanding debt will be paid off within 10 years.

Progress: The last bond rating assessment by S&P, based on FY12 results, found that total governmental fund debt service as a percentage of total governmental funds expenditures was 8.6% and the net direct debt as a percentage of total governmental funds revenues was 58.7%.

VII. WATER ENTERPRISE FUND

Policy: Establish a Water Enterprise Fund that fully supports the annual operating and capital costs, including indirect costs related to the staffing, operation and maintenance of the system, and including debt service, for the Town's water supply and distribution system; and maintain an unencumbered fund balance (retained earnings) of at least 10% of the annual gross water revenues.

Practice: All receipts, revenues and funds, including interest derived from all activities of the enterprise, are deposited into the water enterprise fund. User fees are comprised of tiered rates for consumption based on metered use, a fixed rate meter service charge based upon the meter size, and a fixed rate private fire service based on pipe size (sprinkler system).

The target unencumbered fund balance (retained earnings) of the water enterprise fund should be maintained at a level that is not less than 10% of annual gross water revenues. By vote of the Board of Selectmen and Town Meeting the balance in the fund may fall below this minimum level to fund capital needs or to provide for payment for unanticipated (emergency) repairs to the water supply and distribution system. The unencumbered fund balance (retained earnings) should not be used to subsidize ongoing operations.

Plan: Establish the Water Enterprise Fund within the DPW structure at the 2014 Fall Town Meeting; develop a water rate structure and spending plan to cover all operating and capital costs; establish a minimum 10% unencumbered balance (retained earnings) by FY18; develop and begin implementation of a plan to repair or replace the aging water main infrastructure.

Progress: The Water Enterprise Fund was established at the 2014 Fall Town Meeting. The unencumbered balance (retained earnings) in the Fund was $603,150, or 22.6%, of FY14 gross water revenues as of November 1, 2014. The projected addition to the unencumbered balance (retained earnings) from FY15 operations is $170,000, or 7.1% of the projected FY15 gross water revenues.

VIII. OPEB (Other Post-employment Benefits)

Policy: Fully fund the OPEB obligation not later than 2040 by establishing a fixed expense in the annual budget of $1.5 million or the Annual Required Contribution (ARC) as determined by the required biennial actuarial valuation in accordance with Governmental Accounting Standards Board (GASB) Statements Number 43 and 45 (see Appendix G).

Practice: Holliston's unfunded actuarial accrued liability (UAAL) was valued at $47.8 million as of June 30, 2012. OPEB covers the Town's share of the current and anticipated future health and life insurance benefits costs for the Town's municipal and school employees who retire through the Middlesex Retirement or Massachusetts Teachers Retirement Systems (and firefighters) after having worked for a minimum of 20 hours a week for a minimum of 10 years. This liability is based on the following key assumptions in the actuarial valuation dated October 18, 2012:

- 311 beneficiaries and 302 active participants
- A medical/drug cost trend of 8% decreasing by .5% over 6 years to a level of 5% per year
- An investment rate of return of 6%
- A maximum 30 year amortization period

Plan: Contribute $1.5 million per year, or such other amount as the biennial OPEB actuarial analysis may suggest, to the OPEB Trust Fund in order to reach full funding not later than 2040; monitor OPEB Trust Fund investment performance; and monitor efforts at the state and local levels to contain costs.

Progress: An OPEB Trust Fund was established in 2014 (see Appendix F) and $4,895,479 had been deposited into the Trust as of June 30, 2014. The OPEB Trust Fund Board is in the process of determining the investment vehicle(s). The FY15 appropriation for retiree health benefits plus the FY15 OPEB set-aside total approximately $2.44 million, or 4.7% of the FY15 Omnibus Budget.

IX. RETIREMENT

Policy: Fund the Town's annual assessment from the Middlesex Retirement System (MRS) and make annual payments toward the Town's share of the System's unfunded liability.

Practice: The Town of Holliston has fully funded the annual assessment without fail for more than 50 years. Starting in FY15, the Town has designated the "credit" for early payment toward the Town's share of the System's unfunded liability. The MRS covers the pension benefits for the Town's 100 retired municipal and school non-teaching employees who have worked for the Town for a minimum of 20 hours a week for a minimum of 10 years. (Teachers are covered by the Massachusetts Teacher's Retirement System, which does not currently assess the Town for benefits.)

Plan: Apply the amount of the difference between paying the annual assessment in one installment and paying it in multiple installments to the Town's share of the System's unfunded liability.

Progress: The Town has made payments toward its share of the unfunded liability in FY15 totaling $37,000. The Town's share of the System's unfunded accrued actuarial liability as of June 30, 2012 was $21.9 million. The FY15 appropriation for retiree health benefits plus the FY15 OPEB set-aside plus the FY15 MRS assessment totaled approximately $4.38 million, or 8.4% of the FY15 Omnibus Budget. (Note that one Standard & Poor's benchmark is that the required annual pension payment plus the annual OPEB payment as a percentage of total governmental funds expenditures should be less than 10%.) The Town's liability is based on the following key assumptions in the actuarial valuation of the MRS dated February 5, 2013:

- 4,886 beneficiaries and 8,979 active participants (252 in Holliston)
- Appropriations increase 6.5% per year through 2020, increase at a lower rate thereafter
- An investment return rate of 8%
- Fully funded by 2036

X. APPENDICES

A. U.S. Local Governments General Obligation Ratings: Methodology and Assumptions, Standard and Poor's Rating Services, September 2103

B. Massachusetts General Laws Chapter 44, section 5B (Stabilization Funds)

C. Massachusetts General Laws Chapter 44, section 6 (Reserve Funds)

D. Massachusetts General Laws Chapter 44, section 10 (Debt Limits)

E. Chapter 46 of the Acts of 1993 (Capital Expenditure Fund for Holliston)

F. Chapter 189 of the Acts of 2013 (Other Post-Employment Benefits Trust Fund for Holliston)

G. Other Postemployment Benefits: Plain-Language Summary of GASB Statements No. 43 and No. 45, Governmental Accounting Standards Board

Draft 9/15/14, Rev. 10/21/14, 11/10/14, 11/11/04, 11/25/14, 12/2/14

TOWN OF HOLLISTON
SUMMARY OF FINANCIAL POLICIES

Policy	Summary of Terms	Purpose
Reserve Fund	A minimum of $200,000 and not more than .5% of the Omnibus Budget each year	To provide for extraordinary, unanticipated expenditures or immediate expenditure the event of an emergency.
Stabilization Fund	Maintain a minimum balance equal to 8.1% of General Fund expenditures; target is 10%, maximum is 15%	A "rainy day" fund to provide for financial flexibility in times of economic stress, emergency conditions.
Capital Outlay	Seeks to ensure that the Town of Holliston maintains, preserves and replaces the equipment, vehicles, technology, infrastructure and buildings needed to efficiently and effectively support the Town’s programs and operations by investing in regularly scheduled updates and refreshes to capital assets. • Annually target annual “cash” capital expenditures at 2% of omnibus Minimum balance in the CEF of not less than 2% Omnibus Budget • Annually budget 2% of the Omnibus Budget for capital outlays • Economic life of 5+ years, cost between $10,000 and $1 million	
Free Cash	To be used to increase reserves, to fund capital or other one-time expenditures, to reduce debt – or to reduce the tax levy, and not to support the Omnibus Budget.	
Debt	Debt should be reserved for the purchase of large, non-recurring capital items which have a life of ten years or more. The Town will endeavor to maintain a strong to very strong S&P rating in this category by keeping the General Fund Debt Service to Expenditures rating below 8%; keeping the Net Direct Debt to General Fund revenue ratio between 30 and 60%; and staging debt so that two-thirds of outstanding debt payable within 10 years.	
Water	The Water Enterprise Fund, water rate structure, and spending plan fully supports all direct and indirect annual operating and capital costs for the Town's water supply and distribution system. The Water Enterprise Fund will maintain an unencumbered balance (retained earnings) of 10% of operating costs which can be used to offset seasonal volatility and/or as a "rainy day" fund for the Water Enterprise.	
OPEB	Fully fund the OPEB obligation by establishing a fixed expense in the annual budget of $1.5 million or the Annual Required Contribution (ARC)	
Retirement	Fund the Town’s annual assessment from the Middlesex Retirement System (MRS), and Town’s annual share of the System’s unfunded liability	