Town of Hopkinton

Underride Issue Paper
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Introduction

In the Commonwealth of Massachusetts, tax levy limits are regulated by Proposition 2 ½, which is codified in MA Gen L ch 59 § 21C. Generally, the statute specifies a tax levy limit of 2.5% of the full and fair valuation of taxed real and personal property, but over time the specific levy limit can change in a number of ways:

- Annual increase - the law provides for an automatic annual increase of 2.5%
- New growth - the law provides for an increase to correspond with new tax base growth from construction, improvements and acquisitions, which is entered into the tax levy limit based on full and fair valuation and the prior year's tax rate
- Overrides - A town can permanently increase its levy limit by voting for an override)
- Underride - A town can permanently decrease its levy limit by voting for an underride (required majority vote of the Board of Selectmen
- Debt exclusion - A town can vote to take on and service new debt for specific capital projects outside and above the levy limit)
- Capital outlay expenditure exclusions - A town can vote to tax and spend on specific capital outlays in a single year outside and above the levy limit

For fiscal year 2020, the Hopkinton Town Manager has recommended a budget with uses of funds of just over $90M. That plan involves a spending level that is below the proposition 2 ½ levy limit by $1,180,568. In budgetary terms, that $1,180,568 is the "unused tax levy."

This paper considers the opportunity for the Board of Selectmen to evaluate placing a ballot question at the next election which would reduce the levy limit on a recurring basis for the start of the fiscal year 2021 Town budget process and beyond.

Background

While overrides of the statutory limit on tax levy growth to allow increased spending are quite common; underrides -- giving up taxing authority -- are very rare. A public literature search suggests that only 15 of the Commonwealth's 351 cities and towns have enacted underrides, with Hopkinton, West Newbury, and Williamsburg doing so on two occasions each.

Where they have been enacted, underrides have been characterized as evidence of fiscal discipline; resetting the future-year budget bar to a lower level so that excess tax levy is not viewed as a void to be filled with non-essential taxing and spending.

An underride enacted in the FY 2020 budget process would have no impact on FY 2020 spending and would not reduce any taxpayer's bill in FY 2020. An underride would only impact budget planning for FY 2021 and beyond by establishing a lower budget limit for future year budget preparation. Further, it is noteworthy that both underrides and overrides are reversible by action of the Board of Selectmen and the Town Voters in future years.

<u>Pros of an additional underride in Hopkinton:</u>

- Signals a commitment to control spending at current levels rather than baselining spending on a levy limit that accumulated over a long period.
- Necessitates specific override discussions for substantial future spending increase proposals, with more focus than the normal budget process provides
- Drives Town managers to focus on cost control
- May signal fiscal conservatism to lenders, which could enhance the perception of creditworthiness. (Note: In the current bond market across bond term lengths, the difference in interest costs between the highest bond rating, which Hopkinton has, and the next highest rating is 20 basis points, or two-tenths of one percent. For a ten year borrowing, the highest bond rating provides about a 7.1% discount in interest costs over the next highest bond rating.)
- If exigent conditions arise, an underride can be reversed with an override by the same voting bodies with the same approval requirement, after conscious, public consideration of specific circumstances

<u>Cons of an additional underride in Hopkinton:</u>

- A long standing unused tax levy may be considered an element of financial strength and discipline; and if so, the elimination of unused tax levy could reduce the perception of creditworthiness
- For bond rating purposes, existing unused levy may offset other weaknesses, like the Town's Stabilization Fund Status, which is $459,270, below the target threshold of 5% of the FY 2019 Voted Annual Budget of $82,897,963
- An ongoing cycle of alternating underides and overrides could degrade investor and stakeholder confidence
- The elimination of unused levy could restrict consideration of meritorious service and investment opportunities to the Town's long term detriment

Sensitivity analysis; three possible approaches:

	Reduce unused tax levy by $250,000	Reduce unused tax levy by $500,000	Reduce unused tax levy by $1,000,000
Projected FY 2020 unused tax levy	$1,180,568	$1,180,568	$1,180,568
Less, reduction in unused levy	($250,000)	($500,000)	($1,000,00)
Revised unused tax levy	$930,568	$680, 568	$180,568
] Impact on taxpayers if unused tax levy were to be appropriated in future years instead of being removed by underride.	An increase of 6.3 cents on the existing tax rate of $17.17 per thousand dollars of valuation; or a $37.77 rise on the $10,293 FY19 tax bill on the average (mean) valued $599,500 Hopkinton home.	An increase of 12.6 cents on the existing tax rate of $17.17 per thousand dollars of assessed valuation; or a $75.54 rise on the $10,293 FY19 tax bill on the average (mean) valued $599,500 Hopkinton home.	An increase of 25.2 cents on the existing tax rate of $17.17 per thousand dollars of assessed valuation; or a $151.08 rise on the $10,293 FY19 tax bill on the average (mean) valued Hopkinton home.