Special Report

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Boston's Property Taxes In Limbo

Legislature should restore classification law to pre-2004 status

Highlights

- The Legislature should act on pending classification bills before Boston sets its tax rates in December
- The business classification factor should be set permanently at 175%
- Without new legislation, homeowners could see no relief in their share of the tax levy even with stagnant residential values this year

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In less than three months, the City of Boston is scheduled to set its new property tax rates for fiscal 2008. What the final tax rates for residential and business taxable property and their shares of the tax levy will be depend on the new values as of January 1, 2007 and on what steps the Legislature takes regarding pending bills involving the classification of property. The Research Bureau, in a Special Report in July, recommended that legislation should be approved that restored the classification requirement to its pre-2004 status, which would require the current law to be amended so that:

- the business classification factor would become permanent at the original 175% level
- the current language that prohibits the residential class from bearing a lower percentage of the levy than imposed in the prior year be eliminated.

A significant flaw in the 2004 classification law may result in homeowners paying additional property taxes at a time when residential housing prices are stagnant or declining. With the time approaching when cities and towns will set their tax rates, it is incumbent upon the Legislature to act now on the classification bills submitted that would change the current law. One bill would keep the current 183% for two more years. Mayor Menino has submitted legislation (H3119) consistent with the original agreement on classification in 2004 among state and local officials and business leaders. The Research Bureau supports this legislation.

Classification Compromise in 2004

Faced with very divergent residential and business property value trends that threatened to significantly increase residential tax bills in fiscal 2004 in Boston and several other communities, legislation was passed (Ch.3, Acts of 2004) to shift the business classification factor from 175% to 200% of its share of total taxable value in fiscal 2004. That would mean that the business property share of the tax levy would be 100% higher than it would be if there were no classification and the business share of the tax levy were equal to its share of total taxable value. The law required the business ceiling to be reduced each year until it was restored to its original factor of 175% in fiscal 2008 and be further reduced to 170% in fiscal 2009. As scheduled, the business classification factor dropped to 183% in fiscal 2007.

Ch. 3 of the Acts of 2004 Tax Classification Schedule

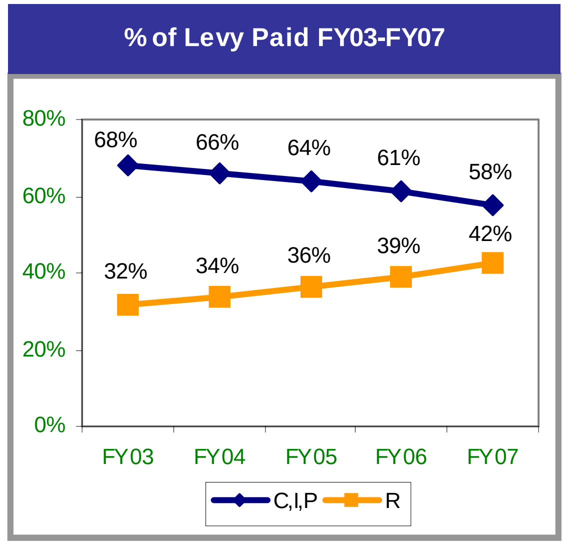
Fiscal Year	Max. CIP Ceiling	Min. R Floor
Prior to change	175%	50%
2004	200%	45%
2005	197%	47%
2006	190%	49%
2007	183%	50%
2008	175%	50%
2009	170%	50%

The original compromise agreement reached among city and state officials and business leaders in 2004 was to increase the business classification factor to 200% for fiscal 2004 and to ratchet down the business factor by a set percentage each year from 200% to the original 175% in fiscal 2008 where it would remain permanently. This agreement was a compromise from the City of Boston's initial plan to increase the business classification factor to 200% permanently. Due to language inserted in the 2004 legislation as it was enacted, the law differed from the compromise by requiring an additional 5% reduction of the business classification factor in fiscal 2009 and by inserting new language that prohibited the residential class from bearing a lower percentage of the total tax levy than the percentage imposed in the prior year. Retaining this language would mean that homeowners would see no relief in their share of the tax levy this fiscal year even with stagnant and slightly declining residential values. The business share of the levy would not increase even though commercial property values are appreciating, especially downtown office properties.

Tax Levy Share Trends

This set of circumstances comes at a time when the business share of the tax levy has decreased each year since fiscal 2003. Since fiscal 1984, business and residential values followed a relatively similar trend and their share of the tax levy hovered at a 70%-30% split respectively. However, in fiscal 2003 this trend started to shift due to economic forces, particularly the high rate of residential property growth, the slowing of commercial property values, the reduction of telecommunication values and the City reaching the business ceiling of 175% in fiscal 2003. The result has been residential owners paying more of the tax bill. The percent of property taxes paid by residential owners increased from 31.9% in fiscal 2003 to 42.4% in fiscal 2007. The business share reduced accordingly from 68.1% in fiscal 2003 to 57.6% of the levy in fiscal 2007.

The recent levy share trends still do not change the fact that business property continues to pay a larger share of the tax levy under the City's application of classification. In fiscal 2007, business property represented 31.5% of taxable value yet paid 57.6% of the tax levy. Residential property represented 68.5% of the value but paid 42.4% of the levy.



Recommendations

The recommendations made here are intended to restore classification to its pre-2004 status and let the relative tax levy shares and tax rates be determined more naturally by the changes in the real estate market.

- The classification compromise agreement should be honored and legislation (H3119) that would make the business classification factor permanent at the original 175% should be enacted. Businesses agreed to the compromise plan in 2004 to help mitigate the large property tax increase faced by homeowners at the time. Since then, business has been paying a larger share of the tax burden than otherwise would have been required.
- Language in the 2004 act that prohibits the residential class from bearing a lower percentage of the total tax levy than the percentage imposed in the prior year should be deleted. H3119 effectively eliminates this arbitrary restriction which would allow the market changes in real estate values to determine the business and residential tax rates and levy shares.