



CITY OF CAMBRIDGE • EXECUTIVE DEPARTMENT

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September 26, 2011

To The Honorable, the City Council:

The establishment of the FY12 property tax rate by the Board of Assessors, subject to the approval of the Massachusetts Department of Revenue, is the final step in the annual fiscal process that begins in the spring of each year with the submission of the annual budget to the City Council. With this memo, I am transmitting to you my recommendations for the required votes necessary to minimize taxes on residential properties. In addition, you will find analyses of the FY12 property tax levy, property values and other supporting information.

OVERVIEW

I am pleased to inform you that the actual FY12 property tax levy of \$299,090,641 reflects a \$15,128,942 or 5.33% increase from FY11, which is lower than the estimated increase projected in May 2011 and lower than the property tax levy percentage increase for FY11. The FY12 Budget adopted by the City Council in May 2011 projected a property tax levy increase of \$18.4 million, or 6.47%, to \$302,322,025 in order to fund operating and capital expenditures. The FY12 operating budget has increased by 1.75%.

In May, I informed the City Council that the actual tax levy increase was likely to change. This was based on potential changes in State Aid, which would not be known until the State finalized its FY12 budget, and the possible use of additional non-property tax revenues, which would become available based on FY11 actual collections.

This assumption again proved correct. The use of additional non-property tax revenue and other adjustments have allowed an overall reduction of \$3,231,384 from the original projected property tax levy. This is possible due to increased non-property tax revenues, which include \$200,000 from hotel/motel excise, \$79,414 from motor vehicle excise, \$2,300,000 from Free Cash, \$200,000 in Parking Fund revenues, a \$1,000,000 increase in Health Claims Trust, \$150,000 in Debt Stabilization and \$250,000 from increases to permit and other revenues. Also, included is \$109,359 in overlay adjustments. A portion of these increases, totaling \$1,057,389, are required to offset a net decrease in Cherry Sheet revenues, prior year overlay deficits and reductions in various revenues based on actual FY11 collections and revised estimates.

| Tax Levy Changes | Amount |
|--------------------------|----------------------|
| Additional Assessments | +\$1,057,389 |
| Non-Property Tax Revenue | -\$4,179,414 |
| Overlay Adjustment | -\$109,359 |
| Net Decrease | - \$3,231,384 |

This resulted in a final property tax levy for FY12 of \$299,090,641, an increase of 5.33%. With approval of these recommendations, the seven-year average increase in the property tax levy will be 4.3%. In addition, in the City Council approved a 0% increase in the FY12 water and sewer rate this past March.

This recommendation includes the use of \$13.3 million in reserve accounts to lower the property tax levy; \$2 million from overlay surplus; and \$11.3 million in Free Cash. It should be noted that the certified Free Cash amount of \$102.2 million is the highest amount in the City’s history and represents a \$12.9 million increase from last year. Also, \$5.2 million from the Debt Stabilization Fund and \$0.6 million from the School Debt Stabilization Fund is used to offset increases in debt service costs that would otherwise have been funded from property taxes.

This strategy of using an increased amount of non-property tax revenues and reserves to lower property taxes will not jeopardize our long-term fiscal health. However, if the City used all of its reserves in one year to artificially reduce property taxes it would mean that in the following year the City would be required to either increase taxes significantly, since the reserves would no longer be available, or dramatically reduce expenditures (services). The City’s prudent and planned use of its reserves has been positively recognized by the three major credit rating agencies and is reflected in our AAA credit rating.

Based on a property tax levy of \$299.1 million, the FY12 residential tax rate will be \$8.48 per thousand dollars of value, which is an increase of \$0.32, or 3.9% from FY11. The commercial tax rate will be \$20.76, which is an increase of \$0.86, or 4.3% from FY11. Both increases in the tax rate are less than FY11.

However, approximately 63.9% of residential taxpayers will see a reduction, no increase or an increase of less than \$100 in their FY12 tax bill. In addition, another 22.8% of residential taxpayers will see an increase between \$100-\$250. Therefore, a total of 86.7% of the residential taxpayers will see no increase or an increase of less than \$250. This will be the seventh year in a row that a majority of residential taxpayers will see a reduction, no change or an increase of less than \$100. This accomplishment should not be taken for granted, given the recent tremendous economic turmoil, including significant reductions in State Aid to the City, while maintaining city and school services that citizens have come to expect and, while providing a strong capital improvement program that includes major projects such as the Mayor Russell/West Cambridge Youth and Community Center, Healy Public Safety Facility, Main Public Library, War Memorial Recreation Center and CRLS Renovations.

TABLE I
Change in the Residential Tax Bills*

| Change in Tax Payment | Number of Parcels | Percentage | Cumulative % |
|----------------------------------|--------------------------|-------------------|---------------------|
| Less than \$0 | 1,140 | 5.4 | - |
| > \$0 and less than \$100.00 | 12,327 | 58.5 | 63.9 |
| >\$100.00 less than \$250.00 | 4,800 | 22.8 | 86.7 |
| >\$250.00 and less than \$500.00 | 1,754 | 8.3 | 95.0 |
| Greater than \$500.00 | 1,052 | 5.0 | 100% |
| Totals | 21,073 | 100% | |

* Based on Single, Two, Three Family and Condominiums and assumes the Residential Exemption for each parcel in both years.

MEDIAN TAX BILLS

The analysis below explains in further detail how the City determines property values and property tax rates for FY12. There are three major factors which determine a property tax bill. These factors are: the Budget, Commercial-Residential Property Tax Classification and Property Values. As discussed below, all three factors contributed to lower tax bills for many homeowners.

The Budget: If the City Council adopts the proposed recommendations, there will be 5.3% increase in the property tax levy required to balance the FY12 Budget. The FY12 property tax levy increase reflects a \$1.3 million reduction in the two major State Aid categories (Unrestricted General Government Aid (UGGA) and Chapter 70 School Aid). Since FY09, the City has seen a reduction of \$10.5 million, or 29% in State Aid from these two categories (budget to budget). In addition, the FY12 Adopted Budget reflects a 1.75% increase which supports the City Council Goal of “evaluating expenditures with a view of maintaining a strong fiscal position and awareness of the impact on taxpayers while providing a high quality of City services.”

Commercial-Residential Property Tax Classification: Tax classification allows municipalities to tax commercial taxpayers at a higher rate than residential taxpayers. In FY12, commercial property owners will pay 65.4% of the property tax levy, the same share as in FY11. Consequently, residential property owners’ share of the FY12 tax levy is 34.6%, also the same as in FY11.

Property Values: Every January 1st, the City of Cambridge must meet Department of Revenue requirements to certify that property values represent full and fair market value. Based on market activity in calendar year 2010, which is the basis of the FY12 property assessment, total residential property values have moderated (approximately 1.3% increase overall). Total commercial property values have also increased by 0.97%. The modest increase in total values reflects the difficult real estate market but has been mitigated by continued new construction in both residential and commercial classes, as well as, the continued desirability of the Cambridge market. These factors, coupled with the City’s improved ability to analyze and incorporate adjustments to residential values using the mass appraisal model, have allowed the City to make changes to various assessment districts.

It should be noted that the City has successfully completed the Department of Revenue’s (DOR) interim year certification process of the City’s real and personal property values, system and methodologies.

The following chart shows the change in the median tax bills by property class. It is important to note that while the overall total residential assessed value increased in FY12, assessed values of existing homes remained relatively stable. The median value is the mid-point value, which has an equal number of values below and above it.

TABLE II
Change in the Median Value and Tax Bill by Property Class*

| | FY11 Value | FY11 Tax Bill | FY12 Value | FY12 Tax Bill | Dollar Change | Percent Change |
|---------------|-------------------|----------------------|-------------------|----------------------|----------------------|-----------------------|
| Single Family | \$670,450 | \$3,870 | \$686,200 | \$4,139 | \$269 | 6.95% |
| Condominium | \$364,100 | \$1,370 | \$366,700 | \$1,430 | \$60 | 4.38% |
| Two Family | \$638,550 | \$3,609 | \$644,600 | \$3,786 | \$177 | 4.90% |
| Three Family | \$721,500 | \$4,286 | \$728,900 | \$4,501 | \$215 | 5.02% |

* Includes Residential Exemption

CITY-WIDE ASSESSED VALUES

FY12 values are based on market activity that occurred during calendar year 2010, during which the overall valuation of the City’s residential property increased by a modest 1.3% and the overall valuation of commercial property increased by 0.97%. This reflects a leveling of commercial rental rates and a slight decrease in commercial vacancies. This has had a moderate impact on existing commercial property values. The major components, which offset any decreases in commercial value, are the construction of life science buildings and the personal property associated with these developments.

For FY12, the total assessed value of taxable property in the City of Cambridge equals \$24,446,955,389, a 1.18% increase over FY11 values. The actual FY12 total assessed value is better than the projections presented to the rating agencies in January 2011.

For several years prior to FY06, escalating residential values outpaced increases in commercial values, resulting in a shift of the tax burden from commercial to residential property owners. However, in FY06, this trend reversed. In FY12 the market for both commercial and residential properties increased slightly, not unlike most of the Greater Boston area, resulting in the continuation of a tax distribution similar to FY11 between commercial taxpayers and residential taxpayers.

The table below breaks out new construction values and tax base levy growth due to new construction by property type. This new construction growth, coupled with moderate budget increases, has allowed the City to maintain the shift in taxes and increase the City’s excess levy capacity.

TABLE III
New Construction Breakdown in FY12

| Property Class | New Value | FY12 Tax Base Levy Growth (New Growth) |
|-------------------------|----------------------|---|
| Commercial Property | \$179,363,961 | \$3,515,946 |
| Personal Property | \$202,553,905 | \$4,022,368 |
| Residential Property | \$157,245,600 | \$1,267,799 |
| Total New Growth | \$539,163,466 | \$8,806,113 |

TABLE IV
Assessed Values (in millions)

| | FY08 | FY09 | FY10 | FY11 | FY12 |
|-----------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Commercial Property | \$8,378 | \$ 8,457 | \$ 8,467 | \$8,379 | \$8,478 |
| Personal Property | \$736 | \$768 | \$911 | \$959 | \$951 |
| Residential Property | \$14,427 | \$14,651 | \$14,894 | \$14,824 | \$15,018 |
| Total Assessed Value | \$23,541 | \$23,876 | \$24,272 | \$24,162 | \$24,447 |

For FY12, the City was able to increase its levy limit by approximately \$18.4 million, to \$401.7 million. Approximately \$8.8 million of this increase was due to new construction. State law allows the City to increase its tax levy limit by an amount equal to the total FY12 value of newly constructed or renovated property, multiplied by the FY11 tax rate. The remaining \$9.6 million is the 2.5% increase over the FY11 levy allowed by Proposition 2½, plus a revised new growth value calculation from FY11. The City's excess levy capacity increased by \$3.3 million, or 3.31%, to \$102.6 million in FY12.

TABLE V
Tax Levy/Tax Levy Limit/Excess Levy Capacity
(in thousands)

| | Actual FY07 | Actual FY08 | Actual FY09 | Actual FY10 | Actual FY11 | Estimated FY12 |
|---|------------------------|------------------------|------------------------|------------------------|------------------------|---------------------------|
| Levy Limit | \$305,445 | \$330,587 | \$347,606 | \$367,222 | \$383,312 | \$401,733 |
| Actual Levy | \$231,787 | \$242,334 | \$254,946 | \$268,663 | \$283,962 | \$299,091 |
| % Actual Levy Increase over Prior Year | 3.96% | 4.55% | 5.20% | 5.38% | 5.69% | 5.33% |
| Excess Levy Capacity | \$73,658 | \$88,253 | \$92,660 | \$98,559 | \$99,350 | \$102,642 |
| % Actual Excess Levy Capacity Increase Over Prior Year | 13.2% | 19.8% | 5.0% | 6.4% | 0.8% | 3.3% |

In addition to providing greater flexibility under Proposition 2½, tax payments from newly constructed properties also work to mitigate increases on existing properties.

For a detailed listing of assessment changes by district, please see Attachment 1.

FY12 VALUATION PROCESS

Each year, the Board of Assessors conducts a reappraisal of all property within the City of Cambridge using the residential and commercial valuation models first introduced in FY05. The City chose FY05 to coincide with the Commonwealth of Massachusetts Department of Revenue (DOR) triennial mass appraisal review and certification process, to ensure a complete and thorough review of the new valuation models. Since that time, the model has been refined each year to reflect market conditions which have impacted assessed values. In FY11, the DOR conducted its triennial review and certification and once again it certified the City's valuation models after a vigorous review.

The FY12 valuation model is based upon sales of property that occurred during calendar year 2010, to establish the market value of all property as of January 1, 2011. For FY12, the number of assessing districts has remained unchanged. In prior years, some consolidation of districts took place to create a larger sales sample size.

The ultimate test for any mass appraisal model is the comparison between actual sales not part of the model building process and the predicted value from the model. Comparing the FY11 model to calendar year 2010 sales data, the model showed the following results:

TABLE VI
Residential Sales Price/Assessment Comparison

| Property Type | Sale Count | Median Sale Price | Median Assessment |
|----------------------|-------------------|--------------------------|--------------------------|
| Single Family | 115 | \$859,000 | \$689,700 |
| Two Family | 34 | \$717,478 | \$678,100 |
| Three Family | 14 | \$712,850 | \$645,600 |
| Condominiums | 671 | \$416,000 | \$378,400 |

The assessment ratios were between 80%-95% of calendar year 2010 sales, which means that the assessed estimate of values for FY11 were below actual market sales.

Although the calendar year 2010 sales demonstrated that the FY11 model was an accurate representation using overall property class statistics, the individual neighborhoods were not as consistent and required review. As a result, FY12 sales data from the calendar year 2010 real estate market has been utilized, along with what was learned from the prior year abatement activity, to establish the FY12 assessed values as of January 1, 2011. Using technologies, such as the Geographical Information System (GIS), allowed for a more in-depth review of data. Using GIS, the Board of Assessors was able to visually display the market activity and thereby validate the assessing districts using this information. For FY12, the number of assessing districts remained at 17, which allowed for adequate sample sizes for the neighborhoods.

Modifications to the model were made, including updating grade and size adjustments, and recalibrating the building condition adjustments. In addition, approximately 3,800 inspections were completed along with a detailed field review of property. These inspections serve to ensure consistency within neighborhoods and across the City. The analysis for determining property values depends on several factors: the trends of the real estate market in the areas of sales; property improvements; changes in the economics of real estate finance; and the high demand for real estate in the City. To arrive at full and fair cash values for approximately 24,088 parcels, the Assessing Department uses a state-of-the-art Computer Assisted Mass Appraisal system (CAMA). Market adjusted cost approach models, extracted from residential sales for calendar year 2010, were refined to best reflect the equity of comparable properties as demonstrated in the various neighborhoods. Sales of 618 houses and condominium units were analyzed to develop these valuation models by property type (one-family, two-family, three-family, and condominium units). The FY12 real property assessments reflect the analysis of the real estate market for the calendar year 2010.

COMMUNITY PRESERVATION ACT SURCHARGE

In November 2001, Cambridge voters approved adoption of the Community Preservation Act (CPA), a State law that allows the City to receive matching funds from the State for money raised locally in support of affordable housing, historic preservation and protection of open space. The local portion of CPA funding is raised through a 3% surcharge on taxes. To date, the City has appropriated/reserved a total of \$111.3 million in CPA funds. The City has received \$42.6 million in state matching funds through FY11 and expects to receive an additional \$1.9 million in October 2011. It should be noted that this is the fourth year that the City will not receive a 100% state match, which is a result of additional communities participating in CPA and a reduction in the CPA Trust Fund collections through the Registry of Deeds. The FY12 state match to be received by the City is estimated at 28%.

The CPA surcharge has an essentially neutral impact on tax bills because funding of affordable housing and historic preservation initiatives has been shifted from the tax levy to the surcharge. The City continues to allocate a similar amount of local funds to these initiatives. However, the State match has enabled the City to leverage the amount of funding appropriated for these initiatives. To date, Cambridge has received more CPA matching funds from the Commonwealth than any other participating community. Consequently, Cambridge residents will benefit from important housing, historic preservation and open space initiatives throughout the City for years to come.

TABLE VII
Community Preservation Act Surcharge

| | FY11 Median CPA Surcharge Amount | FY12 Median CPA Surcharge Amount | FY12 Median Tax | FY12 Median Tax & CPA Surcharge Amount |
|---------------|---|---|----------------------------|---|
| Single Family | \$92 | \$99 | \$4,139 | \$4,238 |
| Condominium | \$17 | \$17 | \$1,430 | \$1,447 |
| Two Family | \$84 | \$88 | \$3,786 | \$3,874 |
| Three Family | \$104 | \$110 | \$4,501 | \$4,611 |

EXPANDED ONLINE BILL PAYMENT OPPORTUNITIES

As part of our ongoing effort to provide additional opportunities to taxpayers to make payments electronically, I am pleased to announce that effective October 1, 2011, taxpayers will be able to pay their real estate and personal property tax bills using a credit card, debit card or electronic check (ACH), subject to a convenience fee. This new feature will be combined with current opportunities for taxpayers to pay their motor vehicle excise and water and sewer bills online.

RECOMMENDATIONS

1. That the City Council authorize the use of \$11,300,000 in Free Cash to reduce the FY12 tax rate.
2. That the City Council vote to authorize \$2,000,000 in overlay surplus/reserves to be used for reducing the FY12 tax levy.
3. That the City Council vote to authorize \$5,150,000 from the Debt Stabilization Fund to be used as a revenue source to the General Fund Budget, \$5.0 million of which was included in the FY12 Adopted Budget.
4. That the City Council vote to authorize \$632,470 from the School Debt Stabilization Fund to be used as a revenue source to the General Fund Budget, which was included in the FY12 Adopted Budget.
5. That the City Council classify property within the City of Cambridge into the five classes allowed for the purpose of allocating the property tax. It is further recommended that the City Council adopt a minimum residential factor of 56.2602%.
6. That the City Council approve the maximum residential exemption factor of 30% for owner occupied homes, which should result in a residential tax rate of \$8.48 and commercial tax rate of \$20.76 upon final approval by the Massachusetts Department of Revenue.
7. That the City Council vote to double the normal value of the statutory exemptions.
8. That the City Council vote to increase the FY12 exemption allowed under Massachusetts General Laws (MGL) Chapter 59, Section 5, Clause 17D from \$280.00 to \$285.00.
9. That the City Council vote to increase the FY12 asset limits allowed under Massachusetts General Laws (MGL) Chapter 59, Section 5, Clause 17E from \$55,775 to \$56,695.
10. That the City Council vote to increase the FY12 income and assets limits. Income limits of \$23,061 to \$23,442 for those who are single and \$34,592 to \$35,163 for those who are married, asset limits of \$46,122 to \$46,883 for those who are single and \$63,418 to \$64,464 for those who are married, as allowed under MGL, Chapter 59, Section 5, Clause 41D.
11. That the City Council vote the income limit for deferral of real estate taxes by elderly persons (at least 65 years old) as determined by the Commissioner of Revenue for the purposes of MGL, Chapter 62, Section 6, subsection (k), for a single person who is not head of household (\$51,000) and for a married couple (\$77,000), as allowed under MGL Chapter 59, Section 5, Clause 41A. The dollar amounts listed may be indexed by Massachusetts DOR for FY12. The reduction of the interest rate to 4% for deferred taxes, which was approved by the City Council previously, will continue.
12. That the City Council vote to accept Clause 56 of G.L. c. 59, Section 5, which allows members of the Massachusetts National Guard or military reservists who are on active duty to obtain a reduction of all or part of their real and personal property taxes for any fiscal year they are serving in a foreign country.

ISSUES/REQUIRED VOTES

As the City Council is aware, by the time the classification vote is taken in the fall of each year, the options for the City are fairly limited. Failure to approve the recommended classification, residential exemption and the doubling of statutory exemptions would result in significantly higher taxes for residential property owners. After the classification vote is taken, the establishment of the tax rate is a fairly simple mathematical calculation: the tax levy required to support the City budget divided by the total assessed valuation equals the tax rate for FY12.

The following is a summary of the votes required by the City Council.

- **Authorize \$11,300,000 in Free Cash to Reduce the FY12 Tax Levy.** For the fiscal year that ended June 30, 2011, the City of Cambridge has a certified Free Cash balance of \$102,239,071, an increase of approximately \$12.9 million from the previous year. This balance represents the highest amount in the City's history.

The \$11,300,000 in the Free Cash authorization is requested at this time from the City's Free Cash balance in order to reduce the property tax levy increase. This amount is \$0.1 million lower than the \$11.4 million used last year. Generally, \$9.0 million has been used for several years but, as like last year, a higher amount is being used to cover the cost of one-time non-recurring items in FY12 such as overlay deficits for FY05, FY06 and FY07.

The Department of Revenue (DOR) does not allow formal authorizations of Free Cash by the City Council until the DOR has certified a Free Cash balance at the conclusion of the fiscal year.

- **Transfer of Excess Overlay Balances.** The City is authorized to increase each tax levy by up to five percent as an "overlay" to provide for tax abatements. If abatements are granted in excess of the applicable overlay, the excess is required to be added to the next tax levy or transfers may be made from surplus balances from prior fiscal years.

Overall, the City has approximately \$12.4 million in overlay balances as of June 30, 2011. However, there are cases pending at the Appellate Tax Board for which the City must have sufficient balances to cover abatements if it loses these cases. Based upon the overall size of the overlay surplus, I am recommending that the City use \$2 million of this surplus to decrease the tax levy. Based on the level of the overall current surplus, the City would continue to use \$2 million for this purpose in future years. This conservative approach will allow the City to maintain a sufficient overlay reserve while reducing older overlay balances to help lower the tax levy.

- **Authorize \$5,150,000 in Debt Stabilization Funds.** In recognition of increases in debt service costs related to major capital projects, the City established a Debt Stabilization Fund and has made contributions to it over the past several years. The balance in this Stabilization Fund is approximately \$5,180,000 as of June 30, 2011. An additional \$150,000 is being coupled with the \$5.0 million used in the Adopted FY12 Budget to offset debt service costs.
- **Authorize \$632,470 in School Debt Stabilization Funds.** In recognition of increases in debt service costs related to major capital projects, the City established a School Debt Stabilization Fund and has made contributions to it over the past several years. The balance in this Stabilization Fund is approximately \$6.1 million as of June 30, 2011. The Adopted FY12 Budget included \$632,470 from this source to fund increases in debt service costs for the War Memorial.

- **Classify Property and Establish Minimum Residential Factor.** Since 1984, the City Council has voted annually to follow State law allowing the classification of property according to use (residential or commercial) and to allocate the legal maximum portion of the tax levy to the commercial class. State law allows the residential portion of the tax levy to be as low as 50% of what it would be if there were single tax rates. However, there are two exceptions to the 50% minimum:

The residential percent of the levy cannot drop to less than its lowest level since classification was initially voted by the City Council (34.5615% in 1985 in Cambridge); and the 50% level does not cause the commercial class to bear a portion of the levy greater than 175% of what it would be if both classes were taxed equally; and

The City Council sets the levy distribution each year by voting for a Minimum Residential Factor. The result of voting for the Minimum Residential Factor of 56.2602%. this year will be a residential property share of the total tax levy of 34.5615%. Commercial property will pay 65.4385% of the levy, which brings the commercial portion of the levy to 170% of what would be with a single tax rate.

- **Residential Exemptions.** Home Rule Legislation allowing the City of Cambridge to increase the residential exemption from 20% to 30% was filed by a unanimous vote of the City Council and signed into law in September 2003. This change enables the City to grant owner occupants of residential properties a deduction of up to 30% of the average residential parcel value before the tax rate is applied. I am recommending that the City Council accept the Maximum Residential Exemption of 30%. This amount is deducted from the assessed value of each owner occupied property prior to applying the tax rate. The residential exemption serves to reduce the effective tax rate on lower valued properties while raising it on higher valued properties. Since the same amount is deducted from every value, its impact is greatest on the lower valued properties. The residential exemption is paid for by raising the residential tax rate sufficiently to cover the number of taxpayers claiming the residential exemption.

For FY12, there are approximately 14,200 residential exemptions on the Assessing Department files. Overall, approximately 91% of the owner occupied homes benefit from the 30% residential exemption.

If Cambridge did not adopt a residential exemption, the residential tax rate would be \$6.88 instead of \$8.48. The higher tax rate results in a "break-even" value over which the higher valued residential properties are assessed higher taxes than would be the case if there were no residential exemption. In FY12, the break-even assessed value is approximately \$1,050,000.

30% Residential Exemption

| | <u>FY2010</u> | <u>FY2011</u> | <u>FY2012</u> |
|----------------|----------------------|----------------------|----------------------|
| Value Exempted | \$198,423 | \$196,226 | \$198,085 |
| Tax Savings | \$1,531.83 | \$1,601.20 | \$1,679.76 |

- **Double Statutory Exemptions/Exemption Increases.** State legislation requires cities and towns to grant a variety of tax exemptions to elderly taxpayers, blind taxpayers, veterans and surviving spouses who qualify by virtue of residency, income and assets. There are also two pieces of legislation which authorize cities and towns to increase the amounts of these exemptions.

The first allows cities and towns to double the statutory amount of exemption for taxpayers whose tax bills have increased over the prior year's bill. The City Council must vote annually for this increase. I am recommending that the Council do this for FY12, as it has since FY87.

The second allows cities and towns under Massachusetts General Laws (MGL) Chapter 59, Section 5, Clause 17D to increase the amount of the exemption for a senior citizen 70 or older, surviving spouse, or minor with a deceased parent by the increase in the cost-of-living as measured by the Consumer Price Index (CPI).

It should be noted that the cost of living adjustment (COLA), as determined by the DOR, is measured by the increase in the United States Department of Labor, Bureau of Labor Statistics Consumer Price Index for Urban Consumers (CPI-U) during the previous calendar year. The percentage increase for this period was 1.65%. Therefore, the FY12 exemption amounts, income limits or asset limits under these local options will increase over the FY11 amounts and limits.

Therefore, FY12 exemption will be \$285. In addition, under Clause 17E, cities and towns can increase the asset amounts by the CPI percentage for this same group. The FY12 amounts increases to \$56,695 from \$55,775.

MGL Chapter 59, Section 5, Clause 41D allows cities and towns to increase the income and assets limits for elderly persons (age 65 or older) by the CPI percentage. For FY12 the income limits will be \$23,442 for those who are single, \$35,163 for those who are married, and the asset limits will be \$46,883 for those who are single and \$64,464 for those who are married.

- **Income Limit for Tax Deferral.** Another form of tax relief available to property owners under state law is found in MGL Chapter 59, Section 3, Clause 41A. This statute allows taxpayers who are at least 65 years old to defer tax payment until they are deceased or the property is transferred. The statutory income limit for this deferral is \$40,000. However, a change in the statute, allows the City Council to vote to increase the income limit for deferral of real estate taxes by elderly persons (at least 65 years old) from \$40,000 to the amount determined by the Commissioner of Revenue for the purposes of subsection (k) of section 6 of chapter 62, (currently \$51,000 for a single person and \$77,000 for a married couple, which may be indexed by Massachusetts DOR for FY12), as allowed under MGL Chapter 59, Section 5, Clause 41A. I am recommending that the City Council vote to adopt the deferral amount. The City Council has previously voted to reduce the interest percentage to 4% on deferred property tax balances.
- **Exemption for National Guard and Reservists.** Adoption of Clause 56 of G.L. c. 59, § 5 will allow members of the Massachusetts National Guard or military reservists who are on active duty to obtain a reduction of all or part of their real and personal property taxes for any fiscal year they are serving in a foreign country. The Board of Assessors has established eligibility criteria for the exemption and the exemption expires two years from after acceptance unless extended by vote of the legislative body.

CONCLUSION

In May, the City Council adopted a FY12 Budget which accomplished the following: 1) Maintains City and school services that citizens have come to expect, supports the City Council Goals and provides for a strong capital plan, which includes funding to begin the multi-year Elementary School Rebuilding Program in conjunction with the recently adopted Innovation Agenda by the School Committee. In addition, it addresses our unfunded pension liability in a prudent and responsible manner. This Budget continues to provide stability and reinvestment in our community and, given the fiscal challenges facing many cities and towns in the Commonwealth, this is a major achievement; and 2) Achieves the above with a moderate increase in the property tax levy, in spite of a continued reduction in State Aid, which supports the City Council Goal of “evaluating expenditures with a view of maintaining a strong fiscal position and awareness of the impact on taxpayers while providing a high quality of city services.”

Approximately 65% of the revenues that fund the City’s budget are raised through property taxes. Massachusetts communities are limited in how they can raise revenues, resulting in a greater reliance on the property tax, since it is the largest and most stable revenue. The City of Cambridge has been able to achieve a lower property tax rate and lower residential property tax bill than surrounding communities due to its ability to generate diverse non-property tax revenues, foster new construction, control budget growth and plan prudent use of reserves. These qualities benefited the City during good economic times and, equally as important, they have allowed the City to weather the current economic climate more favorably than other communities.

Overall, continued sound financial management and planning have enabled the City Council to limit the growth of residential property taxes in FY12, despite continued reductions in State Aid. In addition, with City Council approval the City will use \$19.1 million of Free Cash, overlay reserve and debt stabilization in FY12 to lessen the amount to be raised from the property tax levy, which translates into a lower property tax burden for the taxpayers of the City.

I believe that lessening the tax burden on our taxpayers is a prudent use of the City’s reserve balances that we have created over the years, while maintaining our fiscal flexibility and continuing to position Cambridge as a favorable place to live and do business.

The FY12 property tax levy of \$299,090,641 reflects a 5.33% increase over FY11, which is a lower increase than last year. With approval of these recommendations, the six-year average increase of the property tax levy will be only 4.3%. In addition, the City has been able to achieve stability in its residential and commercial tax rate increases. The average residential tax rate increase over the last 10 years has been 1.7%.

In addition, approximately 63.9% of residential taxpayers will see a reduction, no increase or an increase of less than \$100 in their FY12 property tax bill. In addition, another 22.8% of residential taxpayers will see an increase between \$100-\$250. Therefore, a total of 86.7% of the residential taxpayers will see no increase or an increase of less than \$250. This will be the seventh year in a row that a majority of residential taxpayers will see either a reduction, no change or an increase of less than \$100. The average annual percentage of residential taxpayers who, over the last seven years, will see either a reduction, no change or an increase of less than \$100, stands at 74%. This accomplishment is remarkable, given current fiscal challenges.

The past fiscal year was another solid year for the finances of the City, with total assessed values and excess levy capacity increasing and actual revenues above projections. While the City used approximately \$12.8 million in Free Cash in FY11, it was not only able to replace this amount but

add \$12.9 million, which based on the economic climate, is a major accomplishment.

These strong financial indicators, combined with a AAA credit rating, provide the City with enormous flexibility to respond to the many needs facing this community and to provide the services that the majority of our residents expect from the City, without sacrificing our fiscal stability and flexibility. The strategic use of Free Cash is not only used to reduce the tax levy, but is also available to fund one-time items. This planned approach has allowed us to maintain our Free Cash balances, which is especially important during these uncertain times.

OUTLOOK

While overall economic conditions have improved, there are ongoing uncertainties that will force us to be cautious in the next fiscal year and beyond. These uncertainties include: the impact of significant federal budget reductions on local and state governments; energy costs and their impact on inflation and the economic recovery, which appears to have slowed down in recent months; the impact of increasing health insurance costs; and the impact of future declines in State Aid to cities and towns.

Despite these challenges, Cambridge has survived relatively well in comparison to other municipalities both locally and nationally, while our City continues to move forward. In fact, the City received very positive feedback in the latest biennial Citizen Opinion Survey (2010).

Fortunately, the City Council and Administration have planned for a time when State Aid and non-property tax revenues would stop increasing. We have been prudent in maintaining a healthy excess property tax levy capacity, saving and building our reserves and prudently managing our budget growth, which has allowed us to maintain our City services.

We will continue to use our five year financial and capital plan, debt and reserve policies and the City Council Goals as a blue print for our long-range planning to maintain stability and predictability in our budgeting and financial planning processes. Our financial projections indicate that we will be able to produce future budgets that will reflect a moderate growth in the property tax levy, which is our primary revenue stream. However, the issues noted above could have a negative impact on our financial projections.

The major priority affecting future budgets will be the multi-year Elementary School Rebuilding Program. Our current five year capital plan has \$55 million budgeted for this purpose, with \$3.0 million approved in FY12 for design services for the first elementary school to be upgraded. Therefore, I may be recommending an appropriation to the Debt Stabilization Fund from Free Cash later in the fiscal year to help mitigate the impact of additional tax supported debt in the future for the Elementary School reconstruction plan. However, this recommendation will be contingent upon the overall fiscal position of the City during the current fiscal year.

In addition, the City is in the process of updating its Other Post Employment Benefits (OPEB) actuarial study. It is likely that the City will need to budget additional OPEB contributions on an annual basis in the future until the City's unfunded pension liability is eliminated in 2029, based on the latest funding schedule. The City has appropriated additional funds in FY12 to allow the unfunded pension liability to be funded by 2029, which is well ahead of the state mandated deadline. It is the City's intention to use the excess appropriations that will result when the pension liability is met to fund the City's OPEB liability.

There are some serious fiscal challenges that will continue to affect the City both in the short and long-term. However, the long-term outlook for Cambridge continues to be very strong as long as we continue to manage our resources wisely. This has been confirmed by our continued AAA bond rating. It should also be noted that Moody's Investors Service recently confirmed their Aaa rating of 12 Massachusetts communities and two regional School Districts. However, following the assignment of a negative outlook to the United States, Moody's assigned a negative outlook to the credit rating for 11 of the 14 municipalities, reflecting regional economic sensitivity to federal jobs and funding. Cambridge was 1 of the 3 municipalities, that did not have a negative outlook assigned, primarily due to our healthy reserve balances available to mitigate possible reductions in funding or disruptions in debt markets.

As we are aware, Cambridge is not insulated from ever-changing economic realities, but we have positioned ourselves well to respond to these challenges in order to preserve the high level of municipal services which residents have come to expect, as well as meet the needs of our infrastructure.

It is my belief that we have again collectively listened to the taxpayers and residents through our actions and have responded effectively.

Very truly yours,

Robert W. Healy
City Manager

Attachment

ATTACHMENT 1

| FY2012 Single Family Assessment Data Median Assessed Values | | | | |
|--|-------|--------------|--------------|--------|
| | Count | FY2011 | FY2012 | Change |
| R1 | 393 | \$ 402,300 | \$ 403,500 | 0.30% |
| R2 | 205 | \$ 414,300 | \$ 417,400 | 0.75% |
| R3 | 229 | \$ 729,700 | \$ 743,100 | 1.84% |
| R4 | 87 | \$ 796,400 | \$ 798,600 | 0.28% |
| R5 | 57 | \$ 1,902,600 | \$ 1,877,300 | -1.33% |
| R6 | 347 | \$ 1,279,200 | \$ 1,325,000 | 3.58% |
| R7 | 647 | \$ 460,200 | \$ 466,100 | 1.28% |
| R8 | 223 | \$ 658,800 | \$ 663,700 | 0.74% |
| R9 | 203 | \$ 1,060,000 | \$ 1,082,600 | 2.13% |
| R10 | 333 | \$ 2,433,700 | \$ 2,448,500 | 0.61% |
| R11 | 164 | \$ 1,109,350 | \$ 1,127,300 | 1.62% |
| R12 | 180 | \$ 532,950 | \$ 538,050 | 0.96% |
| R13 | 233 | \$ 552,100 | \$ 568,200 | 2.92% |
| R14 | 134 | \$ 1,020,900 | \$ 1,050,050 | 2.86% |
| R15 | 33 | \$ 708,300 | \$ 748,300 | 5.65% |
| R16 | 151 | \$ 840,500 | \$ 845,600 | 0.61% |
| R17 | 184 | \$ 634,300 | \$ 632,350 | -0.31% |

| FY2012 Condo Assessment Data Median Assessed Values | | | | |
|--|-------|-------------|-------------|--------|
| | Count | FY2011 | FY2012 | Change |
| R1 | 2513 | \$ 389,200 | \$ 391,400 | 0.57% |
| R2 | 638 | \$ 336,750 | \$ 339,650 | 0.86% |
| R3 | 2018 | \$ 347,400 | \$ 348,950 | 0.45% |
| R4 | 650 | \$ 315,300 | \$ 318,750 | 1.09% |
| R5 | 13 | \$1,233,100 | \$1,236,000 | 0.24% |
| R6 | 1625 | \$ 330,300 | \$ 331,500 | 0.36% |
| R7 | 1623 | \$ 331,300 | \$ 333,400 | 0.63% |
| R8 | 389 | \$ 449,500 | \$ 452,100 | 0.58% |
| R9 | 42 | \$ 461,750 | \$ 461,500 | -0.05% |
| R10 | 37 | \$1,275,900 | \$1,269,700 | -0.49% |
| R11 | 515 | \$ 585,100 | \$ 585,100 | 0.00% |
| R12 | 1044 | \$ 350,900 | \$ 351,300 | 0.11% |
| R13 | 1093 | \$ 365,000 | \$ 370,800 | 1.59% |
| R14 | 322 | \$ 465,500 | \$ 465,700 | 0.04% |
| R15 | 0 | \$ - | \$ - | 0.00% |
| R16 | 357 | \$ 362,400 | \$ 362,700 | 0.08% |
| R17 | 507 | \$ 429,300 | \$ 429,300 | 0.00% |

| FY2012 Two Family Assessment Data | | | | |
|--|-------|-------------|-------------|--------|
| Median Assessed Values | | | | |
| | Count | FY2011 | FY2012 | Change |
| R1 | 295 | \$ 444,500 | \$ 449,600 | 1.15% |
| R2 | 177 | \$ 491,300 | \$ 493,600 | 0.47% |
| R3 | 217 | \$ 791,700 | \$ 804,400 | 1.60% |
| R4 | 50 | \$ 942,150 | \$ 947,650 | 0.58% |
| R5 | 12 | \$1,864,550 | \$1,845,450 | -1.02% |
| R6 | 87 | \$1,083,900 | \$1,087,500 | 0.33% |
| R7 | 637 | \$ 575,000 | \$ 580,500 | 0.96% |
| R8 | 219 | \$ 679,000 | \$ 688,500 | 1.40% |
| R9 | 12 | \$ 807,700 | \$ 809,100 | 0.17% |
| R10 | 15 | \$1,916,100 | \$1,915,800 | -0.02% |
| R11 | 36 | \$1,133,850 | \$1,137,800 | 0.35% |
| R12 | 165 | \$ 600,300 | \$ 605,100 | 0.80% |
| R13 | 228 | \$ 643,950 | \$ 661,450 | 2.72% |
| R14 | 215 | \$ 859,400 | \$ 860,300 | 0.10% |
| R15 | 0 | \$ - | \$ - | 0.00% |
| R16 | 90 | \$ 848,700 | \$ 862,350 | 1.61% |
| R17 | 138 | \$ 663,700 | \$ 667,100 | 0.51% |

| FY2012 Three Family Assessment Data | | | | |
|--|-------|-------------|-------------|--------|
| Median Assessed Values | | | | |
| | Count | FY2011 | FY2012 | Change |
| R1 | 243 | \$ 551,200 | \$ 569,200 | 3.27% |
| R2 | 152 | \$ 648,050 | \$ 648,700 | 0.10% |
| R3 | 126 | \$ 922,850 | \$ 928,350 | 0.60% |
| R4 | 32 | \$1,081,400 | \$1,083,600 | 0.20% |
| R5 | 3 | \$2,906,100 | \$2,889,200 | -0.58% |
| R6 | 36 | \$1,228,300 | \$1,231,700 | 0.28% |
| R7 | 184 | \$ 684,500 | \$ 687,950 | 0.50% |
| R8 | 54 | \$ 865,200 | \$ 883,200 | 2.08% |
| R9 | 1 | \$ 530,000 | \$ 530,000 | 0.00% |
| R10 | 1 | \$2,954,400 | \$2,940,300 | -0.48% |
| R11 | 18 | \$1,138,050 | \$1,138,050 | 0.00% |
| R12 | 118 | \$ 718,600 | \$ 718,700 | 0.01% |
| R13 | 162 | \$ 700,700 | \$ 722,400 | 3.10% |
| R14 | 48 | \$ 898,800 | \$ 911,450 | 1.41% |
| R15 | 0 | \$ - | \$ - | 0.00% |
| R16 | 48 | \$ 884,350 | \$ 920,700 | 4.11% |
| R17 | 65 | \$ 770,800 | \$ 774,100 | 0.43% |