

# News Release

For Immediate Release

October 21, 2002

*MTF*

## MTF Report: Weak Economy/State Fiscal Crisis Darken Outlook for Municipal Finances

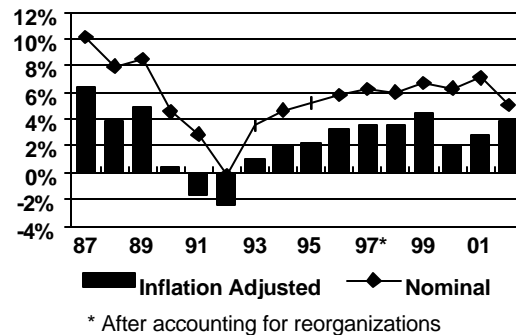
While overall performance remained healthy in 2002, municipal finances have entered a new and much more difficult phase because of continuing weakness in the state economy and the impact of the Commonwealth's fiscal crisis on state aid to cities and towns, according to the Massachusetts Taxpayers Foundation's 32nd annual analysis of local revenues and spending.

The MTF study, *Municipal Financial Data*, reports that total local revenues were up a substantial 5.7 percent in 2002, with almost eight percent growth in aid to schools and a record amount of property tax revenue from new construction.

However, the pace of improvement in local finances slowed perceptibly in fiscal 2002, a trend that will become even more apparent in 2003:

- Overall state aid to municipalities grew just 2.4 percent in 2002 and is flat in 2003, a far cry from the almost nine percent average annual growth for most of the 1990s.
- Excess tax capacity under Proposition 2 1/2 fell 3.4 percent to \$198 million in 2002, the first decline in a decade.
- The dollar value of proposals to override Proposition 2 1/2's tax limit -- and voter approval of overrides -- were at their highest levels in almost ten years.
- Free cash rose only 3.2 percent in 2002 to a total of \$559 million, a rate of increase that was roughly one-fourth the average growth of the previous four years.

**Local Revenues**  
 Annual Percent Change  
 Fiscal 1987-2002



With no sign of an economic recovery in sight and the state enmeshed in serious fiscal difficulties, all signs point to a much harsher local fiscal environment over the next several years, the report concludes. While many municipalities are still benefiting from the boom in new construction at the end of the 1990s, the sluggish economy will increasingly take its toll on local tax rolls. At the same time, the seismic \$2.5 billion drop in state tax revenues in 2002 continues to rock the Commonwealth's finances. Despite major tax increases, spending cuts, and essentially level funding of local aid in 2003, the state still faces a structural deficit of \$1-2 billion in 2004 and has already exhausted most of its reserves in dealing with the enormous revenue declines.

"Given the huge structural deficit in the state budget, future reductions in aid to cities and towns are almost inevitable," said MTF President Michael J. Widmer. "While some communities can rely on rainy day reserves built up in the good times to help buffer the impact of these cuts, many others will face major fiscal problems."

Especially hard hit will be the scores of communities that have benefited little from the large increases in state aid to schools over the last decade or that have missed out on the boom in new construction -- and the resulting growth in property tax revenues -- because of a lack of buildable land. According to the Foundation's analysis, communities at risk include 43 which have stabilization reserves of less than one-half of one percent of their operating budgets, 20 which have already relied heavily on overrides of Proposition 2 1/2 to cope with rapid enrollment growth in the 1990s, and the dozens of communities whose finances are constrained by a scarcity of buildable land.

Despite the signs of fiscal weakening, total local revenues still rose a vigorous 5.7 percent<sup>1</sup> to \$16.2 billion in 2002, as strong growth in property taxes was only partially tempered by the smallest annual increase in local aid since 1993. In 2001, total local revenues increased 6.7 percent. At the same time, property taxes jumped 6.4 percent to \$8.0 billion in 2002, largely because of prior new construction that was added to the tax rolls in 2002. Although new construction revenues rose to the record amount of \$213 million in 2002, the 5.4 percent rate of increase was only one-third the annual pace of growth of the previous two years.

For the first time in almost a decade, state aid grew more slowly than property taxes, up \$105 million, or 2.4 percent, to a total of \$4.5 billion, a dramatic decline from the 11.1 percent peak in 1998 and the almost nine percent average annual growth for most of the 1990s. While school aid to cities and towns increased 7.8 percent in 2002, lottery aid rose only 1.1 percent to \$830.1 million (after adjusting for a shift in timing), sharply below the 8.5 percent growth in 2001. With the slower overall growth in state aid in 2002, the rate of increase in total local spending eased as well, with a rise of 5.2 percent to \$15.8 billion, compared to 7.2 percent in 2001.

The squeezing of local finances was also reflected in several key measures of local fiscal health. In 2002, excess capacity broke a ten-year record of steady growth, with a 3.4 percent drop to \$198 million. The 3.2 percent growth in net free cash (operating surpluses from the previous year less uncollected taxes and other deficits) was sharply below the 11 percent average annual growth over the previous four years. And while fewer towns attempted overrides of Proposition 2 1/2 in 2002, the dollar value of override proposals -- \$52 million -- was the highest in a decade, 43 percent above 2001 and five times the low point in 1998. Override approvals continued to climb upward as well: After averaging less than \$8 million a year for most of the 1990s, approvals tripled to \$21.8 million in 2000, rising further to \$30.6 million in 2001 and \$33.6 million in 2002.

The 32nd edition of *Municipal Financial Data* was presented as a public service with the help of a grant from First Southwest Company.

---

<sup>1</sup> After adjusting for a shift in the timing of distributing unanticipated lottery receipts.