

FPC Meeting 1/22/2019

Present: Melissa Malone (TA); Anna Nolan (NPS Supt)(departed 5:22); Lisa T. (SC chair); Julie McDonough (SC member); Amy Mistrot (BOS chair, FPC Chair); Jonathan Freedman (BOS member, FPC Vice Chair); Patrick Hayes (FinCom Chair, arrived 5:30)

Others Present: Cinder Mc____ (Hilltop Securities); Eileen(?) Jeffers (Hilltop Securities); Bill Chenard, John Townsend, Peter Grey, Rick Jennett, Sue Salamoff, Mike Hickey, Frank Foss, Karen Adelman, Cathi Collins

Meeting was called to order at 5:10.

PUBLIC SPEAK

None.

APPROVE MEETING MINUTES

At 5:12, draft minutes for the 12/12/2018 meeting were approved 6-0-0 on a motion by JF, seconded by AN.

At 5:12, draft minutes for the 1/03/2019 meeting were approved 6-0-0 on a motion by JF, seconded by AN.

REVIEW OF TOWN OF NATICK FINANCIAL MANAGEMENT PRINCIPLES, STABILIZATION FUND BALANCES, AND IMPACT OF USING STABILIZATION FUNDS FOR OPERATIONAL SUPPORT

Ms. Mistrot asked Cinder & Eileen to discuss the Town's recent rating reports recently received from S&P and Fitch, and the potential impacts of using the Town's reserves for operational expenses. The following points were discussed by the representatives of the Town's financial advisors:

- A strong credit profile is needed to receive two AAA credit ratings.
- If split ratings had been received, the markets would likely defer to the lower rating, resulting in higher interest rates and increased interest costs.
- Drawing on reserves could jeopardize the Town's credit rating; free cash is considered part of the Town's reserves.
- It is important to protect the S&P rating, as S&P is seen as more analytical. Only a few communities are rated by Fitch, and there has been a large migration over the years from Fitch to S&P.
- The Town's institutional framework is a material part of the rating; all components, including management, budgetary performance, debt profile (including pension and OPEB), reflect strong management in the eyes of the rating agencies.
- Drawing on reserves would create uncertainty, and could result in a lower credit rating. A significant reason for this is the lack of assurances relating to the Town's ability to regenerate the reserves, particularly free cash.
- Hilltop's recommendation is to use anything but reserves to balance the budget; excess reserves should instead be used for capital purposes as opposed to operational purposes.
- Hilltop further recommends that the Town continue to wean itself off its reliance on the use of free cash for operational needs; one possible action step is to develop a policy relating to surplus funds to target for free cash.

- Hilltop also recommends a multi-year approach for budgetary decision making, that is, the Town should figure out what it will do next year before making decisions for the current year, so as to have a clearer path for how to achieve the long term strategic objectives.
- In response to a question about language in the Fitch report that suggested Natick's reserves are higher than necessary to maintain a AAA rating, Cinder noted that the amount of reserves was a factor in allowing Fitch to feel comfortable with the large amount of debt issuance.
- Both rating agencies took Natick's historical utilization of free cash into account in their analysis, but were not necessarily comfortable with it; Cinder noted that many other communities, including Brockton & Somerville, were in the process of weaning themselves off the use of free cash for operational purposes, as that was not considered a sustainable funding model.
- A question was also raised about the alternative of simply not appropriating free cash to stabilization funds, thereby leaving it available for allocation to operational purposes without drawing on stabilization funds. Cinder informed the committee that the practice would still be viewed as in response to a structural imbalance.
- A question was raised regarding the use of the "rainy day" stabilization fund, and Cinder again noted that the use of a stabilization fund for ongoing operational purposes could be viewed negatively; however, that fund could be used in the context of a sustained global downturn because that is the stated intent of that stabilization fund.
- With respect to pension funding it was noted that Natick is currently targeting to be fully funded by 2030 although the state allows communities until 2040 to achieve fully funded status; a revised funding schedule would free up revenue to be directed to other operational purposes. In response, Cinder noted that rating agencies give credit to communities with aggressive funding schedules, and relaxing the funding schedule would make the rating agencies ask why, thus highlighting the town's structural funding issue. Relaxing the pension funding schedule would also add to the overall costs as well as impacting the Town's OPEB funding strategy. These factors were taken into account by both rating agencies in their recent assessments.
- Cinder noted that Fitch in particular was concerned with the amount of debt that the Town was taking on; the Town's demonstration that the large amount was resulting in a significant savings to the Town; this factor, coupled with the Town's ample reserve position offset Fitch's concerns relating to debt and OPEB requirements.
- Mr. Chenard commented on Cinder's earlier comment about communities weaning themselves off the use of free cash for operations, and he noted that the Town has been working to reduce its reliance on free cash; increasing local receipts projections is one part of the plan, and a second is to reduce reliance on free cash for operations. In his opinion, an appropriate target for free cash use for operations should be \$1.5M-\$2.0M. Earlier, Ms. Malone had noted that Natick's historical average was approximately \$2.3M.

Ms. Mistrot asked if there were any members of the public that had any comments:

- Mr. Foss noted that stabilization funds could be used for anything as directed by Town Meeting. Mr. Foss also cautioned that language should be used consistently and carefully, so as to avoid misunderstandings.
- Ms. Collins asked why the Town always reserved 0.5% of free cash, and Mr. Chenard noted that this was part of the Town's Financial Management Principles, was based on DOR guidance, and was the starting point for the following fiscal year's free cash. There followed a brief discussion of the Town's Financial Management Principles during which the following points were noted:

- Nominal funds were appropriated to the General & Rainy Day Stabilization Funds at the 2018 FATM to demonstrate a good faith effort to the rating agencies in light of the amount of debt that was being taken on in December.
- In Cinder's opinion, Natick's AAA credit rating was not in jeopardy but was at risk due to the large amount of debt being taken on; both Fitch and S&P became comfortable with Natick's financial strength throughout the course of their analysis; since the bulk of the new debt was related to Kennedy Middle School, the inclusion of the incremental debt related to the West Natick Fire Station was not a material factor in this analysis.
- Ms. Collins asked why it was sufficient to fall back on the Financial Management Principles when Town Meeting controlled the money? Mr. Hayes expressed that Town Meeting is not precluded from taking actions contrary to the Administration's recommendations that are based on the Financial Management Principles, and Mr. Freedman further expressed that the Financial Management Principles were often the starting point of a discussion and formed a basis for decision making and evaluation. In Cinder's opinion, adherence to the Financial Management Principles is critical, and it may be better to not have them at all than to not adhere to them.

ADJOURN

At 6:30, the committee voted 5-0-0 to adjourn on a motion by Mr. Hayes that was seconded by JF.