Part 1: Proposition 2 1/2's Levy Limit Components and a Statistical Review over the Last Decade

Joe Boudreau - BOA Field Representative, Tom Guilfoyle - BOA Supervisor of Accounting and Tony Rassias - BOA Deputy Director

This is the first of a three part series reviewing Prop 2 1/2's levy limitation components along with statistics from FY2004 to FY2013. Part One will focus upon levy limit components, and will begin an FY2014 levy limit calculation. Part Two will focus upon the levy ceiling and Part Three will discuss the maximum allowable levy. The levy limit calculation shown in all Parts is organized on the basis of the levy limit worksheet found on Gateway's levy limit report page.

It was a taxpayer revolt! The national economy was in a recession, unemployment was rising, interest rates were double-digits, Washington Public Power Supply System defaulted on $2.25 billion of bonds, Proposition 13 was in, and the Massachusetts four percent tax cap wasn't working. "Taxachusetts," as it was jokingly called, was primed for a strict tax cutting measure which passed by ballot in November of 1980. - A Sketch of the History of the Massachusetts Bureau of Accounts and Related Matters in the Growth and Development of Municipal Finance by Anthony A. Rassias

In November of 1980, the people of Massachusetts passed by ballot vote Proposition 2 1/2 (MGL Chapter 580 of the Acts of 1980), a law that, among other things, placed constraints on city and town property tax levies beginning in FY1982.

Since that time, these levies have been limited by the law's provisions and approved by the Bureau of Accounts as part of the annual tax rate certification process. Even 33 years since its passage, Prop 2 1/2 initiates considerable discussion and debate.

The property tax levy is the revenue a community raises through real and personal property taxes each fiscal year when it sets its tax rate. The law established three types of annual levy limits: a levy limit, a levy ceiling and a maximum allowable levy. The levy limit is incremental and allows a permanent but controlled annual increase to the tax levy. The levy ceiling caps the levy limit for that fiscal year at 2.5 percent of the current fiscal year's total assessed full and fair cash value for real and personal property. The levy limit may be increased or decreased by locally adopted referenda, but may not exceed the levy ceiling. The levy ceiling may be increased temporarily by certain locally adopted exclusions. The maximum allowable levy is the maximum amount of property tax a community may raise in a fiscal year. The following will outline the levy limit components.

Levy Limit Components

The Base or Prior Year Levy Limit

The base or starting point for calculating a community's levy limit is its prior year levy limit.

When Prop 2 1/2 was first implemented in FY1982, however, a community's prior year tax levy was the base for calculating the following fiscal year's levy limit. In 1983, the Legislature made the prior year levy limit the base in order to remove any disincentive to levy below the limit in particular years. (MGL Chapter 641 of the Acts of 1983)

For example, let's assume an FY2013 Levy Limit base of $10,000,000 for our calculations.

Amended Prior Fiscal Year New Growth

This growth, certified by the Bureau of Local Assessment, is based on the value of new construction and/or new articles of personal property omitted or increased and committed for payment after the original commitment. The certified amended amount adds to the Base in the calculation of the following fiscal year's levy limit.

Table 1 shows the total number of communities and total certified tax dollar amounts that affected levy limits from FY2004 to FY2013. The Table shows that although the largest total dollar amount affected the FY2006 levy limits, the largest total number of amended new growth submissions certified affected the FY2008 levy limits.

Table 1 - Amended Prior Fiscal Year New Growth

Amended Prior Fiscal Year New Growth

	Fiscal Years									
	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013
# Certified	40	42	51	57	70	50	51	44	55	47
$ Certified	1,842,242	456,115	2,489,570	1,410,600	1,877,706	1,190,355	1,906,472	816,676	1,857,189	1,450,135

Fiscal Facts:

- The largest amount certified was $1,277,000 in FY2012 for Cambridge, and the smallest amount was $9 in FY2011 for Dracut;
- About 81% of communities certified for FY2013 had also applied at least once before in the decade;

- For FY2013, the average tax dollar growth amount certified was about $31,000. Without including Boston and Cambridge, the average was about $18,000.

Submissions for FY2014 may also reflect the reporting of previously unassessed or misreported articles of personal property assessed after a personal property audit under MGL c. 59, s. 31A, that would have qualified as new growth in certain prior fiscal years. See Section III-F of IGR 13-402 for further details.

Let's assume the following:

FY2013 Omitted and/or increased Residential value	$250,000
FY2012 Residential Tax Rate	x $14.00/000
FY2013 Amended Prior Fiscal Year New Growth	= $3,500

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The Annual 2.5 Percent Increase

Prop 2 1/2 allows an automatic 2.5 percent increase to the Base which includes amended prior fiscal year new growth in calculating the following fiscal year's levy limit.

Let's assume the following:

FY2013 Base	$10,000,000
FY2013 Amended Prior FY New Growth	+ $3,500
Subtotal	= $10,003,500
FY2014 2.5 Percent Increase	x then = $250,088

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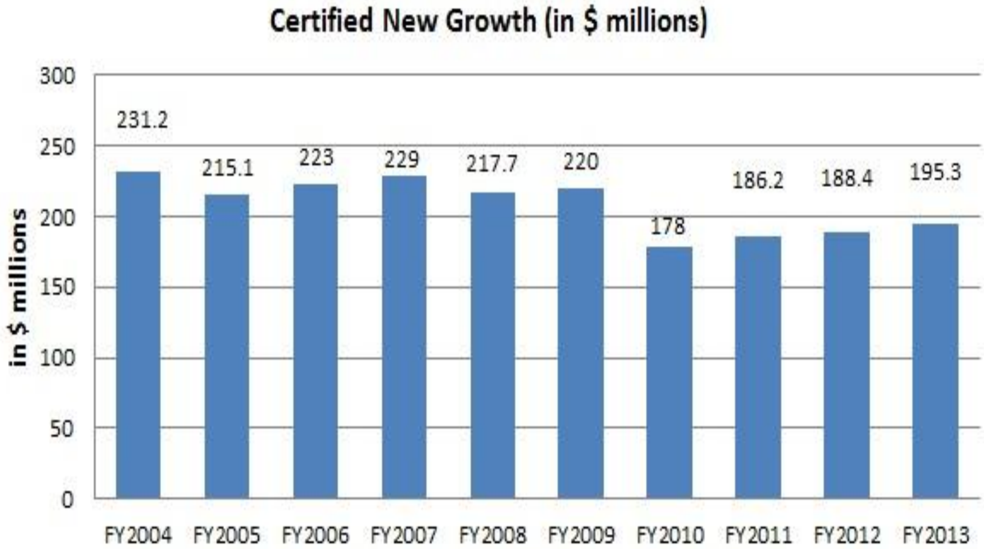
Current Fiscal Year New Growth

Prop 2 1/2 allows for an increase to the levy limit by an amount based on the assessed value of new construction and new articles of personal property.

When first enacted, Prop 2 1/2 had no provision for increasing the levy limit based on the value of new construction. City and town officials argued, and the Legislature agreed, that without such a provision essential government services would be severely impacted as service costs could not keep pace with a growing population. (Chapter 782 of the Acts of 1981)

Chart 1 shows certified tax dollar amounts for new growth from FY2004 to FY2013. FY2004 began this period with the highest amount certified at $231.2 million, which then decreased to the lowest amount certified in FY2010 at $178 million reflecting market conditions at that time, and increased to $195.3 million in FY2013.

Chart 1 - Certified New Growth



Fiscal Facts:

- The largest amount of new growth certified was $37,647,801 in FY2011 for Boston and the smallest amount was $3 in FY2012 for Gosnold;
- Over the decade, communities with greater than $1,000,000 certified in any year had more of it certified from CIP growth; communities with less than $1,000,000 certified in any year had more of it certified from residential growth;
- For FY2013, the largest amounts certified were for Boston ($28.3 million), Cambridge ($9 million), and Springfield ($5.9 million);
- For FY2013, the largest percentages of residential new growth applied to the levy limit were for Dover (99 percent), Groton (97 percent) and Mount Washington (96 percent).

Let's assume the following:

FY2014 Residential New Growth Value	$26,000,000
FY2014 CIP New Growth Value	$2,000,000
Subtotal Total Growth Value	$28,000,000
FY2013 Tax Rate for all Property Classes	x $12.00/000
FY2014 Total Current Fiscal Year New Growth	= $336,000

New Growth Adjustment

Certified new growth that included an extraordinary assessment on property or properties subsequently granted an abatement in large part, may be reduced by the Bureau of Local Assessment in any year. Any 2.5 percent increment added to that certified growth amount in any subsequent fiscal year may also be reduced. This levy limit component has affected less than ten communities over the last several fiscal years.

Let's assume that FY2012 certified new growth included $175,000 in tax dollars attributable to a parcel subsequently granted an abatement in large part and that a New Growth Adjustment of $150,000 was required by the Bureau of Local Assessment.

FY2012 Certified New Growth Adjustment	$150,000
2.5 Percent FY2013 Increment Adjustment	x then + $3,750
Subtotal	= $153,750
2.5 Percent FY2014 Increment Adjustment	x then + $3,844
FY2014 New Growth Adjustment	= $157,594

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Overrides: MGL c.59, s.21C (e,g) & Underrides: MGL c.59, s.21C (h)

The law enacted two types of adjustments in the levy limit that may be approved by the voters in a referendum: Overrides and Underrides.

Overrides

The first is an override, (MGL c. 59, s. 21C (g)), which permanently increases the levy limit beginning in the particular fiscal year indicated in the vote. A majority vote of the board of selectmen or town or city council (with the mayor's approval if required by law) may place an unlimited number of override questions on a regular or special municipal election ballot, but only three on a state biennial election ballot. Overrides may not be placed on the ballot by a town meeting vote or by any local initiative referendum procedure authorized by law. This first form of override:

- has specific wording written in the law which includes a dollar amount, purpose(s) and applicable fiscal year;
- may vote a permanent increase to the levy limit up to the levy ceiling;
- may be voted as a single question (with general or specific spending purposes), as multiple questions "pyramid style" (with different dollar amounts but same purpose(s), highest dollar amount voted prevails) or "menu style" funding different services or programs;
- requires a majority vote of the electorate for approval.

In a second form of override, (MGL c. 59, s. 21C (e)), which has not been voted since the 1980s, the tax levy is over the levy ceiling and a levy reduction equal to the lesser of: a.) 15 percent of the prior fiscal year's tax levy or b.) the amount by which the prior fiscal year's levy exceeds the current fiscal year's levy ceiling is required. This situation could occur in a community that taxed at its levy ceiling in one year and experiences a large assessed value reduction in the next. This form of override reduces the amount of required levy reduction and will be discussed more so in Part Two of this series.

Table 2 shows that there were 1,081 override votes taken from FY2004 to FY2013. Over the decade, the percentage of override losing votes exceeded winning votes and in only three fiscal years did the number of winning votes exceed losing votes.

Table 2 - Override Wins and Losses: FY2004 to FY2013

	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013	#	%
Wins	79	80	92	52	48	60	33	26	21	19	510	47%
Losses	81	79	78	88	53	81	28	30	31	22	571	53%
Totals	160	159	170	140	101	141	61	56	52	41	1081	100%

Fiscal Facts:

- 510 wins were voted by 155 communities (150 towns and five cities) and 571 losses were voted by 147 communities (135 towns and 12 cities);
- 59 percent of communities with winning votes had populations of under 10,000;
- 78 percent of communities with populations under 15,000 had winning votes;
- 52 percent of communities with losing votes had populations of under 10,000;
- 73 percent of communities with losing votes had populations of under 15,000;
- 62 percent of communities with losing votes also had winning votes.

Table 3 - Override Wins in Tax Dollars

Override Wins in Tax Dollars	
FY2004	$39,613,252
FY2005	$27,003,697
FY2006	$49,226,762
FY2007	$33,972,216
FY2008	$35,828,357
FY2009	$37,096,518
FY2010	$16,381,529
FY2011	$13,017,907
FY2012	$15,281,365
FY2013	$10,181,069

Fiscal Facts:

- For the past decade, the fiscal year with the largest total override amount was FY2006 with about $49.2 million and the smallest was FY2013 with about $10.2 million;
- Override winning vote amounts ranged from $6,490,000 for Arlington in FY2012 to $750 for Northfield in FY2006 and losing vote amounts from $8,459,000 for Dartmouth in FY2008 to $182 for Tolland in FY2006;
- The town with the most winning votes in the decade was Edgartown with 26 over eight fiscal years; the town with the most losing votes was Aquinnah with 27 over four fiscal years;
- 140 cities and towns did not take an override vote over the decade.

For our example, let's assume an FY2014 override vote passed for $100,000.

Underrides

Underrides permanently decrease the levy limit beginning in the particular fiscal year indicated in the vote. A majority vote by the board of selectmen, city or town council (with the mayor's approval if required by law) may place an unlimited number of underride questions on a regular or special municipal election ballot, but only three on a state biennial election ballot. Underrides may be placed on a ballot by a local referendum procedure authorized by charter or special act. An underride: a.) has specific wording written in MGL c. 59, s. 21C (h) which includes a dollar amount, and applicable fiscal year; b.) may be voted in any amount; and c.) requires a majority vote of the electorate for approval.

Fiscal Facts:

- Eight underride votes were taken in seven different communities (six towns and one city);
- Seven winning votes ranged from a required reduction of $1,032,724 for Lancaster in FY2005 (won by one vote) to $10,833 for Gill in FY2005;
- The losing vote was for $1,000,000 in Amesbury for FY2008.

Now, let's assume an FY2014 underride vote passed for $20,000.

Levy Limit Calculation for FY2014:

Step 1:	The FY2013 Base (Prior Year Levy Limit)	$10,000,000
Step 2:	Add Amended Prior Fiscal Year New Growth	+ $3,500
Step 3:	Subtotal Step 1 and Step 2	= $10,003,500
Step 4:	Multiply subtotal by 2.5 percent	x then + $250,088
Step 5:	Add FY2014 New Growth	+ $336,000
Step 6:	Subtract FY2014 New Growth Adjustment	- $157,594
Step 7:	Add FY2014 Override	+ $100,000
Step 8:	Subtract FY2014 Underride	- $20,000
Step 9:	Subtotal Steps 3 through 8	= $10,511,994
Step 10:	Compare to FY2014 Levy Ceiling	$xx,xxx,xxx

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Conclusion

With the exception of amended prior fiscal year new growth, the new growth adjustment, and certain perfecting amendments passed soon after the law's enactment, the levy limit's calculation has remained to this point much the same. Comparing the preliminary (incremental) levy limit to the levy ceiling, such as in Steps 9 and 10 above, will be the focus of Part Two of this series.

For further information, see the Division of Local Services' Publications Levy Limits: A Primer on Proposition 2 1/2 and Proposition 2 1/2 Ballot Questions - Requirements and Procedures.

Part 2: Prop 2 1/2's Levy Limit Components and a Statistical Review over the Last Decade - Has Your Levy Limit "Hit the Ceiling?"

Brenda Cameron - Bureau of Local Assessment Deputy Chief, Steve Sullivan - Bureau of Local Assessment Boston Office Certification Supervisor and Tony Rassias - BOA Deputy Director

This is the second of a three part series reviewing Prop 2 1/2's levy limitation components along with statistics from FY2004 to FY2013. Part Two will focus on levy ceilings, how override capacity has diminished in recent fiscal years, what it means to "hit the ceiling," and why assessors and budget officers in certain cities and towns should be concerned. It will also include suggestions from the Bureau of Local Assessment and Bureau of Accounts and a continuation of an FY2014 levy limit calculation. The levy limit calculation shown in all Parts is organized on the basis of the levy limit worksheet found on Gateway's levy limit report page.

The levy limitation began as a two-tiered calculation: (1) a 2.5% factor increase or 15% or lesser percentage decrease from the FY1981 tax levy and (2) a 2.5% or lower percentage factor as determined by FY1979's property tax multiplied by the full and far cash valuation of the city or town. Where a full and fair cash value was not available, an equalized value was used. Many communities found this an added incentive to assess at full and fair cash value. - A Sketch of the History of the Massachusetts Bureau of Accounts and Related Matters in the Growth and Development of Municipal Finance by Anthony A. Rassias

In November of 1980, the people of Massachusetts passed by ballot vote Proposition 2 1/2 (Chapter 580 of 1980), a law that, among other things, placed constraints on city and town property tax levies beginning in FY1982.

Since that time, these levies have been limited by the law's provisions and approved by the Bureau of Accounts as part of the annual tax rate certification process. Even 33 years since its passage, Prop 2 1/2 initiates considerable discussion and debate.

Levy Ceilings

The property tax levy is the revenue a community raises through real and personal property taxes each fiscal year when it sets its tax rate. The law established three types of annual levy limits: a levy limit, a levy ceiling and a maximum allowable levy. The levy limit is incremental and allows a permanent but controlled annual increase to the tax levy. The levy ceiling caps the levy limit for that fiscal year at 2.5 percent of the current fiscal year's total assessed full and fair cash value for real and personal property. The levy limit may be increased or decreased by locally adopted referenda, but may not exceed the levy ceiling. The levy ceiling may be increased temporarily by certain locally adopted exclusions. The maximum allowable levy is the maximum amount of property tax a community may raise in a fiscal year.

When Prop 2 1/2 was first implemented, many levy ceilings were calculated at 2.5 percent of updated biennial equalized values. Cities and towns that had not yet assessed their property at full and fair value found this an added incentive to do so because, at that time, the higher the levy ceiling, the less the required levy reduction and the more chance for a levy limit increase from the prior fiscal year.

The difference between the levy limit and levy ceiling is called override capacity. When override capacity exists, a city or town may override the levy limit by local ballot and maximize it up to 2.5 percent of total assessed full and fair cash value. When override capacity has been depleted, there is no credit for an override, the levy limit becomes the levy ceiling, and the levy limit is said to have "hit the ceiling."

The levy ceiling is an annual calculation reflecting market value fluctuation of real and personal property and the addition and removal of property from the tax roll.

As the below chart shows, levy ceilings increased from $18.3 billion in FY2004 to $24.8 billion in FY2008. Feeling the effects of the depressed Massachusetts real estate market, these ceilings began to slide beginning in FY2009. Levy ceilings have fallen almost 8.8 percent from $24.8 billion in FY2008 to $22.6 billion in FY2013. For the decade, however, ceilings increased by 23.4 percent.

Chart 1 - Levy Ceilings

Source: DLS Data Bank

Let's assume a total taxable assessed value of $421,200,000.

Table 1(below) reviews the percent change to levy ceilings by category. Note that from FY2004 to FY2008, levy ceilings increased as a percentage more so in communities with less than a $10 million ceiling while from FY2008 to FY2013, total levy ceilings in dollars decreased as a percentage more so in communities with a ceiling between $10 million and less than $50 million.

Table 1 - Percent Change to Levy Ceilings by Category

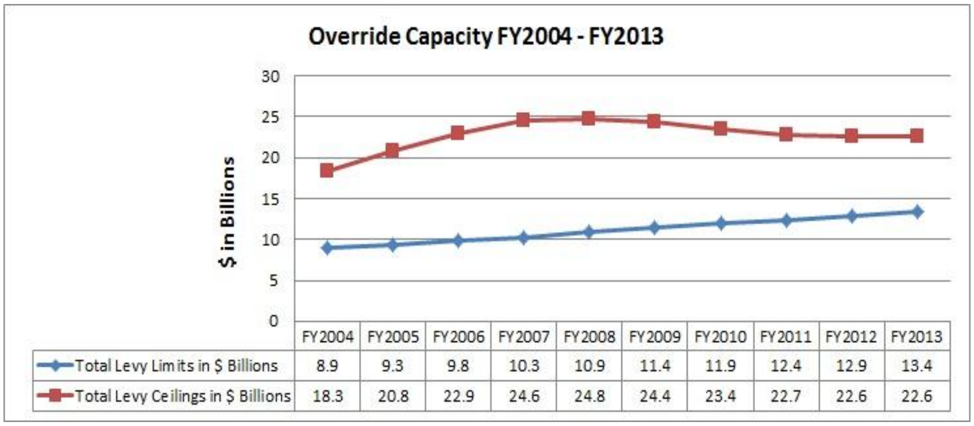
% Changes to Levy Ceilings		
Category	FY2004 to FY2008	FY2008 to FY2013
< $10 million	56.3%	-4.0%
$10 million to < $50 million	41.3%	-11.6%
$50 million to < $100 million	36.7%	-10.3%
>$100 million	31.2%	-7.7%

Source: DLS Data Bank

Override Capacity: FY2004 - FY2013

Chart 2 (below) shows that the combination of rising levy limits and falling levy ceilings from FY2004 to FY2013 has compressed override capacity to its narrowest point in the decade in FY2013.

Chart 2 - Override Capacity



	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013
Total Levy Limits in $ Billions	8.9	9.3	9.8	10.3	10.9	11.4	11.9	12.4	12.9	13.4
Total Levy Ceilings in $ Billions	18.3	20.8	22.9	24.6	24.8	24.4	23.4	22.7	22.6	22.6

Source: DLS Data Bank

"Hitting the Ceiling"

Although Chart 2 shows in total that there is sufficient override capacity to sustain cities and towns for the time being, this is not necessarily the case for individual cities and towns. For some, the levy limit has risen faster than the levy ceiling to the point where it has collided with the ceiling. In other cases, the levy ceiling has fallen either due to market conditions or to an extraordinary circumstance, to the point where it has collided with a rising levy limit. In any case, the levy limit is said to have "hit the ceiling."

When collisions occur, the city or town potentially loses a portion of the Base (prior year levy limit) in the calculation, but is more likely to lose a portion or the entire amount of:

- the annual 2.5 percent increase;
- amended prior fiscal year new growth;
- current fiscal year new growth; and/or
- any current fiscal year override (not including exclusions - to be discussed more in Part Three).

Continued loss of taxable assessed value exacerbates the matter and there is no process to recoup these losses. Despite "hitting the ceiling," a city or town may still be subject to a new growth adjustment or underride vote as described in Part 1 of this series.

Table 2 (below) shows the number of cities and towns that have "hit the ceiling" over the last decade and the number of municipalities approaching their levy ceiling, where the levy limit is greater than 90 percent of the ceiling.

Table 2 - Cities and towns that have "hit the ceiling" or where the ceiling is approaching

Fiscal Year	"Hit the Ceiling"	Ceiling is Approaching
2004	1	4
2005	1	0
2006	0	1
2007	0	1
2008	0	1
2009	0	1
2010	0	2
2011	2	2
2012	1	5
2013	4	5

Source: DLS Data Bank

Override for Cities and Towns that have "hit the ceiling"

In a second form of override which has not been voted since the 1980s, the tax levy is over the levy ceiling and a levy reduction equal to the lesser of (a) 15 percent of the prior fiscal year's tax levy or (b) the amount by which the prior fiscal year's tax levy exceeds the current fiscal year's levy ceiling is required.

This situation could occur in a community that taxed at its levy ceiling in one year and experiences a large assessed value reduction in the next. By two-thirds vote, the board of selectmen or town or city council (with the mayor's approval if required by law) may place a question or questions on a special election ballot to reduce the amount of the required reduction. This override:

- has specific wording written in MGL c. 59, s. 21C(e) which includes a dollar amount and applicable fiscal year;
- may include two questions on the same ballot with only one specifying an amount greater than one-half the required reduction. If both questions are approved, the one requiring a two-thirds vote prevails;
- requires a majority vote for approval if the amount is less than one-half the required reduction and a two-thirds vote if the amount is greater than one-half.

Should Assessors and Budget Officers be concerned?

For most cities and towns, the levy limit, not the levy ceiling, is the immediate concern. But for others, the levy ceiling is their concern and without an immediate and positive change in the real estate market, a limit collision already has occurred or may occur. For FY14, there are indications that the number of cities and towns "hitting the ceiling" and the number for those where the ceiling is approaching will both likely increase.

Assessors and budget officers should review their city or town's levy ceiling situation for FY2014 and FY2015. The good news is that apart from the partial or total incremental loss, a limit collision may not be cause for budget panic if the tax levy is set comfortably below the ceiling and/or if sufficient locally approved exclusions to the ceiling (the next focus of this series) apply. For some FY2014 communities, this is the case. For others, it is not.

Our Suggestions

To cities and towns that levy a property tax to their levy ceiling ("tax to the max"), have no exclusions and a limit collision has occurred in FY2014 or may occur in FY2015, the Bureau of Local Assessment and Bureau of Accounts offer some suggestions.

Bureau of Local Assessment:

1. Communicate. Assessors must make budget officers aware of a possible collision as soon as possible to prevent further complications such as a delay in setting the tax rate;
2. Stay vigilant. Be sure to capture the value of new construction within your boarders and maintain a data collection program to ensure that the most current/accurate data is applied in the valuation process;
3. Assess properly. All taxable real and personal property must be assessed at 100 percent of full and fair value on an annual basis and keep in mind certain properties such as power generating facilities, and others granted TIFs and DIFs that are allowed special value arrangements.

Bureau of Accounts:

1. Communicate. Budget officers must become aware of the assessors' value determination as soon as possible to properly prepare the budget and consider alternative revenue sources if need be;
2. Plan ahead. Because the property tax is the largest local government revenue source, a good contingency plan discussed with the city or town's financial management team is necessary;

3. Build reserves. "Rainy day" funds such as free cash and stabilization for the General Fund or retained earnings for the enterprise fund should be supplemented and appropriated to support spending if needed.

Levy Limit Calculation for FY2014: Continued from Part 1

Levy Limit Calculation for FY2014: Continued from Part 1

Step 1:	The FY2013 Base (Prior Year Levy Limit)		$10,000,000
Step 2:	*Add* Amended Prior Fiscal Year New Growth	+	$ 3,500
Step 3:	*Subtotal* Steps 1 and 2	=	$10,003,500
Step 4:	*Multiply* subtotal by 2.5 percent	x then +	$ 250,088
Step 5:	*Add* FY2014 New Growth	+	$ 336,000
Step 6:	*Subtract* FY2014 New Growth Adjustment	-	$ 157,594
Step 7:	*Add* FY2014 Override	+	$ 100,000
Step 8:	*Subtract* FY2014 Underride	-	$ 20,000
Step 9:	*Subtotal* Steps 3 through 8	=	$10,511,994
Step 10:	*Compare* to current fiscal year's levy ceiling *@ 2.5 percent x $421,200,000*	=	$10,530,000

Step 10 now reveals that the community has a levy limit which is under the levy ceiling by $18,006. This is the community's FY2014 override capacity. If the calculation stopped here, the following fiscal year's levy limit Base would begin with $10,511,994.

(Had Step 10 been calculated @2.5 percent of $420,000,000, or $10,500,000, the levy limit would have "hit the ceiling," a portion of the calculation would have been lost, and the following fiscal year's levy limit Base would begin with $10,500,000.)

Step 11:	Calculate the Maximum Allowable Levy		$10,511,994

Conclusion

For most cities and towns, "hitting the ceiling" may never apply. But for others, the matter is serious enough to affect public services. As it was once said, "to be forewarned is to be forearmed." For cities and towns where hitting the ceiling could occur, consider yourselves forewarned and please contact either the Bureau of Local Assessment or Bureau of Accounts if you need further assistance.

The final part of this series will focus on the components of the maximum allowable levy and will complete the FY2014 maximum allowable levy calculation. For further information, see the Division of Local Services Publications: Levy Limits: A Primer on Proposition 2 1/2 and Proposition 2 1/2 Ballot Questions - Requirements and Procedures. Part One of this series is available in the June 19th, 2014 edition of City & Town.

Part 3: Proposition 2 1/2's Levy Limit Components and a Statistical Review Over the Last Decade: Does Your Community "Tax to the Max?"

Joe Markarian - Former MDM/TAB Director of Financial Management Assistance, Tom Guilfoyle - BOA Supervisor of Accounting and Tony Rassias - BOA Deputy Director

This is the third and final part in this series reviewing Prop 2 1/2's levy limitation components along with statistics from FY2004 to FY2013. Part Three will focus on the maximum allowable levy, the common and not-so-common exclusions that allow the levy limit and levy ceiling to be exceeded, completion of an FY2014 maximum allowable levy calculation, and finally tax levies and "excess levy capacity." The levy limit calculation shown in all parts is organized on the basis of the levy limit worksheet found on Gateway's levy limit report page.

The passage of Proposition 2 1/2 on the November 1980 ballot was enormous. The new law changed the way cities, towns and districts budget to the present day. - A Sketch of the History of the Massachusetts Bureau of Accounts and Related Matters in the Growth and Development of Municipal Finance by Anthony A. Rassias

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Since that time, these levies have been limited by the law's provisions and approved by the Bureau of Accounts as part of the annual tax rate certification process. Even 33 years since its passage, Prop 2 1/2 initiates considerable discussion and debate.

The Maximum Allowable Levy

The property tax levy is the revenue a community raises through real and personal property taxes each fiscal year when it sets its tax rate. The law established three types of annual levy limits: a levy limit, a levy ceiling and a maximum allowable levy. The levy limit is incremental and allows a permanent but controlled annual increase to the tax levy. The levy ceiling caps the levy limit for that fiscal year at 2.5 percent of the current fiscal year's total assessed full and fair cash value for real and personal property. The levy limit may be increased or decreased by locally adopted referenda, but may not exceed the levy ceiling. The levy ceiling may be increased temporarily by certain locally adopted exclusions. The maximum allowable levy is the maximum amount of property tax a community may raise in a fiscal year.

The maximum allowable levy may or may not be greater than the levy ceiling. If the community has not voted any locally adopted exclusions to the levy limit, the lesser of the levy limit or levy ceiling becomes the maximum allowable levy. In any case, the actual tax levy for the fiscal year, as reported on the annual Tax Rate Recapitulation form, cannot exceed the maximum allowable levy.

Exclusions that Impact the Maximum Allowable Levy

Apart from the debt and capital expenditure exclusions, the other maximum allowable levy components are not-so-commonly used. All of these components are considered "temporary" because the applicable dollar amounts (a) are included in the annual total of tax dollars to be raised, but are not included in the Base (prior year levy limit) for calculating the following fiscal year's tax limitation and (b) have a future end date, although that date may be one year or well into the future.

Debt Exclusion: MGL c. 59, s. 21C(j,k)

The two types of debt exclusions that may be voted are:

1. For debt service on city, town and assessed regional debt incurred prior to November 4, 1980 (called Pre-Prop 2 1/2 debt);

2. For debt service on city, town or assessed regional debt issued after November 4, 1980, (initially called Post-Prop 2 1/2 debt, now simply called the debt exclusion).

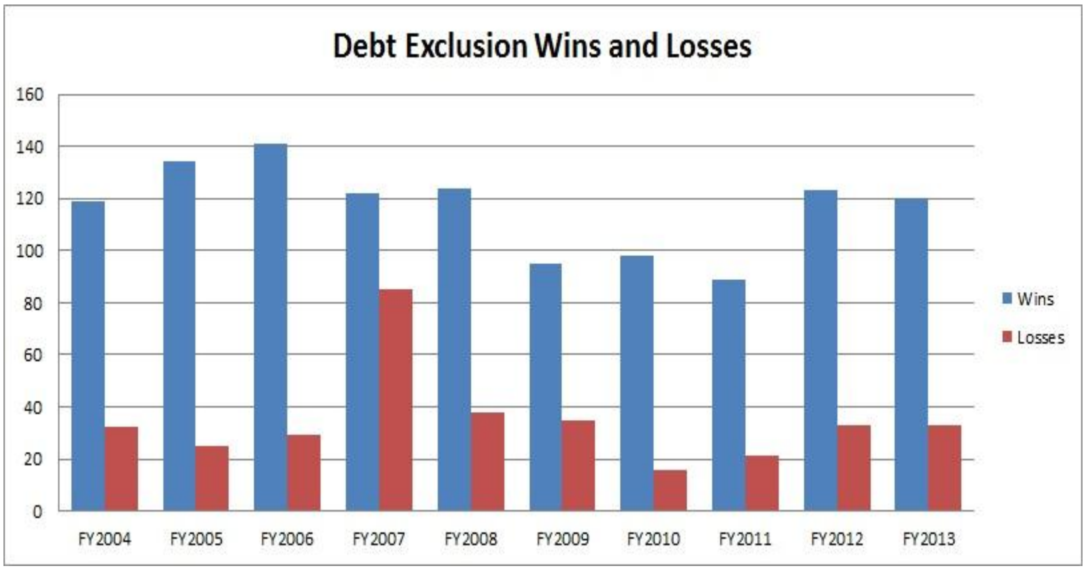
This section will review only Post-Prop 2 1/2 debt exclusion votes. Few pre - Prop 2 1/2 debt exclusion votes were taken and none since the mid-1980s.

The debt exclusion has been and continues to be by far the most frequently used form of exclusion. A debt exclusion requires a two-thirds vote of the board of selectmen, or town or city council (with the mayor's approval if required by law) to be placed on a ballot. A majority vote of the electorate is required for approval. Once voted, the debt exclusion allows the community to raise the additional tax revenue needed to pay debt service for each fiscal year on the borrowing issued to fund the specified project until the debt is retired. The excluded amount is offset by any reimbursements and certain premiums received per Bureau instruction. See Bulletin 2013-01B. The debt exclusion:

- must be presented using wording specified by the law which includes only the borrowing purpose;
- applies to temporary or permanent debt service;
- may be negative if reimbursements in any year exceed debt service;
- must be reserved for the following fiscal year if the amount of debt service excluded exceeded the amount expended;
- is reduced if excluded debt proceeds are transferred to a non-excluded project.

Chart 1 indicates debt exclusion votes taken between FY2004 and FY2013. There were 1,512 debt exclusion votes taken, of which 1,165 or 77 percent were wins and 347 or 23 percent were losses.

Chart 1 - Debt Exclusion Wins and Losses: FY2004 to FY2013



Source: DLS Data Bank

Fiscal Facts:

- Total excluded dollars grew about 25 percent from $314 million in FY2004 to $391.7 million in FY2013;

- For the decade, the largest total debt exclusion was in FY2013 for Wellesley ($10,322,960) and the smallest, also in FY2013, was for Wakefield ($120);

- Of the 120 winning votes for FY2013, 65 were for schools, 17 for public safety, 15 for construction and repairs to town owned buildings, 12 for public works and 11 for assorted other purposes;

- Of the 33 losing votes for FY2013, eight were for schools, seven for public works, five for public safety, six for construction and repairs to town buildings, and seven for assorted other purposes;

- For FY2013, 287 or 82 percent of all cities and towns had at least one active debt exclusion, which when combined, totaled about $391.7 million.

Let's assume an FY2014 debt exclusion of $550,000.

Capital Expenditure Exclusion - MGL c. 59, s. 21C (i1/2)

Enacted by Chapter 562 of 1986, this exclusion has been less popular than the debt exclusion, but has been used more often than other maximum allowable levy components. It allows additional funds to be raised for any item for which the city or town could borrow, but has chosen to fund by appropriation, or for the city or town's apportioned share of a regional capital expenditure. This exclusion requires a two-thirds vote of the board of selectmen, or town or city council (with the mayor's approval if required by law) to be placed on a ballot. A majority vote of the electorate is required for approval. Once voted, the capital expenditure exclusion allows the community to raise the amount included in the vote, or the amount appropriated, whichever is less, minus any state or federal reimbursement received for the acquisition or purpose for the year voted. In addition, the capital expenditure exclusion:

- must be presented using wording specified by law including a dollar amount, purpose(s) and fiscal year;

- authorizes a temporary tax increase to the lesser of the levy limit or levy ceiling;

- has the same wording as an override and must be properly distinguished to the electorate.

Table 1 indicates capital expenditure exclusion votes taken between FY2004 and FY2013. In total, there were 318 votes taken; 219 or 69 percent were wins and 99 or 31 percent were losses.

Table 1: FY04 - FY13 - Capital Expenditure Exclusion Wins and Losses

Capital Expenditure Exclusion Votes - FY2004 to FY2013

	FY2004	FY2005	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011	FY2012	FY2013	#	%
Wins	20	34	31	23	26	24	25	15	10	11	219	69
Losses	11	16	12	14	15	9	7	7	7	1	99	31
Totals	31	50	43	37	41	33	32	22	17	12	318	100

Source: DLS Data Bank

Fiscal Facts:

- For the decade, the largest number of capital exclusion votes was in FY2009 at $5,770,361 and the smallest in FY2004 at $2,200,283;

- For the decade, about 67 percent of wins were for public safety, public works, schools and road repairs;

- For the decade, the largest capital exclusion vote was $2,360,000 for Dennis in FY2009 and the least was $5,000 for Cummington in both FY2011 and FY2012;

- For FY2013, there were 11 winning votes taken by 10 towns totaling $3,050,000;

- For FY2013, winning votes included three for public safety, two for library, two for public works and three for assorted other purposes. The lone loss involved renovation of an athletic field.

Let's assume an FY2014 capital expenditure exclusion of $100,000.

Other Adjustment - Cape Cod Commission

Chapter 716 of the Acts of 1989 created the Cape Cod Commission, a regional planning and land-use regulatory agency that serves Barnstable county. All Barnstable county towns have individually voted to become members of the Commission. Pursuant to s. 18 of the enabling Act, the annual assessment by the Commission to a member is exempt from Prop 2 1/2 and no further local action is necessary.

Let's assume for FY2014 that this provision is not applicable, $0.

Other Adjustment - Chapter 111 s. 127B1/2 and Other Special Legislation

Chapter 111, s.127B 1/2 exempts from Prop 2 1/2 any city or town tax levy appropriation or debt service for the purpose of municipal removal of a residential underground fuel storage tank, the removal of dangerous levels of lead paint as determined by MGL c. 111 s. 194, or repair, replacement or upgrade of a home's septic system required by MGL c. 21A s. 13. No further local action is necessary. For FY2013, only Marion and Wrentham used the Chapter 111 exclusion.

Special legislation approved for Wellesley in 2007 excluded funding for its Other Post-Employment Benefits obligations.

Let's assume for FY2014 that these provisions are not applicable, $0.

Other Adjustment - Regional Refuse Management Districts

The Greater New Bedford Refuse Management District (Chapter 652 of 1987) and the Martha's Vineyard Regional Refuse Disposal District (Chapter 303 of 1985) assess debt service upon their respective member communities and pursuant to their legislation, their debt service assessments are excluded from Prop 2 1/2. No further local action is necessary.

For FY2013, Dartmouth, a member of the Greater New Bedford District and four members of the Martha's Vineyard District used this exclusion.

Let's assume for FY2014 that these provisions are not applicable, $0.

The Water/Sewer Rate Shift, MGL c. 59 s. 21C(n)

The board of selectmen, the town or city council (with the mayor's approval where required by law) may vote to exclude water and sewer debt service. No further local action is required. If voted, the city or town:

- recovers water and sewer debt service costs from the property tax rather than from user charges;
- must then reduce its water and sewer charges by the amount of the debt service being transferred to the tax levy;
- may choose either an all taxpayers or residential taxpayers only option.

Once adopted, the percentage or stated amount of the exclusion remains the same unless changed by a new vote of the board of selectmen, town or city council (with the mayor's approval where required by law). IGR 93-207 has further details.

For FY2013, there were 13 Water/Sewer Rate Shifts totaling about $13.3 million. One community, Winchester, used the residential taxpayers-only option.

Let's assume that the FY2014 water/sewer debt shift was voted as $150,000.

Calculating the Maximum Allowable Levy: Assumptions Continued from Part 2

Step 1:	The FY2013 Base (Prior Year Levy Limit)		$10,000,000
Step 2:	*Add* Amended Prior Fiscal Year New Growth	+	$ 3,500
Step 3:	*Subtotal* Steps 1 and 2	=	$10,003,500
Step 4:	*Multiply* subtotal by 2.5 Percent	x then +	$ 250,088
Step 5:	*Add* FY2014 New Growth	+	$ 336,000
Step 6:	*Subtract* FY2014 New Growth Adjustment	-	$ 157,594
Step 7:	*Add* FY2014 Override	+	$ 100,000
Step 8:	*Subtract* FY2014 Underride	-	$ 20,000
Step 9:	*Subtotal S*teps 3 through 8	=	$10,511,994
Step 10:	*Compare* to current fiscal year's levy ceiling @ 2.5 percent of $421,200,000	=	$10,530,000

If no further components are applicable, the tax levy reported on the Tax Rate Recapitulation form cannot exceed the lesser amount shown in either Step 9 or 10 above. Otherwise, the calculation continues with the lesser amount.

From Step 9:			$10,511,994
Step 11: Add FY2014 Debt Exclusion	+	$	550,000
Step 12: Add FY2014 Capital Expenditure Exclusion	+	$	100,000
Step 13: Add FY2014 Other Adjustment – Cape Cod Comm.	+	$	0
Add FY2014 Other Adjustment – Chapter 111 s127B½	+	$	0
Add FY2014 Other Adjustment – Special Legislation	+	$	0
Add FY2014 Other Adjustment – Reg. Refuse Mgt.	+	$	0
Step 15: Add FY2014 Water/Sewer Debt Shift	+	$	150,000
Step 16: Calculate FY2014 Maximum Allowable Levy	=		$11,311,994

Steps 11 through 15 recur annually, but do not add to the Base for the following fiscal year.

Step 16 reveals the maximum allowable levy which the tax levy reported on the Tax Rate Recapitulation form cannot exceed.

The Tax Levy and Excess Levy Capacity

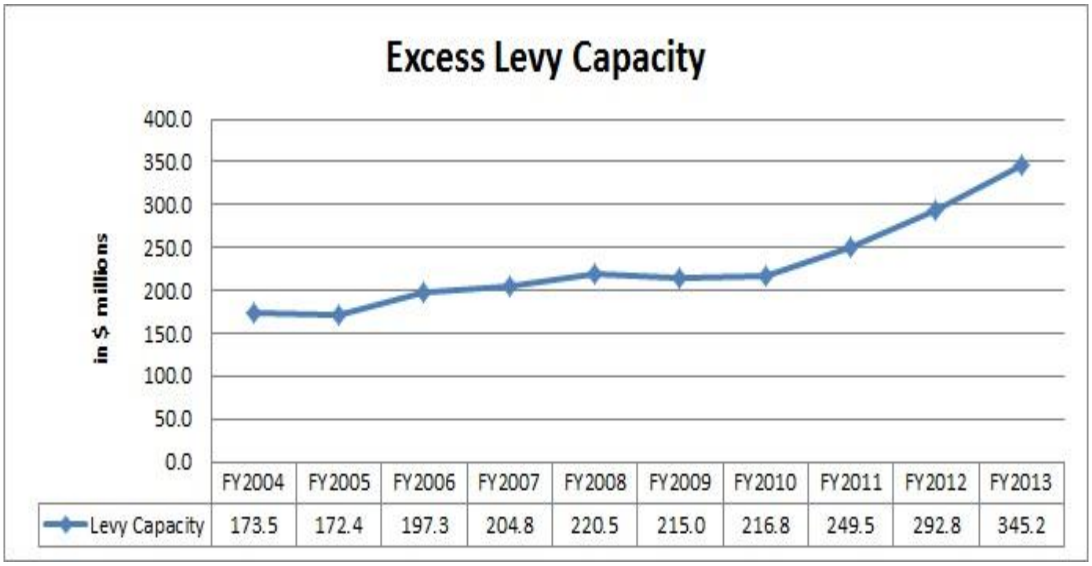
The tax levy is the annual amount of taxes assessed upon real and personal property in the city or town as reported on the Tax Rate Recapitulation form. The levy cannot exceed the maximum allowable levy as calculated above. The dollar difference, or "excess levy capacity," is the amount by which the community may have legally levied, but chose not to do so.

Depending upon the actual tax levy amount, excess levy capacity may or may not be forever lost. For example, if this fiscal year's actual tax levy is $10,500,000, this fiscal year's excess levy capacity is $811,994 ($11,311,994 - $10,500,000). The difference between $10,511,994 and $10,500,000, or $11,994, is lost for the current fiscal year but returns in the following fiscal year as part of the Base that begins with $10,511,994. The remainder, $800,000, is lost forever.

Chart 2 shows the growth in excess levy capacity from FY2004 to FY2013. The greatest amount of excess levy capacity during this decade was in

FY2013 at $345.2 million and the least amount in FY2005 at $172.4 million.

Chart 2 - Excess Levy Capacity: FY2004 to FY2013



Source: DLS Data Bank

Fiscal Facts:

- For the decade, the greatest amount of excess levy capacity was for Cambridge, in FY2013, at $104,103,959 and the least was for Freetown, in FY2006, at $11;
- For the decade, the median average for excess levy capacity was about $24,000;
- For FY2013, the median average for excess levy capacity was about $52,000;
- For FY2013, five communities had excess levy capacity greater than $10,000,000; Marlborough had greater than $20,000,000 and Cambridge had greater than $100,000,000.

Conclusion

This concludes the three Part series on Prop 2 1/2's levy limit components along with statistics from FY2004 to FY2013. Please visit the Division of Local Services' website and create your own customized financial, demographic and economic reports. You can also review publications such as Informational Guideline Releases, Bulletins and other annual guidance for more details on tax levies, levy limits, levy ceilings, new growth, ballot questions and more.

For further information, see the Division of Local Services Publications Levy Limits: A Primer on Proposition 2 1/2 and Proposition 2 1/2 Ballot Questions - Requirements and Procedures.