

## GENERAL QUESTIONS ON REVENUES AND TAXES

### What is an override?

In November 1980, Massachusetts voters approved referendum Proposition 2 ½, which requires that voters must be consulted and approve certain increases to the tax levy. Prop. 2 ½ took its name from the twin limits it imposed on property taxes. The primary limitation is that the total tax levy of a city or town cannot exceed 2.5 percent of the full and fair cash value of all taxable property. A second limitation is that the increase in the annual tax levy beyond the 2.5 percent plus new construction requires voter approval.

A Proposition 2 ½ override gives Massachusetts cities and towns the opportunity to increase their level limits beyond the constraints of Proposition 2 ½. It allows a community to vote on the assessment of taxes in excess of the automatic annual 2.5 percent increase and any increase due to new growth. If an operational override is passed, a permanent increase is made to the level limit of a community, which, as part of the level limit base, increases at a rate of 2.5 percent each year.

### What is the difference between an operational override and a debt-exclusion override?

Operational overrides permanently increase the tax rate to provide funds for a city's or town's operating budget. Operational overrides are frequently needed to help pay for the services that residents have come to expect to receive from their local government departments — services that might be compromised or lost if the override fails.

Debt-exclusion overrides enable a city or town to borrow money to pay for a capital project such as the construction or renovation of a town building (such as the library) or the purchase of a major piece of property. Taxes are raised only for a limited period, until the debt is repaid. The increase in taxes will vary over the period of loan. Generally, the tax increase will be small in the first few years, will rise to its peak over the next few years, and decrease in the last few years, disappearing entirely when the debt is repaid.

Debt-exclusion overrides are sometimes called capital overrides.

### If our tax increases are capped by Proposition 2 1/2, why did my tax bill increase so much last year?

The total increase in taxes received by the Town is capped. However, as property values changes, the relative share of the taxes paid by each property owner changes. The amount of your taxes is determined by the value of your property relative to that of your neighbors in the Town. When the Town does a general revaluation of properties, most people's values increase, sometimes significantly (as happened this year). If everyone's property went up at the same rate, each person's taxes would only increase to cover their share of the increased tax levy (2 1/2% + any increase in debt exclusion payments). Each person's taxes would then also increase exactly the same amount.

But, if one family's property went up 30%, while another family's went up 10%, the first family's property would now represent a larger portion of the total value of the Town. Therefore, they will be paying proportionally more of the total bill than their neighbors and their taxes will go up faster.

Here's an example of how differences in revaluation might change one family's taxes from 2005 to 2006. There are three amounts representing four different valuation increases from 10% to 30%. (17% is the increase in the average home value).

Increase in assessed value 2005-06	Year	Assessed Value	Tax Rate	Taxes	\$ Increase in Taxes	% Increase in taxes
	2005	574,000	9.61	\$5,516		
0%	2006	574,000	8.80	\$5,051	(-\$465)	(-8.4%)
10%	2006	631,400	8.80	\$5,556	\$40	0.7%
17%	2006	671,580	8.80	\$5,910	\$394	7.1%
20%	2006	688,800	8.80	\$6,061	\$545	9.9%
30%	2006	746,200	8.80	\$6,657	\$1,050	19.0%

Put another way, if your house didn't change in value from 2005 to 2006, your taxes would be 8.4% **lower** this year than last. If your house increased 10% in value, you're paying just 0.7% **more** this year than last. If your house increased 20%, you're paying 9.9% **more** in taxes and if your house increased 30% in value, you're paying 19.0% more. The percentages apply whatever the actual value of your property is.

### What exactly can only go up 2 1/2% each year?

Each year, the Town can increase the amount of money it raises through the property taxes (this is known as the "levy") by 2 1/2%. The increase is calculated as 2 1/2% of the previous year's amount. This total is spread over the property owners of the Town, based on their share of the total property value.

### Are there other increases in the total levy?

Yes. When there is new growth in the Town (see section below for a definition of "new growth"), the Town can further increase the levy to account for that growth. The reason is that new growth often drives a demand for new services, so the town should be able to generate new revenue to pay for those new services.

For example, there was \$127 million in new growth in Needham this past year. That amount of "new growth" is multiplied by the current year's tax rate to calculate the dollar amount of "new growth" taxes the town can raise. For 2006, this came to \$1.6 million dollars. This dollar figure represents the amount the owners of these new and improved properties will pay.

This amount can vary significantly from year to year with the economy and building trends. For example, in 2005, the Town only gained \$1 million in revenue from new growth. As a percentage, that's 2.6% in 2006 but only 1.7% in 2005. Because of the time involved in the certification process, the new growth amount tends to lag the actual new growth (construction) itself by about eighteen months.

When the Town votes a "debt exclusion override", the amount necessary to pay down those debts each year is added to the levy before the total is spread over all the taxpayers but after the 2 1/2% increase is calculated. In 2006, for example, \$4,318,354 of the \$68,981,920 raised by the levy was "excluded debt" raised to pay for construction projects covered by debt exclusion overrides.

Finally, when the Town votes an "operational override," that amount gets added to the levy that year and becomes part of the base for the future.

### **What is "new growth"?**

New growth is defined as an addition to the value of the property in the Town. The value of that growth is provided by the Assessors to the State, which "certifies" the amount. Once the state has certified the new growth, the Town can tax it.

Some examples of new growth:

- A new house is built on vacant land, increasing the total value of the property (land plus house)
- A significant addition is made to a structure, increasing its value (an addition to a house, for example)
- A property is converted to a new use, increasing its value (from warehouse to office space, for example)
- A teardown of a small house and replacement by a bigger one. BUT, the amount of new growth is NOT equal to the sales price of the house. Rather, it will usually be the difference between the value of the old structure (not including the land) and the COST of building the new one.

Some things that are NOT new growth:

- Repairs to a property (like a new roof)
- Reassessment to reflect increased property values

### **Once the amount of the levy has been determined, how does that get spread among the property owners?**

Theoretically, the total amount raised is spread over the property owners based on how much they own. For example, if the total valuation of all the property in Needham were \$7 billion and your home were worth \$700,000, you would be responsible for paying 1/100 of 1 percent of the total levy. If the levy were \$70,000,000, your property taxes would come to \$7,000.

Unfortunately, it's a bit more complicated than that, because Needham is one of the communities that has adopted a "split rate." Under this provision of the law, commercial property owners actually pay more than residential property owners. Once the Selectmen determine how they want to split the taxes (currently, the commercial property owners pay 175% of their fair value, the maximum allowed by law) the resulting amounts of the levy are then spread across the total valuation for that class of property. That calculation sets the tax rate.

For example, for fiscal year 2006, the total residential valuation in Needham is \$6,200,927,943 and the residential share of the levy is \$54,568,168, so the residential tax rate is \$8.80 per thousand dollars of property ( $54,568,168 / \$6,200,927,943$ ). The commercial tax rate is \$17.16. As a result of the split rate, even though residential property represents 88% of the total property in Needham, the residential taxpayers pay only 79% of the taxes.

### **How much did the revenues to the Town from the property tax increase last year?**

The town raised \$56,685,264 from property taxes for fiscal 2003 and \$53,954,053 in 2002. This represents an increase of \$2,731,311, or 5%. Of that amount, just over half (53%) came from new growth.

### **How does the tax levy relate to the total revenue the Town generates each year? What are the sources of revenue for the Town of Needham?**

In fiscal year 2006, the town's total revenue is expected to be \$104,381,920. The breakdown of sources is as follows:

- **\$69.0 million** (66%) comes from the property tax levy
- **\$13.2 million** (12.7%) was raised for and can be used only by Enterprise Funds (such as water & sewer).
- **\$7.5 million** (7.2%) was raised through local receipts. The motor vehicle excise tax is the largest of these, representing just over 50% of the total. The balance of local receipts comes from various licenses, fees and fines.
- **\$6.6 million** (6.3%) in state aid, almost 2/3 of which is for education.
- **\$3.6 million** (3.2%) in "free cash". Since the Town is not allowed to spend more than it takes in, it typically has some unexpended funds at the end of each year. Those funds are known as "free cash", and once certified by the state, can be used for future spending.
- **\$1, 2 million** (1.2%) from the Community Preservation Act. This is the surcharge only; we will shortly start receiving matching funds from the state.

### **Why isn't that enough to run the town? Don't we have a spending problem?**

The Town's revenue has been capped for 26 years by Proposition 2 1/2. Even with new growth included (much of which places additional burden on the Town in the way of services provided), the Town's revenue from the property tax has increased at an average annual rate of only **4.6%** over the last 22 years. During that time, the Consumer Price Index has increased

at an average annual rate of **3.9%** and the median US household income has increased at a rate of **4.3%** nationally. Here in the Boston area, the per capita personal income in the Boston area has increased at an average annual rate of **6.1%**, while average wage growth in the Boston metro area over that period has been **5.6%** (Since most of the Town's expenses are for salaries, the increase in per capita income or wages more accurately reflects the actual inflation the Town experiences than the CPI, which measures goods and services). **Overall, depending on which measure you choose, the growth in the town's tax revenues either only slightly exceeds or is slightly less than the rate of inflation over 26 years – and that's a mark of good management.**

Now consider some of the other things that have changed in the last 26 years:

- Health care costs have risen much faster than inflation, especially in recent years
- Electricity and fuel costs have been increasing significantly, with a huge bump in 2005.
- In 1980, the Town hadn't built a new building in years. The only outstanding construction bond at that time was for a renovation to the Steven Palmer School in **1971**, eight years earlier. The town was spending about \$900,000 on debt service. Thirty-five years later, we are now beginning to address years of neglect by investing in new and renovated buildings. Debt service in FY 2006 is nearly \$10 million.
- In 1980, the town's budget for road maintenance was less than \$150,000. In 2003, that amount has increased to only \$240,000 and state aid for road repair and reconstruction had dropped 35% below its mid-nineties peak to \$467,000. Additional state and local funds since the 2003 override have helped, but that limited impact will erode next year, as cost increases of 30% or more for asphalt are reflected in a new contract.
- New laws and increased mandates, such as for Special Education and environmental protection and management, add costs that were not conceived of in 1980. The costs for the mandates falls very heavily on local taxpayers, despite commitments made when those mandates were created. For example, when the Congress passed the legislation mandating Special Education services, it committed to federal funding for 40% of the total cost. The \$10.6 billion in Special Education grants in 2006 is more than **\$14 billion** short of the 40% commitment.

2.5% yearly increases in the property tax, even supplanted by new growth revenues, can't possibly support those increased expenses. That's why the Town, as envisioned by the authors of Proposition 2 1/2, comes to the voters to ask for additional funds, either as operational or debt exclusion overrides.