

## **Title**

# **Southborough Real Estate Tax Policy**

## **Tax Rate Policy Alternatives Benefiting Residential Tax Payers**

### **Abstract**

*This report compares Southborough's real estate tax policy and demographics to the 350 other cities and towns in Massachusetts. The goal of the report is to identify alternatives to Southborough's current tax structure that may better serve the needs of residential property owners.*

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## **Introduction**

Because the Town of Southborough is facing difficult decisions as tax revenues are predicted to fall well below planned spending, all options for meeting the projected budget shortfalls should be considered. This report looks at the relationship between tax policy, home values and commercial development within Massachusetts to identify plausible alternatives to dire spending cuts or to significant residential property tax increases. The data used in this comparison is from the Massachusetts Department of Revenue website and represents the collected experience of the 351 cities and towns in Massachusetts.

## **Southborough Demographics**

Data for the tax year 2012 have been used for this report. The data from the Massachusetts Department of Revenue specific to Southborough are presented as a reference. The following specific data are relevant to this analysis:

### **Southborough Assessed Property Values**

All Property	\$ 2,058,537,537
Residential	\$ 1,660,192,647
Commercial	\$ 218,948,090
Industrial	\$ 108,793,900
Personal	\$ 70,602,900
Total Com./Ind./Pers.	\$ 398,344,890
Percent Com./Ind./Pers. (CIP)	19.4 %

### **Southborough Single-Family Home Data**

Average Single-Family Home	\$ 516,361
Single-Family Homes	2,797
Average Tax Bill	\$ 8,334
Tax Rate	\$ 16.15

## **Southborough's Unique Position**

Of the 351 municipalities in Massachusetts, only 49 municipalities have average home values above \$500,000. Southborough is one of these 49 municipalities in 2012 with an average home value of \$516,361. Of this group of 49 municipalities, 18 have less than 5% of their tax base identified as commercial/industrial/personal (CIP) property. Increasing the CIP property threshold to 10% expands the group to 37 municipalities of the 49. Expressed in another fashion, 75% of the 49 municipalities in Massachusetts with average home values greater than \$500,000 have less than 10% CIP property. Southborough, with CIP property of 19.4%, has twice to three times the CIP property of the majority of these 49 mainly residential towns and is one of only 6 municipalities in this group of 49 with CIP property above 15%. Helping to manage this unique position in the best interests of the residents of Southborough is the goal of this report. The report compares Southborough to many other municipalities in Massachusetts with the goal of singling out those cities and towns that have been successful in maintaining residential property values with affordable real estate tax rates.

## ***Lowering Residential Tax Rates with Increasing Development***

In 2012 only 2 of the previously identified 49 municipalities—Andover and Bedford—have CIP property greater than Southborough's 19.4% and a residential tax rate lower than Southborough's. Both of these municipalities have average home values similar to Southborough's. Their reduced residential tax rate is achieved by applying higher tax rates to CIP property than to residential property. Southborough does not use this so-called "split tax rate". Southborough charges the same tax rate for residential, commercial, industrial and personal property. Andover and Bedford charge CIP property owners one and one half (1.5) times (Andover) or two (2.0) times (Bedford) their residential rates. If these 2 towns were to restore a single tax rate, the result would be residential taxpayers in both towns paying higher tax rates of \$1.86 (Andover) or \$3.77 (Bedford) per thousand. Expressing the tax savings in terms of the tax payment for the average home in these towns, the annual tax increase would be \$1,026 in Andover and \$1,955 in Bedford.

There are of course many municipalities with lower tax rates than Southborough's and CIP property greater than Southborough's, but they have lower to significantly lower average home assessed values. Expansion of commercial and industrial development to reduce residential tax rates has its risks as discussed later in this report.

If Southborough were to adopt a split tax rate policy similar to the policies in Andover and Bedford, the average taxpayer in Southborough would save either \$750 or \$1500 per year depending on which town Southborough used as a model. This tax savings could be achieved without endangering residential property values with increased commercial and industrial development and could provide a buffer against the tax rate escalations anticipated by recent budget forecasts.

Andover and Bedford are not isolated examples of towns using higher tax rates for CIP property owners. In 2012 there were 110 Massachusetts municipalities with a split tax rate structure. This number is steadily increasing each year. Surprisingly, a number of these towns with the percentage of CIP property (i.e., commercial development) lower than Southborough's 19.4 % provide significant tax relief to residential taxpayers.

## ***The Case for a "Split" Tax Rate***

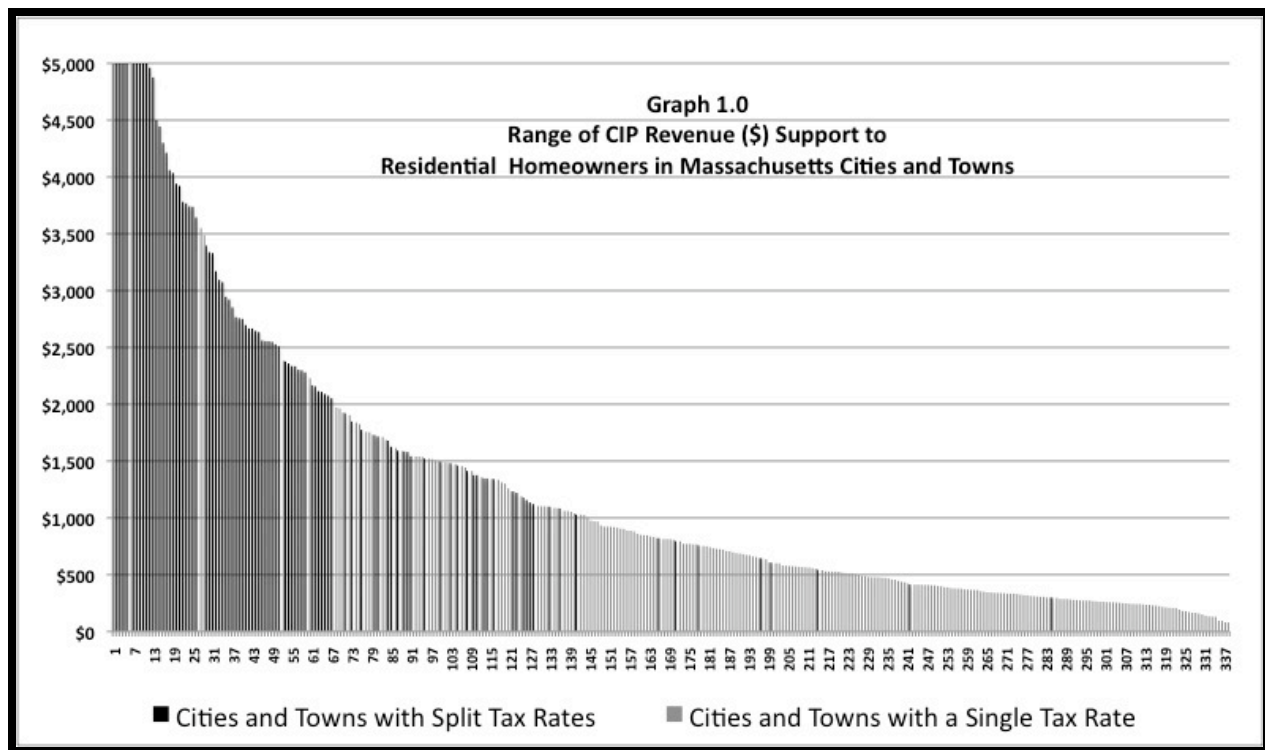
Before continuing it is important to note the substantial financial support presently provided by Southborough's commercial/industrial/personal property owners. This is part of Southborough's unique position in the State. To quantify this financial support a few simple calculations are required:

- First, divide the total value of the CIP property in town by the number of single-family homes. For Southborough in 2012 this result is \$142,419 of CIP property per single-family home. Ranking Southborough against the other 350 cities and towns in Massachusetts, using this same calculation, places Southborough as 29<sup>th</sup> highest in the State. This simple comparison contradicts the notion that Southborough, when compared to other cities and towns in the State, is a community deficient in CIP tax base.

# Real Estate Tax Policy

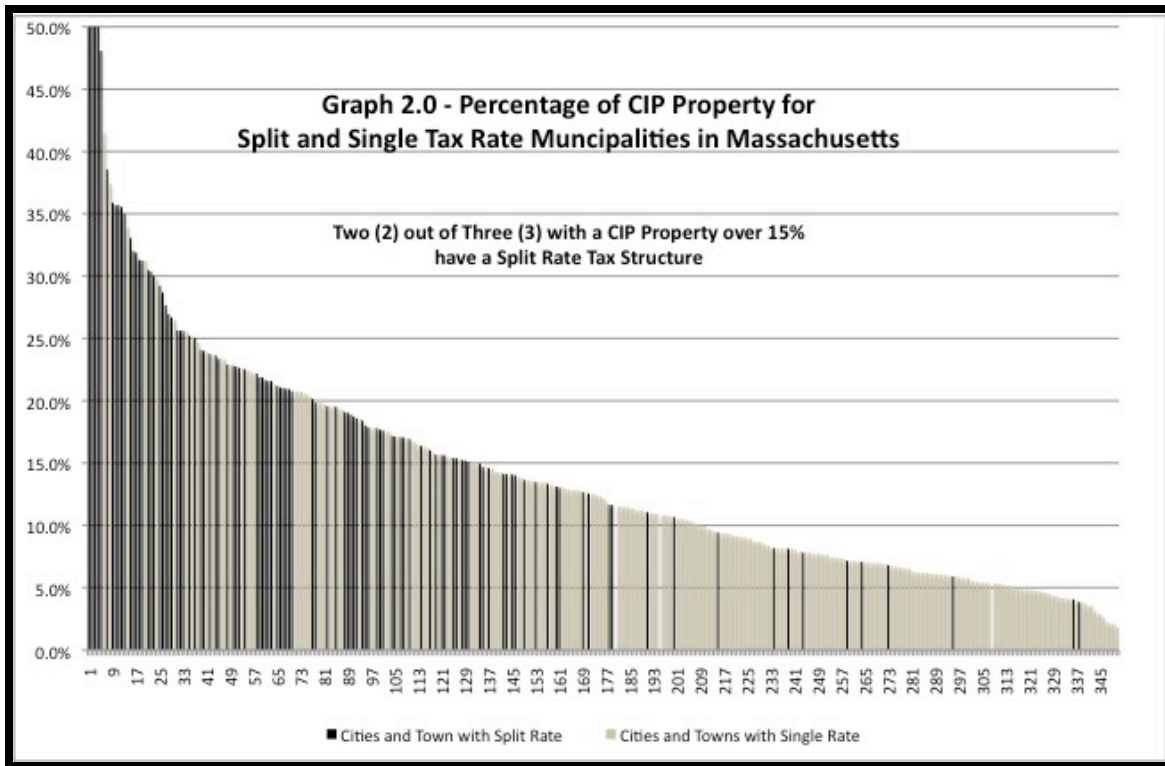
- Second, multiply the \$142,419 of CIP property per single-family home by Southborough's 2012 single tax rate of \$16.15. This shows that \$2,300 in tax revenue is provided by CIP property owners for each single-family dwelling in Southborough. Loss of this revenue would require Southborough residents to bear a significantly increased tax burden. To put the significance of this support in perspective, for one-half of the cities and towns in Massachusetts the equivalent contribution is less than \$750 per single-family home.

There are cities and towns in Massachusetts that do derive more financial support from their CIP property base in terms of revenue per single-family dwelling than Southborough, but they do not accomplish this by increasing the size of the CIP tax base. A graphic of the range in the CIP tax dollars per homeowner for cities and towns in Massachusetts is presented in the Graph 1.0. As the graph clearly illustrates, cities and towns with a split rate tax structure (darker bars) provide individual residential homeowners with greater tax dollar support than those who continue to use a single tax rate (lighter bars).



As this graph demonstrates, the selection of tax policy has a significant impact on the tax burden to residential property owners. Those cities and towns using a split rate tax policy deliver the greatest benefit to residential homeowners.

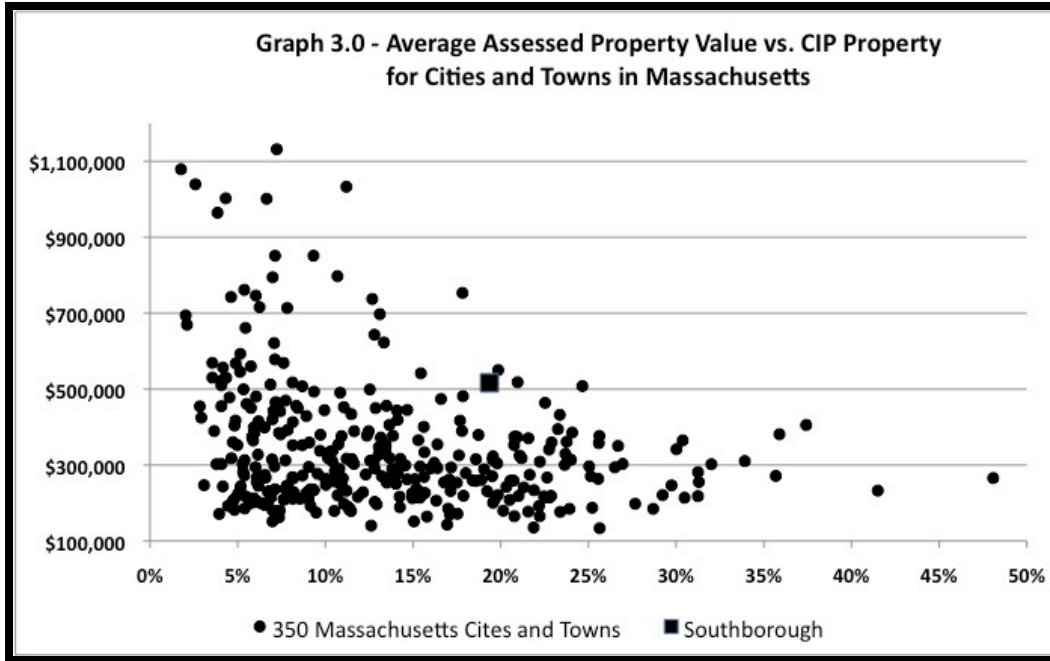
Of the 351 cities and towns in Massachusetts, it is of interest to look at which have split rate tax structures. Graph 2.0 breaks down this population of municipalities into split and single rate municipalities and plots them by the percentage of CIP property. Looking at this chart you can see municipalities with greater CIP property levels are more likely to have a split tax rate. Of the municipalities with a CIP property level over 15 %, two (2) out of three (3) the cities and towns have a split rate tax structure. Southborough at 19.4 % is within this grouping.



With the number of cities and towns adopting a split rate structure increasing each year, the question now becomes why does Southborough, at 19.4%, continue to maintain a single tax rate? Is Southborough creating financial hardship on our local government and residents by persisting with a single tax rate?

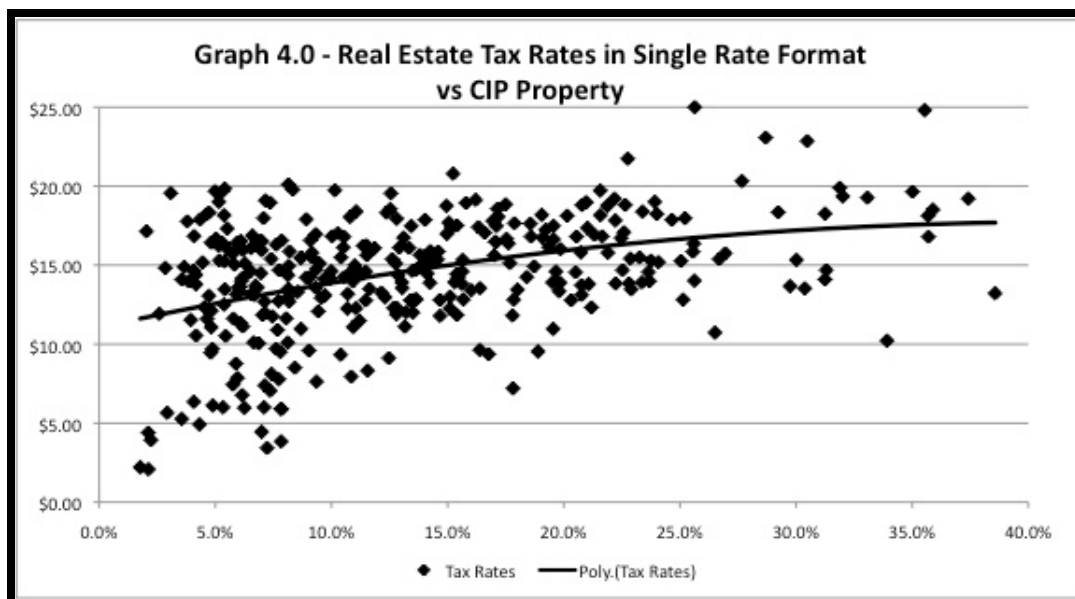
## ***The Impact of Commercial and Industrial Development On Residential Assessed Values***

The relationship between CIP property and average home value is a complex one. Earlier in this report it was noted that Southborough is an anomaly in Massachusetts—with high average residential property values (\$516,361) and a high percentage (19.4%) of CIP property. There are no municipalities in Massachusetts with average home values greater than Southborough's and a CIP property percentage above 21%. Attempting to increase CIP tax revenues by expansion of development in the town is a risky proposition, as it may result in lowering of average home values. For example, the statewide data shows that there are no municipalities in the State with average residential property values above \$410,000 and a CIP property percentage above 25 %—so attempting to achieve even a modest 5% tax reduction for residents by pushing the town's CIP property percentage near 25% could result in a substantial reduction in average home values. The highest average residential property value for a town with a CIP property percentage above 25% is Westborough's, at \$405,503. Graph 3.0 presents a visual representation of the relationship between residential property values and commercial development.



This graphic clearly indicates that a policy of increasing the percentage of CIP property in the Southborough could have serious negative impact on average residential property values. Residents and public officials should not pursue this approach without understanding the likely consequences.

As far as the expectation that tax rates drop with increasing CIP property value, this expectation is challenged by a look at the tax rates on property across Massachusetts. To compare the tax rates between towns a common measure of tax burden is needed. The simplest means to accomplish this is to compare tax rates in the form of single tax rate as they exist or as the equivalent calculated single rate where split rates have been implemented. Presenting these single tax rates verse the CIP property of each town produces the following graphic.

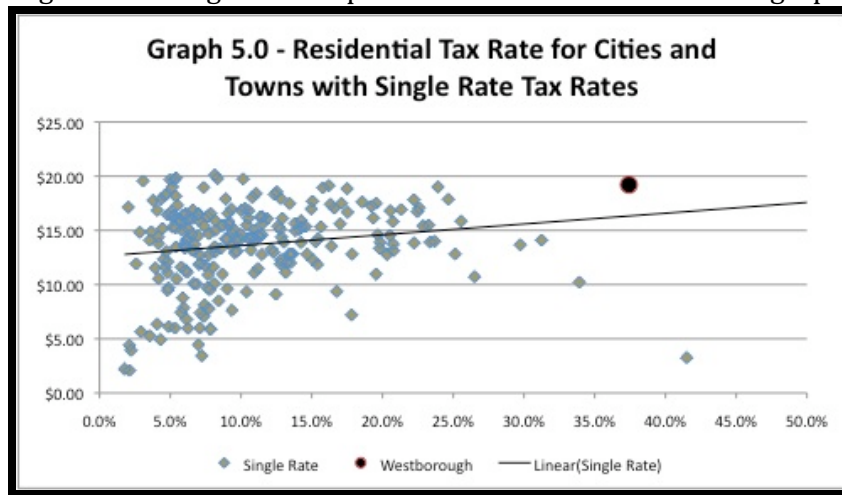


# Real Estate Tax Policy

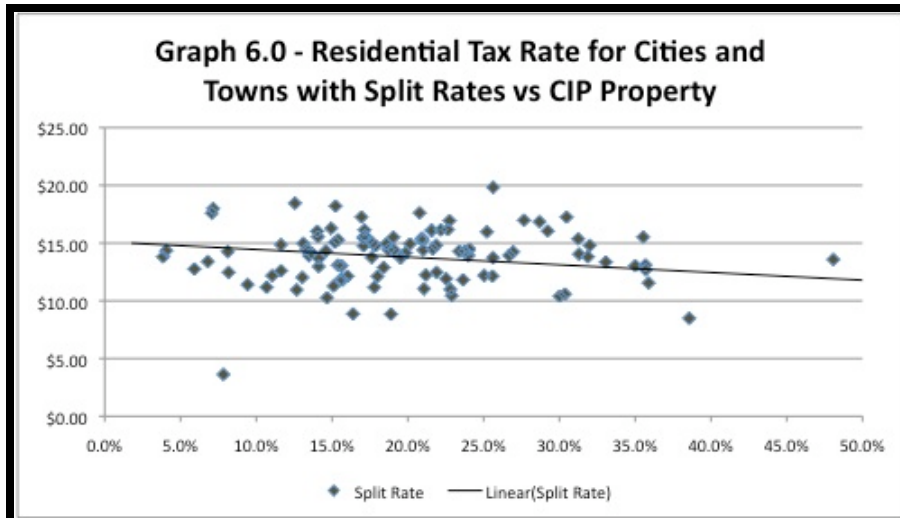
As the trend line on Graph 4.0 indicates, with an increase in the proportion of CIP property within Massachusetts cities and towns, the real estate tax rate on assessed property tends to increase. Rates vary across the State but the trend is clear: with increased levels of CIP property, higher real estate tax rates are more likely. This result argues against those advocating for broadening the CIP property tax base by increasing commercial development and thereby reducing real estate tax rates.

To better demonstrate the benefits a split tax rate, the data from Graph 4.0 is plotted using actual tax rates as two populations, one population of cities and towns with a single rate tax structure and another for split tax rate communities.

Graph 5.0 is the plot of residential tax rates for those cities and towns using a single tax rate. As with Graph 4.0, higher CIP property levels tend to ensure higher residential tax rates. Westborough, as shown on the graph, stands as a singular example of this trend with one of the highest tax rates in the state while having a significant CIP property base. An addendum to this report called "The Westborough Paradox" demonstrates the direct impact tax policy can have on residential property owners by comparing Westborough with a split rate town with similar demographics.



Graph 6.0 is plot of residential tax rates for those cities and towns with a split rate tax structure. As graph 6.0 clearly shows, the trend is for tax rates to diminish as the CIP property level increase. This is the scenario where residential property owners finally benefit from increased CIP property levels.



## **Summary and Next Steps**

**What should Southborough residents conclude from this data?** Southborough does currently enjoy a significant financial contribution from the existing CIP property tax base. If the experience of the 351 cities and towns in Massachusetts is to be believed, the most effective path to providing tax relief to residential property owners via the CIP property tax base is to employ the split tax structure now used by over 100 Massachusetts municipalities. It bears repeating that two thirds (2/3) of the cities and towns in Massachusetts with similar levels of CIP property have a split rate tax structure. Southborough should not ignore the evidence provided by the other 350 cities and towns in Massachusetts.

**What will be the likely responses to this report?** There are several possibilities, including:

- CIP property owners and a variety of real estate and business interests will very likely object to use of a split tax rate, as they have objected previously when a split tax rate has been considered in Southborough. The reason for this objection is clear, as the economic advantage that these interests enjoy with the current tax policy would be in jeopardy.
- Some residential property owners may simply believe it is unfair to impose higher tax rates on CIP property owners and are willing to accept the associated costs and risks of this principle.
- The proposal that Southborough adopt a split rate tax structure will be viewed as an anti-business posture. To counter this opposition it can be pointed out that the two model towns used in this report, Andover and Bedford, have higher average property values, a higher CIP property base and a split tax rate. Maintaining these three factors in harmony protects the interest of the residents and makes future CIP property development a benefit to the residents.
- There may be those who believe a split tax rate policy can backfire and result in diminished tax benefits to the extent that it causes CIP property owners to leave town or to not pursue commercial development in Southborough. Graph 1.0 illustrates a counter to this concern with the greater tax benefits realized by communities employing a split tax rate. If a split tax rate does indeed diminish the benefits to residential property owners, the bar graph would look very different showing those communities with split tax rates on the right side of the bar graph—and this is clearly not the case. In fact, the residents of municipalities with a single tax rate, like Southborough, are the ones who see diminished benefits.
- Some may question the data or the analysis in this report. The data are from the Massachusetts Department of Revenue. This information is collected/presented in a consistent way for all cities and towns and is the best available for the analysis. There may be concern that the relationships shown in the graphics are evidence of “correlation” but not “causality”. This is technically correct. While it would be preferable to have irrefutable evidence of causality between the data variables and the results, the overwhelming evidence of correlation can be a useful guide to public policy.
- Finally, most residential taxpayers can look at this information and conclude that Southborough is overdue in implementing a split tax rate as a reasonable policy to mitigate rising public expenditures and residential property tax rates.



## *Addendum*

### The Westborough Paradox

There can be an instant in time when what you have considered a normal everyday experience is suddenly transformed by the discovery there are others who are living in similar circumstances but with entirely different results. This experience is called a paradox. For the people of Westborough and the real estate taxes they pay every year, there is a parallel but very different experience in Burlington, MA. The circumstances are similar; the results are very, very different, as you will see. For Westborough residents this paradoxical experience is not limited to Burlington, there are 110 other cities and towns in Massachusetts that could be used for comparison, Burlington just happens to be the community that most closely matches Westborough demographically and best illustrates what could be in Westborough.

To bring this paradox into focus, data from the Massachusetts Department of Revenue year 2012 is used. The key parameter making Westborough and Burlington a closely matched pair is the nearly identical commercial and industrial tax base. Westborough's tax base is 37 % commercial/industrial while Burlington has a base of 36%. Compared to most communities this is a large percentage of the tax base and is commonly considered a benefit to the community.

For Burlington the residential tax rate in 2012 was \$11.55 per thousand dollar of assessed property. Burlington, unlike Westborough, has a split tax rate structure with the commercial/industrial rate at \$ 30.95. Westborough has a single rate tax structure of \$19.15 for all property in the town. Knowing just the information provided here, the equivalent single tax rate for Burlington can be calculated; it would be \$18.53. With the single tax rates of \$19.15 and \$18.53, the two towns again have similar characteristics.

Another common characteristic of the two towns is the average assessed value of the residential property. Westborough's average is \$405,000 and Burlington's is \$381,000. Now, using the average assessed value of a residence in Burlington, if the single rate of \$18.53 per thousand were used to calculate the average annual tax bill in Burlington, it would create a \$2,651 tax increase for the average homeowner in Burlington. Clearly the residents in Burlington would have no interest in a single rate tax structure.

Now flipping the calculation and using Burlington's split rate residential to commercial tax rate ratio, not the actual rates, the equivalent tax rates in Westborough would be \$ 11.82 (residential) and \$ 31.56 (commercial/industrial). The applying these rates would represent a savings of \$2,968 for the average residential taxpayer. This would be a \$250 per month savings for the average homeowner in Westborough.

So now the paradox is clear. The residents of Burlington see an annual savings of \$2,651 in their tax bills while homeowners in Westborough pay \$2,968 with the same basic demographics. Homeowners that are experiencing different existences under similar conditions.