BOC Position Paper on
Greenwich’s Looming Budget Crisis

The Representative Town Meeting has charged its Budget Overview Committee (BOC) with “suggesting guidelines and making recommendations” regarding the budget of the Town of Greenwich.

The BOC has been concerned in recent years about the growth of the Town’s budget at rates well in excess of inflation and personal earnings growth. Moreover, for reasons explained below, the BOC has now become especially concerned that excess growth in the budget cannot continue without jeopardizing much of why we have chosen to live here.

In a letter on June 16, the BOC asked those who prepare the proposed budget for the next year – members of the Board of Estimate and Taxation, the Board of Education and the First Selectman Office - that they consider lower growth rates, if any, for the proposed budget for next fiscal year. None of these entities, however, have yet responded to our recommendations.

This paper summarizes the reasons why the BOC is concerned and what actions the Town will need to consider.

Recent Financials Appear Healthy

For fiscal 2017 (year ending June 2017), budgeted General Fund expenses, fixed charges and other payments total $431 million. Budgeted funding of this will be property tax collections of $358 million, new borrowings of $64 million and state and federal aid, draw-downs from various funds and other. It is arguably a balanced budget.

Additionally, when compared to other towns and cities in Connecticut (and to those in other states, for that matter), Greenwich possesses the following two enviable tax-related attributes.

- **Highest Tax Base**
  
  Greenwich’s total taxable assessment (aka the Grand List), which must equal 70% of estimated fair market value by state law, was $32.5 billion for the current fiscal year. By far and away the highest of all Connecticut towns and cities, the Greenwich total assessment is about 50% higher than that of second-highest Stamford, and only three other Connecticut towns (Norwalk, Fairfield and Westport) have total assessments above $10 billion. This disparity becomes even more pronounced when examined on a *per capita* basis; Greenwich has about $525,000 assessed value per resident. By comparison Westport, the town with the next highest ratio, is only about half as high.
Lowest Mill Rate

Largely attributable to its sizeable tax base, the Greenwich mill rate (11.202 this year) is the lowest in the state. By comparison, several hamlets in northwest Connecticut have mill rates between 13 and 16, next lowest in Fairfield County is Darien at a 17 rate and the highest in the state is Hartford at a 74 rate.

Appearances are Deceptive

The Town’s current costs and incurred future liabilities have been rising at rates above inflation

- For the ten-year period from 2006 through 2015, the Town’s annual General Fund expenditures have grown from $311 million to $427 million, or over 3.2% compounded per annum. This compares with an average US inflation rate of 1.9% over the same time period.

To fund the increasing costs, the Town has had to steadily increase local property taxes.

- In recent years, the Town’s Grand List has remained essentially unchanged. For the past ten years, it has actually declined slightly from $33.06 billion in 2007 to $32.5 billion in 2016.
- Because the tax base has not grown, the tax mill rates had to be increased. Over the same ten-year period, the mill rate has grown from 7.50 to 11.27, or almost 4.2% annually or over 50% in total.
- Moreover, because the aggregate personal income of Greenwich residents over the similar time period has grown only about 2%, the affordability of these tax increases has become a growing real burden.

Increased property taxes alone, however, have not been sufficient to cover increasing costs.

- The Town has meaningfully expanded its use of debt. Over the ten-year period from the end of 2006 through the end of fiscal 2015, total long- and short-term debt owed by Greenwich has increased from $45 million to $220 million (or over a 17% compounded annual growth rate).
- Over the same period, the amount of unfunded pension and other post-employment benefits (primarily healthcare) have also increased significantly. At a discount rate of 7%, the pension was under-funded at year-end fiscal 2015 by $125 million (fiscal 2016 datum not yet available).

Taken together, the annual incremental debt, and increases in future committed pension expenses and OPEB expenses approximate an estimated $60 million or about 14% of the Town’s operating budget. In other words, Greenwich effectively is running a sizeable deficit budget.
Future Budget Challenges

As we look ahead, however, the crux of our concerns comprise (a) the Town’s limited control on expenses and (b) clear trends that will negatively affect the future earnings of residents and the future value of their property.

Personnel Expenses

Wages, retirement benefits and health care costs comprise about three-quarters’ of the Town’s budget and are difficult to control. :

• Union Contracts

In recent years, Town employee wages have risen at rates more than twice the inflation rate.

  o Nine unions represent 90% of the Town’s 2,715 full-time employees. We assume the compensation is attractive, in part because the turnover among the Town’s unionized employees is well below rates seen in the private sector.

  o When a union contract is up for renewal and the Town and the union cannot agree on renewal terms, a State arbitration panel would decide. The State arbitration panel historically exhibits a strong union bias. The Town is currently in arbitration with the firefighters and teachers unions.

• Defined Benefit Pensions

The Town’s safety employees – firefighters and police – have defined benefit pension plans. At year-end fiscal 2015, the pension plans were only 76% funded, and as mentioned earlier the under-funded portion was $125 million.

Likely the under-funding is very much understated. The Town this fiscal year reduced the discount rate the pension liability (to 6.75%) and also reduced the assumed investment return on pension assets (also to 6.75%). Although both rates are consistent with governmental accounting standards, these standards are not consistent with the standards followed by the private sector. Moreover, the two rates need not equal each other.

  o The discount rate on the pension liability used by the Town understates the size of the liability. Because (a) the discount rate should reflect its riskiness and (b) the pension liability is relatively certain, most academics and corporate sponsors favor use of a lower discount rate, such as the yield the high quality long-term corporate bonds (recently, 3.5% on 20-year AA-rated corporate debt).

  o The assumed investment return on pension assets is possibly too high. In today’s markets, with risk-free yields (long-term Treasuries) less than 2.5%, to expect a 6.75% return, on a blended portfolio of stocks and bonds, could be seen as generous. As with a too high liability discount rate, a too high assumed investment return understates the pension underfunding.
More fundamentally, there is a philosophical issue with defined benefit pensions: why should the Town assume the pension investment risk for the (increasingly-longer) lifetimes of employees and their spouses? The private sector has rejected the defined benefit pension model; why has the public sector not done so? Admittedly, this issue transcends Greenwich.

• HealthCare

Budgeted healthcare cost of current employees is both large ($53 million is budgeted for this fiscal year) and growing at high rates (the current budget expectations are as high as 19%). Under the rubric of other post-employment benefits (“OPEB”), the cost of funding heath care costs of retirees is budgeted at (only) $6 million this year and is expected to grow at higher rates as the Town’s workforce ages. Unlike pensions, future OPEB expenses have neither (a) partially offsetting assets nor (b) an estimate of their present value.

Debt Service Costs

No longer following a modified ‘pay-as-you-go’ approach to funding capital projects, the Town has increased its use of debt significantly. Although the amount of the outstanding debt is not a concern (now), we are concerned about the rate of growth of the debt and the Town’s increasing comfort in using it.

Revenues

In addition to concerns about rising future costs, we are equally concerned about several trends that will reduce the ability of the Town to tax its way out of budget problems:

• Weak Economy

Although the weak economy, in the US overall and more so in Connecticut, has affected Greenwich generally, it has been the decline of the financial services industry since 2008 that has specifically and significantly harmed the earnings of Town residents and the values of their housing. Further, few expect the economic growth rates seen in the past to return in the foreseeable future.

• State Budget Woes

Facing a sustained period of ever-increasing billion dollar-plus annual budget deficits, the State of Connecticut ranks among the bottom five states in terms of economic performance.

Greenwich has been a critical source of financial support for the State; through payment of state income taxes and property transfer taxes, residents of Greenwich contribute approximately 14% of the state’s $19 billion of revenues.
Precisely because Greenwich is “where the money is”, the State will likely seek to capture more dollars from Greenwich:

- First, the State might reduce or eliminate what remaining grants it provides the Town. This may include not just the annual general school grant (reduced to $1.5 million this year) but also budgeted receipt of State funding up to 80% approximately of the $30 million-plus cost the New Lebanon School.

- Second, there has been discussion in Hartford about raising taxes through higher tax rates and new forms of taxation (e.g., State property tax) that would clearly affect Greenwich residents.

Moreover, we are also concerned that the State’s budget crisis will also discourage future investment, and thereby future economic growth, here.

- **Demographic Shifts**

  Additionally, Greenwich suffers from recent trends among segments of the population:

  - In part because of the recent increases in the State’s tax rates, the former tax advantage for high-income earners to choose Connecticut over New York has been substantially eroded.

  - In addition to the long-seen preference of an aging population to seek warmer and tax-friendly climes, more recently it appears that the younger population (a portion of which is not so young) is increasingly seeking urban, versus suburban, locales.

**What to Do**

The Town will need to consider the following actions:

1. **Limit Mill Rate Increases**

   We must resist any increases to the mill rate above inflation rate. This is possible. For example, this past year, Darien, Fairfield and Wilton have each actually reduced their non-school operating budgets. Why not Greenwich?

2. **Limit and/or Reduce Headcount**

   Because public employees are expensive and the Town has little control on how much more expensive they will become in the future, it is critical to control headcount. We have not done this well in the past - since 1970 the population of Greenwich has grown 5% and the number of Town employees has grown 50%. We must do better in the future.
3. **Reduce Borrowing**

   A good reason to borrow is to match a liability with an asset; this is especially true when the borrowing need in any one-year is exceptional. Greenwich, however, has a portfolio of capital projects and the total capital expenditure in any one-year does not differ dramatically from the next. Therefore, the Town’s borrowing is tantamount merely to deferring the payment for the project. This should be discouraged. Ideally, the Town should return to pay-as-you-go funding of capital projects.

4. **Reduce the Number and Scope of Capital Projects**

   The Town continues to tax or borrow funds for capital projects that are not completed within the year as stated in the Charter. Currently, with the new projects added last fiscal year, there are $189 million of open capital projects that need to be completed. Further, many of the new projects have dramatically increased the footprint that likely will require additional personnel to run and maintain the larger facilities.

5. **Reduce Town Services**

   Ultimately, the Town may need to either transfer or curtail certain services.

   - For example, the Town has long subsidized the operations of The Nathaniel Witherell, a facility that has evolved from a skilled nursing home into more of a rehabilitation facility. The budgeted payment this fiscal year is $6.5 million, of which $5.3 million is characterized as a “one-time” payment. Is this a critical mission for the Town? Is the Town better suited than, say, Greenwich Hospital to run the facility?

**Conclusion**

Let’s not be that proverbial frog sitting in the increasingly hot water; we need to jump, now!