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CITY OF CAMBRIDGE • EXECUTIVE DEPARTMENT

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October 4, 2010

To The Honorable, the City Council:

The establishment of the FY11 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 FY11 property tax levy, property values and other supporting information.

OVERVIEW

I am pleased to inform you that the actual FY11 property tax levy of $283,961,699 reflects a $15,298,715 or 5.69% increase from FY10, which is lower than the estimated increase projected in May 2010. The FY11 Budget adopted by the City Council in May 2010 projected a property tax levy increase of $17 million, or 6.3%, to $285,647,600 in order to fund operating and capital expenditures. The FY11 operating budget has increased by 3.1%. However, due to a calendar anomaly, $1.2 million has been added to the budget to cover the cost of a 53rd pay period in FY11 for employees who are paid on Thursdays. Without this addition the FY11 Budget increase would have been 2.8%.

In May, I informed the City Council that the actual tax levy increase was likely to change. This was based on potential changes in State Aid that would not be known until the State finalized its FY11 budget and the possible use of additional non-property tax revenues that would be available based on FY10 actual collections.

This assumption again proved correct. The use of additional non-property tax revenue and other adjustments has allowed an overall reduction of $1,685,901 from the original projected property tax levy. This is possible due to the use of increased non-property tax revenues, which includes $675,000 from the local option meals excise, $2,400,000 from Free Cash, $100,000 in Parking Fund revenues and $400,000 from increases to permit and other revenues. Also, included is $204,578 in overlay adjustments. A portion of these increases, totaling $2,093,677 are required to offset a net decrease in Cherry Sheet revenues, prior year overlay deficits and reductions in various revenues based on actual FY10 collections.

Tax Levy Changes	**Amount**
State Aid Adj. –Revenues and Assessments (Actual)	+$2,093,677
Non-Property Tax Revenue	-$3,575,000
Overlay Adjustment	-$204,578
Net Decrease	**- $1,685,901**

This resulted in a final property tax levy for FY11 of $283,961,699, an increase of 5.69%. With approval of these recommendations, the six-year average increase in the property tax levy will be 4.1%.

This recommendation includes the use of $13.4 million in reserve accounts to lower the property tax levy; $2 million from overlay surplus; and $11.4 million in Free Cash. Also, $8.3 million from the Debt Stabilization Fund and $1.2 million from the School Debt Stabilization Fund is used to offset increases in debt service costs that would otherwise have been funded from property taxes.

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

Based on a property tax levy of $284.0 million, the FY11 residential tax rate will be $8.16 per thousand of value, which is an increase of $0.44, or 5.7% from FY10. The commercial tax rate will be $19.90, which is an increase of $1.15, or 6.1% from FY10.

However, approximately 51.7% of residential taxpayers will see a reduction, no increase or an increase of less than $100 in their FY11 tax bill. In addition, another 32.2% of residential taxpayers will see an increase between $100-$250. This will be the sixth year in a row that a majority of residential tax payers will see a reduction, no change or an increase of less than $100. This accomplishment should not be taken for granted based on the tremendous economic turmoil over the last three fiscal years.

TABLE I
Change in the Residential Tax Bills*

Change in Tax Payment	Number of Parcels	Percentage
Less than $0	2,580	12.4
> $0 and less than $100.00	8,208	39.3
>$100.00 less than $250.00	6,733	32.2
>$250.00 and less than $500.00	2,238	10.7
Greater than $500.00	1,127	5.4
Totals	20,886	100 %

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

MEDIAN TAX BILLS

The analysis below explains in further detail how the City determines property values and property tax rates for FY11. 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 5.69% increase in the property tax levy required to balance the FY11 Budget. The FY11 property tax levy increase reflects a $1.3 million reduction in the two major State Aid categories (Unrestricted General Government Aid (UGGA) and Chapter 70 School Aid). Since FY09, the City has seen a reduction of $9.3 million, or 26% in State Aid from these two categories. In addition, the FY11 Adopted Budget reflects a 3.1% 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."

Commercial-Residential Property Tax Classification: Tax classification allows municipalities to tax commercial taxpayers at a higher rate than residential taxpayers. In FY11, commercial property owners will pay 65.4% of the property tax levy, the same share as in FY10. Consequently, residential property owners' share of the FY11 tax levy is 34.6%, also the same as in FY10.

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 2009, which is the basis of the FY11 property assessment, total residential property values have moderated (approximately 0.47% decrease overall). Total commercial property values have also decreased by 0.41%. The modest decline 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) triennial full certification process of the City's real and personal property values, system and methodologies.

The chart below shows the change in the median tax bills by property class. It is important to note that while the overall total residential assessed value decreased in FY11, 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*

	FY10 Value	FY10 Tax Bill	FY11 Value	FY11 Tax Bill	Dollar Change	Percent Change
Single Family	$660,100	$3,564	$670,450	$3,870	$306	8.59%
Condominium	$365,950	$1,293	$364,100	$1,370	$77	5.96%
Two Family	$648,800	$3,477	$638,550	$3,609	$132	3.80%
Three Family	$733,700	$4,132	$721,500	$4,286	$154	3.73%

* Includes Residential Exemption

CITY-WIDE ASSESSED VALUES

FY11 values are based on market activity that occurred during calendar year 2009, during which the overall valuation of the City's residential property decreased by a modest 0.47% and the overall valuation of commercial property decreased by 0.41%. This reflects a leveling of commercial rental rates and a slight increase in commercial vacancies. This has had a moderate impact on existing commercial property values. The major components, which offset the decrease in commercial value, however, continues to be new construction of life science buildings and the personal property associated with these developments.

For FY11, the total assessed value of taxable property in the City of Cambridge equals $24,162,077,598, a 0.45% decrease over FY10 values. The actual FY11 total assessed value is consistent with the projections presented to the rating agencies in January 2010.

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 FY11 the market for both commercial and residential properties declined not unlike most of the Greater Boston area, resulting in the continuation of a tax distribution similar to FY10 between commercial taxpayers and residential taxpayers.

The table below break out new construction value 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 FY11

Property Class	New Value	FY11 Tax Base Levy Growth (New Growth)
Commercial Property	$96,104,506	$1,801,960
Personal Property	$203,207,080	$3,810,133
Residential Property	$135,006,796	$1,042,252
Total New Growth	**$434,318,382**	**$6,654,345**

TABLE IV
Assessed Values (in millions)

	FY07	FY08	FY09	FY10	FY11
Commercial Property	$ 7,372	$8,378	$ 8,457	$ 8,467	$8,379
Personal Property	$659	$736	$768	$911	$959
Residential Property	$14,136	$14,427	$14,651	$14,894	$14,824
Total Assessed Value	**$22,167**	**$23,541**	**$23,876**	**$24,272**	**$24,162**

For FY11, the City was able to increase its levy limit by approximately $16 million, to $383.2 million. Approximately $6.7 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 FY11 value of newly constructed or renovated property, multiplied by the FY10 tax rate. The remaining $9.3 million is the 2.5% increase over the FY10 levy allowed by Proposition 2½, plus a revised new value calculation from FY10. The City's excess levy capacity increased by $0.7 million, or 0.7%, to $99.2 million in FY11.

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

	Actual FY06	**Actual FY07**	**Actual FY08**	**Actual FY09**	**Actual FY10**	**Estimated FY11**
Levy Limit	$288,048	$305,445	$330,587	$347,606	$367,222	$383,176
Actual Levy	$222,960	$231,787	$242,334	$254,946	$268,663	$283,962
% Actual Levy Increase over Prior Year	0%	3.96%	4.55%	5.20%	5.38%	5.69%
Excess Levy Capacity	$65,088	$73,658	$88,253	$92,660	$98,559	$99,214
% Actual Excess Levy Capacity Increase Over Prior Year	45.6%	13.2%	19.8%	5.0%	6.4%	0.7%

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.

FY11 VALUATION PROCESS

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

The FY11 valuation model is based upon sales of property that occurred during calendar year 2009, to establish the market value of all property as of January 1, 2010. For FY11, 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 FY10 model to calendar year 2009 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	102	$685,000	$583,000
Two Family	34	$691,250	$661,800
Three Family	18	$785,250	$707,303
Condominiums	618	$404,750	$373,200

The assessment ratios were between 85%-96% of calendar year 2009 sales, which means that the assessed estimate of values for FY10 were below actual market sales.

Although the calendar year 2009 sales demonstrated that the FY10 model was an accurate representation using overall property class statistics, the individual neighborhoods were not as consistent and required review. As a result, FY11 sales data from the calendar year 2009 real estate market has been utilized, along with what was learned from the prior year abatement activity, to establish the FY11 assessed values as of January 1, 2010. 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 FY11, the number of assessing districts remained at 17, which allowed for adequate sample sizes for the neighborhoods.

Modifications to the model were made, which included lowering of residential land values in most areas, lowering the condominium base rate and recalibrating the building condition adjustments. In addition, approximately 3,800 inspections were completed along with a detailed field review of property. These inspections serve to ensure consistency within neighborhoods and across the City.
The analysis for determining property values depends on several factors: the trends of the real estate market in the areas of sales; property improvements; changes in the economics of real estate finance; and the high demand for real estate in the City. To arrive at full and fair cash values for approximately 24,015 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 2009, were refined to best reflect the equity of comparable properties as demonstrated in the various neighborhoods. Sales of 873 houses and condominium units were analyzed to develop these valuation models by property type (one-family, two-family, three-family, and condominium units). The FY11 real property assessments reflect the analysis of the real estate market for the calendar year 2009.

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 $101.7 million in CPA funds. The City has received $40.7 million in state matching funds through FY10 and expects to receive an additional $2.1 million in October 2010. It should be noted that this is the third 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 FY11 state match to be received by the City is estimated at 30%.

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

	FY10 Median CPA Surcharge Amount	FY11 Median CPA Surcharge Amount	FY11 Median Tax	FY11 Median Tax & CPA Surcharge Amount
Single Family	$84	$92	$3,870	$3,962
Condominium	$16	$17	$1,370	$1,387
Two Family	$81	$84	$3,609	$3,693
Three Family	$101	$104	$4,286	$4,390

RECOMMENDATIONS

1. That the City Council authorize the use of $11,400,000 in Free Cash to reduce the FY11 tax rate.

2. That the City Council vote to authorize $2,000,000 in overlay surplus/reserves to be used for reducing the FY11 tax levy.

3. That the City Council vote to authorize $8,300,000 from the Debt Stabilization Fund to be used as a revenue source to the General Fund Budget, which was included in the FY11 Adopted Budget.

4. That the City Council vote to authorize $1,198,615 from the School Debt Stabilization Fund to be used as a revenue source to the General Fund Budget, which was included in the FY11 Adopted Budget.

5. That the City Council classify property within the City of Cambridge into the five classes allowed for the purpose of allocating the property tax. It is further recommended that the City Council adopt a minimum residential factor of 56.3344%.

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 $8.16 and commercial tax rate of $19.90 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 the FY11 exemption of $280.00 allowed under Massachusetts General Laws (MGL) Chapter 59, Section 5, Clause 17D. There is no change authorized in FY11 from the DOR.

9. That the City Council vote the FY11 asset limits of $55,775 allowed under Massachusetts General Laws (MGL) Chapter 59, Section 5, Clause 17E. There is no change authorized in FY11 from the DOR.

10. That the City Council vote the FY11 income and asset limits. Income limits of $23,061 for those who are single and $34,592 for those who are married, asset limits of $46,122 for those who are single and $63,418 for those who are married, as allowed under MGL, Chapter 59, Section 5, Clause 41D. There is no change authorized in FY11 from the DOR.

11. That the City Council vote the income limit for deferral of real estate taxes by elderly persons (at least 65 years old) as determined by the Commissioner of Revenue for the purposes of MGL, Chapter 62, Section 6, subsection (k), for a single person who is not head of household ($51,000) and for a married couple ($77,000), as allowed under MGL Chapter 59, Section 5, Clause 41A. The 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 lower the interest rate by 4% to 14% for overdue water and sewer bills in FY11.

13. That the City Council vote to accept MGL Chapter 200A, Section 9A, which allows for an alternative procedure for disposing of abandoned funds held in custody by the City as provided for in the recently enacted municipal relief legislation.

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 FY11.

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

- **Authorize $11,400,000 in Free Cash to Reduce the FY11 Tax Levy.** For the fiscal year that ended June 30, 2010, the City of Cambridge has a certified Free Cash balance of $89,315,773, an increase of approximately $4.7 million from previous year. This balance represents the second highest amount in the City's history.

  The $11,400,000 in the Free Cash authorization is requested at this time from the City's Free Cash balance in order to reduce the property tax levy increase. This amount is $2.4 million higher than the $9.0 million which has been used for several years and reflects covering the cost of one-time non-recurring items in FY11. These one-time costs included the purchase of recycling toters to implement single stream recycling and to cover overlay deficits for FY05 and FY06.

  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 $16.1 million in overlay balances as of June 30, 2010. 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 $8,300,000 in Debt Stabilization Funds.** In recognition of increases in debt service costs related to major capital projects, the City established a Debt Stabilization Fund and has made contributions to it over the past several years. The balance in this Stabilization Fund is approximately $13.4 million as of June 30, 2010. The Adopted FY11 Budget included $8.3 million from this source to fund increases in debt service costs.

- **Authorize $1,198,615 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 $7.3 million as of June 30, 2010. The Adopted FY11 Budget included $1,198,615 from this source to fund increases in debt service costs for the War Memorial and to cover the drop-off in School Building Authority reimbursements prior to the completion of the principal and interest payments for elementary school projects.

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

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

  The City Council sets the levy distribution each year by voting for a Minimum Residential Factor. The result of voting for the Minimum Residential Factor of 56.3344% 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 169% 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 FY11, there are approximately 14,156 residential exemptions on the Assessing Department files. Overall, 91% of the owner occupied homes benefit from the 30% residential exemption.

If Cambridge did not adopt a residential exemption, the residential tax rate would be $6.62 instead of $8.16. 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 FY11, the break-even assessed value is approximately $1,040,000.

30% Residential Exemption

	FY2009	**FY2010**	**FY2011**
Value Exempted	$201,161	$198,423	$196,226
Tax Savings	$1,520.78	$1,531.83	$1,601.20

- **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 FY11, 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 0%. Therefore, the FY11 exemption amounts, income limits or asset limits under these local options are the same as the FY10 amounts and limits.

Therefore, FY11 exemption remains at $280. In addition, under Clause 17E, cities and towns can increase the asset amounts by the CPI percentage for this same group. The FY11 amounts remains at $55,775.

MGL Chapter 59, Section 5, Clause 41D allows cities and towns to increase the income and assets limits for elderly persons (age 65 or older) by the CPI percentage. For FY11 the income limits remain at $23,061 for those who are single, $34,592 for those who are married, and the asset limits remain $46,122 for those who are single and $63,418 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, due to a change in the statute, which 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, ($51,000 for a single person and $77,000 for a married couple, which will be indexed yearly), as allowed under MGL Chapter 59, Section 5, Clause 41A. I am recommending that the City Council vote to adopt this increased deferral amount. The City Council has previously voted to reduce the interest percentage to 4% on deferred property tax balances.

- **Interest Rate Reduction.** A recommendation to lower the Water Interest rate by 4% to 14% is another form of economic relief for Cambridge citizens. The interest rate decrease was discussed during City Council meetings over the last three years at the time of the setting the water and sewer rate. During these discussions, it was stated that if water consumption stabilized, it would allow the opportunity for a potential recommendation to reduce the interest rate percentage. Now that consumption has stabilized, I am recommending this change.

- **Disposal of Abandoned Property.** The acceptance of MGL Chapter 200A, section 9A, which was part of the recently enacted municipal relief legislation, will allow for an alternative procedure for disposing of abandoned funds (outstanding checks) held in custody of the City. This statute allows the City to be solely responsible for notifying the public through its web page, mail and local newspaper of uncashed checks issued by the City, which are over one year old. By using the provisions of the statute, the City will be better able to notify the public of checks not cashed in a more efficient, effective and timely fashion. Funds which remain unclaimed after the notification process has been completed will be deemed abandoned and will revert back to the City.

CONCLUSION

In May, the City Council adopted a FY11 Budget which accomplished the following: 1) maintains City and school services that citizens have come to expect and provides for a strong capital plan, which provides stability and reinvestment in our community that is important during these difficult times and, given the current economic climate and the fiscal challenges facing many cities and towns in the Commonwealth, is a major achievement; and 2) achieved the above with a moderate increase in the property tax levy in spite of a continued reduction in State Aid, which supports the City Council Goal of "evaluating expenditures with a view of maintaining a strong fiscal position and awareness of the impact on taxpayers."

Approximately 63% 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 but, 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 FY11, despite continued reductions in State Aid. In addition, with City Council approval the City will use $22.9 million of Free Cash, overlay reserve and debt stabilization in FY11 to lessen the amount to be raised from the property tax levy, which translates into a lower property tax burden for the taxpayers of the City.

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

The FY11 property tax levy of $283,961,699 reflects a 5.69% increase over FY10. With approval of these recommendations, the six-year average increase of the property tax levy will be only 4.1%.

In addition, approximately 51.7% of residential taxpayers will see a reduction, no increase or an increase of less than $100 in their FY11 property tax bill. In addition, another 32.2% of residential taxpayers will see an increase between $100-$250. This will be the sixth 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 over the last six years, will see either a reduction, no change or an increase of less than $100 stands at 75%. This accomplishment is remarkable, given the current fiscal challenges.

Despite the economic crisis, the past fiscal year was another solid year for the finances of the City: with the excess levy capacity increasing and actual revenues above projections. While the City used approximately $10.2 million in Free Cash in FY10, it was not only able to replace this amount but add $4.7 million, which based on the economic climate, is a major accomplishment.

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

OUTLOOK

As it appears that the current economic crisis is slowly diminishing, the City should be proud but humbled, that we have survived relatively well in comparison to other municipalities both locally and nationally, while our City continues to move forward. Sometimes it is easy to forget how fortunate we are and how quickly circumstances can change.

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

There are some serious fiscal challenges that will continue to affect the City both in the short and long-term.

The following issues will impact future City budgets in the near term: 1) The Commonwealth and the federal government remain vital financial partners in the delivery of our services. The significant reductions in the level of state support over the past two years have made it difficult for the City to absorb them without impacting the property tax levy, even with limited growth in our budget. As resources from the American Recovery and Reinvestment Act begin to disappear in FY12 at the State level, cities and towns may be vulnerable to reductions in State Aid. Unfortunately, it has become a necessity to be concerned that mid-year State budget cuts are a real possibility. FY11 will be no different. This will be especially true if the ballot questions in November are passed by the voters, which would repeal the sales tax on alcohol and reduce the sales tax percentage to 3% from 6.25%, effective January 2011. 2) As the projected total federal budget deficit continues to grow at some point there will be a need to reduce federal spending, which will impact us through a reduction in direct federal grants or a reduction in federal through state grant programs. 3) The City has received the results of our actuarial study regarding our unfunded pension liability. The current liability is scheduled to be retired in 2029, which is well before the 2040 deadline. However, this reflects an extension of the funding schedule from the previous study of 2013 and was expected due to the unprecedented decline in the stock market. 4) The City has also completed an updated OPEB actuarial study and will continue to develop short and long term funding strategies. 5) The City and Schools will begin the process of developing an Elementary School reconstruction plan. The ultimate size and scope of the plan will have an impact on Capital Budget for other projects. Therefore, I may be recommending an appropriation to the Debt Stabilization Fund from Free Cash late in the fiscal year to help mitigate the impact of additional tax supported debt in the future for the Elementary School reconstruction plan. However, this recommendation will be contingent upon some of the items noted above and the overall fiscal position of the City during the current fiscal year.

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. We will continue to use our five year financial and capital plan, debt and reserve policies and the City Council Goal of "evaluating expenditures with a view of maintaining a strong fiscal position and awareness of the impact on taxpayers" as a blue print for our long-range planning to maintain stability and predictability in our budgeting and financial planning processes.

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

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

Very truly yours,

Robert W. Healy
City Manager

Attachment

ATTACHMENT 1

FY2011 Single Family Assessment Data

	Count	Median Assessed Value FY10	Median Assessed Value FY11	Change
R1	394	$ 396,550	$ 402,750	1.56%
R2	205	$ 412,100	$ 414,300	0.53%
R3	223	$ 698,000	$ 721,000	3.30%
R4	85	$ 779,800	$ 796,400	2.13%
R5	56	$ 2,088,600	$ 1,899,350	-9.06%
R6	341	$ 1,278,300	$ 1,283,700	0.42%
R7	650	$ 457,300	$ 459,800	0.55%
R8	225	$ 639,700	$ 659,200	3.05%
R9	203	$ 1,027,800	$ 1,060,000	3.13%
R10	332	$ 2,535,200	$ 2,442,300	-3.66%
R11	164	$ 1,118,250	$ 1,109,350	-0.80%
R12	179	$ 532,000	$ 533,600	0.30%
R13	233	$ 550,100	$ 552,100	0.36%
R14	132	$ 970,650	$ 1,024,050	5.50%
R15	33	$ 704,100	$ 708,300	0.60%
R16	149	$ 833,800	$ 837,900	0.49%
R17	182	$ 609,600	$ 634,300	4.05%

FY2011 Condo Assessment Data

	Count	Median Assessed Value FY10	Median Assessed Value FY11	Change
R1	2,469	$ 414,800	$ 391,500	-5.62%
R2	611	$ 333,200	$ 336,400	0.96%
R3	1,997	$ 347,600	$ 345,500	-0.60%
R4	647	$ 315,300	$ 315,300	0.00%
R5	13	$ 1,233,100	$ 1,233,100	0.00%
R6	1,597	$ 331,400	$ 331,000	-0.12%
R7	1,607	$ 329,000	$ 331,100	0.64%
R8	373	$ 442,400	$ 442,400	0.00%
R9	42	$ 461,750	$ 461,750	0.00%
R10	37	$ 1,275,900	$ 1,275,900	0.00%
R11	515	$ 588,500	$ 585,100	-0.58%
R12	1,023	$ 352,100	$ 349,500	-0.74%
R13	1,079	$ 363,300	$ 363,900	0.17%
R14	312	$ 465,500	$ 465,400	-0.02%
R15	-			
R16	357	$ 360,600	$ 362,400	0.50%
R17	499	$ 428,000	$ 427,700	-0.07%

FY2011 Two Family Assessment Data			
		Median Assessed Value		
	Count	FY10	FY11	Change
R1	296	$ 450,250	$ 443,250	-1.55%
R2	179	$ 493,900	$ 492,900	-0.20%
R3	219	$ 812,800	$ 793,700	-2.35%
R4	50	$ 962,500	$ 942,150	-2.11%
R5	13	$ 2,109,700	$ 1,929,700	-8.53%
R6	86	$ 1,109,550	$ 1,083,750	-2.33%
R7	635	$ 583,600	$ 577,200	-1.10%
R8	220	$ 683,200	$ 679,250	-0.58%
R9	12	$ 828,800	$ 807,700	-2.55%
R10	16	$ 2,124,700	$ 1,912,650	-9.98%
R11	37	$ 1,177,900	$ 1,130,700	-4.01%
R12	167	$ 608,400	$ 599,600	-1.45%
R13	233	$ 658,600	$ 643,700	-2.26%
R14	222	$ 836,800	$ 860,850	2.87%
R15	0			
R16	92	$ 868,600	$ 848,700	-2.29%
R17	140	$ 673,600	$ 661,850	-1.74%

FY2011 Three Family Assessment Data				
		Median Assessed Value		
	Count	FY10	FY11	Change
R1	242	$ 560,200	$ 551,200	-1.61%
R2	152	$ 652,350	$ 648,050	-0.66%
R3	130	$ 943,400	$ 925,200	-1.93%
R4	32	$ 1,109,950	$ 1,081,400	-2.57%
R5	4	$ 2,539,150	$ 2,671,850	5.23%
R6	38	$ 1,252,300	$ 1,228,300	-1.92%
R7	189	$ 696,200	$ 686,500	-1.39%
R8	54	$ 873,600	$ 865,200	-0.96%
R9	1	$ 579,900	$ 530,000	-8.60%
R10	1	$ 3,075,400	$ 2,954,400	-3.93%
R11	18	$ 1,178,050	$ 1,138,050	-3.40%
R12	118	$ 726,300	$ 718,600	-1.06%
R13	162	$ 714,950	$ 699,900	-2.11%
R14	48	$ 879,750	$ 898,800	2.17%
R15	0			
R16	48	$ 909,300	$ 884,350	-2.74%
R17	68	$ 781,850	$ 780,200	-0.21%

Residential Tax Districts
FY 2011
City of Cambridge, Massachusetts
Cambridge Assessor's Office