CITY OF CAMBRIDGE • EXECUTIVE DEPARTMENT

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To The Honorable, the City Council:

The establishment of the FY13 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 FY13 property tax levy, property values and other supporting information.

OVERVIEW

I am pleased to inform you that the actual FY13 property tax levy of $316,947,770 reflects a $17,857,132 or 5.97% increase from FY12, which is lower than the estimated increase projected in May 2012. The FY13 Budget adopted by the City Council in May 2012 projected a property tax levy increase of $19.7 million, or 6.6%, to $318,818,195 in order to fund operating and capital expenditures. The FY13 operating budget has increased by 2.87%.

Based on a property tax levy of $316.9 million, the FY13 residential tax rate will be $8.66 per thousand dollars of value, which is an increase of $0.18, or 2.1% from FY12. The commercial tax rate will be $21.50, which is an increase of $0.74, or 3.6% from FY12. Both increases in the tax rate are less than FY12.

In May, I informed the City Council that the actual tax levy increase was likely to change. This was based on the possible use of additional non-property tax revenues, which would become available based on FY12 actual collections.

This assumption again proved correct. The use of additional non-property tax revenue and other adjustments have allowed an overall reduction of $1,870,425 from the original projected property tax levy. This is due to increased non-property tax revenues, which include $346,387 from hotel/motel and meals excise, $1,500,000 from increases to building permit revenues, $250,000 from parking fund revenues and $150,000 in other non property tax revenues. Also included is a reduction of $52,230 in overlay adjustments. A portion of these increases, totaling $428,192, are required to offset a net decrease in Cherry Sheet revenues, prior year overlay deficits and reductions in various revenues based on actual FY12 collections and revised estimates.

Tax Levy Changes	Amount
Additional Assessments /Revenue Reductions	+$428,192
Non-Property Tax Revenue	-$2,246,387
Overlay Adjustment	-$52,230
Net Decrease	**- $1,870,425**

This resulted in a final property tax levy for FY13 of $316,947,770, an increase of 5.97%. With approval of these recommendations, the eight-year average increase in the property tax levy will be 4.52%. In addition, the City Council approved a 0% increase in the FY13 water and sewer rate for the second consecutive year, this past March.

This recommendation includes the use of $11 million in reserve accounts to lower the property tax levy; $2 million from overlay surplus; and $9 million in Free Cash. It should be noted that the certified Free Cash amount of $115.8 million is the highest amount in the City's history and represents a $13.6 million increase over last year. Also, $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.

Additionally, I am recommending that $10 million from Free Cash, as was stated at the time of the budget, be appropriated to the City's Debt Stabilization Fund to offset anticipated debt service costs in the future for the City's major capital projects especially in relation to the Elementary School reconstruction plan. This appropriation will help stabilize tax levy increases related to these projects in future years. This practice of using the Debt Stabilization Fund to offset debt service costs has resulted in a successful capital projects program, while maintaining stable property tax levy growth in past years.

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.

Approximately 74.9% of residential taxpayers will see a reduction, no increase or an increase of less than $100 in their FY13 tax bill. In addition, another 15.8% of residential taxpayers will see an increase between $100 and $250. Therefore, a total of 90.7% of the residential taxpayers will see no increase or an increase of less than $250. This will be the eighth 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 national economic uncertainties, while maintaining city and school services that citizens have come to expect and while providing a strong capital improvement program highlighted by 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.

TABLE I
Change in the Residential Tax Bills*

Change in Tax Payment	Number of Parcels	Percentage	Cumulative %
Less than $0	4,123	19.5%	-
> $0 and less than $100.00	11,735	55.4%	74.9
>$100.00 less than $250.00	3,340	15.8%	90.7
>$250.00 and less than $500.00	1,026	4.8%	95.5
Greater than $500.00	948	4.5%	100%
Totals	**21,172**	**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 determined property values and property tax rates for FY13. 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 5.97% increase in the property tax levy required to balance the FY13 Budget. In addition, the FY13 Adopted Budget reflects a 2.87% 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 FY13, commercial property owners will pay 65.4% of the property tax levy, the same share as in FY12. Consequently, residential property owners' share of the FY13 tax levy is 34.6%, also the same as in FY12.

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 2011, which is the basis of the FY13 property assessment, total residential property values have moderated (approximately 3.65% increase overall). Total commercial property values have also increased by 1.17%. 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 FY13, 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*

	FY12 Value	FY12 Tax Bill	FY13 Value	FY13 Tax Bill	Dollar Change	Percent Change
Single Family	$686,200	$4,139	$699,000	$4,298	$159	3.84%
Condominium	$366,700	$1,430	$375,300	$1,495	$65	4.55%
Two Family	$644,600	$3,786	$649,100	$3,866	$80	2.11%
Three Family	$728,900	$4,501	$732,300	$4,586	$85	1.89%

* Includes Residential Exemption

CITY-WIDE ASSESSED VALUES

FY13 values are based on market activity that occurred during calendar year 2011, during which the overall valuation of the City's residential property increased by a modest 3.65% and the overall valuation of commercial property increased by 1.17%. 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 FY13, the total assessed value of taxable property in the City of Cambridge equals $25,213,972,501, a 3.14% increase over FY12 values. The actual FY13 total assessed values are greater than the projections presented to the rating agencies in January 2012.

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 FY13 the market for both commercial and residential properties has increased slightly, not unlike most of the Greater Boston area, resulting in the continuation of a tax distribution similar to FY12 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 FY13

Property Class	New Value	FY13 Tax Base Levy Growth (New Growth)
Commercial Property	$160,949,687	$3,339,199
Personal Property	$222,268,130	$4,612,377
Residential Property	$156,096,511	$1,317,774
Total New Growth	**$539,314,328**	**$9,269,350**

TABLE IV
Assessed Values (in millions)

	FY09	FY10	FY11	FY12	FY13
Commercial Property	$ 8,457	$ 8,467	$8,379	$8,478	$8,577
Personal Property	$768	$911	$959	$951	$1,070
Residential Property	$14,651	$14,894	$14,824	$15,018	$15,567
Total Assessed Value	**$23,876**	**$24,272**	**$24,162**	**$24,447**	**$25,214**

For FY13, the City was able to increase its levy limit by approximately $19.3 million, to $421.1 million. Approximately $9.3 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 FY13 value of newly constructed or renovated property, multiplied by the FY12 tax rate. The remaining $10 million is the 2.5% increase over the FY12 levy allowed by Proposition 2½. The City's excess levy capacity increased by approximately $1.5 million, or 1.42%, to $104.1 million in FY13.

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

	Actual FY08	Actual FY09	Actual FY10	Actual FY11	Actual FY12	Estimated FY13
Levy Limit	$330,587	$347,606	$367,222	$383,312	$401,733	$421,052
Actual Levy	$242,334	$254,946	$268,663	$283,962	$299,091	$316,948
% Actual Levy Increase over Prior Year	4.55%	5.20%	5.38%	5.69%	5.33%	5.97%
Excess Levy Capacity	$88,253	$92,660	$98,559	$99,350	$102,642	$104,104
% Actual Excess Levy Capacity Increase Over Prior Year	19.8%	5.0%	6.4%	0.8%	3.3%	1.4%

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.

FY13 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 vigorous triennial review and certification and once again it certified the City's valuation models. In the interim years a statistical analysis is performed and approved by the DOR.

The FY13 valuation model is based upon sales of property that occurred during calendar year 2011, to establish the market value of all property as of January 1, 2012. For FY13, 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 FY12 model to calendar year 2011 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	**104**	**$784,238**	**$703,700**
Two Family	**26**	**$696,125**	**$649,900**
Three Family	**10**	**$800,000**	**$761,000**
Condominiums	**651**	**$400,000**	**$374,500**

The assessment ratios were between 90%-95% of calendar year 2011 sales, which means that the assessed estimate of values for FY12 were below actual market sales.

Although the calendar year 2011 sales demonstrated that the FY12 model was an accurate representation using overall property class statistics, the individual neighborhoods were not as consistent and required review. As a result, FY13 sales data from the calendar year 2011 real estate market has been utilized, along with what was learned from the prior year abatement activity, to establish the FY13 assessed values as of January 1, 2012. 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 FY13, the number of assessing districts remained at 17, which allowed for adequate sample sizes for the neighborhoods.

Modifications were made to the residential and condominium models, as well as to the residential land values. The residential land had minor adjustments for neighborhood and size, while the residential model was recalibrated for grade and condition adjustments. The condominium model was adjusted by neighborhood for market conditions as of the assessment date. In addition, approximately 4,300 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 2011, were refined to best reflect the equity of comparable properties as demonstrated in the various neighborhoods. Sales of 651 houses and condominium units were analyzed to develop these valuation models by property type (one-family, two-family, three-family and condominium units). The FY13 real property assessments reflect the analysis of the real estate market for the calendar year 2011.

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 $121 million in CPA funds. The City has received approximately $44.6 million in state matching funds through FY12 and expects to receive an additional $1.7 million in October 2012. It should be noted that this is the fifth 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 FY13 state match to be received by the City is estimated to be 22%. A recent change in the law does provide a mechanism for an increase in the state match in future years, but this is not guaranteed.

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

	FY12 Median CPA Surcharge Amount	FY13 Median CPA Surcharge Amount	FY13 Median Tax	FY13 Median Tax & CPA Surcharge Amount
Single Family	$99	$103	$4,298	$4,401
Condominium	$17	$19	$1,495	$1,514
Two Family	$88	$90	$3,866	$3,956
Three Family	$110	$112	$4,586	$4,698

RECOMMENDATIONS

1. That the City Council vote to authorize the use of $9,000,000 in Free Cash to reduce the FY13 tax rate.

2. That the City Council vote to authorize $2,000,000 in overlay surplus/reserves to be used for reducing the FY13 tax rate.

3. That the City Council vote to authorize $609,570 from the School Debt Stabilization Fund to be used as a revenue source to the General Fund Budget, which was included in the FY13 Adopted Budget.

4. That the City Council appropriate $10,000,000 from Free Cash to the City Debt Stabilization Fund.

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 55.9809%.

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 $8.66 and commercial tax rate of $21.50 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 FY13 exemption allowed under Massachusetts General Laws (MGL) Chapter 59, Section 5, Clause 17D from $285.00 to $293.00.

9. That the City Council vote to increase the FY13 asset limits allowed under Massachusetts General Laws (MGL) Chapter 59, Section 5, Clause 17E from $56,695 to $58,197.

10. That the City Council vote to increase the FY13 income and assets limits for elderly persons (age 65 or older). Income limits of $23,442 to $24,063 for those who are single and $35,163 to $36,095 for those who are married, asset limits of $46,883 to $48,125 for those who are single and $64,464 to $66,172 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 ($52,000) and for a married couple ($78,000), as allowed under MGL Chapter 59, Section 5, Clause 41A. The dollar amounts listed may be indexed by Massachusetts DOR for FY13. 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 MGL Chapter 59, Section 5, Clause 56, 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.

13. That the City Council vote to accept MGL Chapter 59, Section 5N, which allows for the creation of a work-off abatement program for veterans.

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 FY13.

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

- **Authorize $9,000,000 in Free Cash to Reduce the FY13 Tax Levy.** For the fiscal year that ended June 30, 2012, the City of Cambridge has a certified Free Cash balance of $115,826,900, an increase of approximately $13.6 million from the previous year. This balance represents the highest amount in the City's history.

  The $9,000,000 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.

  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, 2012. 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 $609,570 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 $5.5 million as of June 30, 2012. The Adopted FY13 Budget included $609,570 from this source to fund increases in debt service costs for the War Memorial.

- **Authorize the use of $10,000,000 in Free Cash to the City's Stabilization Fund.** This Free Cash authorization of $10,000,000 to the City's Stabilization Fund will be used to offset anticipated debt service costs in future years for the City's major capital projects especially in relation to the Elementary School reconstruction plan. This appropriation will help stabilize tax levy increases in future years.

- **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 55.9809% 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 171% 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 FY13, there are approximately 14,400 residential exemptions on the Assessing Department files. Overall, approximately 91% of the owner occupied homes benefit from the 30% residential exemption. The Assessing Department conducts random audits and responds to inquiries about individuals claiming the residential exemption, to ensure the validity of the program.

  If Cambridge did not adopt a residential exemption, the residential tax rate would be $7.04 instead of $8.66. 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 FY13, the break-even assessed value is approximately $1,083,565.

30% Residential Exemption

	FY2011	**FY2012**	**FY2013**
Value Exempted	$196,226	$198,085	$202,699
Tax Savings	$1,601.20	$1,679.76	$1,755.37

- **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 FY13, 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 2.65%. Therefore, the FY13 exemption amounts, income limits or asset limits under these local options will increase over the FY12 amounts and limits.

  Therefore, the FY13 exemption will be $293. In addition, under Clause 17E, cities and towns can increase the asset amounts by the CPI percentage for this same group. The FY13 amounts increases to $58,197 from $56,695.

  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 FY13 the income limits will be $24,063 for those who are single, $36,095 for those who are married, and the asset limits will be $48,125 for those who are single and $66,172 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 $52,000 for a single person and $78,000 for a married couple, which may be indexed by Massachusetts DOR for FY13), 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 after acceptance unless extended by vote of the legislative body.

- **Veteran Work-off Abatement Program.** Adoption of Section 5N of G.L. c. 59, will allow the creation of a work-off abatement program for veterans. This law was part of Section 8A of Chapter 108 of the Acts of 2012, more commonly known as the "The Valor Act." Under the program, veterans may earn abatements of their property taxes by working for the community at hourly earnings not exceeding the state minimum wage, for a maximum of 125 hours of service with the earned abatement not exceeding $1,000. The Board of Assessors has established additional eligibility criteria for the exemption. The earned abatement is not income for state tax and worker's compensation purposes.

CONCLUSION

In May, the City Council adopted a FY13 Budget which accomplishes 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; and 2) achieves the above with a moderate increase in the property tax levy, 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." 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.

Approximately 67% 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 FY13. In addition, with City Council approval, the City will use $11.6 million of Free Cash, overlay reserve and debt stabilization in FY13 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. Additionally, the appropriation of $10 million from Free Cash to the City's Debt Stabilization Fund will be used to offset anticipated debt service costs in future years for the City's major capital projects, especially in relation to the Elementary School reconstruction plan. This appropriation will help stabilize tax levy increases in future years.

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 FY13 property tax levy of $316,947,770 reflects a 5.97% increase over FY12, which is a lower increase than included in the adopted budget. With approval of these recommendations, the eight-year average increase of the property tax levy will be only 4.52%. The City has been able to achieve stability in its residential and commercial tax rate increases; with the average annual residential tax rate increase over the last 10 years at 1.8%.

In addition, approximately 74.9% of residential taxpayers will see a reduction, no increase or an increase of less than $100 in their FY13 property tax bill. Another 15.8% of residential taxpayers will see an increase between $100 and $250. Therefore, a total of 90.7% of the residential taxpayers will see no increase or an increase of less than $250. This will be the eighth 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 eight years, will see either a reduction, no change or an increase of less than $100, stands at 74%. This accomplishment is remarkable, given the fiscal challenges over the same time frame.

The past fiscal year was another exceptional year for the finances of the City, with total assessed values and excess levy capacity increasing and actual revenues far exceeding projections and prior year collections. While the City used approximately $23.5 million in Free Cash in FY12, it was not only able to replace this amount but add $13.6 million which, based on the economic climate, is a major accomplishment. However, it would not be prudent for the City to expect or project future revenues based on FY12 actuals. The City will continue to monitor revenues and will adjust projections once reliable trends have been established.

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 the economic climate; the impact of increasing health insurance costs; and the impact of future declines in State Aid to cities and towns.

Fortunately, the City Council and Administration have planned for a time when State Aid 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 debt schedule has $127.5 million budgeted for this purpose, with $81.5 million approved in FY13, in addition to the $3.0 million approved in FY12, for reconstruction of the first elementary school. The City hopes to partially offset some of the costs with MSBA reimbursements as we update our financial analysis of future debt. Additionally, I am recommending an appropriation of $10 million to the Debt Stabilization Fund from Free Cash to help mitigate the impact of additional tax supported debt in the future, particularly in relation to the Elementary School reconstruction plan.

The City is preparing for its Other Post Employment Benefits (OPEB) actuarial study as of January 1, 2013. In addition, the City began its annual appropriation of $1.0 million funding to the OPEB Liability Trust Fund in FY13, yielding a total of $3.0 million in contributions to date. It is the City's intention to use the excess appropriations that will result when the pension liability is met, which is targeted for 2029, to increase our contributions to the OPEB Liability Trust fund.

The City updated its Pension Actuarial study as of January 1, 2012 and, based on the results, I am pleased to announce the funding schedule will remain the same as in 2010 to meet our current target, to be fully funded by 2029.

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.

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 and responded to the taxpayers and residents through our actions, which has been aided by prudent financial planning.

Very truly yours,

Robert W. Healy
City Manager

Attachment

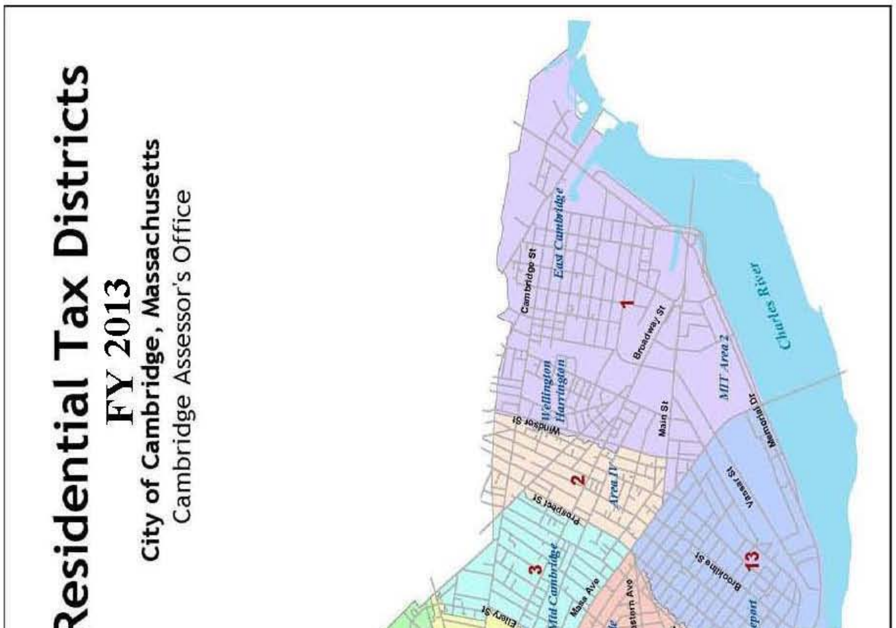
ATTACHMENT 1

FY2013 Single Family Assessment Data Median Assessed Values				
		FY2012	FY2013	
	Count	Median	Median	Change
R1	391	$ 403,500	$ 396,600	-1.71%
R2	206	$ 419,000	$ 433,300	3.41%
R3	229	$ 743,100	$ 760,200	2.30%
R4	86	$ 794,450	$ 786,350	-1.02%
R5	58	$ 1,876,900	$ 2,009,900	7.09%
R6	345	$ 1,325,000	$ 1,316,700	-0.63%
R7	648	$ 467,300	$ 470,500	0.68%
R8	223	$ 663,700	$ 689,300	3.86%
R9	202	$ 1,085,050	$ 1,072,000	-1.20%
R10	333	$ 2,448,500	$ 2,576,900	5.24%
R11	164	$ 1,127,300	$ 1,123,150	-0.37%
R12	180	$ 540,350	$ 543,800	0.64%
R13	232	$ 567,200	$ 578,400	1.97%
R14	136	$ 1,047,850	$ 1,056,750	0.85%
R15	32	$ 753,800	$ 818,450	8.58%
R16	151	$ 845,600	$ 846,000	0.05%
R17	184	$ 632,350	$ 632,800	0.07%

FY2013 Condo Assessment Data Median Assessed Value				
		FY2012	FY2013	
	Count	Median	Median	Change
R1	2514	$ 391,300	$ 394,200	0.74%
R2	657	$ 342,700	$ 345,400	0.79%
R3	2025	$ 350,300	$ 356,400	1.74%
R4	644	$ 317,400	$ 321,900	1.42%
R5	15	$ 1,171,100	$1,248,100	6.58%
R6	1630	$ 331,600	$ 338,350	2.04%
R7	1646	$ 333,700	$ 337,400	1.11%
R8	406	$ 445,700	$ 450,700	1.12%
R9	42	$ 461,500	$ 466,400	1.06%
R10	37	$ 1,269,700	$1,312,400	3.36%
R11	517	$ 585,100	$ 596,900	2.02%
R12	1054	$ 351,950	$ 355,800	1.09%
R13	1141	$ 373,800	$ 385,500	3.13%
R14	330	$ 465,850	$ 470,900	1.08%
R16	357	$ 362,700	$ 375,900	3.64%
R17	515	$ 430,300	$ 432,900	0.60%

FY2013 Two Family Assessment Data Median Assessed Value				
		FY2012	FY2013	
	Count	Median	Median	Change
R1	292	$ 449,450	$ 435,000	-3.22%
R2	174	$ 491,300	$ 499,350	1.64%
R3	215	$ 801,900	$ 808,100	0.77%
R4	49	$ 949,300	$ 949,300	0.00%
R5	11	$ 1,916,900	$ 2,034,300	6.12%
R6	86	$ 1,087,150	$ 1,092,750	0.52%
R7	631	$ 578,900	$ 578,700	-0.03%
R8	219	$ 687,100	$ 700,300	1.92%
R9	12	$ 809,100	$ 822,750	1.69%
R10	15	$ 1,915,800	$ 2,054,800	7.26%
R11	37	$ 1,138,100	$ 1,138,100	0.00%
R12	162	$ 603,150	$ 603,250	0.02%
R13	224	$ 658,200	$ 667,900	1.47%
R14	215	$ 860,300	$ 867,500	0.84%
R16	89	$ 856,800	$ 868,800	1.40%
R17	138	$ 669,300	$ 678,200	1.33%

FY2013 Three Family Assessment Data Median Assessed Values				
		FY2012	FY2013	
	Count	Median	Median	Change
R1	240	$ 568,150	$ 557,350	-1.94%
R2	150	$ 648,700	$ 663,400	2.22%
R3	126	$ 929,700	$ 937,550	0.84%
R4	32	$ 1,083,600	$ 1,077,350	-0.58%
R5	3	$ 2,889,200	$ 3,043,900	5.08%
R6	34	$ 1,291,150	$ 1,291,150	0.00%
R7	182	$ 689,350	$ 699,100	1.39%
R8	54	$ 883,200	$ 912,250	3.18%
R9	1	$ 530,000	$ 530,000	0.00%
R10	1	$ 2,940,300	$ 3,168,500	7.20%
R11	18	$ 1,138,050	$ 1,138,050	0.00%
R12	117	$ 718,400	$ 717,100	-0.18%
R13	161	$ 719,500	$ 731,300	1.61%
R14	45	$ 903,600	$ 925,400	2.36%
R16	48	$ 920,700	$ 979,700	6.02%
R17	61	$ 773,400	$ 773,400	0.00%


Residential Tax Districts
FY 2013
City of Cambridge, Massachusetts
Cambridge Assessor's Office
East Cambridge
Wellington Harrington
MIT Area 2
Charles River
Area IV
Mid Cambridge
Cambridgeport
Riverside
Agassiz
Neighborhood 9
Neighborhood 10
North Cambridge
Cambridge Highlands
Fresh Pond
Strawberry Hill
Feet