# Commonwealth of Massachusetts

DLS
DIVISION OF LOCAL SERVICES
MA DEPARTMENT OF REVENUE

**Supporting a Commonwealth of Communities**

## Massachusetts School Building Authority (MSBA) Superintendent Roundtable

*Sean Cronin, Senior Deputy Commissioner for Local Services*
*June 16, 2022*

## Municipal Finances

Local government services funded by property taxes, local receipts, state aid, issuance of debt and use of reserves

Income and sales taxes levied by state government

## Proposition 2 ½

Approved by voters via a ballot initiative in 1980

Places annual limits on property taxes

1. Property tax levy cannot exceed 2.5% of the municipality's total assessed property valuation

2. Annual property tax levy cannot increase by more than 2.5%, except for "New Growth"
   - Can ask local voters to exceed the 2.5% annual growth limit via an "operating override" or a "debt exclusion"

# Property Tax Levy Building Blocks

| | |
|---|---|
| **Levy Ceiling** | **2.5% of total Assessed Value (AV)**<br>**ex: 2.5% x $1B of AV = $25M** |
| **Levy Limit** | **Formula essentially =**<br>**(Prior year Levy Limit X 2.5%) + New Growth + Overrides** |
| **Levy** | **Determined annually as part of budget process** |

## New Growth

- New growth reflects certain increases in the tax base and becomes a permanent part of the levy limit base:
  - properties that have increased in assessed valuation since the prior year because of development or other changes
  - exempt real property returned to the tax roll
  - new personal property
  - new subdivision parcels and condominium conversions

- New growth does not include market value increases

Example: vacant parcel valued at $50K in prior year now valued at $450K because of construction of single family home

- $400,000 included in New Growth calculation
- if tax rate was $14.90, $5,960 in additional revenue

# Annual Levy Limit – Pt. 1

| | FY1 | FY2 | FY3 | FY4 | FY5 |
|---|---|---|---|---|---|
| Prior Year Levy Limit | $30,000,000 | $31,200,000 | $32,480,000 | $33,817,000 | $35,162,425 |
| 2.5% Increase | $750,000 | $780,000 | $812,000 | $845,425 | $879,061 |
| New Growth | $450,000 | $500,000 | $525,000 | $500,000 | $450,000 |
| Sub-Total | $31,200,000 | $32,480,000 | $33,817,000 | $35,162,425 | $36,491,486 |
| Assessed Value | $2,000,000,000 | $2,060,000,000 | $2,080,600,000 | $2,018,182,000 | $1,917,272,900 |
| Levy Ceiling | $50,000,000 | $51,500,000 | $52,015,000 | $50,454,550 | $47,931,823 |

## Referenda Questions

# Overrides

1. Any Legal Spending Purpose

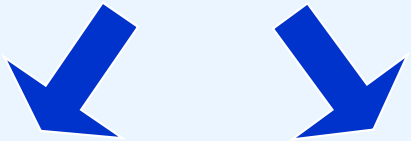
2. Permanent

3. Amount Limited by Ceiling

# Exclusions

1. Only Capital Purchases

2. Temporary



Debt
(Life of Bond)

Capital
(1 Year)

3.No Limit on the Number or Dollar Amount

# Annual Levy Limit – Pt. 2

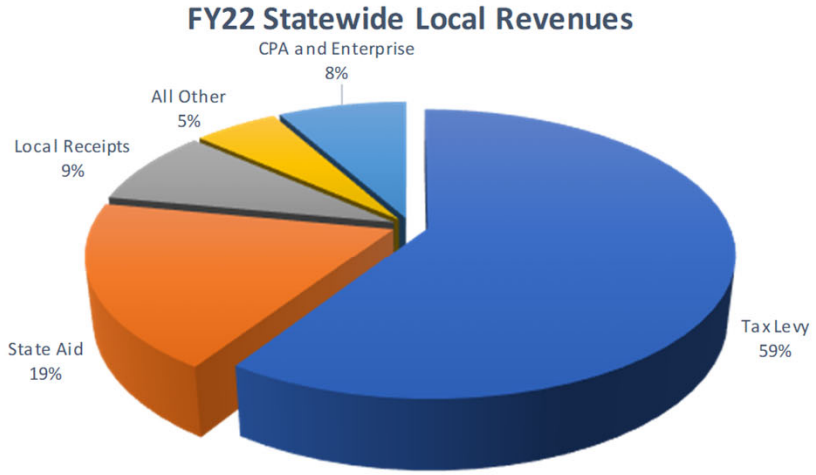
| | FY1 | FY2 | FY3 | FY4 | FY5 |
|---|---|---|---|---|---|
| Prior Year Levy Limit | $30,000,000 | $31,200,000 | $32,480,000 | $34,817,000 | $36,187,425 |
| 2.5% Increase | $750,000 | $780,000 | $812,000 | $870,425 | $904,686 |
| New Growth | $450,000 | $500,000 | $525,000 | $500,000 | $450,000 |
| Sub-Total | $31,200,000 | $32,480,000 | $33,817,000 | $36,187,425 | $37,542,111 |
| Override | $0 | $0 | $1,000,000 | $0 | $0 |
| **Levy Limit** | **$31,200,000** | **$32,480,000** | **$34,817,000** | **$36,187,425** | **$37,542,111** |
| Debt Exclusion | $0 | $0 | $0 | $2,000,000 | $1,900,000 |
| **Max. Allowable Levy** | **$31,200,000** | **$32,480,000** | **$34,817,000** | **$38,187,425** | **$39,442,111** |
| Assessed Value | $2,000,000,000 | $2,060,000,000 | $2,080,600,000 | $2,018,182,000 | $1,917,272,900 |
| Levy Ceiling | $50,000,000 | $51,500,000 | $52,015,000 | $50,454,550 | $47,931,823 |

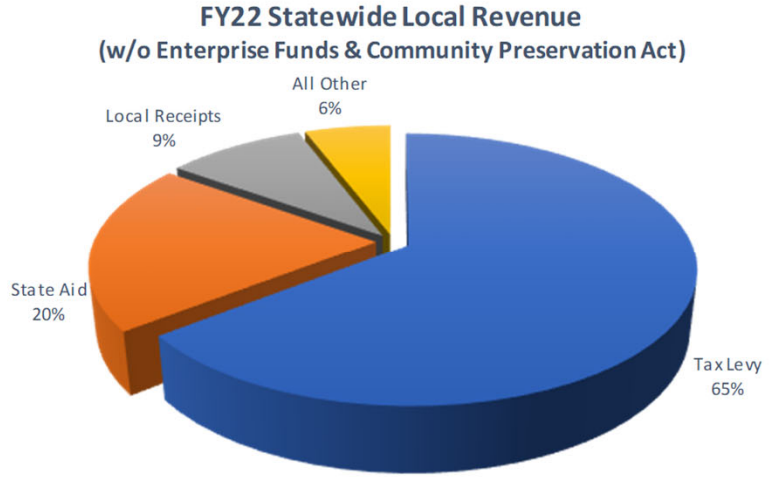
## Overview of Municipal Finances

All data used on the following slides come from annual municipal reporting requirements to DLS that municipalities must comply with

- “Tax Recap” to set the Tax Rate
- Balance Sheet to calculate Free Cash
- Schedule A year-end revenue/expense report

# Local Revenues



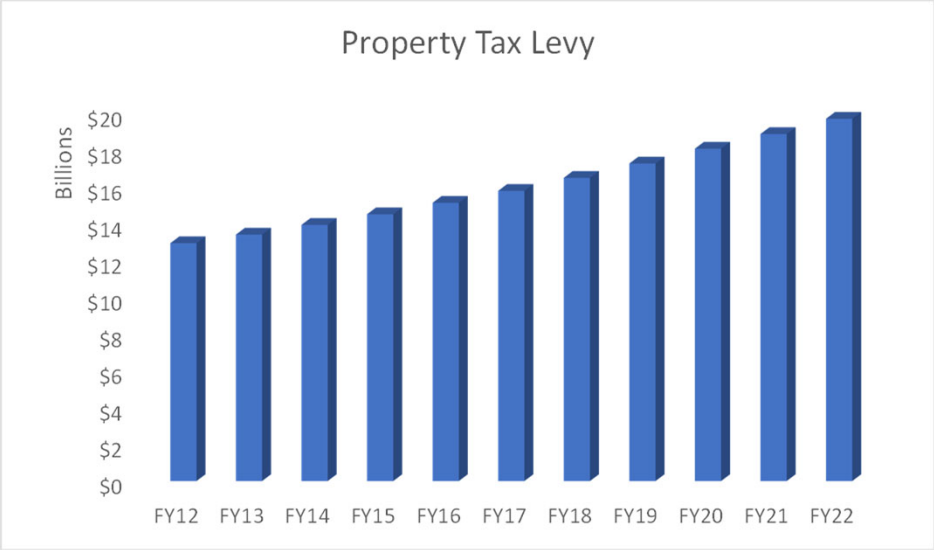

- While data shows 65% of local revenue comes from Property Taxes, more than 1/3 of municipalities have Property Taxes comprising 75%+ of revenue

| Property Tax as % of Gen Fund Revenue | |
|---|---|
| Range | # muni's |
| 80% + | 74 |
| 70% - 79% | 147 |
| 60% - 69% | 69 |
| 50% - 59% | 35 |
| 40% - 49% | 14 |
| 30% - 39% | 10 |
| < 30% | 1 |

- $2.4B of Enterprise Funds revenues
  - Water/Sewer, Golf, Airport, Parking, etc.
  - Not available for General Fund expenditures
- $355M of Community Preservation Act (CPA) monies
  - Not available for General Fund expenditures

# Property Taxes

- Between FY12 – FY22, total statewide Property Tax levy increased $6.8B (52%) from $13B to $19.8B

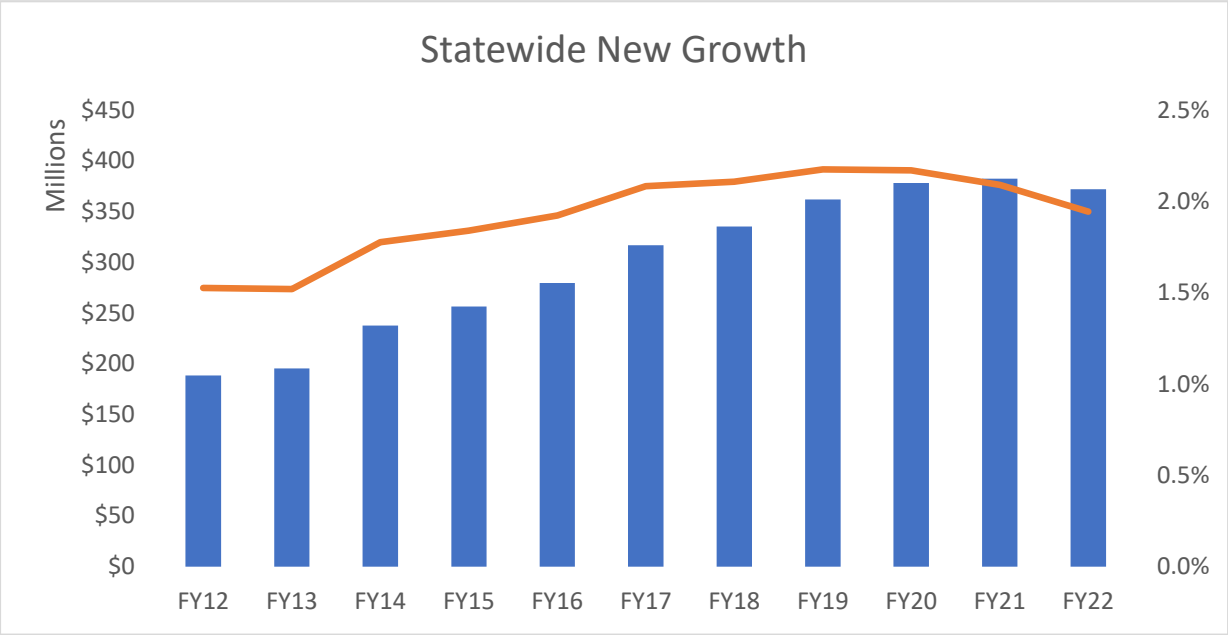



- Under Prop 2 ½, if every municipality simply increased its levy by 2.5%, the total levy would have grown from $13B to $16.6B, or $3.6B (28%)
  - So where did the additional taxation came from?
    - New Growth ~$3B
    - Overrides ~$185M
    - Debt/Capital Exclusions ~$244M

- Over the same period, the Avg Single Family Tax Bill grew ~$2K (43%) to $6,719
  - 80 municipalities with increases of greater than 50%
  - 30 municipalities with increases of less than 25%

# New Growth

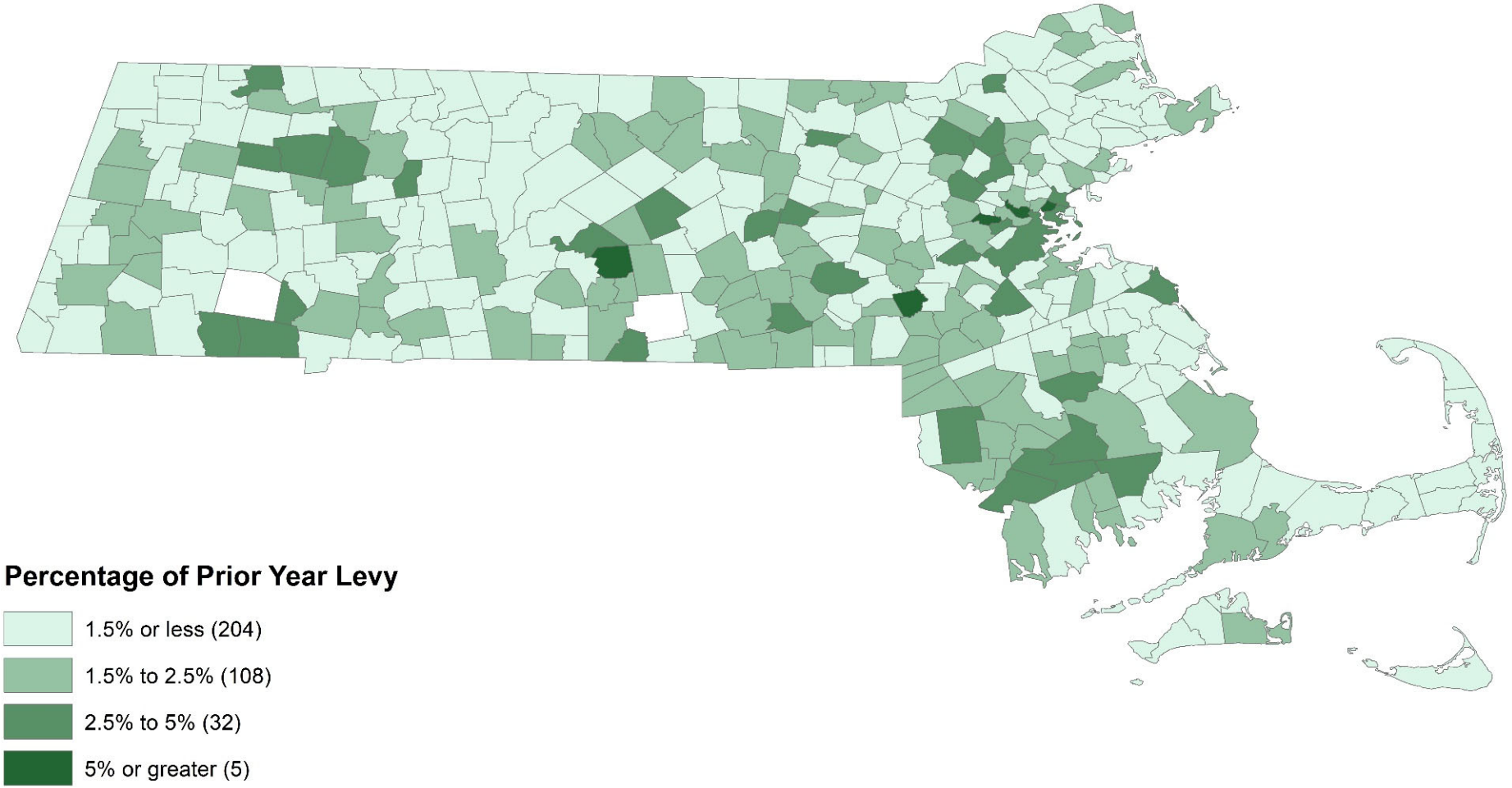
- Between FY12 – FY22, New Growth totaled $3.3B




- Not all parts of the state seeing the same positive experience
  - The top 15 municipalities account for more than 40% of all New Growth (Boston alone = 22%)
  - In FY22:
    - » 190 municipalities had New Growth equal to less than 1.5% of the previous year's levy
    - » 40 municipalities had New Growth equal to more than 2.5% of the previous year's levy

## New Growth Map

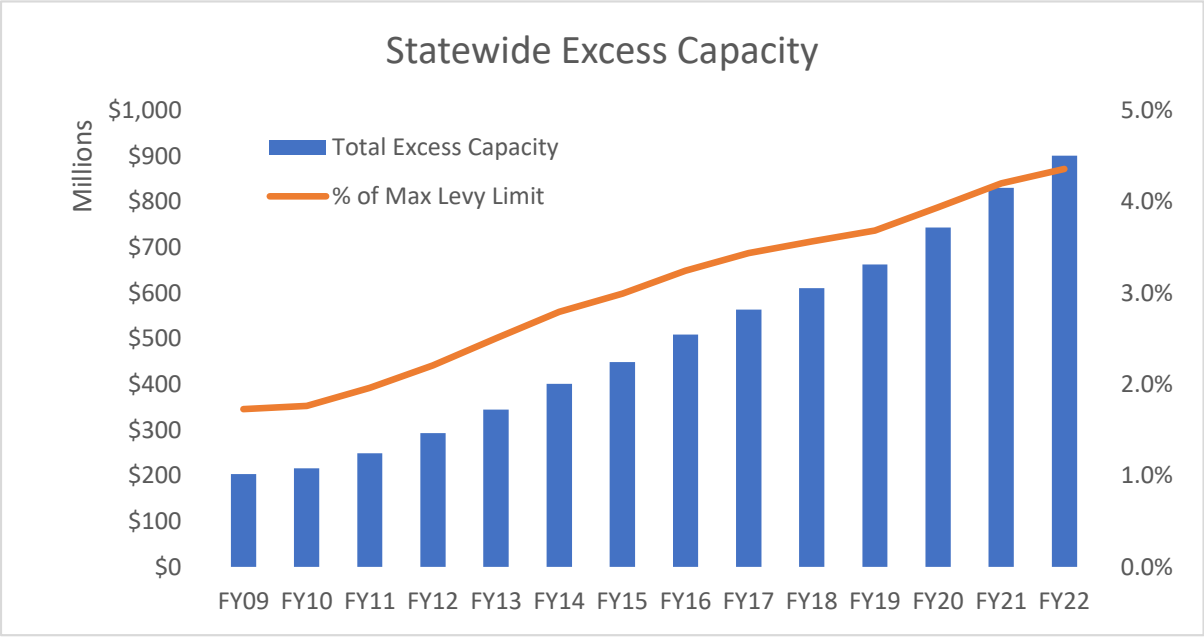
# FY2022 New Growth Applied to Tax Levy



# Excess Capacity

- Excess Capacity is the difference between what a municipality can levy and does levy

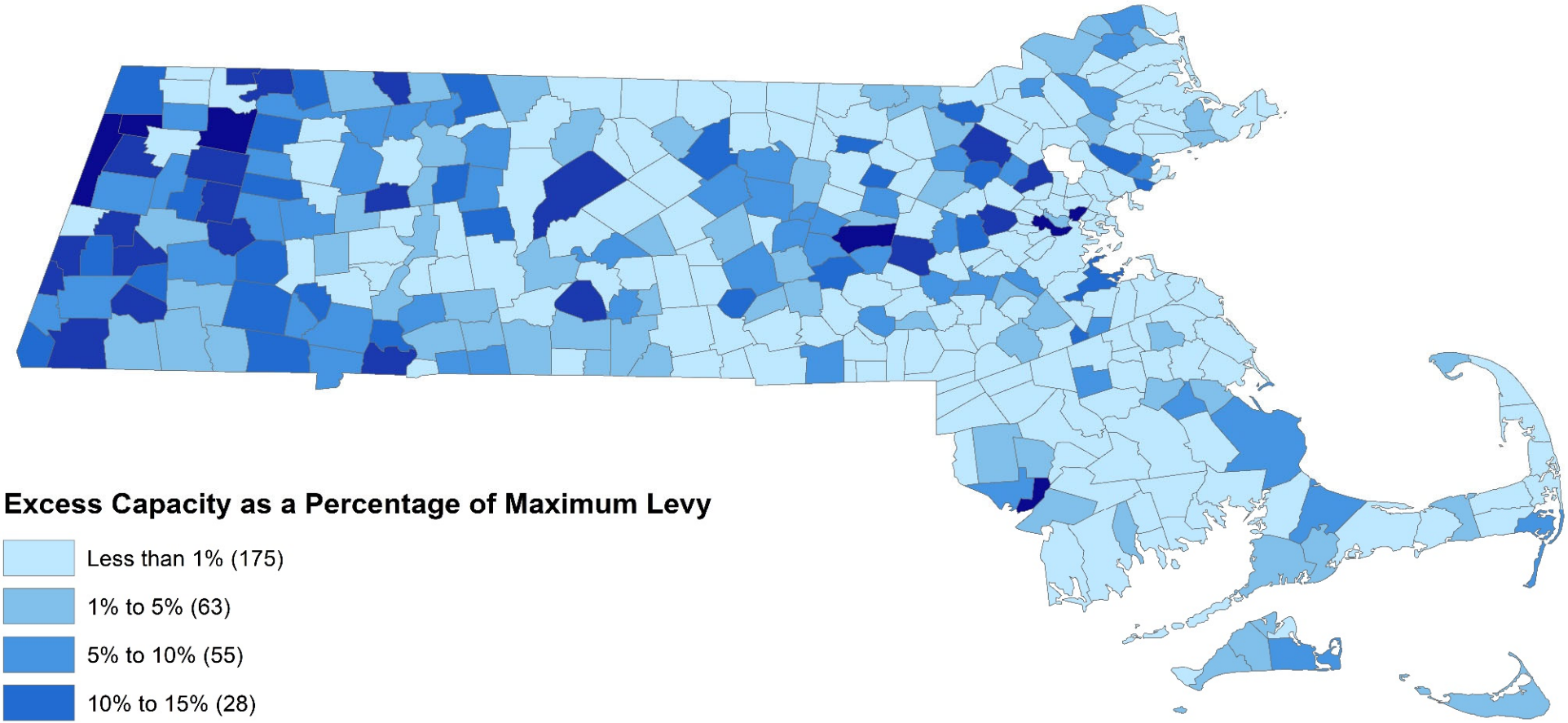
| | |
|---|---|
| Prior Year Levy | $10,000,000 |
| 2.5% Increase | $250,000 |
| New Growth | $150,000 |
| Maximum Levy | $10,400,000 |
| Actual Levy | $10,250,000 |
| Excess Capacity | $150,000 |




- The top 10 municipalities account for 58% of all Excess Capacity (Cambridge alone = 22%)
- Most municipalities have small amounts of Excess Capacity:
  - 177 municipalities have Excess Capacity equal to less than 1% of the maximum levy
  - Statewide median is 0.9%

# Excess Capacity Map

## FY2022 Excess Levy Capacity

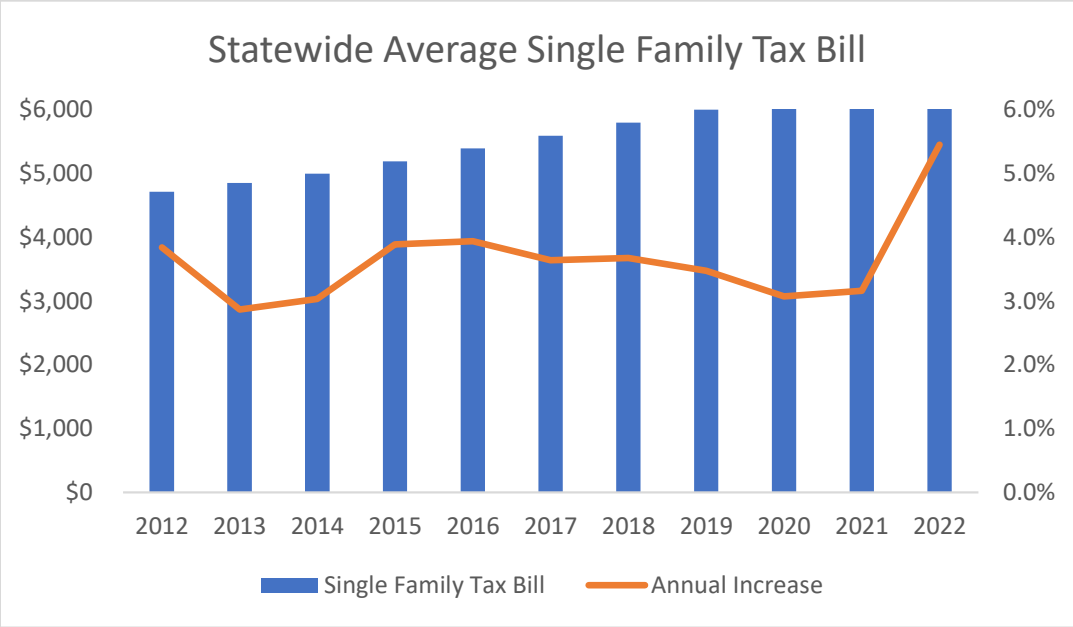


**Excess Capacity as a Percentage of Maximum Levy**

- Less than 1% (175)
- 1% to 5% (63)
- 5% to 10% (55)
- 10% to 15% (28)
- 15% to 25% (21)
- Greater than 25% (7)

# Single Family Tax Bill

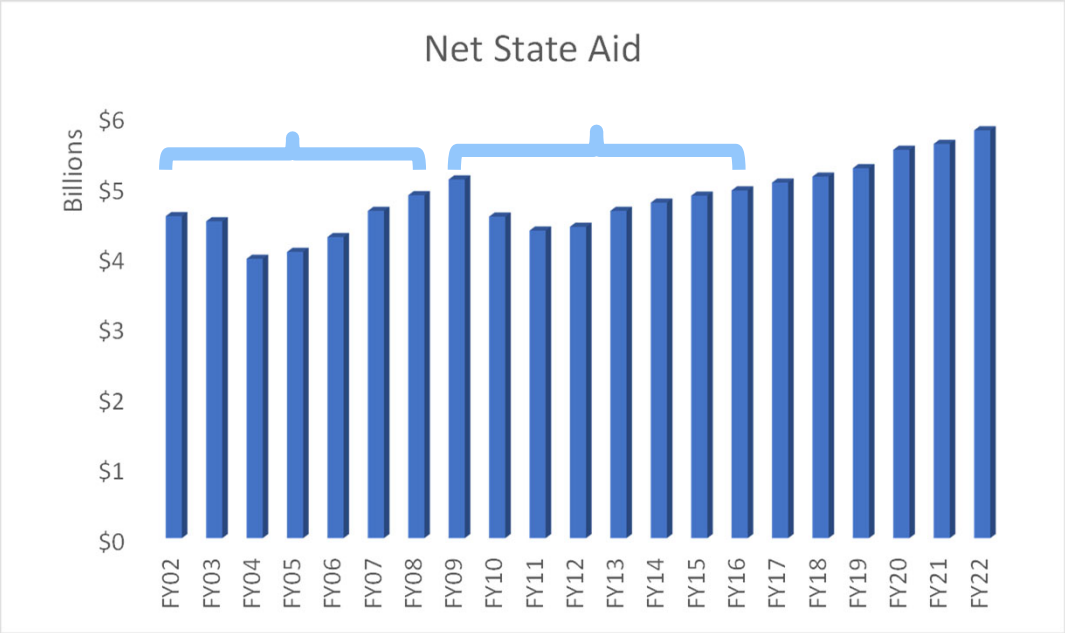
- As previously noted, between FY12 – FY22, the Average Single Family Tax Bill increased ~$2K (43%) to $6,719




- Increase would have been greater if not increased levels of Excess Capacity

## State Aid

- Outside a municipality's control and dependent on overall economy
- In FY22, $7.1B of "Cherry Sheet" aid
- Two major programs:
  - Ch. 70 Education Aid - $5.5B in FY22
  - Unrestricted General Government Aid (UGGA) - $1.2B in FY22
- Historically, fluctuates with the economy




- After Dot-Com bust, took 5 years to get to previous level of aid
- After Great Recession, took 7 years to get to previous level of aid

# Local Receipts

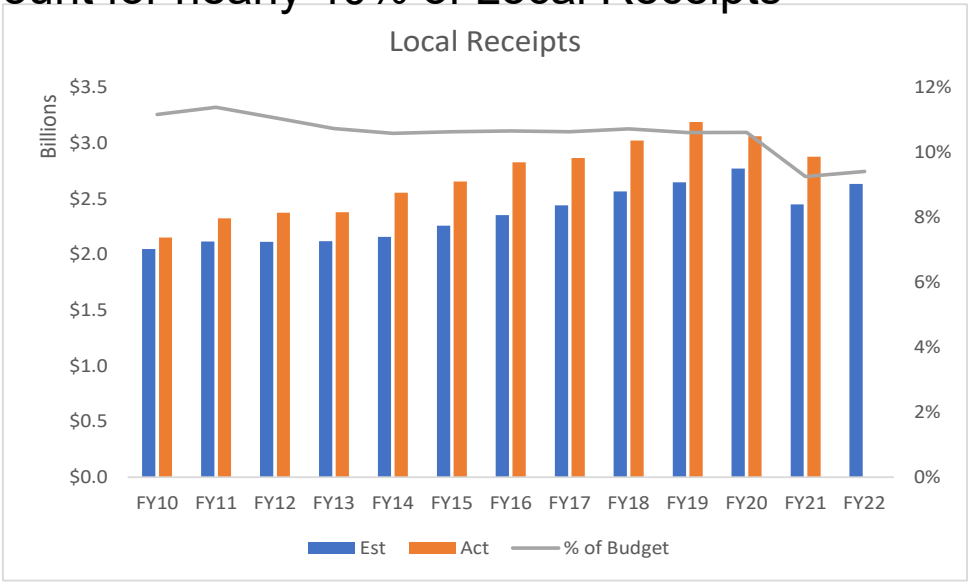
- Local Receipts come from a variety of sources other than property taxes, including excise taxes, regulatory fees, user fees, departmental revenues, investment income

- In FY22 (budgeted), totaled $2.6B, or 9% of total revenue
  - Largest is MVE ($825M, or 29% of all local receipts)
  - MVE formula set by state law; no municipal ability to alter it for additional revenue

- For FY10, new Meals Tax and increase in Room Occupancy Tax enacted
  - Meals now totals $177M [using FY20 because of COVID]
  - Room Occupancy has grown to $207M (from $87M) [using FY20 because of COVID]
  - Maximum percentages set by state law

- The 3 excise taxes (MVE, Meals, Lodging) account for nearly 40% of Local Receipts
  - all formulas or percentages set by state law
  - all economically-sensitive

- Between FY10 – FY20, $781M (35%) increase
  - the 3 excise taxes account for 63% of the increase
  - licenses and permits another significant factor in increase
  - most others flat or declining



## Free Cash

- Free Cash is the amount of unrestricted funds, as of July 1, from operations of the previous FY based on the balance sheet as of June 30

- Includes
  - actual receipts in excess of estimates
  - unspent amounts in budget line items for the year just ending
  - unexpended Free Cash from the previous year

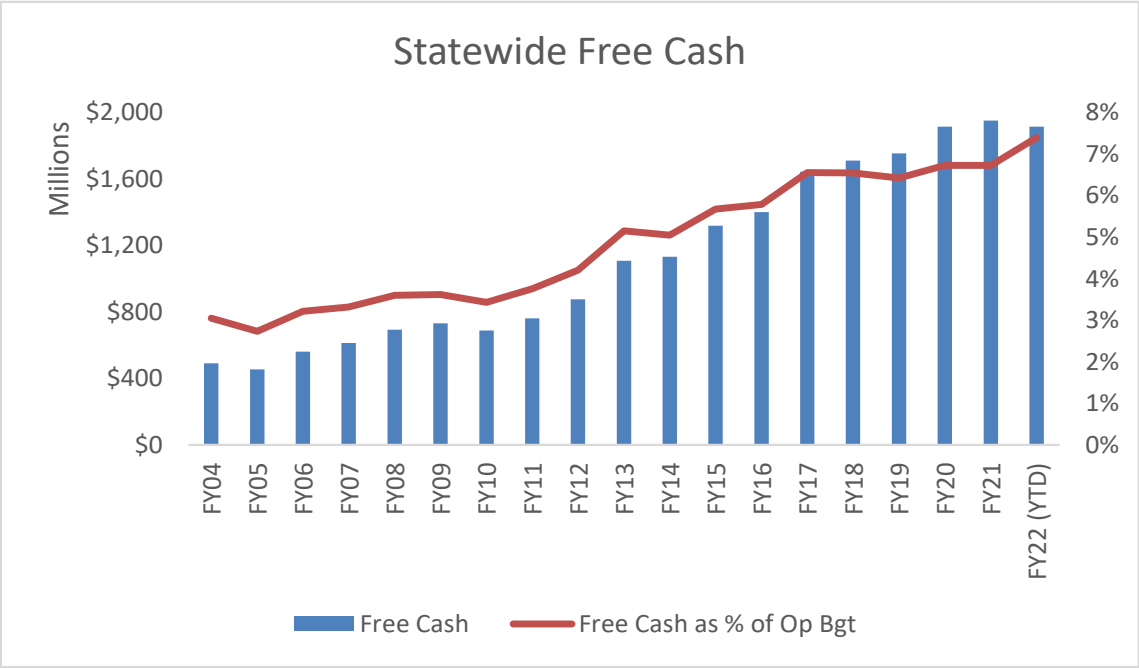
- Offset by property tax receivables and certain deficits, so can be a negative number

- Free Cash is the culmination of multiple years' operating results and is not an annual "budget surplus"

- As a nonrecurring revenue source, should be restricted to paying 1-time expenditures, funding capital projects or put toward reserves
  - do not use for on-going expenses

- Recommended that Free Cash be maintained at a level equivalent to 3%-5% of budget

# Free Cash (con't.)




- In FY22 YTD, $2.3B of Free Cash certified statewide [340 muni's]
  - Boston and Cambridge account for 25%
  - Top 20 municipalities accounted for 44% of the total

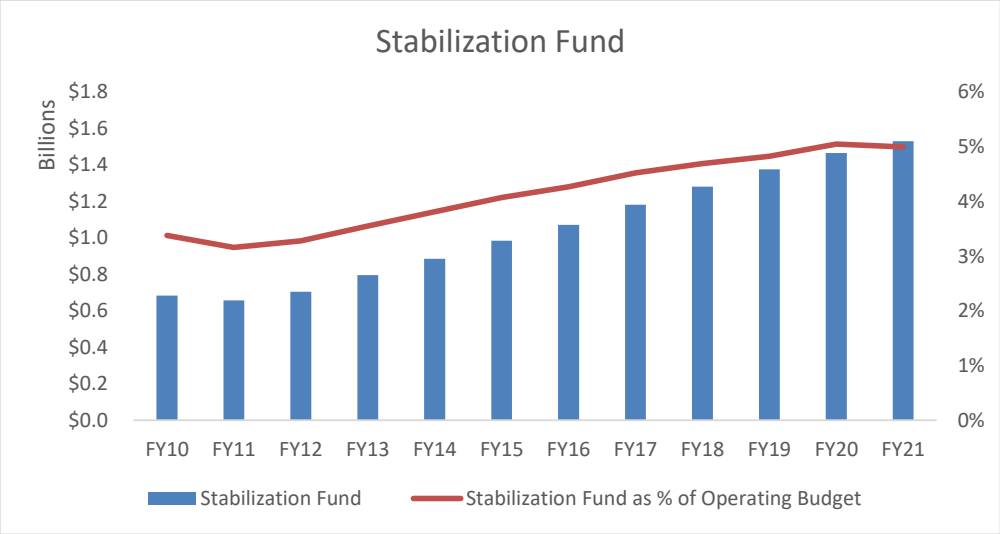
- Backing out the ~90 muni's with a budget of less than $15M:
  - 73 have Free Cash equivalent to less than 5% of budget
  - 186 have Free Cash equivalent of at least 5% of budget

# Reserves

- Two types:
  - Annual budget reserve – appropriated for “extraordinary or unforeseen expenditures”
    - Any balance closes out at the end of the FY
  - Stabilization Fund – appropriated to set aside monies for future spending purposes
    - Any balance as of 6/30 remains in the fund
    - Two types:
      - General – the “Rainy Day Fund”
      - Special Purpose – monies dedicated for specific purposes (e.g., capital, facility maintenance, public safety equipment); can only be used for the specific purpose the legislative body voted

- Recommended that General Stabilization Fund be maintained at a level equivalent to 3%-5% of budget

# Reserves (con't.)




Note: FY21 data for 327 muni's

- For these 327 muni's with FY21 data, $1.5B of Stabilization Funds statewide
  - Top 25 municipalities accounted for 41% of the total
- Backing out the muni's with a budget of less than $15M:
  - 108 have Stabilization Funds equivalent to less than 5% of budget
  - 140 have Stabilization Funds equivalent of at least 5% of budget
- When add Free Cash + Stabilization Fund:
  - 82 less than 10%
  - 183 between 10% - 20%
  - 79 greater than 20% (41 of these are muni's with budgets of less than $5M)

## Personnel Costs

- Personnel costs (wages and benefits) comprise 70% - 80% of a municipality's budget
  - No surprise since local government is a service industry that requires employees to deliver those services

- Critical that municipalities:
  - provide COLA's that are affordable and sustainable
  - continuously look at ways to contain health insurance costs

# Summary

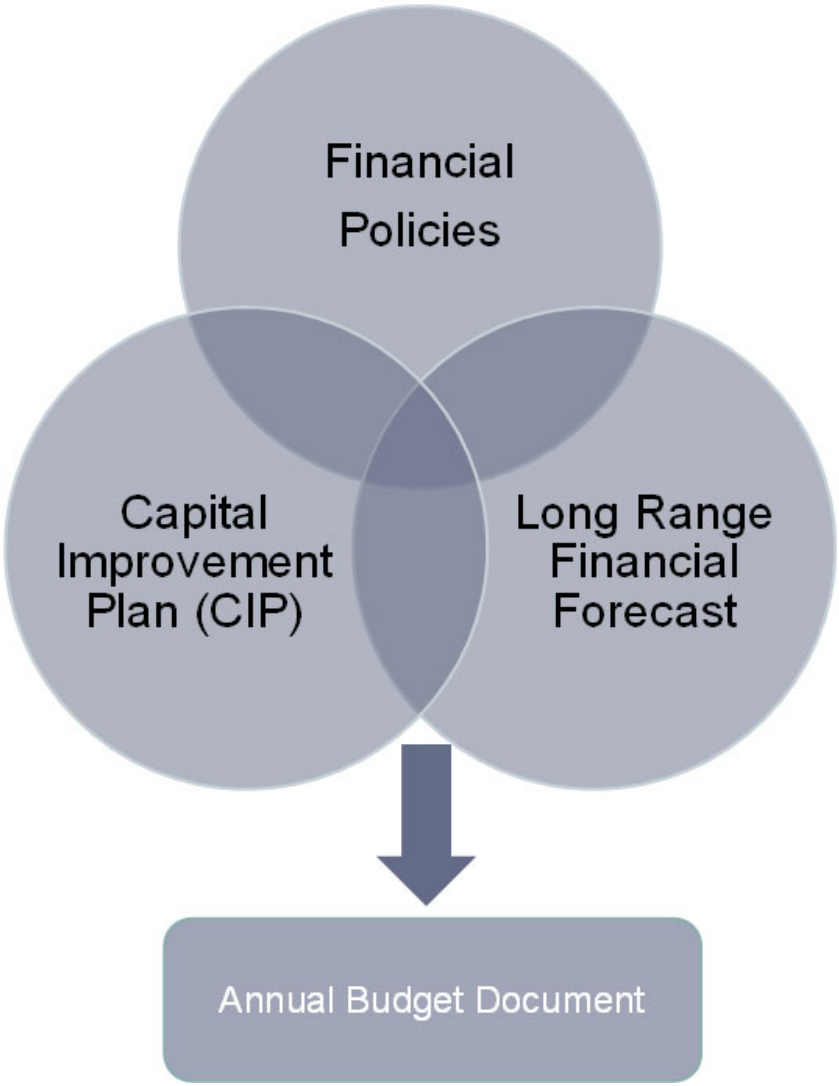
- Property Taxes capped by Proposition 2 ½
- New Growth experience varies greatly across the state
- Majority of municipalities annually levy property tax to the maximum extent possible
- State Aid is heavily dependent on the economy and is mostly for education
- Local Receipts grow minimally except for economically-sensitive items
  - and those can actually decline during economic downturns
- The largest Local Receipt items (MVE, Meals Excise, Lodging Excise) have formulas or percentages set by state law
- Free Cash experience varies greatly across the state
- Reserves (Stabilization Funds and Free Cash) should be equivalent to 6%-10% of revenue and be used for one-time expenses
- Pensions and Health Insurance annual budget challenges
- Municipalities limited in financial flexibility

## Municipal Management Team

- Selectmen/Mayor/City Manager
- Town Administrator/Town Manager
- City Council/Town Meeting
- Finance Committee
- Assessors
- Collector
- Treasurer
- Accountant/Auditor
- Clerk

➢ Teamwork and communication among the members of the municipal management team is essential for the efficient operation of the municipality

# Essential Financial Management Concepts



## Financial Policies

- Bond rating agencies and audit firms want to see policies adopted and followed

- Every municipality is different – develop policies that work best for your community

- Use financial modeling when developing policies to see the long-range impacts

## Examples of Financial Policies

- **Reserve Policies**
  - Annual budget reserve – x% of revenue
  - Unassigned Fund Balance – maintain at x% of revenue
  - Overlay Reserve – establish process for annual review/declaration of surplus

- **Free Cash Policy**
  - Use only for one-time expenses
  - Prioritization of use – e.g., annual budget reserve, unassigned fund balance, special reserves, CIP, housing trust, reduce unfunded liabilities

- **CIP Policies**
  - Definition ($ value, etc.)
  - Evaluation process
  - Financing
    - X% of revenue to support debt service + Y% of revenue to support pay-as-you-go capital
    - Free Cash
    - Enterprise funds = self-supporting
  - Debt Management
    - Amortization (e.g., 50% shall mature within 10 yrs)
    - Total outstanding debt shall not exceed X% of Assessed Value
    - Total outstanding debt per capita shall not exceed $X
    - Total outstanding debt shall not exceed X% of per capita income
    - Debt service shall not exceed X% of revenue

## Long Range Financial Forecast

- Should serve as the cornerstone of the budgeting process
- Assesses long-term financial implications of current and proposed policies, programs
- Helps determine what is available for collective bargaining
- Acts as a bridge between the operating budget and the CIP, bringing all fiscal policy and economic variables together to establish coordinated managerial direction
- Major assumptions include:
  - New Growth
  - State Aid
  - Local Receipts
  - Wage adjustments
  - Utility costs
  - Net School Spending (NSS) requirements
  - Benefits (Health Insurance, Pensions, OPEB's)
  - CIP funding (debt service)

# Debt

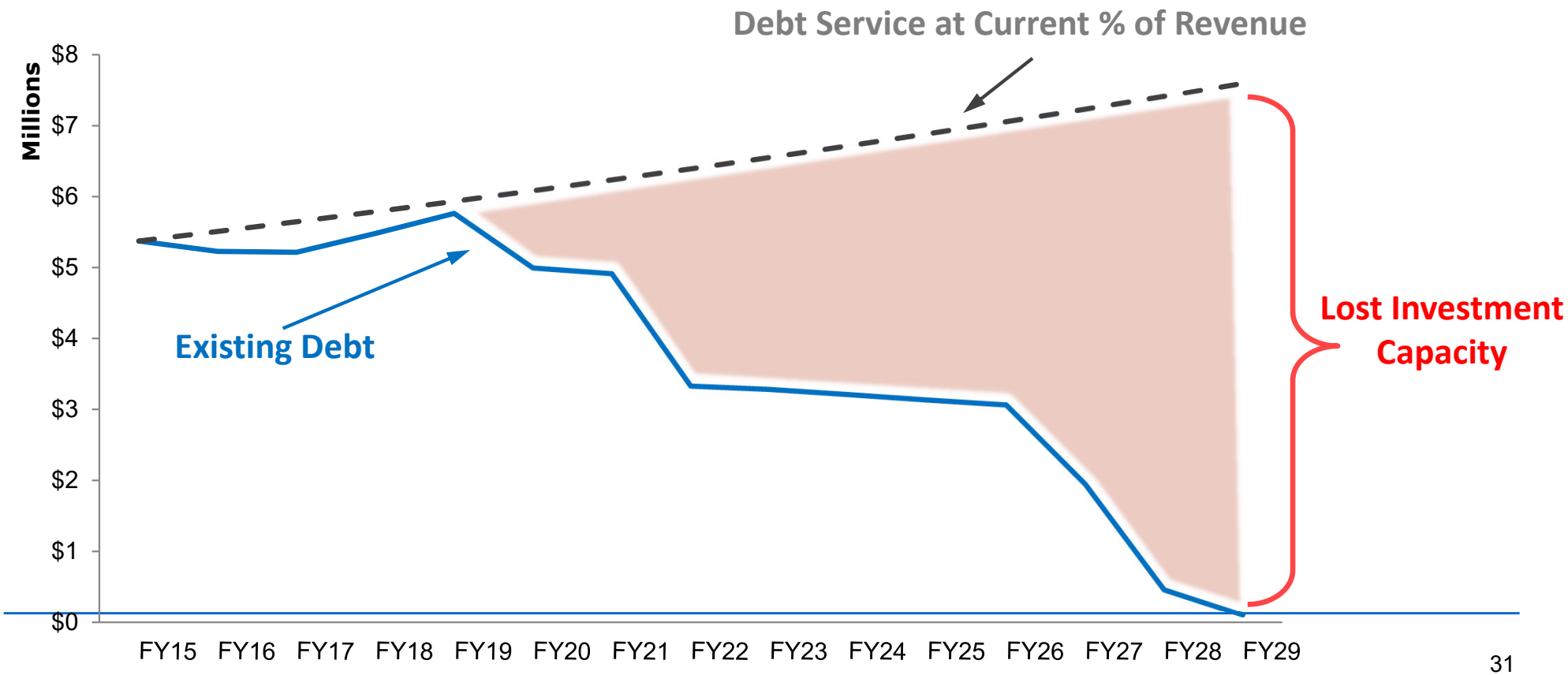
- Debt management is a critical function for local finance managers

- Mismanaging debt can cripple a municipality's finances

- Municipalities must maintain its infrastructure
  - Schools, public safety facilities, other municipal buildings
  - Parks, playgrounds, other open spaces
  - Water, sewer systems
  - Streets, sidewalks, bridges, culverts
  - Information Technology
  - Heavy equipment (e.g., fire trucks, DPW trucks)

# Maintain a Steady Balance of Capital Investment

- Because of its critical nature and large financial obligation, municipalities should reinvest decreases in debt service
  - don't use it for "operating budget relief"
  - maintain debt service as a constant percent of revenue
- Lack of reinvestment leads to lost capacity



# Debt Management Plan

| PROJECT | BOND AUTH. | BOND AMT | TERM | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Funded Within 6% CIP Policy | | | | | | | | | | | | |
| Runkle School - Constr. (previously authorized) | $17.580 | $0.500 | 10 | $0.068 | $0.066 | $0.064 | $0.062 | $0.061 | $0.059 | $0.057 | $0.055 | $0.054 |
| Roof Repairs/Replacements (previously authorized) | $1.350 | $1.350 | 10 | $0.182 | $0.178 | $0.173 | $0.168 | $0.163 | $0.159 | $0.154 | $0.149 | $0.144 |
| Fisher Hill Park (previously authorized) | $1.200 | $1.200 | 10 | $0.162 | $0.158 | $0.154 | $0.149 | $0.145 | $0.141 | $0.137 | $0.133 | $0.128 |
| Old Lincoln School (previously authorized) | $3.000 | $3.000 | 15 | $0.313 | $0.305 | $0.298 | $0.290 | $0.283 | $0.275 | $0.268 | $0.260 | $0.253 |
| MSC Renovations (previously authorized) | $2.500 | $1.500 | 10 | $0.203 | $0.197 | $0.192 | $0.187 | $0.182 | $0.176 | $0.171 | $0.166 | $0.161 |
| Carlton St. Footbridge (previously authorized) | $1.400 | $1.245 | 10 | | $0.177 | $0.172 | $0.167 | $0.162 | $0.156 | $0.151 | $0.146 | $0.140 |
| Muddy River (previously authorized) | $0.745 | $0.745 | 10 | | $0.104 | $0.101 | $0.098 | $0.095 | $0.092 | $0.089 | $0.086 | $0.083 |
| Ladder #2 (future authorization) | $0.900 | $0.900 | 10 | | $0.128 | $0.124 | $0.121 | $0.117 | $0.113 | $0.109 | $0.105 | $0.101 |
| Rear Landfill (future authorization) | $4.600 | $4.600 | 20 | | $0.449 | $0.438 | $0.427 | $0.416 | $0.405 | $0.394 | $0.383 | $0.372 |
| MSC Renovations (future authorization) | $2.500 | $1.000 | 10 | | $0.143 | $0.138 | $0.134 | $0.130 | $0.126 | $0.121 | $0.117 | $0.113 |
| Pierce Playground (future authorization) | $0.920 | $0.920 | 10 | | | $0.131 | $0.127 | $0.123 | $0.119 | $0.115 | $0.112 | $0.108 |
| Roof Repairs/Replacements (future authorization) | $1.050 | $1.150 | 10 | | | $0.164 | $0.159 | $0.154 | $0.149 | $0.144 | $0.139 | $0.135 |
| Envelope/Fenestration Repairs (future authorization) | $1.300 | $1.300 | 10 | | | $0.185 | $0.180 | $0.174 | $0.169 | $0.163 | $0.158 | $0.152 |
| Corey Hill + Emerson Garden (future authorization) | $1.170 | $1.170 | 10 | | | | $0.167 | $0.162 | $0.157 | $0.152 | $0.147 | $0.142 |
| Driscoll School Addition (future authorization) | $27.300 | $10.000 | 20 | | | | $0.975 | $0.951 | $0.928 | $0.904 | $0.880 | $0.856 |
| Driscoll School Addition (future authorization) | $27.300 | $17.300 | 20 | | | | | $1.687 | $1.646 | $1.605 | $1.563 | $1.522 |
| Fire Maintenance/Training Facility (future authorization) | $4.125 | $4.125 | 20 | | | | | $0.402 | $0.392 | $0.383 | $0.373 | $0.363 |
| High School Addition (future authorization) - BAN | $48.750 | $5.000 | 1 | | | | | | $0.100 | | | |
| Larz Anderson Park (future authorization) | $2.700 | $2.700 | 15 | | | | | | $0.302 | $0.293 | $0.285 | $0.277 |
| Roof Repairs/Replacements (future authorization) | $3.500 | $3.500 | 15 | | | | | | $0.391 | $0.380 | $0.370 | $0.359 |
| High School Addition (future authorization) - BAN | $48.750 | $38.000 | 1 | | | | | | | $0.700 | $0.000 | $0.000 |
| Roof Repairs/Replacements (future authorization) | $2.500 | $2.500 | 10 | | | | | | | $0.356 | $0.346 | $0.335 |
| Larz Anderson Park (future authorization) | $2.200 | $2.200 | 10 | | | | | | | $0.314 | $0.304 | $0.295 |
| High School Addition (future authorization) - BAN | $48.750 | $48.750 | 1 | | | | | | | | $0.910 | |
| High School Addition (future authorization) | $48.750 | $48.750 | 25 | | | | | | | | | $4.388 |
| Larz Anderson Park (future authorization) | $2.500 | $2.500 | 15 | | | | | | | | | $0.279 |
| Cypress Playground / Athl Field (future authorization) | $1.400 | $1.400 | 10 | | | | | | | | | $0.200 |
| Baldwin School (future authorization) | $2.250 | $2.250 | 15 | | | | | | | | | $0.251 |
| **NEW GEN FUND DEBT SERVICE (cumulative)** | | | | **$0.927** | **$1.904** | **$2.334** | **$3.411** | **$5.406** | **$6.053** | **$7.160** | **$7.187** | **$11.211** |
| | | | | | | | | | | | | |
| Debt Exclusions | | | | | | | | | | | | |
| Devotion School - Design/Constr. (future authorization) | $77.000 | $10.000 | 25 | | | $0.727 | $0.727 | $0.727 | $0.727 | $0.727 | $0.727 | $0.727 |
| Devotion School - Design/Constr. (future authorization) | $77.000 | $50.000 | 25 | | | | $3.637 | $3.637 | $3.637 | $3.637 | $3.637 | $3.637 |
| Devotion School - Design/Constr. (future authorization) | $77.000 | $17.000 | 25 | | | | | $1.237 | $1.237 | $1.237 | $1.237 | $1.237 |
| **NEW DEBT EXCLUSION DEBT SERVICE (cumulative)** | | | | **$0.000** | **$0.000** | **$0.727** | **$4.364** | **$5.601** | **$5.601** | **$5.601** | **$5.601** | **$5.601** |

# Can We Afford It?

- A common question is “Can the city/town afford this project?”

- How do we determine that?
  - That question is asked in two different environments: debt exclusion vs. within levy

## Debt Exclusion

- Ultimate question is “what is the increase on my tax bill”
- Factors include: cost, interest rate, bond term, bond structure

## Within Levy

- Key is what capacity exists in the CIP
- What amount of existing debt is running off over each of the next few years (Debt Mgmt Plan)?
- What other projects are planned? Could they re-ordered?
- Could the muni increase resources available for capital (i.e., modify policies)?