FINANCIAL ISSUES
FOR THE
FY 2008 BUDGET SEASON

- Continued maximization of the tax levy and reduction in the tax levy as a percentage of assessed value:

FY	Levy Limit without Debt & Capital Exclusions	Maximum Levy Limit	Total Tax Levy	Excess Capacity	Excess as a % of Maximum Levy	Tax Levy Ceiling	Assessed Value	Tax Levy as % of Assessed Value
2007	$41,119,263	$44,686,206	$44,644,721	$41,485	0.09%	$128,881,988	$5,155,279,506	0.87%
2006	$39,143,375	$43,235,918	$43,214,514	$21,404	0.05%	$116,922,387	$4,676,895,485	0.92%
2005	$37,653,331	$41,425,381	$41,399,263	$26,118	0.06%	$106,260,943	$4,250,437,722	0.97%
2004	$36,196,865	$40,381,102	$39,549,134	$831,968	2.06%	$99,670,197	$3,986,807,862	0.99%
2003	$34,764,572	$39,797,377	$37,027,303	$2,770,074	6.96%	$87,328,544	$3,493,141,773	1.06%
2002	$33,131,548	$36,263,184	$36,060,964	$202,220	0.56%	$66,386,164	$2,655,446,563	1.36%
2001	$31,465,027	$32,315,523	$32,224,086	$91,437	0.28%	$64,707,000	$2,588,280,006	1.24%
2000	$29,312,849	$30,160,105	$28,627,015	$1,533,090	5.08%	$53,648,830	$2,145,953,181	1.33%

Fiscal Year	Unused Capacity
1999	$1,537,605
1998	$1,084,657
1997	$112,269

Actual unused capacity in FY 2003 was $365,056 due to the use of the $2,385,000 bond premium via Free Cash

- Growth in the area of the tax levy and continued shift to the residential sector. Town of Shrewsbury tax burden continues to be below communities in the region (Exhibits 1.1, 1.2 and 1.3):

FY	Residential	Open Space	Commercial	Industrial	Personal Property	Total	Res/OS as % of Total	CIP as % of Total***
2007	$39,398,448	$27,101	$3,171,601	$1,687,643	$359,927	$44,644,720	88.31	11.69
2006	$38,039,674	$24,760	$3,101,144	$1,688,763	$360,174	$43,214,515	88.08	11.92
2005	$36,287,392	$31,000	$3,116,629	$1,601,200	$363,043	$41,399,264	87.73	12.27
2004	$34,417,527	$28,748	$3,093,957	$1,624,559	$384,343	$39,549,134	87.10	12.90
2003	$31,669,588	$23,373	$3,155,765	$1,584,456	$594,120	$37,027,302	85.59	14.41
2002	$30,155,270	$26,203	$3,428,258	$1,647,785	$803,448	$36,060,964	83.70	16.30
2001	$26,894,514	$23,913	$3,079,012	$1,487,858	$738,789	$32,224,086	83.54	16.46
2000	$24,079,563	$31,178	$2,770,717	$1,343,662	$401,896	$28,627,016	84.22	15.78
1999	$22,321,588	$30,133	$2,585,052	$1,243,499	$406,542	$26,586,814	84.07	15.93
1998	$21,102,676	$48,130	$2,542,846	$1,200,366	$388,515	$25,282,533	83.66	16.34
1997	$21,076,940	$28,184	$2,513,025	$1,111,899	$436,011	$25,166,059	83.86	16.14

***** Selected CIP Percentages**
Boylston (8.9%), Franklin (20.3%), Grafton (7.6%), Northborough (19.8%), Westborough (38.0%), Worcester (18.5%)

- FY 2007 saw the first increase in new growth since FY 2001. Question is whether this is a trend or an anomaly (Exhibit 2.1):

Fiscal Year	New Growth
2007	$997,304
2006	$548,711
2005	$551,544
2004	$563,179
2003	$804,735
2002	$879,895
2001	$1,419,357
2000	$833,094
1999	$1,122,922
1998	$713,090
1997	$726,315
1996	$689,741
1995	$585,810

- Status of personal property valuation for high tech firms

Fiscal Year	Total PP Value	High Tech Value	% of High Tech
2007	$41,561,998		
2006	$38,979,835	$6,000,000	15.39%
2005	$37,273,381	$5,900,000	15.83%
2004	$38,744,224	$5,000,000	12.90%
2003	$56,049,097	$30,823,841	54.99%
2002	$59,164,147	$26,645,361	45.04%
2001	$59,340,454	$26,656,001	44.92%
2000	$30,127,106	$18,140	0.06%

Change of HP to a manufacturing corporation resulted in loss of high tech value. Previous designation allowed for equipment to be taxed as personal property

- Status of school choice and charter schools assessments and reimbursements. The Charter School program is heavily subsidized (Exhibit 3.1) and a change in formula or practice will have an impact to the bottom line. Recently, the School Committee expressed concern over the impact of the new Marlborough Academy for Math & Science.

Fiscal Year	Number of Students (FTE)	Net Cost of Charter School Tuition	Number of Students (FTE)	Cost of School Choice Program
2006	38.30	$204,783	18.5	$97,394
2005	25.48	$168,898	17.1	$104,140
2004	20.00	$160,161	16.5	$78,761
2003	23.50	$170,601	10.7	$46,558
2002	21.15	$94,256	13.2	$53,319
2001	24.44	$52,736	4.7	$21,108
2000	29.24	$26,307	7.9	$32,859
1999	18.00	$0	7.7	$37,470

- The status of State Aid in FY 2008 and beyond (Exhibit 3.1). This is the area of great uncertainty due to the new administration taking office. Will new formulas be adopted? What funding levels will be proposed? Will there be true revenue sharing (Exhibit 3.2)? What is the true condition of the Commonwealth's finances (Exhibit 3.3)? Also, State Charges and Offsets may top $1 Million in FY 2008:

Fiscal Year	Total State Aid
2007	$23,727,465
2006	$21,077,629
2005	$18,621,647
2004	$16,744,700
2003	$12,679,840
2002	$11,648,532
2001	$10,595,853
2000	$9,596,115
1999	$8,693,528
1998	$7,850,691

$3,697,772 SBAB

- Status of local receipts in light of current economic climate (Exhibit 4.1). It appears that the bottom was reached in FY 2005 but motor vehicle excise continues to mystify (See Exhibit 4.2).

- The status of surplus lottery or other distributions. The future of the lottery program relative to the uncapping. Can growth be sustained?

Fiscal Year	Lottery Distributions	Surplus Distribution (Received in next Fiscal Year)
2007	$3,107,117	$0 (est)
2006	$2,493,603	$0
2005	$2,110,492	$0
2004	$2,110,492	$269,859
2003	$2,250,774	$0
2002	$2,482,932	$0
2001	$2,324,233	$172,153
2000	$2,123,910	$275,198
1999	$1,896,262	$275,930

- Projected increases in health insurance expenses resulting from premium increases and changes in enrollment for both active and retired employees. FY 2006 saw the first decrease in actual spending in may years. School Department has increased its level of contribution for benefits costs from school lunch and after school programs.

Fiscal Year	Amount Expended
2006	$5,376,598
2005	$5,529,698
2004	$4,483,109
2003	$3,836,906
2002	$2,991,004
2001	$2,573,606
2000	$1,879,964
1999	$1,701,899
1998	$1,637,322

- Growth in the Medicare Match Account continues but in FY 2006 at a far less rate than in previous years. School Department has increased its level of contribution for benefits costs from school lunch and after school programs.

Fiscal Year	Amount	Percent Increase	Notes
06	$534,477	4.26%	No transfer required ($575,000 aprtn)
05	$512,640	12.89%	Transfer of $7,360 was required
04	$454,086	11.46%	No transfer required ($480,000 aprtn)
03	$407,410	12.15%	No transfer required ($453,000 aprtn)
02	$363,278	11.60%	No transfer required ($375,000 aprtn)
01	$325,524	20.79%	$13,000 Transfer was not Required

00	$269,474	13.01%	$44,747 Transfer was Required
99	$238,445	25.60%	$40,000 Transfer was Required
98	$189,852	12.12%	
97	$169,329	16.55%	
96	$145,286	18.83%	
95	$127,638	6.61%	
94	$119,720		

- Bottom may have been reached for investment earnings in FY 2006. Question is raised however about the future on inertest rates and the amount of cash on hand to invest:

Fiscal Year	Total Income
2006	$1,126,738
2005	$932,675
2004	$1,229,492
2003	$1,561,045
2002	$980,007
2001	$1,753,148
2000	$1,721,010
1999	$1,605,296
1998	$1,597,405
1997	$1,701,900
1996	$1,507,650
1995	$940,115

Affect of call provisions of bondholders taking advantage of lower interest rates

- Question over a projection of Motor Vehicle Excise Tax receipts in FY 2007 as no trend is apparent:

Fiscal Year	Total Income
2006	$4,688,251
2005	$4,680,209
2004	$4,260,729
2003	$4,438,140
2002	$4,127,776
2001	$3,919,368
2000	$3,770,230
1999	$3,291,131

- Medicare billing for certain costs associated with the Special Education Program has rebounded to above $100,000 and is projected to stay at this level with some growth anticipated:

Fiscal Year	Reimbursement
2006	$107,257
2005	$51,139
2004	$49,779
2003	$185,266
2002	$129,032
2001	$70,106
2000	$98,263
1999	$130,056

- Supplemental Tax Program that was started in 2001 has tracked downward in keeping with the slow down of new construction.

Fiscal Year	Commitment	Note	Revenue
2006	$ TBA	$ TBA billed in FY 07	$47,040
2005	$80,084	$3,075 billed in FY 06	$169,937
2004	$180,715	$13,287 billed in FY 05	$178,455
2003	$98,631	$26,813 billed in FY 04	$89,088
2002	$145,835	$38,209 billed in FY 03	$104,070
2001	$159,457		$142,235

- The MBTA assessment will continue to trend upward (Exhibit 5.1 (TBA)):

Fiscal Year	Amount
FY 2008	$151,839 (est)
FY 2007	$132,034
FY 2006	$112,991
FY 2005	$91,481
FY 2004	$42,430
FY 2003	$0

- In FY 2008 the continued effects of a non fully funded pension system will be realized. A new valuation of the system was completed (as of January 1, 2006) for implementation in FY 2008:

Date	Funded Ratio	Unfunded Accrued Liability	Required Appropriation
January 1, 2006	71.3%	$21,831,496	$2,466,000 (est)
January 1, 2004	77.9%	$14,419,434	$1,866,223
January 1, 2002	78.9%	$12,533,566	$1,240,656
January 1, 2000	97.1%	$1,414,990	$1,559,742
January 1, 1999	83.9%	$7,517,187	$1,541,285

- There has been a rebound in the reserve position of the Town with increased Free Cash and Stabilization balances (Exhibits 6.1 & 6.2) Moody's continues to express concern over the Town's reserve position (Exhibit 6.3).

- The size of any Fiscal Year 2007 budget deficit. Previous operational deficits that were handled at the Annual Meeting were:

Fiscal Year	Deficit Made Up At Town Meeting From Free Cash
2006	$203,000
2005	$523,000
2004	$388,000
2003	$366,000
2002	$95,000
2001	$731,000
2000	$103,000

FINANCIAL ISSUES
FOR THE
FY 2008 BUDGET SEASON AND BEYOND

1. Were the increases in water and sewer rates sufficient to cover the costs associated with the new EPA & DEP standards and other infrastructure needs.

2. Impact on Sewer Rates of Chapter 23 of the Acts of 2005 which now allows the tax levy subsidy of the sewer operation to fall to zero from 25% (8.3% tax levy support in FY 2007).

3. Capital Budget requests for the period FY 07 to FY 10 far in excess of available revenue stream. Facility requests in the area of school, parks, police, public works and libraries.

4. Ongoing status of "Budget Busters" (Health, Medicare, Pensions, General Insurance)

5. Status of Town's exempted debt obligation with consideration of additional debt to come on line resulting from Fire Station Project(Exhibit 7.1)

6. The future of coal ash revenue and Phase V at the monofill.

7. School enrollment trends (Exhibits 8.1 & 8.2)

8. Impact on the Town's vehicle fleet in light of continued deferral of replacement.

9. The impact of GASB 45 that deals with Retiree Health Insurance. Current evaluation is underway.

PRIMARY FINANCIAL QUESTIONS

FISCAL YEAR 2008

1. Was the "bottom" reached in FY 2005?

2. At what rate will employee benefit costs continue to rise understanding that an immediate, $600,000± increase in the pension assessment is required?

3. Understanding it will be a new day in 2008, In what direction can we expect state aid to move and at what rate?

4. How does the Town keep a lid on spending with so much pressure building in most municipal departments in addition to pressure on the school budget?

5. How is the increase in solid waste disposal cost to be handled?

6. Does the Town need to update the K-12 Facilities Plan and include municipal department facilities?

7. How will the Fiscal Study Committee final report impact the FY 2008 budget process?

8. In what form, manner and schedule will the discussion of the need of an operational override occur?

EXHIBIT 1.1
TAX RATE RECAPITULATIONS
FISCAL YEAR 2000 TO 2007

	ACTUAL FY 07	ACTUAL FY 06	ACTUAL FY 05	ACTUAL FY 04	ACTUAL FY 03	ACTUAL FY 02
CHARGES						
APPROPRIATIONS	$ 88,001,485.28	$ 83,343,541.82	$ 77,611,947.00	$ 76,082,196.81	$ 68,397,505.02	$ 64,314,219.38
TAX TITLE		$ -	$ -	$ -	$ -	$ -
COURT JUDGMENTS		$ -	$ -	$ -	$ -	$ 126,963.64
OVERLAY DEFICITS		$ -	$ -	$ -	$ -	$ -
CHERRY SHEET OFFSETS	$ 73,331.00	$ 73,909.00	$ 67,387.00	$ 61,412.00	$ 62,215.00	$ 62,973.00
CMRPC	$ 7,078.82	$ 6,906.06	$ 6,737.74	$ 6,573.53	$ 6,413.43	$ 4,776.68
STATE AND COUNTY CHARGES	$ 882,906.00	$ 840,584.00	$ 694,057.00	$ 434,305.00	$ 205,797.00	$ 194,113.00
OVERLAY	$ 484,866.41	$ 451,928.88	$ 334,362.58	$ 465,564.36	$ 301,261.36	$ 257,908.21
TOTAL TO BE RAISED	$ 89,449,667.51	$ 84,716,869.76	$ 78,714,491.32	$ 77,050,051.70	$ 68,973,191.81	$ 64,960,953.91
REVENUE						
STATE AID	$ 23,727,465.00	$ 21,077,629.00	$ 18,621,647.00	$ 16,746,262.00	$ 12,679,840.00	$ 11,648,532.00
OVERESTIMATES	$ -	$ -	$ -	$ -	$ 331.00	$ 2,850.00
SCHEDULE A RECEIPTS	$ 11,400,000.00	$ 10,388,000.00	$ 10,415,000.00	$ 10,244,000.00	$ 9,521,090.00	$ 9,693,984.00
FREE CASH	$ 1,250,000.00	$ 2,000,000.00	$ 2,380,000.00	$ 3,000,000.00	$ 1,501,785.00	$ 1,056,826.92
OTHER AVAILABLE FUNDS						
SALE OF CEMETERY LOTS	$ 18,000.00	$ 25,000.00	$ 25,000.00	$ 25,000.00	$ 25,000.00	$ 25,000.00
SEWER SURPLUS	$ 2,970,000.00	$ 3,566,654.82	$ 2,300,000.00	$ 2,000,400.00	$ 2,140,000.00	$ 1,650,000.00
LIGHT REVENUE	$ 258,939.00	$ 262,767.00	$ 273,150.00	$ 280,490.00	$ 329,010.00	$ 1,860,260.00
CATV REVENUE	$ 484,635.00	$ 499,545.00	$ 514,456.00	$ 529,365.00	$ 736,140.00	$ 820,863.00
STABILIZATION	$ -	$ 170,000.00	$ 635,000.00	$ 185,000.00	$ -	$ 275,000.00
OTHER FUNDS (CHAPTER 90)	$ 1,397,858.00	$ 508,066.00	$ 422,311.00	$ 424,566.71	$ 431,754.76	$ 425,098.66
BUDGET/FUND TRANSFERS	$ 149,868.00	$ 566,713.66	$ 400,223.00	$ 500,000.00	$ 42,316.26	$ 339,500.00
HOME FARM WELL INTEREST		$ -	$ -	$ 1,450,000.00	$ -	$ -
TITLE V RESERVE	$ 15,128.00	$ 16,248.00	$ 4,831.00	$ 4,831.00	$ 4,831.00	$ 4,831.00
INTEREST/PREMIUM RESERVE		$ -	$ -	$ -	$ -	$ 300,000.00
WATER SYSTEM IMPRVMNTS	$ 305,702.00	$ 500,000.00	$ -	$ 930,000.00	$ 430,000.00	$ -
WATER CONSERVATION FUND	$ 50,000.00	$ 30,000.00	$ -	$ -	$ -	$ -
CEMETERY TRUST FUNDS		$ 75,000.00	$ 71,500.00	$ -	$ -	$ -
SPECIAL FUNDS - COAL ASH	$ 425,000.00	$ 275,000.00	$ 250,000.00	$ -	$ -	$ -
HIGHWAY IMPROVEMENTS		$ 400,000.00	$ -	$ -	$ -	$ -
SURPLUS SBAB (FLORAL)		$ 89,681.00	$ -	$ -	$ -	$ -
SALE OF PROPERTY	$ 194,220.00					
SEWER CONSTRUCTION	$ 258,000.00					
FREE CASH (REDUCE LEVY)	$ 500,000.00	$ 500,000.00	$ 500,000.00	$ 728,416.00	$ 2,885,000.00	$ 435,000.00
MUNICIPAL LIGHT (REDUCE LEVY)	$ 115,441.00	$ 121,995.00	$ 115,606.00	$ 118,531.00	$ 113,132.00	$ 112,244.00
CATV REVENUE (REDUCE LEVY)	$ 454,691.00	$ 430,056.00	$ 386,503.91	$ 334,056.00	$ 283,927.00	$ 250,000.00
BOND INTEREST RESERVE	$ 800,000.00	$ -	$ -	$ -	$ 821,732.00	$ -
TOTAL REVENUE	$ 44,774,947.00	$ 41,502,355.48	$ 37,315,227.91	$ 37,500,917.71	$ 31,945,889.02	$ 28,899,989.58
TOTAL LEVY	$ 44,674,720.51	$ 43,214,514.28	$ 41,399,263.41	$ 39,549,133.99	$ 37,027,302.79	$ 36,060,964.33
TAX RATE	$ 8.66	$ 9.24	$ 9.74	$ 9.92	$ 10.60	$ 13.58

11/16/2006

EXHIBIT 1.2
Summary of Single Family Tax Bills
Fiscal Years 1988 to 2007

FY	Assessed Value	Parcels	Average Value	Tax Rate	Single Family Tax Bill	Increase	Percent Increase	Hi-Lo Rank	# of Towns Included	State Median	Variance to State Median
1988	$ 597,062,402	6,130	$ 97,400	$ 14.62	$ 1,424			118	293	$ 1,301	$ 123
1989	$ 1,050,029,027	6,260	$ 167,736	$ 9.36	$ 1,570	$ 146	10.25%	96	297	$ 1,326	$ 244
1990	$ 1,072,459,683	6,314	$ 169,854	$ 10.02	$ 1,702	$ 132	8.41%	112	323	$ 1,504	$ 198
1991	$ 1,099,088,583	6,400	$ 171,733	$ 10.40	$ 1,786	$ 84	4.94%	99	265	$ 1,640	$ 146
1992	$ 972,972,119	6,447	$ 150,919	$ 11.93	$ 1,800	$ 14	0.78%	133	339	$ 1,663	$ 137
1993	$ 1,015,893,420	6,677	$ 152,148	$ 12.22	$ 1,859	$ 59	3.28%	136	339	$ 1,747	$ 112
1994	$ 1,067,739,013	6,938	$ 153,897	$ 12.74	$ 1,961	$ 102	5.49%	132	340	$ 1,808	$ 153
1995	$ 1,082,234,386	7,135	$ 151,680	$ 13.38	$ 2,029	$ 68	3.47%	137	340	$ 1,872	$ 157
1996	$ 1,124,419,977	7,319	$ 153,630	$ 13.84	$ 2,126	$ 97	4.78%	133	340	$ 1,959	$ 167
1997	$ 1,166,241,040	7,485	$ 155,810	$ 14.42	$ 2,247	$ 121	5.69%	129	340	$ 2,031	$ 216
1998	$ 1,274,284,500	7,718	$ 165,106	$ 13.32	$ 2,199	$ (48)	-2.14%	155	340	$ 2,121	$ 78
1999	$ 1,340,116,000	7,952	$ 168,526	$ 13.45	$ 2,267	$ 68	3.09%	155	340	$ 2,191	$ 76
2000	$ 1,473,016,300	8,225	$ 179,090	$ 13.34	$ 2,389	$ 122	5.38%	148	340	$ 2,297	$ 92
2001	$ 1,753,632,800	8,441	$ 207,752	$ 12.45	$ 2,587	$ 198	8.29%	140	340	$ 2,418	$ 169
2002	$ 1,817,609,000	8,572	$ 212,040	$ 13.58	$ 2,880	$ 293	11.33%	124	340	$ 2,577	$ 303
2003	$ 2,466,221,700	8,672	$ 284,389	$ 10.60	$ 3,015	$ 135	4.69%	136	340	$ 2,709	$ 306
2004	$ 2,860,861,900	8,760	$ 326,582	$ 9.92	$ 3,240	$ 225	7.45%	133	339	$ 2,894	$ 346
2005	$ 3,069,672,100	8,861	$ 346,425	$ 9.74	$ 3,374	$ 134	4.15%	138	340	$ 3,067	$ 307
2006	$ 3,402,311,500	8,890	$ 382,712	$ 9.24	$ 3,536	$ 162	4.80%	142	338	$ 3,202	$ 334
2007	$ 3,718,735,600	8,950	$ 415,501	$ 8.66	$ 3,598	$ 62	1.75%				
							95.88%				

11/10/2006

EXHIBIT 1.3

Municipal Market Basket
Comparison of Single Family Tax Bills
Fiscal Year 2005 to 2006
Selected Communities From the Market Basket Project

Rank	Community	Ave Residential Tax Bill (2005)	Ave Residential Tax Bill (2006)	Change
1	Fitchburg	$2,365.00	$2,449.00	$84.00
2	Leicester	$2,264.00	$2,498.00	$234.00
3	Auburn	$2,580.00	$2,602.00	$22.00
4	Oxford	$2,519.00	$2,665.00	$146.00
5	Clinton	$2,654.00	$2,722.00	$68.00
6	Northbridge	$2,581.00	$2,734.00	$153.00
7	Bellingham	$2,684.00	$2,783.00	$99.00
8	Worcester	$2,781.00	$2,879.00	$98.00
9	Leominster	$2,801.00	$2,881.00	$80.00
10	Norwood	$2,961.00	$2,987.00	$26.00
11	Millbury	$2,643.00	$2,999.00	$356.00
12	**Shrewsbury*** **	**$3,374.00**	**$3,536.00**	**$162.00**
13	Hudson	$3,200.00	$3,544.00	$344.00
14	Sutton	$3,208.00	$3,557.00	$349.00
15	Milford	$3,424.00	$3,574.00	$150.00
16	Grafton	$3,486.00	$3,583.00	$97.00
17	Tewksbury	$3,343.00	$3,610.00	$267.00
18	Billerica	$3,449.00	$3,696.00	$247.00
19	Holden	$3,576.00	$3,705.00	$129.00
20	Franklin	$3,515.00	$3,742.00	$227.00
21	West Boylston	$3,638.00	$3,843.00	$205.00
22	Paxton	$3,800.00	$3,866.00	$66.00
23	Danvers	$3,751.00	$3,883.00	$132.00
24	Millis	$4,083.00	$4,180.00	$97.00
25	Foxborough	$3,878.00	$4,230.00	$352.00
26	Sterling	$3,885.00	$4,282.00	$397.00
27	Framingham	$4,129.00	$4,306.00	$177.00
28	Upton	$4,119.00	$4,379.00	$260.00
29	Canton	$4,147.00	$4,445.00	$298.00
30	Boylston	$4,385.00	$4,504.00	$119.00
31	Natick	$4,303.00	$4,559.00	$256.00
32	Mansfield	$4,533.00	$4,625.00	$92.00
33	Chelmsford	$4,467.00	$4,688.00	$221.00
34	Walpole	$4,499.00	$4,727.00	$228.00
35	Berlin	$4,519.00	$4,813.00	$294.00
36	Ashland	$4,713.00	$5,067.00	$354.00
37	Northborough	$4,891.00	$5,078.00	$187.00
38	Medway	$4,961.00	$5,283.00	$322.00
39	Holliston	$5,293.00	$5,548.00	$255.00
40	Norfolk	$4,859.00	$5,556.00	$697.00
41	Westborough	$5,922.00	$6,234.00	$312.00
42	Andover	$6,009.00	$6,400.00	$391.00
43	Hopkinton	$6,015.00	$6,440.00	$425.00
44	Southborough	$6,667.00	$6,884.00	$217.00
45	Acton	$6,900.00	$7,724.00	$824.00
46	Marlborough	$3,796.00	N/A	

*** Shrewsbury was 15th on this list in FY 2005

EXHIBIT 2.1
NEW GROWTH AND BUILDING PERMIT ANALYSIS
FISCAL YEAR 2000 TO 2007

Property Class	FY 2007	FY 2006	FY 2005	FY 2004	FY 2003	FY 2002	FY 2001	FY 2000
Residential								
Single Family	$47,161,250	$38,246,930	$39,569,980	$25,091,945	$38,944,480	$63,437,300	$66,927,300	$65,342,800
Condominium	$20,834,200	$9,406,380	$8,578,464	$2,760,528	$600,589	$6,186,700	$7,546,300	$2,102,800
Two & Three Family	$2,300,750	$545,300	$0	$2,348,365	$320,700	$0	$1,354,900	$1,873,700
Multi-Family	$21,621,100	$0	$809,800	($599,200)	$0	$27,700	$0	$1,393,200
Vacant Land	$4,054,800	$767,350	$191,853	$5,048,600	$1,196,697	($7,024,900)	($8,007,509)	($11,949,650)
All Others	$76,071	$0	$0	$1,067,968	$22,346	$346,550	$1,159,496	$1,400
Total Residential	$96,048,171	$48,965,960	$49,150,097	$35,718,206	$41,084,812	$62,973,350	$68,980,487	$58,764,250
Open Space	$475,200	$0	$284,800	$0	$0	$8,800	$0	$21,576
Commercial	$3,721,970	$4,062,627	$3,708,079	$2,532,670	$4,657,056	$5,146,950	$4,244,792	$1,475,601
Chapter 61, 61A, 61B	$0	$0	$0	$24,245	$0		$0	$67,689
Industrial	$3,111,375	$1,887,400	$0	$9,791,846	$8,281,675	$1,832,400	$1,837,300	$844,750
Personal Property	$4,576,584	$1,419,891	$2,456,200	$5,063,106	$5,235,268	$712,768	$31,335,878	$766,210
Total Valuation Growth	$107,933,300	$56,335,878	$55,599,176	$53,130,073	$59,258,811	$70,674,268	$106,398,457	$61,940,076
Tax Rate	$9.24	$9.74	$9.92	$10.60	$13.58	$12.45	$13.34	$13.45
New Growth	$997,304	$548,711	$551,544	$563,179	$804,735	$879,895	$1,419,355	$833,094
Building Permits (Selected Areas)	**2005**	**2004**	**2003**	**2002**	**2001**	**2000**	**1999**	**1998**
One Family	53	68	96	128	126	178	244	269
Two Family	11	2	0	5	0	8	17	13
Apartment/Condos	12	7	34	16	6	8	8	22
Residential Alterations	309	308	345	297	293	238	216	201
Commercial	5	6	5	11	8	8	14	5
Commercial Alternations	40	34	46	41	62	42	35	36
Industrial	0	0	0	1	0	0	0	0
Industrial Alterations	0	0	4	0	1	0	2	5
Total	430	425	530	499	496	482	536	551

New One-Family Homes 1990 to 1996	1990	61	1994	222
	1991	125	1995	157
	1992	288	1996	221
	1993	256	1997	261

EXHIBIT 3.1 - STATE AID AND CHARGES
FISCAL YEAR 2000 TO 2007

Line Item	Fiscal Year 2008 Projection	Fiscal Year 2007 Actual	Fiscal Year 2006 Actual	Fiscal Year 2005 Actual	Fiscal Year 2004 Actual	Fiscal Year 2003 Actual	Fiscal Year 2002 Actual	Fiscal Year 2001 Actual	Fiscal Year 2000 Actual
REVENUE									
A. EDUCATION									
1. Chapter 70	$ 15,898,949	$ 15,898,949	$ 13,800,607	$ 11,948,701	$ 10,287,704	$ 8,745,774	$ 7,590,859	$ 6,394,912	$ 5,616,512
2. School Transportation	$ -	$ -	$ -	$ -	$ -	$ 247,393	$ 250,825	$ 342,826	$ 322,292
3. School Construction (Removed in FY 2006)	$ -	$ -	$ -	$ 3,702,732	$ 3,697,772	$ 496,000	$ 496,000	$ 496,000	$ 598,150
5. Charter School Tuition Reimbursement	$ 222,350	$ 222,350	$ 193,772	$ 131,443	$ 10,440	$ -	$ -	$ -	$ -
5. Tuition State Wards	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 67,163	$ 17,978
6. Chater School Capital Facility Reimbursement	$ -	$ -	$ 34,870	$ 28,196	$ -	$ -	$ -	$ -	$ -
8. School Lunch (Offset)	$ 26,597	$ 26,597	$ 28,245	$ 26,723	$ 27,247	$ 25,019	$ 22,775	$ 20,307	$ 20,177
Sub-Total	**$ 16,147,896**	**$ 16,147,896**	**$ 14,057,494**	**$ 15,837,795**	**$ 14,023,163**	**$ 9,514,186**	**$ 8,360,459**	**$ 7,321,208**	**$ 6,575,109**
B. GENERAL GOVERNMENT									
1. Lottery, Beano & Charity Games	$ 3,107,117	$ 3,107,117	$ 2,493,603	$ 2,110,492	$ 2,110,492	$ 2,250,774	$ 2,482,932	$ 2,324,233	$ 2,123,910
2. Additional Assistance	$ 298,861	$ 298,861	$ 298,861	$ 298,861	$ 298,861	$ 318,726	$ 376,077	$ 376,077	$ 376,077
3. Highway Fund	$ -	$ -	$ -	$ -	$ -	$ -	$ 51,858	$ 207,431	$ 207,431
6. Police Career Incentive	$ 159,050	$ 159,050	$ 166,024	$ 150,155	$ 140,291	$ 129,068	$ 119,784	$ 101,872	$ 78,330
8. Veteran's Benefits	$ 13,048	$ 13,048	$ 12,907	$ 3,406	$ 3,738	$ 14,598	$ 16,918	$ 8,202	$ 7,020
9. Exemptions	$ 31,591	$ 31,591	$ 31,025	$ 34,421	$ 34,499	$ 30,907	$ 30,431	$ 30,772	$ 31,608
10. Exemptions (Elderly)	$ 22,782	$ 22,782	$ 22,768	$ 22,670	$ 22,328	$ 21,017	$ 22,042	$ 22,700	$ 22,726
11. State Owned Land	$ 107,973	$ 107,973	$ 156,870	$ 123,183	$ 78,725	$ 98,335	$ 148,013	$ 163,750	$ 135,760
12. Public Libraries	$ 46,734	$ 46,734	$ 45,664	$ 40,664	$ 34,165	$ 37,196	$ 40,018	$ 39,608	$ 38,144
Sub-Total	**$ 3,787,156**	**$ 3,787,156**	**$ 3,227,722**	**$ 2,783,852**	**$ 2,723,099**	**$ 2,900,621**	**$ 3,288,073**	**$ 3,274,645**	**$ 3,021,006**
Total State Aid	**$ 19,935,052**	**$ 19,935,052**	**$ 17,285,216**	**$ 18,621,647**	**$ 16,746,262**	**$ 12,414,807**	**$ 11,648,532**	**$ 10,595,853**	**$ 9,596,115**
CHARGES									
County Tax	$ 49,947	$ 49,947	$ 49,947	$ 49,947	$ 49,947	$ 49,947	$ 49,947	$ 49,947	$ 49,947
Mosquito Control	$ 56,482	$ 56,482	$ 52,245	$ 47,364	$ 47,261	$ 40,895	$ 35,818	$ 39,250	$ 39,459
Mosquito Control (Underestimate)	$ -	$ -	$ -	$ -	$ -	$ 3,659	$ -	$ -	$ -
Air Pollution Districts	$ 9,076	$ 9,076	$ 8,834	$ 8,484	$ 8,187	$ 7,860	$ 7,368	$ 7,104	$ 6,838
RMV Non-Renewal Surcharge	$ 20,240	$ 20,240	$ 16,700	$ 13,500	$ 16,400	$ 17,880	$ 17,340	$ 21,360	$ 25,980
WRTA Assessment	$ 68,366	$ 68,366	$ 71,306	$ 82,522	$ 80,509	$ 78,546	$ 76,630	$ 74,368	$ 73,563
Special Education	$ -	$ -	$ -	$ 9,648	$ 5,501	$ 7,010	$ 7,010	$ 9,529	$ 18,155
MBTA	$ 132,034	$ 132,034	$ 112,991	$ 91,481	$ 42,430	$ -	$ -	$ -	$ -
School Choice Tuition	$ 99,364	$ 99,364	$ 104,140	$ 78,761	$ 45,890	$ -	$ -	$ -	$ -
Charter School Tuition	$ 447,240	$ 447,240	$ 424,421	$ 312,350	$ 138,180	$ -	$ -	$ -	$ -
Sub-Total	**$ 882,749**	**$ 882,749**	**$ 840,584**	**$ 694,057**	**$ 434,305**	**$ 205,797**	**$ 194,113**	**$ 201,558**	**$ 213,942**
Overestimate - Mosquito Control	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 1,666	$ 482
Overestimate - Special Education	$ (157)	$ (157)	$ -	$ -	$ -	$ 331	$ 2,850	$ 3,316	$ -
Overestimate - Regional Transit	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Sub-Total	**$ (157)**	**$ (157)**	**$ -**	**$ -**	**$ -**	**$ 331**	**$ 2,850**	**$ 4,982**	**$ 482**
Total Net Charges	**$ 882,906**	**$ 882,906**	**$ 840,584**	**$ 694,057**	**$ 434,305**	**$ 205,466**	**$ 191,263**	**$ 196,576**	**$ 213,460**
School Lunch Offset	$ 26,597	$ 26,597	$ 28,245	$ 26,723	$ 27,247	$ 25,019	$ 22,775	$ 20,307	$ 20,177
Library Offset	$ 46,734	$ 46,734	$ 45,664	$ 40,664	$ 34,165		$ 40,018	$ 39,608	$ 38,144
Total Off-Sets	**$ 73,331**	**$ 73,331**	**$ 73,909**	**$ 67,387**	**$ 61,412**	**$ 25,019**	**$ 62,793**	**$ 59,915**	**$ 58,321**

Line Item	Fiscal Year 2008 Projection	Fiscal Year 2007 Actual	Fiscal Year 2006 Actual	Fiscal Year 2005 Actual	Fiscal Year 2004 Actual	Fiscal Year 2003 Actual	Fiscal Year 2002 Actual	Fiscal Year 2001 Actual	Fiscal Year 2000 Actual
"Education" Local Aid	$ 16,147,896	$ 16,147,896	$ 14,057,494	$ 12,135,063	$ 10,325,391	$ 9,018,186	$ 7,864,459	$ 6,825,208	$ 5,976,959
"General Government" Local Aid	$ 3,787,156	$ 3,787,156	$ 3,227,722	$ 2,783,852	$ 2,723,099	$ 2,900,621	$ 3,288,073	$ 3,274,645	$ 3,021,006
Charges and Offsets	$ 956,237	$ 956,237	$ 914,493	$ 761,444	$ 495,717	$ 230,485	$ 254,056	$ 256,491	$ 271,781
Total	$ 18,978,815	$ 18,978,815	$ 16,370,723	$ 14,157,471	$ 12,552,773	$ 11,688,322	$ 10,898,476	$ 9,843,362	$ 8,726,184

Indicates amount after "9C" reduction was made

Exhibit 3.2

Communities at risk: Fiscal ties between the Commonwealth and its localities

John P. Hamill

FACING RISING COSTS, LIMITED LOCAL AID, AND RESTRICTIONS ON RAISING REVENUES, MASSACHUSETTS CITIES AND TOWNS ARE EXPERIENCING A SERIOUS FISCAL SQUEEZE.

Virtually all Massachusetts cities and towns face financial problems. With many costs, especially for health care, rising faster than revenues from local taxes and fees, localities are left with virtually no ability to tap new revenue sources or to significantly increase existing taxes and fees. State aid for localities has dropped dramatically in recent years. And since the mid-1990s, a growing proportion of it has been reserved for education, with restrictions that do not allow local governments to redirect this local aid revenue to non-education uses.

This article is based on *Local Communities At Risk: Revisiting the Fiscal Partnership Between the Commonwealth and Cities and Towns*, a comprehensive report by the Municipal Finance Task Force, a group of private sector, public sector and academic experts that was chaired by Sovereign Bank Chairman John P. Hamill. This article also draws upon material contained in *Local Services, Local Aid, and Common Challenges*, a Rappaport Institute for Greater Boston policy brief by Phineas Baxandall, Rappaport's then- assistant director. The full report can be found at http://www.ksg.harvard.edu/rappaport/downloads/policybriefs/brief_finance.pdf.

Local source revenues in total, including property tax, local receipts and other revenue, have grown only 0.8 percent annually between fiscal 1981 and 2004. (See Figure 1.) As a percentage of municipal budgets, total local source revenues have decreased from 80.1 percent in fiscal 1981 to a low point of 69.0 percent in fiscal 1988, they then rose to 75.6 percent in fiscal 2004, which was their highest point in ten years.

For the fiscal 1981 to 2004 period, total local source revenues increased on average for all regions, income quintiles and population groups, except Boston. In general, communities with higher income and smaller population groups experienced greater annual average increases in total local source revenues than their poorer and larger counterparts.

Figure 1. Average Annual Change in Total Local Source Revenues

Constant Dollars Per Capita

	1981 – 1984	1984 – 2004	1981 – 2004
Municipal Total	-4.9%	2.0%	0.8%
REGION			
Berkshire	-7.6%	2.6%	1.1%
Pioneer Valley	-4.7%	2.0%	0.9%
Central	-7.3%	2.5%	0.9%
Boston Metro	-4.9%	2.3%	1.0%
Boston	-5.9%	1.0%	-0.2%
Northeast	-2.3%	1.6%	0.8%
Southeast	-5.3%	2.3%	1.1%
Cape and Islands	-2.7%	2.5%	1.7%
INCOME			
Lowest 5th	-7.0%	1.6%	0.2%
Second 5th	-5.2%	2.0%	0.8%
Boston	-5.9%	1.0%	-0.2%
Third 5th	-5.9%	2.4%	1.0%
Fourth 5th	-2.7%	2.2%	1.2%
Highest 5th	-3.1%	2.5%	1.6%
POPULATION			
50 – 1,999	-5.2%	2.9%	1.6%
2,000 – 4,999	-4.0%	3.1%	2.1%
5,000 – 9,999	-4.9%	3.0%	1.8%
10,000 – 19,999	-4.0%	2.7%	1.6%
20,000 – 49,999	-4.0%	2.0%	1.0%
50,000 +	-5.9%	1.6%	0.3%
Boston	-5.9%	1.0%	-0.2%

Source: Massachusetts Department of Revenue, Division of Local Services

Behind today's local aid picture

Proposition 2½, which Massachusetts voters approved in 1980, set limits on the total amount by which localities can increase local property tax revenues to no more than 2.5 percent a year. The measure also set limits on how fast those revenues can increase each year. Initially, new infusions of local aid buffered the impact of the new law: on a constant-dollar, per capita basis, local aid grew by 10.4 percent a year between 1981 and 1984 and by 8.4 percent a year from 1985 to 1989. During the sharp recession of the 1980s and early 1990s, however, real per capita local aid fell by 13.3 percent a year from 1989 through 1992. As a result, local aid, which peaked in fiscal year 1988 at 20 percent of total state expenditures, fell to 13.4 percent of state spending in fiscal year 1993.

Patterns of local aid began to change dramatically after the Massachusetts Supreme Judicial Court ruled in 1993 that great disparities in funding between schools in poor and affluent communities meant that the state was not meeting its constitutional obligation to provide an adequate level of education for all students. The Education Reform Act of 1993, which was signed into law soon after that ruling, greatly increased state aid for education and revamped the formulas used to distribute it. Under the Act, the state calculates each locality's "foundation budget," which is how much each locality needs to spend to provide an adequate education for students in its schools. The state also calculates how much each locality can (and must) raise in local property taxes and makes up the difference between needed spending and available funds.

As a result of that law and an improved state economy, per capita, constant-dollar state aid for K-12 education, which had increased modestly in the mid-1980s and declined sharply during the recession, increased by 8.6 percent per year until 2004. In contrast, per capita, constant-dollar state aid for the two major local aid programs that can be used for non-educational purposes — Additional Assistance and Lottery Aid — declined during the same period. The state cut Additional Assistance sharply during the late 1980s recession and has reduced or level-funded it every year since. While per capita local aid from the lottery grew (after inflation) by 11.3 percent between 1981 and 1992, a maturing lottery market and legislative diversion of some proceeds into the Commonwealth's general fund reduced growth in such aid to only 3.5 percent between 1993 and 2004.

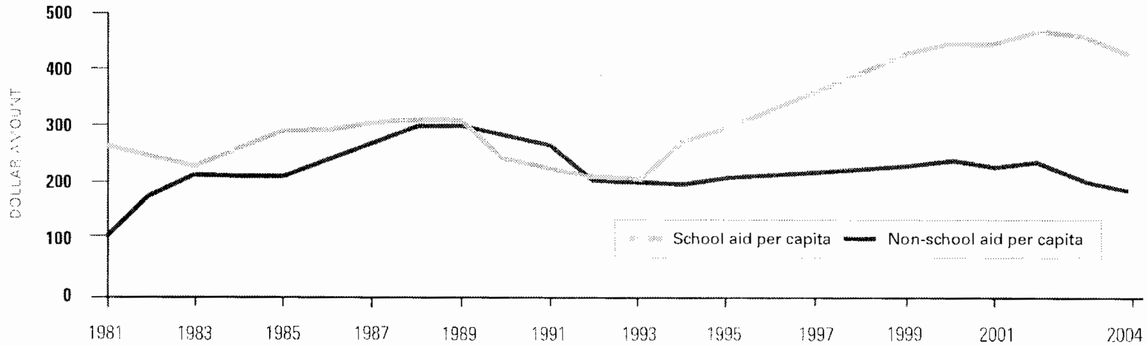
The recession of the early part of this decade, along with cuts in the state income tax rate, caused state revenues to decline by 15 percent in 2002. As a result, per capita local aid (including aid for education), which had risen 5.3 percent per year in inflation-adjusted terms between 1992 and 2002, fell by 8.6 percent a year between 2002 and 2004.

Proposition 2½, which Massachusetts voters approved in 1980, set limits on the total amount by which localities can increase local property tax revenues to no more than 2.5 percent a year.

Patterns of local aid began to change dramatically after the Massachusetts Supreme Judicial Court ruled in 1993 that great disparities in funding between schools in poor and affluent communities meant that the state was not meeting its constitutional obligation to provide an adequate level of education for all students.

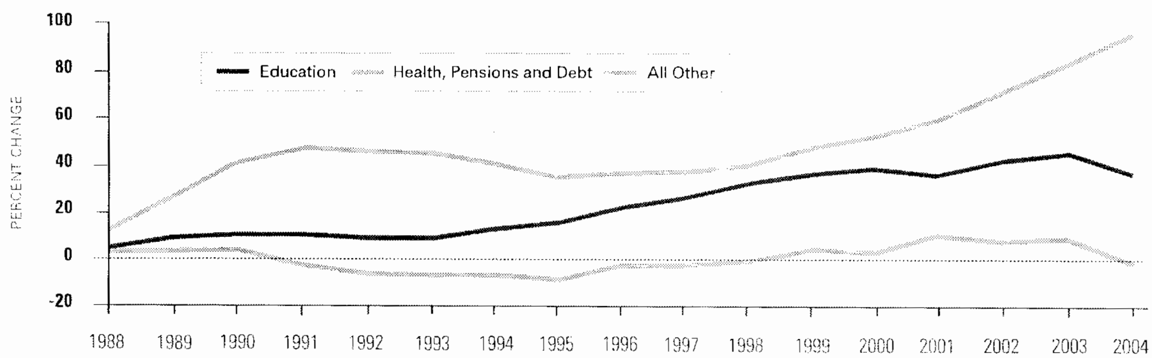
The reductions in local aid came at a time of rapidly rising health insurance costs, which especially strained local governments because public services tend to be highly labor-intensive. Municipal spending for health insurance increased by 63 percent between 2001 and 2005, according to *A Mounting Crisis for Local Budgets: The Crippling Effects of Soaring Municipal Health Costs*, a survey of a sample of municipalities released by the Massachusetts Taxpayers Foundation (MTF) in July 2005. The increase in health insurance costs consumed approximately 80 percent of the 2.5 percent annual growth in taxes on existing properties allowed under Proposition 2½. Examining separate cost data from the Department of Revenue on all 351 cities and towns in the Commonwealth, the MTF report found an even more dire situation: increases in municipal health insurance costs, on average, exceeded this allowable revenue growth by an average of 8 percent a year during the same period.

Figure 2. Per Capita School vs. Non-School Local Aid, 1981–2004
2004 Constant Dollars



Source: Massachusetts Department of Revenue, Division of Local Services

Figure 3. Areas of Expenditure Pressure, 1988–2004
Cumulative annual percentage change; Constant dollars per capita



Source: Massachusetts Department of Revenue, Division of Local Services

In response to such pressures, many municipalities focused on new development, which was exempt from Proposition 2½'s limits. Most localities that were not already at one of the limits imposed by Proposition 2½ raised property taxes and many others asked voters to approve overrides to Proposition 2½ (though voters often turned down those requests).

As a result of these factors and skyrocketing residential property values, the average yearly residential tax bill for families increased 36 percent, or $910, before adjusting for inflation between fiscal years 2000 and 2005, according to the Massachusetts Department of Revenue. In 2004, property taxes provided 53 percent of localities' total revenues, up from 46 percent in 1988, and user fees provided another 17.6 percent of revenue, up from 16.5 percent in 1988. By contrast, local aid provided only 24 percent of local revenues in 2004, down from 31 percent in 1988.

Health insurance costs and mandated local spending on education have forced localities to constrain spending on non-educational public services, such as police, fire, public works, parks, public health, community development and libraries. Between 1987 and 2004, real per capita expenditures by local governments for debt service increased by an average of 3.1 percent annually and per capita spending on other fixed costs — health insurance, pensions, unemployment, workers compensation and other employee benefits — grew by an annual average of 2.2 percent. Similarly, per capita school spending, the largest spending item for most municipalities, increased an average of 2.1 percent per capita annually after adjusting for inflation. (See Figure 3). By contrast, municipal expenditures for non-educational services declined 0.3 percent a year in real per capita terms. This drop, however, was far from uniform. Police and fire expenditures increased in real terms at rates that averaged 1.5 percent and 0.7 percent per capita between 1987 and 2004. Spending on public works, such as roads, waste collection, water distribution and snow removal, declined in constant-dollar, per capita terms by an average of 1.2 percent per year during this period. And per capita, constant-dollar spending on local health and welfare, which includes public health, clinics and veterans' services, fell by an even sharper average of 2.7 percent a year.

Health insurance costs and mandated local spending on education have forced localities to constrain spending on non-educational public services, such as police, fire, public works, parks, public health, community development and libraries.

The underlying constraints on local budgets were particularly severe when the state cut local aid during the recent recession. Cities and towns cut their workforces by 5.2 percent between February 2002 and August 2004, eliminating 14,200 jobs, according to MTF. Moody's Economy.com, a Pennsylvania research firm, estimates that municipalities in Massachusetts reduced their workforces more steeply than any other state in the nation between 2001 and 2005.

The property tax and life with Proposition 2½

The property tax — the total amount a municipality raises by placing a levy on real and personal property — is arguably the most important source of revenue available to municipalities. Compared to other revenue sources, the tax has a number of advantages, including its relative stability, predictability, and difficulty of evasion. At the same time, the tax tends to be regressive, is highly visible, and is perceived by some to be the result of a subjective assessment process. These characteristics can create complex political, social and economic consequences for municipalities.

Before Proposition 2½, the local property tax was unrestricted and was both the principal source of revenue for most municipalities and the major source of budget flexibility to fund additional spending. In fiscal 1981, the year before Proposition 2½'s implementation, the property tax supported 59.1 percent of local budgetary

Moody's Economy.com, a Pennsylvania research firm, estimates that municipalities in Massachusetts reduced their workforces more steeply than any other state in the nation between 2001 and 2005.

spending statewide, reflecting the very heavy reliance of cities and towns on this revenue source. Although Proposition 2½ initially reduced the percentage of local budgets funded by the property tax, this situation is now reversing. By fiscal 2004, the percentage of local budgets supported by the property tax was at its highest level in more than 20 years. This increasing reliance on the property tax can be traced to the hole that was left in municipal budgets after the loss of equalizing Additional Assistance aid in the late 1980s and the diversion of lottery revenue to the general state budget in the 1990s and 2000s, often resulting in the need to pass overrides to meet cost increases.

As a result of Proposition 2½, the levy declined as a percentage of local budgets for almost two decades, before beginning its recent increase. Whereas the property tax represented 59.1 percent of municipal budgets in fiscal 1981, this figure dropped to a low of 46.1 percent in fiscal 1988 and increased to 52.9 percent in fiscal 2004. Between fiscal 1981 and 2004, the total levy increased by $5.67 billion from $3.35 billion to $9.02 billion, with an average annual per capita rate of increase of 0.6 percent after adjusting for inflation.

Before Proposition 2½, the local property tax was unrestricted and was both the principal source of revenue for most municipalities and the major source of budget flexibility availability to fund additional spending.

Figure 4. Proposition 2½ Overide Attempts, Passage and Value of Passed Initiatives
Fiscal Years 1983 – 2004 aggregate current dollars

	Attempts	Passed	Total Value
REGION			
Berkshire	199	54.8%	$7,055,323
Boston Metro	428	51.2%	$159,929,807
Cape and Islands	817	48.7%	$51,714,370
Central	545	25.9%	$22,571,625
Northeast	415	35.9%	$37,876,248
Pioneer Valley	787	35.7%	$39,406,671
Southeast	392	28.1%	$29,545,167
Massachusetts	3,583	39.27%	$348,099,211
INCOME PERCENTILE			
Lowest 5th	487	27.3%	$32,241,655
Second 5th	703	27.3%	$21,432,650
Third 5th	766	37.9%	$34,414,526
Fourth 5th	947	42.7%	$97,827,739
Highest 5th	680	57.1%	$162,182,641
Massachusetts	3583	39.3%	$348,099,211
POPULATION			
50 - 1,999	609	49.4%	$12,647,751
2,000 - 4,999	860	45.8%	$36,240,538
5,000 - 9,999	1,171	36.1%	$54,202,011
10,000 - 19,999	582	30.2%	$93,315,949
20,000 - 49,999	313	30.7%	$90,644,842
50,000 +	48	35.4%	$61,048,120
Massachusetts	3,583	39.3%	$348,099,211

Source: Massachusetts Department of Revenue, Division of Local Services

Many municipalities have attempted to override the limits of Proposition 2½. Nearly 3,600 separate overrides — roughly 160 per year and an average of $235,000 per override — have gone to local voters since fiscal 1983, with 39 percent of them approved. More overrides have been adopted than rejected in only eight of the past 22 years. In fiscal 1991, the year of highest activity, only 168 of 594 — or 28 percent — of override attempts were successful. From fiscal 1983 through 2004, overrides that were approved added $348.1 million to levy limits; those that failed kept $494.1 million out of the levy limit.

The Berkshire region has had the fewest override attempts but has had the most success in passing them, with 54.8 percent gaining approval. The Cape and Islands have attempted the most overrides (817), with a 48.7 percent success rate. The least successful region has been the Southeast, which passed just 110 of 392, or 28.1 percent, of its override attempts.

Local aid fluctuates

The second major revenue component of municipal budgets is local aid, which is state revenues distributed to local governments through a wide array of programs. The importance of local aid cannot be understated in a climate of otherwise restricted local revenue growth. Since Proposition 2½, municipalities have become more dependent on state aid. As noted above, during the early 1980s, many municipalities were forced to make substantial cuts to municipal budgets to comply with the newly approved limits on local property taxes. In order to manage these decreases and fill the gap between the cost of services and local revenues, a state and local agreement was established that led to increasing state aid allocations for cities and towns.

From fiscal 1981 to 2004, the Commonwealth's expenditures on local aid (net of municipal charges) increased $2.88 billion, while total state spending (excluding local aid) increased $13.95 billion. The net local aid increase translates into an inflation-adjusted, per capita increase of 3.0 percent per year, outpacing the state expenditures increase of 2.0 percent per year. State expenditures on net local aid as a percentage of total state spending (including local aid) have ranged from a high of 20 percent in fiscal 1988 to a low of 13.4 percent fiscal 1993. In fiscal 2004, the Commonwealth allocated 16.4 percent of its budget to net local aid.

Overall, local aid has fluctuated substantially from year to year, barely exceeding the rate of inflation in certain periods. In fiscal 2004, inflation-adjusted net local aid dollars were less than in fiscal 1989. As Figure 5 indicates, the annual growth in the Commonwealth's net local aid expenditures generally follows the growth in its overall expenditures, except during economic contractions. In such downturns, direct local aid declines at a substantially higher rate than overall state expenditures. This phenomenon is closely related to the structure of the state budget. For the Commonwealth (as well as for municipalities), increases in mandatory costs force reductions in discretionary programs. Local aid is one of the largest "discretionary" programs. At the outset of Proposition 2½ in fiscal 1981, net local aid receipts accounted for about 15.3 percent of total municipal revenues. This percentage peaked in fiscal 1988 at 28.4 percent and fell to 22.0 percent in fiscal 2004. Net local aid receipts increased from $868.3 million in 1981 to $3.75 billion in 2004. After adjusting for inflation, this increase translates into annual average growth per capita of 3.0 percent.

Overall, local aid has fluctuated substantially from year to year, barely exceeding the rate of inflation in certain periods.

Figure 5. Annual Change in Total Massachusetts Expenditures vs. Expenditures on Net Local Aid

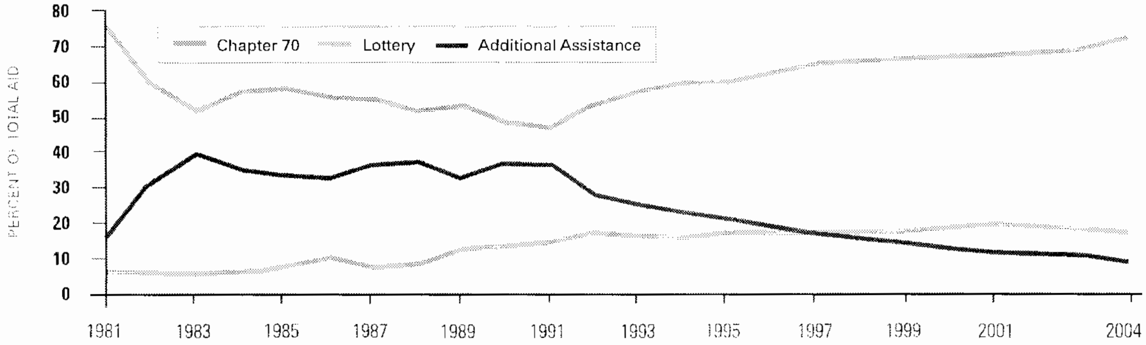
Constant dollars per capita

Context	Fiscal Year	Total Expenditures	Net Local Aid
IMPLEMENTATION OF PROPOSITION 2 1/2	1982	-3.1%	16.1%
	1983	-1.6%	9.7%
	1984	3.8%	5.4%
NEEDS BASED AID FORMULA IN USE	1985	7.2%	9.0%
	1986	10.5%	10.0%
	1987	6.3%	14.5%
	1988	1.9%	5.0%
	1989	5.6%	3.2%
RECESSION/STATE FISCAL CRISIS	1990	3.4%	-13.9%
	1991	-0.9%	-10.6%
	1992	-3.4%	-15.3%
EDUCATION REFORM	1993	10.1%	4.6%
	1994	2.6%	4.9%
	1995	0.7%	5.5%
	1996	0.0%	7.2%
	1997	3.0%	7.6%
	1998	3.0%	8.2%
	1999	3.1%	7.3%
	2000	2.8%	4.1%
	2001	-2.8%	0.4%
	2002	-4.1%	2.9%
RECESSION/STATE FISCAL CRISIS	2003	-4.1%	-3.2%
	2004	1.4%	-13.9%

Source: Massachusetts Department of Revenue, Division of Local Services and the Massachusetts Taxpayers Foundation

Growth in net local aid was greatest in the period immediately following Proposition 2½, at 10.4 percent annually, and lowest during the steep economic decline in the early 1990s, falling 13.3 percent annually. After the recession, growth in net local aid was lower during the period of economic expansion in the mid- and late 1990s than it had been in the 1980s. The ensuing difficult years of the early 2000s were less severe than the recession of the early 1990s. While growth was fairly uneven across the different regions and in municipalities of all kinds, the highest income municipalities saw the largest increase in net local aid in the 1990s,

Fig 6. Major Sources of Local Aid, 1981 – 2004
Percentage of total net local aid
2004 constant dollars



Source: Massachusetts Department of Revenue, Division of Local Services and Massachusetts Taxpayers Foundation

mainly because other items, such as state reimbursements for school construction, are included in the definition of total net local aid.

Recessionary periods tend to have lasting impacts on municipalities, especially in regard to local aid. From fiscal 1981 to 2004, there have been two periods of substantial reductions in net local aid to municipalities: 1989–1992 and 2002–2004. Both periods coincide with economic recessions and ensuing state fiscal difficulties.

Expenditures

Total municipal spending in Massachusetts from fiscal 1987 to fiscal 2004 has grown in constant dollars by 1.3 percent annually per capita, with wide variation in growth among major spending categories. Only a few expenditure categories, namely debt service, fixed costs (including employee health insurance, pensions and other benefits) and education, grew faster than this average increase in total municipal expenditures, which has the effect of forc-

A VITAL DISTINCTION: SCHOOL VERSUS NON-SCHOOL LOCAL AID

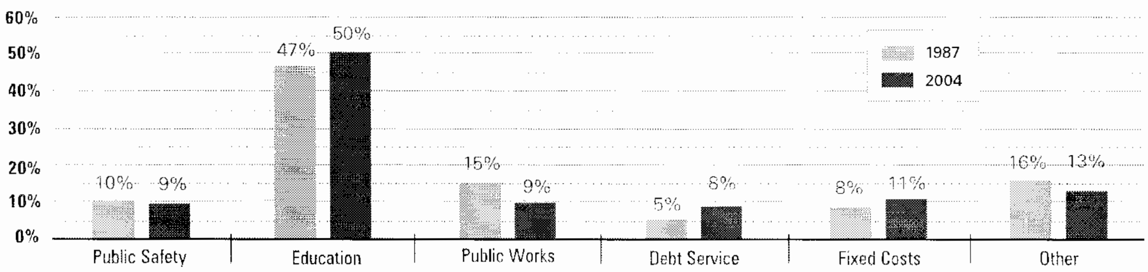
In the 1980s, Chapter 70 was considered "unrestricted aid," meaning it could be used for schools or any other purpose. Not until the Education Reform Act of 1993 did the distinction between school and non-school aid take on importance, as Chapter 70 funds became earmarked solely for school spending.

It is likely that this change would not have emerged as an issue if municipalities had the option of adjusting their local education spending as the state took on a larger share of school funding. However, the Education Reform Act required a minimum local contribution to education that began as roughly equal to the amount most municipalities were already spending on schools. Earmarked education aid, in combination with the required minimum local contribution from local revenue sources, meant that communities had little discretion in school spending and could no longer divide their total revenue "pie" as local residents or officials might choose.

The vast majority of direct aid increases since the early 1990s have gone to Chapter 70 aid, with sharp declines in another Section Three account, Additional Assistance. This trend toward dedicated school aid and away from general-purpose aid has been a major contributor in limiting the discretion of local policy-makers to fund general government services.

ing reductions in other expenditure areas under a balanced budget framework. Figure 7 illustrates the growth, stability or decline in major expenditure areas as a percent of total municipal expenditures in 1987 and 2004. Combined, the spending areas of education, fixed costs and debt service have consumed approximately 80 percent of annual budget growth since 1987, with education alone taking up 52 percent of all new budget growth.

Figure 7. Major Expenditure Areas as a Percent of Total Municipal Expenditures FY1987 vs. FY2004



Source: Massachusetts Department of Revenue, Division of Local Services

LOCAL LABOR COSTS: DEFYING THE STEREOTYPE

Some contend that Massachusetts localities create their own budget woes by hiring excessive personnel or paying workers too much. The Massachusetts Taxpayers Foundation, however, reached a different conclusion in a recent report: "Although some observers occasionally suggest that some municipal employment contracts have been overly generous in recent years, it seems that most have been conservative enough to produce annual average growth per employee of only 0.7 percent, in inflation-adjusted terms, between 1994 and 2003, compared to 1.8 percent for private sector and 1 percent for state employees over the same period."[1]

Several other studies also suggest that in general, local government in Massachusetts is neither overstaffed nor overpaid, at least when compared to other governments around the country. Nick Turner and E. Matthew Quigley, two researchers at the Federal Reserve Bank of Boston, for example, found that in 2003, local governments in Massachusetts employed only 356 people per 100,000 residents, less than the national average of 398 employees per 10,000 residents. Combined, state and local government in Massachusetts employ 498 people for every 10,000 residents, well below the national average of 542 employees and less than any other state in New England.

Turner and Quigley also found that while salaries for state and local government workers in Massachusetts were 12 percent higher than the national average ($46,535 compared to $41,508), these generally higher wages reflect the higher living costs and private-sector salaries in New England and also mask considerable differences across public sector occupations. Correctional officers in Massachusetts, for instance, earn 30 percent more than the national average, but local public welfare employees earn 11 percent less. Turner and Quigley also found that for every $1,000 in personal income earned by Massachusetts residents, $4.96 went to state and local payroll, compared to an average of $6.08 nationally. By this measure, the only category of public employees for which payroll exceeded the national average were not municipal, but non-educational state employees, a category that also garnered the highest average salaries.

– Phineas Baxandall

[1] Massachusetts Taxpayers Foundation, *A Mounting Crisis for Local Budgets: The Crippling Effects of Soaring Municipal Health Costs*. July 2005. http://www.mma.org/policies_positions/press_releases/MTFhealthfinal.pdf.

The remaining expenditure categories received only 20 percent of annual budget growth. The largest three areas (police, fire and general government) accounted for 7.1 percent, 4.5 percent and 6.0 percent of annual growth respectively. The remaining groups in total (other public safety, public works, health and welfare, culture and recreation, intergovernmental and other) accounted for only 2.4 percent of annual growth.

Crowding out: Losing local budgetary discretion

Recent local government expenditure history has been characterized by an increasing loss of budgetary discretion. Pressures resulting from the rising costs of employee benefits and the demands of meeting state and federal education mandates — combined with limited local revenue raising capacity and stagnant general-purpose aid — have left local officials with limited resources to meet current needs, expand existing services or adequately plan for the future.

The net result of these combined pressures has been more local fees and property taxes and fewer direct local services. Across the Commonwealth, municipalities have made layoffs, implemented hiring freezes, reduced hours of operation, cut discretionary programs and, in some cases, eliminated programs and services altogether to maintain budget balance.

Without serious policy attention, many cities and towns will be forced to continue to implement service reductions and/or seek voter-approved overrides to fund local services. Modifying this trend will require a new state-local partnership that recognizes cost differences and revenue constraints to establish a more responsive local finance system.

John P. Hamill, Chairman of Sovereign Bank New England, chaired the Municipal Finance Task Force.

RAISING LOCAL REVENUE: LESS FLEXIBILITY THAN IN OTHER STATES

Cities and towns in Massachusetts face problems similar to municipalities in other states but are more vulnerable to fluctuations in local aid because of their limited revenue-raising options and strict responsibility for schools. Examining 53 American cities in 2003–2004 (including Boston, Fall River and Worcester), Bruce Wallin, a professor of political science at Northeastern University, found that chief financial officers in those cities tend to report greater financial strain when, as in Massachusetts, they lack powers to levy local income or sales taxes.[1]

Similarly, municipalities in Massachusetts wield less flexibility when courts declare existing financing arrangements unconstitutional and mandate reductions in school finance disparities. According to Katherine Baicker and Nora Gordon, professors of economics at Dartmouth College and the University of California, San Diego, across the nation, "Each dollar of increased educational funding a locality received from the state resulted in an average decline in funds from the state for other purposes of about 20 cents."[2] They also found that localities tend to respond to increased education aid by reducing their own-source spending on both education and other programs. While the local aid story in Massachusetts is consistent with nationwide patterns described by Baicker and Gordon, state laws since 1994 have made it virtually impossible for Massachusetts localities to reduce their contribution to school spending.

– Phineas Baxandall

[1] Wallin, Budgeting for Basics: *The Changing Landscape of City Finances, Brookings Institution Metropolitan Policy Program Discussion Paper*, August 2005. http://www.brookings.edu/metro/pubs/20050823_budgetingbasics.htm.

[2] Baicker and Gordon, *The Effect of Mandated State Education Spending on Total Local Resources*. National Bureau of Economic Research Working Paper 10701, August 2004. Available at http://www.nber.org/papers/w10701.

Exhibit 3.3

The Long-Term Mismatch Between Available Resources and Important State Priorities

A Five-Year Fiscal Analysis

SEPTEMBER 2006

The Massachusetts Taxpayers Foundation is a nationally recognized, nonprofit research organization working to promote the most effective use of tax dollars, improve the operations of state and local governments, and foster positive economic policies. Our credibility is based on independent, objective, and accurate analysis of state and local spending, taxes and the economy. The quality and impact of the Foundation's work is reflected in ten prestigious national awards earned over the past decade for research on business costs, capital spending, state finances, MBTA restructuring, state government reform, and health care.

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The Long-Term Mismatch Between Available Resources and Important State Priorities: A Five-Year Fiscal Analysis

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Introduction

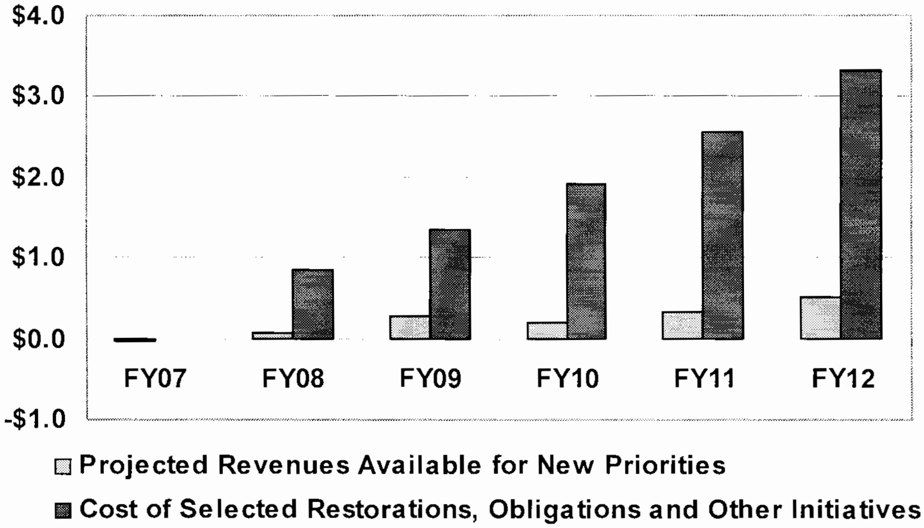
Despite the better-than-expected revenue performance in fiscal 2006, the state's leaders will soon have to grapple with a large and rapidly growing disparity between available resources and the costs of a broad array of important priorities. Dealing with this challenge is likely to dominate the financial decision making of the next Governor and Legislature for the foreseeable future.

The mismatch between expected revenues – and the costs of widely held goals such as greater local aid, additional spending for higher education, and increased capital investment – is staggering. Even with careful targeting on only those priorities of greatest importance for the long-term health of the Massachusetts economy, their costs are likely to exceed available resources by billions of dollars, according to a detailed analysis of the state's financial outlook over the next five years (see Figure 1). And contrary to the common belief that the Commonwealth can finance its unmet needs through economic growth, addressing any substantial portion of these spending ambitions would push the state budget deeply into deficit under any reasonable set of assumptions about future tax receipts and spending growth.

The situation is further complicated by proposals to cut the income tax rate from 5.3 to 5.0 percent, with an annual revenue impact of almost $700 million. The more accelerated the tax cut, the greater the impact on funding for various spending priorities, including providing relief to hard-pressed local property taxpayers via the

Figure 1

Long-Term Mismatch Between Available Revenues and Important State Priorities
($, billions)



Foundation's recommendation to dedicate 40 percent of tax revenues to cities and towns.[1]

The Foundation's comprehensive new analysis examines the potential impact on the state budget through fiscal 2012 of a tightly focused list of initiatives that MTF believes are crucial to the state's long-term economic competitiveness.

The initiatives – a selected set of restorations, obligations and priorities – include rebuilding the financial capacity of cities and towns through the Foundation's proposal to dedicate 40 percent of tax revenues to local aid, restoring and increasing the state's investment in public higher education, maintaining and expanding the capital infrastructure, and preserving the Commonwealth's credit-worthiness by addressing the looming unfunded liability for the medical costs of state retirees (see Table 1).

Table 1

Selected Restorations, Obligations and Priorities Considered in the Analysis

Restorations Highlighted by MTF

- "40%" local aid proposal
- Additional funding for higher education
- Raising the capital spending cap

Other Spending Priorities

- Pay-as-you-go capital spending
- Routine infrastructure maintenance and repair
- Partial restoration of prior agency spending cuts

Looming Obligations

- Unfunded liability for medical costs of state retirees

In estimating the budgetary resources that are likely to be available to address these priorities, the Foundation prepared a baseline projection for fiscal 2008-2012 that uses reasonable assumptions about future revenue growth and the expectation of very tight annual budgeting. The analysis is predicated on annual tax growth of just over six percent, reflecting the long-term average rate of real growth of the Massachusetts economy and inflation of three percent a year. It assumes spending growth that is limited to largely unavoidable increases in areas such as Medicaid, pensions, and debt service, the costs of existing commitments such as school construction, and inflation in other state programs.[2]

Using these assumptions, the analysis projects a tiny budgetary surplus of only $62 million, or 0.2 percent of total revenues, in 2008; that figure would rise to about $500 million, or 1.4 percent of revenues, in 2012. However, achieving these surpluses would be possible only by adhering to strict maintenance budgeting, with no expansion in areas such as local aid, higher education, and human services beyond the rate of inflation, and no further restorations of the deep spending cuts during the fiscal crisis. Although those cuts undoubtedly eliminated some unnecessary spending, their magnitude – 2007 spending in these areas remains 15 percent below 2001 after adjusting for inflation – required significant reductions in services across state government.

Even under the favorable assumptions of the baseline projection – healthy revenue growth and sustained budgetary discipline –

[1] Under existing law, the 5.3 percent income tax rate will decline to 5.0 percent over an eight-year period if revenues remain strong.

[2] The analysis assumes an annual inflation rate of 3.0 percent for both revenues and spending.

the costs of the new priorities considered in the analysis would still far exceed available revenues. Taken in combination, the selected initiatives would require additional annual spending of $840 million in 2008 and rising to $3.3 billion in 2012, or more than six times the projected $500 million surplus in 2012.

While the new Governor and Legislature could well choose a different list of priorities than the ones considered here – including, for example, other large-scale initiatives such as greatly expanding early childhood education at a cost of up to $1 billion annually – they would still confront the same problem: a lack of sufficient resources to finance the additional spending.

And although the set of priorities to be considered could be trimmed, the major finding of the analysis – a huge disparity between the costs of new initiatives that could be undertaken and the state's ability to manage those costs – would remain essentially unchanged. Even if the priorities to be pursued, and their costs, were reduced by half, the state budget would still be unable to accommodate the required new spending.

The Foundation's analysis, if anything, overstates the state's capacity to take on new priorities. Far from a worst-case scenario, the baseline projection assumes that revenues will grow at the healthy rate of 6.2 percent a year over the next five years, without an evaporation of the capital gains and other volatile tax receipts that have supported the recent rapid growth in revenues, and without a recession. It also assumes that spending for current services and commitments will be held tightly in check, with the kind of fiscal discipline the state has rarely been able to sustain.

At the same time, the analysis makes no provision for cuts in the income tax beyond those that are already authorized in law, which include a restoration of personal exemptions to their 2002 levels and the gradual reduction of the income tax to 5.0 percent if revenue performance remains healthy. Nor does it add to the state's stabilization fund beyond the 0.5 percent of tax revenues that is required to be contributed annually under current law.

Although it is conceivable that the state's revenues could perform better for the next year or two than the roughly six percent rate of growth assumed in the analysis, the additional revenues would make only a small dent in the gap identified in the

Table 2
Fiscal 2006 and 2007 Finances
($, millions)

	FY06	FY07
Revenues		
Taxes (using consensus forecast for FY07)	$17,286	$17,604
Other revenues	9,052	9,555
Total	26,338	27,159
Estimated spending	25,951	27,722
Revenue minus estimated spending	387	-563
FY07 spending financed from prior year surplus revenues (not included in the 2007 spending total shown above)		805
End-of-year stabilization reserves, including impact of projected FY07 operating deficit	1,939	1,500

Note: The figures presented here are based upon administration estimates published in the August 17, 2006 Official Statement of the Commonwealth, adjusted to include certain off-budget spending, primarily for Medicaid costs, and the revenues supporting that spending. Tax revenues exclude sales taxes dedicated to the MBTA and School Building Authority, which total $1.2 billion in fiscal 2006 and $1.29 billion in fiscal 2007. FY07 spending does not include $200 million of bond-funded expenditures that were authorized at the end of fiscal 2006 for use in FY07 and future years. Fiscal 2006 stabilization reserves include $305 million of balances in the Transitional Escrow Fund which are reported separately in the Official Statement. The FY07 stabilization balance of $1.5 billion assumes a transfer from the stabilization fund to the General Fund to offset the projected $563 million operating deficit; this withdrawal would require legislative authorization.

analysis. However, that performance is unlikely, with employment that remains almost 150,000 below the pre-recession peak, a national economy that is starting to slow, and the heavy reliance on volatile capital gains and corporate receipts to achieve the well-above-average rate of revenue growth in 2006.

It is possible as well that a portion of the spending growth for some existing state programs that has been assumed in the analysis will not be necessary, but any such savings are almost certain to be offset by unforeseen requirements in other programs.

Dealing with this challenging fiscal outlook will be even more difficult given the buoyant atmosphere that marked the close of fiscal 2006. With baseline revenue growth topping nine percent[3] and an estimated surplus approaching $400 million, fiscal 2006 ended in a wave of last-minute authorizations that added almost $1 billion to the budget, almost all of which will carry forward for expenditure in 2007, including $200 million that will be financed through long-term borrowing (see Table 2).[4] These additional appropriations completely used up the 2006 surplus and required dipping into 2006 reserves as well. Despite public claims, there was no $1 billion surplus in 2006, and the much smaller actual surplus has already been spent.

Both those who are pressing for major expansions in spending and those who are advocating for a more rapid reduction in the income tax rate will have to come to grips with the far less positive fiscal reality that lies ahead.

That reality begins with a fiscal 2007 budget that is not even in structural balance. Using the consensus revenue forecast (which appears conservative given the 2006 performance), the 2007 budget is more than $500 million out of balance.[5] Attaining balance will require revenue growth slightly greater than the 6.2 percent assumed in our analysis, and almost two percentage points greater than the underlying rate of growth assumed in the consensus forecast on which the 2007 budget was built. While the 6.2 percent rate of growth may be achievable, it is by no means certain.

The detailed results of the Foundation's analysis are presented in the following sections of the report, including the assumptions on which it is built, the year-by-year projections of revenues and spending used in the baseline analysis, and the annual costs of the selected restorations, obligations and initiatives considered in the analysis.

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[3] The growth in baseline tax revenues (before law changes) was 9.1 percent in 2006, according to the Department of Revenue; actual collections rose by 8.2 percent.

[4] Approximately two-thirds of the additional authorizations are for one-time purposes.

[5] In the absence of stronger revenue growth, the 2007 authorized spending (excluding prior appropriations carried forward from 2006) that is in excess of the consensus revenue forecast will have to be financed from reserves.

Five-Year Analysis

The Foundation built its analysis on three elements that are critical to assessing the fiscal capacity of the Commonwealth over the next five years:

1. The revenues that will be available to meet future needs.
2. The costs of maintaining the state's current budgetary commitments and obligations.
3. The future financial impact of addressing new priorities and initiatives that already command widespread support.

Revenues

The Foundation's baseline analysis assumes that over the next five years state tax revenues will grow by 6.2 percent a year, before adjusting for already authorized tax cuts (see Table 3). While this rate of growth is substantially less than the 9.1 percent baseline increase in fiscal 2006, it reflects the historical performance of the state's economy, as measured by the average annual growth in total personal income.

In several respects, the 6.2 percent growth assumption is optimistic, at least over the five-year time horizon of the analysis. It does not take into account the potential evaporation of the recent surge in volatile revenue sources such as capital gains and corporate profits, or the possibility of an economic recession. As the Commissioner of Revenue noted in announcing final tax receipts for fiscal 2006, these two sources

Table 3
Five-Year Baseline Budget Analysis
(Before Selected Spending Restorations, Obligations and Priorities)
($, millions)

	FY07	FY08	FY09	FY10	FY11	FY12
Revenues						
Taxes						
Baseline taxes at 6.2% growth*	$19,633	$20,850	$22,143	$23,516	$24,974	$26,522
Increase personal exemption	-60	-120	-120	-120	-120	-120
Triggered income tax cut to 5%	0	0	-51	-191	-331	-494
Other authorized tax cuts	-46	-77	-57	-57	-57	-57
Total taxes	19,528	20,653	21,915	23,148	24,466	25,851
Non-tax revenues						
Lottery at 3% growth	920	948	976	1,005	1,035	1,067
All other excluding Medicaid (0%-1%)	4,194	4,214	4,234	4,254	4,275	4,295
Total revenues	$24,642	$25,815	$27,125	$28,407	$29,776	$31,213

* Tax revenues shown include income taxes dedicated to pension costs and sales taxes dedicated to the MBTA and School Building Authority.

Table 3 - Continued
Five-Year Baseline Budget Analysis
(Before Selected Spending Restorations, Obligations and Priorities)
($, millions)

	FY07	FY08	FY09	FY10	FY11	FY12
Spending						
Health care at 7% growth						
Medicaid net of federal reimbursements	$3,750	$4,013	$4,293	$4,594	$4,915	$5,260
Employee health costs	1,064	1,138	1,218	1,303	1,394	1,492
Senior pharmacy (not incl. in Medicaid)	64	68	73	78	83	89
Health reform (7% growth beyond FY10)	200	200	200	400	428	458
Uncompensated care	290	200	200	200	200	200
Total health care	5,367	5,618	5,984	6,575	7,021	7,498
Local aid						
Chapter 70 at 3% growth	3,506	3,611	3,719	3,831	3,945	4,064
Lottery at 3% growth	920	948	976	1,005	1,035	1,067
Additional assistance	380	380	380	380	380	380
Other local aid at 3% growth	789	812	837	862	888	914
Total local aid	5,594	5,750	5,911	6,077	6,248	6,424
Other major commitments						
Pensions	1,358	1,419	1,483	1,550	1,619	1,692
Debt service - $1.25 billion spending cap	1,987	2,066	2,149	2,235	2,325	2,417
MBTA sales tax at 6.2% growth	734	780	828	879	934	992
School Building Authority phase-in	557	770	866	971	1,086	1,153
Total other major commitments	4,636	5,036	5,326	5,635	5,963	6,254
All other programs at 3% growth	8,975	9,245	9,522	9,808	10,102	10,405
Required stabilization fund deposit	98	103	110	116	122	129
Total spending and stabilization deposit	24,670	25,752	26,853	28,211	29,457	30,711
Revenue minus spending and stabilization deposit	-$29	$62	$272	$197	$319	$502

Note: Totals may not add exactly due to rounding.

led the growth in revenues in 2006.[6]

Revenue collections from these sources are notoriously volatile, responding in the case of corporate profits to national trends that are closely tied to the business cycle, and in the case of capital gains and other investment-related income to the often sharp fluctuations in national and worldwide capital markets. In 2002, the headlong plunge in tax collections was attributable in large part to the collapse of the stock market. And while economists cannot predict with any certainty when the next downturn will come, the possibility of a recession, perhaps a severe one, is very real over the next five years.

Fiscal 2007 revenue performance further highlights the risks in the 6.2 percent growth assumption. Tax receipts in July and August fell short of the benchmark for the consensus forecast (which is approximately $600 million lower than the 2007 revenues assumed in the baseline analysis). Although

[6] The 6.2 percent rate of growth is also assumed for fiscal 2007, producing a revenue figure that is $598 million higher than the conservative consensus forecast upon which the 2007 budget was built.

collections in these two months account for a relatively small share of the annual total, the weak performance so far is an inauspicious start for a year in which the consensus forecast must be exceeded by more than one-half billion dollars in order to achieve structural balance in the budget.

Current Budgetary Commitments

In calculating the costs of the state's existing programs and commitments over the next five years, the Foundation assumed a "bare bones" approach to budgeting that provides only the minimum amounts needed to sustain current services and obligations and to honor commitments that have already been made. This approach makes no provision for the costs of restoring prior spending cuts in local aid, higher education, and other areas or taking on new initiatives and obligations. The analysis includes the following major assumptions about future spending requirements (see Table 3 on page 6):

- Growth in health care spending of 7.0 percent a year, including the costs of Medicaid (net of federal reimbursements), employee health benefits, and the senior pharmacy program.

- Carrying forward the $200 million funding of health care reform in 2007 to 2008 and 2009, with an additional $200 million in 2010.

- Growth in Chapter 70 aid of 3.0 percent a year – the rate of inflation assumed in the analysis – in order to meet the state's obligation to assure an adequate level of school spending in poorer school districts. This rate of increase assumes the foundation budget as currently defined, with no legislative adjustments or expansions.

- Annual lottery aid growth of 3.0 percent a year; and level-funding of additional assistance.

- Increases in annual pension contributions that are consistent with the most recently approved pension funding schedule, which provides for growth of about 4.5 percent a year.

- Projected increases of about 4.0 percent a year in the costs of debt service, assuming that annual bond-funded capital spending is held within the current $1.25 billion cap.

- Growth in sales-tax-funded contributions to the MBTA at the assumed rate of overall tax growth.

- Phasing in of sales-tax-funded contributions to the School Building Authority over seven years ending in fiscal 2011, as provided in the Authority's enabling legislation.

- Spending growth for all other state programs at the assumed inflation rate of 3.0 percent a year, resulting in level funding of these programs in inflation-adjusted dollars.

- Annual contributions to the stabilization fund at the statutorily required amount of 0.5 percent of total tax revenues.

As previously noted, the overall spending totals in the analysis make no accommodation for reversing prior spending cuts beyond the restorations already implemented in recent budgets, or for any initiatives beyond those already enacted. Under the analysis, total spending[7] would grow by an average of 4.5 percent a year over the next five years, well below the

[7] Excluding federally reimbursed Medicaid spending.

Table 4
Selected Restorations, Obligations and Priorities
(Increase over 2006 in millions of dollars)

	FY07	FY08	FY09	FY10	FY11	FY12
Priorities highlighted by the Foundation						
"40%" local aid proposal (10-yr. phase-in)	$0	$159	$369	$632	$956	$1,340
Additional higher education funding	0	59	120	184	251	325
Increase in capital spending cap to $1.5 billion	0	13	42	75	113	157
Other spending priorities						
Restoration of 50% of prior cuts over 5 years	0	131	270	417	573	738
Pay-as-you-go capital spending (5-yr. phase-in)	0	50	103	159	219	281
Routine capital maintenance and repair	0	50	52	53	55	56
Looming obligations						
Unfunded medical costs of state retirees	0	378	391	401	408	415
Total	$0	$841	$1,347	$1,921	$2,575	$3,313

roughly seven percent growth in the 2007 budget and also less than the approximately five percent rate of annual increase that the administration has set as an informal guideline for prudent budgeting.

Even with this tight budgeting, the state would have very little room for program restorations or new priorities. Based on the bottom-line results of the analysis, in 2012 the revenues available for new initiatives would total $500 million, a modest amount in the context of the overall budget and in relation to the potential new funding needs.

Selected Restorations, Obligations and Priorities

The third element of the analysis is the broad array of new priorities, commitments and obligations that are now being considered or that address long-recognized needs. We have not attempted to identify a comprehensive roster of potential future initiatives, but instead have concentrated the analysis on a short list of priorities that the Foundation considers crucial to the long-term health of the state economy and on obligations that are so pressing that they cannot be ignored.

The initiatives included in the analysis fall into three broad categories (see Table 4):

- Major priorities that the Foundation has highlighted over the last 12 months.
- Other expansions that would help strengthen the state's competitiveness.
- Looming obligations that will be difficult, if not impossible, to avoid.

Table 5
Mismatch Between Projected Surplus Revenues and Selected Restorations, Obligations and Priorities
($, millions)

	FY07	FY08	FY09	FY10	FY11	FY12
Projected surplus revenues	-$29	$62	$272	$197	$319	$502
Selected restorations, obligations and priorities						
Priorities highlighted by the Foundation	0	232	531	891	1,320	1,822
Other spending priorities	0	231	425	629	846	1,076
Looming obligations	0	378	391	401	408	415
Total	0	841	1,347	1,921	2,575	3,313
Projected surplus revenues minus priorities and obligations	-$29	-$779	-$1,075	-$1,724	-$2,256	-$2,811

Priorities Previously Highlighted by the Foundation Three proposals supported by the Foundation have been considered in the analysis.

- *Dedicating 40 percent of income, sales, and corporate taxes to the state's major local aid accounts.* This MTF proposal would restore the deep cuts in aid during the state's fiscal crisis and expand future aid for our cash-strapped municipalities. Cities and towns face a long-term financial crunch due to dependence on uncertain state aid, rapidly rising costs, particularly for employee health care, and limited ability to raise revenues. The proposal would give local taxpayers much needed relief, while providing local officials with a degree of certainty about the ongoing share of state resources on which they can rely.

  The analysis assumes that the 40 percent goal would be phased in over ten years, with the first five years of the phase-in during 2008-2012.[8] At this pace of implementation, the plan would require an additional $160 million in 2008.[9] Due to the combined effect of the phase-in schedule and the assumed growth in annual tax revenues, this figure would rise to $1.3 billion in 2012.

- *Restoring the state's financial commitment to public higher education* along the lines proposed by the Joint Committee on Higher Education. In the Foundation's view, reversing the deep cuts in state support for higher education during the fiscal crisis is crucial to preparing our future workforce. Despite recent increases, 2007 funding for UMass and the state and community colleges remains almost one-third below 2001 levels after adjusting for inflation.

  The Committee's plan combines the additional funding with affordability safeguards for students and parents, a system to ensure that the new dollars are

[8] Under the Foundation's proposal, an amount equal to 40 percent of the actual income, corporate, and sales taxes in the calendar year preceding the beginning of the fiscal year would be made available to fund that year's Chapter 70 school aid, lottery, and additional assistance. The comparable figure for fiscal 2007 is 32 percent (2007 aid divided by calendar year 2005 tax collections).

[9] The additional dollars would come on top of the inflationary increases in the three main local aid accounts that have been assumed in the baseline projection (approximately $130 million in 2008).

distributed among campuses based on educational need, and governance reforms.

Based on MTF's estimates, this proposal would require approximately $60 million of additional appropriations in 2008, increasing gradually to about $325 million in 2012.

- *Raising the cap on bond-funded capital spending* from its current level of $1.25 billion to $1.5 billion in 2008, an amount that reflects the inflation in construction costs for state and local government since 2002, with additional annual adjustments in the cap in 2009 and beyond to keep up with inflation. The Foundation estimates that this action would require average increases in debt service of $30-$40 million a year over the next five years.

Other Spending Priorities The priorities emphasized by the Foundation represent only a small portion of the numerous initiatives and expansions which been identified since the state emerged from the recent fiscal crisis. We have not attempted to determine the potential fiscal impacts of a comprehensive list of these other spending priorities, but instead focused on a small number of potential program restorations and expansions, including additional capital investments.

- *Restoring a portion of the prior cuts in human service, environmental, and other programs.* The analysis assumes that half of these cuts would be restored over the next five years, requiring $130 million of additional spending in 2008 (beyond the three percent inflationary increase that is built into the analysis), rising to roughly $750 million in 2012.

- *Pay-as-you-go capital spending* Given the Commonwealth's enormous capital needs, it makes sense to use operating revenues as well as to raise the bond cap to help meet those needs. The analysis assumes that the additional pay-as-you-go capital expenditures would be phased in over five years beginning in fiscal 2008, reaching a total of $250 million a year (before adjusting for inflation) in 2012.

  Over the next ten years, the measure would support $2.4 billion of additional investments outside the capital spending cap. Although a substantial sum, this amount falls woefully short of the many billions of dollars more that are needed to proceed with capital projects that cannot be accommodated within the cap or that are not yet authorized.

- *Capital maintenance.* Providing $50 million a year for annual upkeep and repair would make at least a small dent in the large accumulation of deferred maintenance needs for state bridges, parks, campuses and other facilities.

Looming Obligations While the baseline analysis includes contractually or legally required costs, such as debt service payments to buyers of state bonds and refunds to taxpayers under the *Peterson* case, the state faces another major obligation that will soon have to be addressed:

- *The large unfunded liability for the future medical costs of state retirees.* These costs are now funded on a pay-as-you-go basis. In the recent actuarial valuation prepared for the state comptroller, the unfunded liability for these medical benefits was estimated at $7.6 billion (assuming that the state pays down the liability using the approach that was adopted for erasing the unfunded pension liability).

According to the valuation, if the state immediately adopted a funding schedule to eliminate the liability over 30 years, an additional $378 million would need to be appropriated in 2008. By 2012, the necessary funding would rise to $415 million, a figure that would continue to grow in subsequent years.

Although the Commonwealth may be able to put off addressing this obligation for a year or two, it will eventually have to be dealt with in order to protect the state's credit rating. However, the longer the delay, the larger the accumulated liability that will have to be funded.

Cities and towns will likewise face major unfunded liabilities for the medical costs of municipal retirees – the costs of which are not included in this analysis. In the absence of additional state assistance, such as that provided by MTF's "40 percent" aid proposal, these costs will inevitably have to be borne by local residents in the form of higher property taxes, reduced services, or both.

In combination, these three sets of initiatives – Foundation recommendations, other spending priorities, and the looming retiree medical obligation – would require an estimated $840 million of additional resources in 2008, increasing to $3.3 billion in 2012. These costs dwarf the surpluses projected in the baseline analysis, which range from $62 million in 2008 to $500 million in 2012.

This enormous mismatch does not take into account proposals to cut the income tax rate to 5.0 percent more rapidly than authorized in current law. While accelerating the tax cut would have only a modest impact in the final years of the analysis, over the short term it would even further limit the state's ability to take on new initiatives.

Far from exaggerating the disparity between resources and need, the Foundation's analysis, if anything, understates the financial challenges that lie ahead. On the revenue side, our assumption of 6.2 percent annual revenue growth does not account for an economic recession or for the loss of capital gains receipts that would result from a substantial downturn in the stock market. According to the analysis, the evaporation of the capital gains "bonus" that has pushed up receipts over the last two years would wipe out the projected surpluses under the "bare-bones" budgeting assumed in the analysis, throwing the state's finances into the red before addressing any of the priorities we have identified (see Table 6).[10] A recession would result in even larger deficits, requiring cuts in existing programs and precluding any consideration of restorations or expansions.

At the same time, a more optimistic revenue outlook would do little to change the overall picture. As Table 6 shows, even under the highly unrealistic assumption that baseline tax revenues continue to grow for another two years at the rapid 9.1 percent pace of 2006, the resulting strong surpluses – ranging from $1.2 billion in 2008 to $1.9 billion in 2012 – would still be insufficient to accommodate the initiatives we have considered.

Each of these alternative revenue scenarios assumes that the tight rein on spending growth built into the analysis can actually be achieved. The baseline projection – a rate of spending growth of 4.5 percent a year on

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[10] The use of a more conservative revenue assumption along the lines considered prudent by the administration would result in greater deficits still. Assuming 5.0 percent, rather than 6.2 percent, annual growth in tax revenues over the next five years would produce deficits ranging from more than $300 million in fiscal 2008 to almost $600 million in 2012 – before accounting for the costs of initiatives.

Table 6
Analysis Using Alternative Revenue Assumptions
($, millions)

	FY07	FY08	FY09	FY10	FY11	FY12
Revenue growth at long-term average						
Assumed rate of tax revenue growth	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%
Revenue minus Table 3 spending	-29	62	272	197	319	502
Revenue minus Table 3 spending minus Table 4 restorations, obligations, and priorities	-29	-779	-1,075	-1,724	-2,256	-2,811
Strong revenue performance through FY08						
Assumed rate of tax revenue growth	9.1%	9.1%	6.2%	6.2%	6.2%	6.2%
Revenue minus Table 3 spending	505	1,168	1,443	1,431	1,621	1,877
Revenue minus Table 3 spending minus Table 4 restorations, obligations, and priorities	505	327	96	-490	-954	-1,436
Evaporation of capital gains "surprise"						
Assumed rate of tax revenue growth	3.1%	6.2%	6.2%	6.2%	6.2%	6.2%
Revenue minus Table 3 spending	-599	-484	-370	-481	-397	-254
Revenue minus Table 3 spending minus Table 4 restorations, obligations, and priorities	-599	-1,325	-1,717	-2,402	-2,972	-3,567

average – would require that much of state government be level-funded (after taking inflation into account) for the next five years, while making no provision for further restoration of previous spending cuts or for any significant expansions. This kind of spending discipline has rarely been sustained over any significant period of time – and then only in response to fiscal crisis, not in years of healthy revenue growth.

Although it is certainly possible to scale back the selected priorities and initiatives – by setting less ambitious goals or by implementing the initiatives at an even slower pace than we have assumed – the basic conclusions of the analysis again would remain essentially unchanged.

For example, if the pace of implementation of the Foundation's 40 percent local aid plan were stretched out from the ten years assumed in the analysis to an untenably long twenty years, the costs of that initiative in 2012 would still consume essentially all of the projected available revenues for that year, before addressing any of the other priorities. Even if the scope of all of the priorities were reduced by half, the amounts needed to finance them would exceed available resources by more than $1 billion.

Conclusion

Considering the Foundation's analysis as a whole, it is clear that the state's fiscal leaders, both current and future, will face enormous challenges through the end of the decade. On the one hand, the analysis demonstrates that the Commonwealth will have sufficient resources to meet its current obligations and commitments – but *only* if it maintains the kind of fiscal discipline that enabled the state to weather successfully the recent fiscal crisis. It is equally clear that the state budget can accommodate only a small fraction of the long list of expensive initiatives that are now under consideration – which include further significant restorations of the severe spending cuts during the fiscal crisis – *and* that it will not be possible for the state to grow its way out of the mismatch between available resources and spending ambitions.

As the Foundation underscored in a recent *Bulletin*,[11] the 2007 budget process provides an example of the kind of decision making that must be avoided if the state is to maintain fiscal stability. In both its rate of spending growth and in its reliance on the stabilization reserve to support that growth, the 2007 budget reflects a worrisome lapse of fiscal discipline. It creates expectations for annual spending growth that cannot be sustained, and it risks the reserves that will be needed in the event of an economic downturn.

There is no question that the Commonwealth has sufficient cash on hand to pay for the spending that has been authorized in the budget, as well as in the economic stimulus and supplemental spending bills that were adopted at the end of fiscal 2006. Although the recent weak performance raises some concerns, we continue to believe that 2007 tax revenues will be sufficient to avoid a draw on the rainy day fund in order to support ongoing operating costs.

However, the Foundation's analysis paints a picture that is starkly at odds with the expansionary mood that has driven the budgetary choices for 2007. The financial proposals and decisions of the last six months have taken place in what can only be described as a misguidedly festive atmosphere. In light of the Foundation's new findings, the party will soon be over.

Methodology

The five-year financial analysis is intended to provide a framework for identifying longer-term trends in the state's finances, not to forecast specific financial results. For the purposes of presenting a fuller picture of the Commonwealth's tax-supported finances, the analysis includes spending for pensions, the MBTA, and school building construction, as well as the dedicated income and sales tax receipts which support that spending, and excludes the portion of Medicaid spending that is financed from federal reimbursements. Non-tax revenues other than Medicaid federal reimbursements are included in the analysis, with annual growth rates that average a modest three percent or less, reflecting historical performance that is much less robust than tax revenues.

Because of these and other accounting differences, the total revenue and expenditure amounts calculated in the analysis would differ from those reported in the Comptroller's official financial statements and those appearing in the General Appropriation Act ("the budget").

The analysis makes use of several simplifying assumptions in calculating the future impacts of initiatives, both currently authorized and proposed. These modeling simplifications in some instances may affect the timing of the initiatives' impacts in individual fiscal years, but should not materially change their cumulative effects.

Although the analysis of spending growth builds in annual inflationary increases in the costs of existing programs, it does not assume any "efficiency" gains that would reduce spending for those programs below inflation. Approximately two-thirds of the state budget is dedicated to fixed costs such as debt service and pensions, pass-through payments such as local aid to cities and towns and revenues set aside for the MBTA, and difficult-to-control Medicaid and other health care costs. A significant portion of the remaining one-third supports the direct delivery of human and other services.

[11] *State Budget 2007: Fanning the Expansionary Flames*, June 22, 2006.

EXHIBIT 4.1
SCHEDULE A RECEIPTS
FISCAL YEAR 2000 TO 2007

ITEM	PROJECTED FY 07	ACTUAL FY 06	ACTUAL FY 05	ACTUAL FY 04	ACTUAL FY 03	ACTUAL FY 02	ACTUAL FY 01	ACTUAL FY 00	ACTUAL FY 99
MOTOR VEHICLE EXCISE	$ 4,700,000	$ 4,688,251	$ 4,680,209	$ 4,260,729	$ 4,438,140	$ 4,127,776	$ 3,919,368	$ 3,770,230	$ 3,291,131
OTHER EXCISE	$ 46,000	$ 49,047	$ 47,454	$ 44,571	$ 52,128	$ 69,073	$ 75,927	$ 63,055	$ 56,185
PENALTIES AND INTEREST	$ 200,000	$ 217,472	$ 220,875	$ 203,838	$ 158,815	$ 131,076	$ 177,166	$ 171,002	$ 241,921
PAYMENT IN LIEU OF TAXES	$ 27,000	$ 28,152	$ 27,057	$ 29,515	$ 29,908	$ 26,568	$ 26,689	$ 26,282	$ 22,894
CHARGES FOR SERVICES - WATER	$ 3,100,000	$ 2,939,701	$ 2,827,012	$ 2,750,427	$ 2,687,023	$ 2,778,081	$ 2,625,987	$ 2,531,831	$ 2,484,425
CHARGES FOR SERVICES - ASH DISPOSAL	$ 500,000	$ 580,000	$ 570,000	$ 961,582	$ 1,098,492	$ 893,950	$ 592,754	$ 453,309	$ 2,138,382
FEES	$ 200,000	$ 97,333	$ 118,150	$ 138,184	$ 198,556	$ 120,026	$ 89,679	$ 88,006	$ 99,020
RENTALS	$ 15,000	$ 12,702	$ 15,698	$ 12,764	$ 13,238	$ 12,240	$ 13,391	$ 11,791	$ 6,796
DEPARTMENTAL REVENUE - SCHOOLS	$ -	$ 45,958	$ 40,501	$ -	$ -	$ -	$ 180	$ 725	$ 6,034
DEPARTMENTAL REVENUE - LIBRARIES	$ -	$ -	$ -	$ -	$ -	$ 97	$ 456	$ 541	$ 860
DEPARTMENTAL REVENUE - CEMETERIES	$ 31,000	$ 42,297	$ 31,380	$ 34,820	$ 31,905	$ 30,798	$ 36,935	$ 30,844	$ 34,432
OTHER DEPARTMENTAL REVENUE	$ 300,000	$ 295,018	$ 227,967	$ 337,487	$ 328,916	$ 198,007	$ 189,727	$ 138,407	$ 218,129
LICENSE AND PERMITS	$ 700,000	$ 1,237,994	$ 373,429	$ 423,937	$ 385,023	$ 618,764	$ 354,409	$ 422,312	$ 402,511
SPECIAL ASSESSMENTS	$ 31,000	$ 35,150	$ 31,575	$ 21,584	$ 47,422	$ 35,456	$ 84,848	$ 21,434	$ 22,615
FINES AND FORFEITS	$ 200,000	$ 271,803	$ 186,372	$ 310,446	$ 298,028	$ 273,867	$ 270,726	$ 208,634	$ 227,023
INVESTMENT INCOME	$ 1,100,000	$ 1,126,738	$ 932,675	$ 1,229,492	$ 1,561,045	$ 980,007	$ 1,753,148	$ 1,721,010	$ 1,605,296
MISCELLANEOUS RECURRING	$ -	$ -	$ -	$ -	$ -	$ 17,221	$ 22,722	$ 32,809	$ 27,181
MISCELLANEOUS NON-RECURRING	$ 150,000	$ 150,070	$ 172,413	$ 185,840	$ 247,705	$ 2,835,775	$ -	$ -	$ -
MEDICAID REIMBURSEMENT	$ 50,000	$ 107,257	$ 51,139	$ 49,779	$ 185,266	$ 129,032	$ 70,106	$ 98,263	$ 130,056
SUPPLEMENTAL TAX PROGRAM	$ 50,000	$ 47,040	$ 169,937	$ 178,455	$ 89,088	$ 104,070	$ 142,235	$ -	$ -
	$ 11,400,000	$ 11,971,983	$ 10,723,843	$ 11,173,450	$ 11,850,698	$ 13,381,884	$ 10,446,453	$ 9,790,485	$ 11,014,891
ESTIMATE		$ 10,388,000	$ 10,415,000	$ 10,244,000	$ 9,521,090	$ 9,693,984	$ 9,302,066	$ 9,343,600	$ 8,341,900
OVER(UNDER)		$ 1,583,983	$ 308,843	$ 929,450	$ 2,329,608	$ 3,687,900	$ 1,144,387	$ 446,885	$ 2,672,991
PERCENT OVER(UNDER)		15.2%	3.0%	9.1%	24.5%	38.0%	12.3%	4.8%	32.0%

FY 2002 total includes a bond premium of $2,384,623 AP Account Closeout of $449,443, building permit fee of $252,000 on the State Street Bank project and coal ash revenue of $180,806

FY 2003 total includes a bond premium of $247,705 and coal ash revenue of $364,000

FY 2006 total includes permit fees for the Charles River Labs & Avalon Shrewsbury Projects

Exhibit 4.2
Analysis of Motor Vehicle Excise Tax
Commitments One Through Four 1998 to 2006

Commitment #1

Year	# of Bills	Increase	Value	Increase	Value Per Bill	Increase
1998	22,597		$1,970,266.25		$87.19	
1999	23,282	685	$2,210,410.00	$240,143.75	$94.94	$7.75
2000	24,003	721	$2,408,810.00	$198,400.00	$100.35	$5.41
2001	25,289	1,286	$2,695,761.25	$286,951.25	$106.60	$6.24
2002	25,832	543	$2,816,752.50	$120,991.25	$109.04	$2.44
2003	26,328	496	$2,949,453.75	$132,701.25	$112.03	$2.99
2004	26,574	246	$2,987,201.25	$37,747.50	$112.41	$0.38
2005	27,271	697	$3,168,876.25	$181,675.00	$116.20	$3.79
2006	27,640	369	$3,235,402.50	$66,526.25	$117.06	$0.86

Commitment #2

Year	# of Bills	Increase	Value	Increase	Value Per Bill	Increase
1998	2,159		$493,780.32		$228.71	
1999	1,948	(211)	$470,501.32	($23,279.00)	$241.53	$12.82
2000	2,379	431	$635,405.71	$164,904.39	$267.09	$25.56
2001	2,011	(368)	$560,287.49	($75,118.22)	$278.61	$11.52
2002	2,264	253	$661,474.00	$101,186.51	$292.17	$13.56
2003	2,078	(186)	$577,754.71	($83,719.29)	$278.03	($14.14)
2004	2,233	155	$539,389.00	($38,365.71)	$241.55	($36.48)
2005	1,826	(407)	$435,094.27	($104,294.73)	$238.28	($3.28)
2006	2,300	2,300	$656,190.48	$221,096.21	$285.30	$47.02

Commitment #1 & #2

Year	# of Bills	Increase	Value	Increase	Value Per Bill	Increase
1998	24,756		2,464,047		$99.53	
1999	25,230	474	2,680,911	$216,864.75	$106.26	$6.73
2000	26,382	1,152	3,044,216	$363,304.39	$115.39	$9.13
2001	27,300	918	3,256,049	$211,833.03	$119.27	$3.88
2002	28,096	796	3,478,227	$222,177.76	$123.80	$4.53
2003	28,406	310	3,527,208	$48,981.96	$124.17	$0.37
2004	28,807	401	3,526,590	($618.21)	$122.42	($1.75)
2005	29,097	290	3,603,971	$77,380.27	$123.86	$1.44
2006	29,940	843	3,891,593	$287,622.46	$129.98	$6.12

Commitment #3

Year	# of Bills	Increase	Value	Increase	Value Per Bill	Increase
1998	1,391		$209,487.53		$150.60	
1999	1,505	114	$298,072.60	$88,585.07	$198.05	$47.45
2000	1,671	166	$296,445.55	($1,627.05)	$177.41	($20.65)
2001	1,569	(102)	$259,439.78	($37,005.77)	$165.35	($12.05)
2002	1,344	(225)	$193,487.40	($65,952.38)	$143.96	($21.39)
2003	1,543	199	$239,761.26	$46,273.86	$155.39	$11.42

Exhibit 4.2
Analysis of Motor Vehicle Excise Tax
Commitments One Through Four 1998 to 2006

2004	1,361	(182)	$243,943.55	$4,182.29	$179.24	$23.85
2005	1,832	471	$400,772.00	$156,828.45	$218.76	$39.52
2006	1,414	(418)	$211,119.74	($189,652.26)	$149.31	($69.46)

First Three Commitments

Year	# of Bills	Increase	Value	Increase	Value Per Bill	Increase
1998	26,147		$ 2,673,534.10		$102.25	
1999	26,735	588	$ 2,978,983.92	$305,449.82	$111.43	$9.18
2000	28,053	1,318	$ 3,340,661.26	$361,677.34	$119.08	$7.66
2001	28,869	816	$ 3,515,488.52	$174,827.26	$121.77	$2.69
2002	29,440	571	$ 3,671,713.90	$156,225.38	$124.72	$2.94
2003	29,949	509	$ 3,766,969.72	$95,255.82	$125.78	$1.06
2004	30,168	219	$ 3,770,533.80	$3,564.08	$124.98	($0.79)
2005	30,929	761	$ 4,004,742.52	$234,208.72	$129.48	$4.50
2006	31,354	425	$4,102,712.72	$97,970.20	$130.85	$1.37

Commitment #4

Year	# of Bills	Increase	Value	Increase	Value Per Bill	Increase
1998	1,533		$211,593.46		$138.03	
1999	1,791	258	$252,737.88	$41,144.42	$141.12	$3.09
2000	1,394	(397)	$222,543.72	($30,194.16)	$159.64	$18.53
2001	1,745	351	$274,920.67	$52,376.95	$157.55	($2.10)
2002	1,934	189	$353,606.28	$78,685.61	$182.84	$25.29
2003	1,613	(321)	$262,934.60	($90,671.68)	$163.01	($19.83)
2004	1,748	135	$375,342.02	$112,407.42	$214.73	$51.72
2005	1,752	4	$357,486.13	($17,855.89)	$204.04	($10.68)
2006	1,416	(336)	$232,231.20	($125,254.93)	$164.01	($40.04)

First Four Commitments

Year	# of Bills	Increase	Value	Increase	Value Per Bill	Increase
1998	27,680		$2,885,127.56		$104.23	
1999	28,526	846	$3,231,721.80	$346,594.24	$113.29	$9.06
2000	29,447	921	$3,563,204.98	$331,483.18	$121.00	$7.71
2001	30,614	1,167	$3,790,409.19	$227,204.21	$123.81	$2.81
2002	31,374	760	$4,025,320.18	$234,910.99	$128.30	$4.49
2003	31,562	188	$4,029,904.32	$4,584.14	$127.68	($0.62)
2004	31,916	354	$4,145,875.82	$115,971.50	$129.90	$2.22
2005	32,681	765	$4,362,228.65	$216,352.83	$133.48	$3.58
2006	32,770	89	$4,334,943.92	($27,284.73)	$132.28	($1.20)

EXHIBIT 6.1
FREE CASH ESTIMATE
FISCAL YEAR 2007

FISCAL YEAR END	BALANCE AS OF 7/1	AMOUNT APPROPRIATED	FOLLOWING YEAR BALANCE	GAIN/(LOSS)
2006	$4,137,833			
2005	$1,930,113	$1,750,000	$4,137,833	$2,207,720
2004	$2,832,695	$2,500,000	$1,930,113	($902,582)
2003	$3,616,392	$2,880,000	$2,832,695	($783,697)
2002	$6,958,805	$6,113,416	$3,616,392	($3,342,413)
2001	$4,087,506	$2,077,612	$6,958,805	$2,871,299
2000	$2,884,606	$1,468,606	$4,087,506	$1,202,900
1999	$5,588,576	$3,928,000	$2,884,606	($2,703,970)
1998	$4,611,834	$3,010,784	$5,588,576	$976,742
1997	$4,555,647	$3,418,656	$4,611,834	$56,187
1996	$2,996,394	$1,300,000	$4,555,647	$1,559,253
1995	$3,909,803	$3,294,500	$2,996,394	($913,409)
1994	$2,672,855	$1,864,000	$3,909,803	$1,236,948
1993	$3,039,269	$2,030,500	$2,672,855	($366,414)
1992	$2,275,622	$1,122,000	$3,039,269	$763,647
1991	$1,560,672	$867,000	$2,275,622	$714,950
1990	$1,269,570	$850,000	$1,560,672	$291,102

Indicates balance influenced by bond premium that was run through Free Cash in the amount of $2,385,000

11/16/2006

EXHIBIT 6.2
STABILIZATION FUND

Town Meeting Vote May-99 Transfer to Stabilization	250,000.00	
Interest FY 00	6,172.90	
Balance 6/30/00		256,172.90
Town Meeting Vote May-00 Transfer to Stabilization	250,000.00	
Interest FY 01	22,243.90	
Balance 6/30/01		528,416.80
Town Meeting Vote 5/1/2001 For FY 02 Transfer to Stabilization	250,000.00	
Interest FY 02	39,917.53	
Balance 6/30/02		818,334.33
Transfer to Gen Fd (FY 02)	(275,000.00)	
Transfer to Stabilization FY 03	250,000.00	
Interest FY 03	62,644.86	
Balance 6/30/03		855,979.19
Transfer to Stabilization FY 04	250,000.00	
Transfer to Gen Fd Boathouse	(185,000.00)	
Interest FY 04	34,390.88	
Balance 6/30/04		955,370.07
Transfer to Gen Fd FY 05	(485,000.00)	
Transfer to Gen Fd FY 05	(150,000.00)	
Interest FY 05	22,408.60	
Balance 6/30/05		342,778.67
Transfer to Gen Fd FY 06	(170,000.00)	
Interest FY 06	8,028.04	
Balance 6/30/06		180,806.71
Transfer from the Gen Fd FY 07	388,348.00	
Interest FY 06	525.67	
Balance 9/30/06		569,680.38

Moody's Investors Service

Global Credit Research
New Issue
8 NOV 2006

Exhibit 6.3

Save as PDF

New Issue: Shrewsbury (Town of) MA

MOODY'S ASSIGNS MIG 1 RATING TO TOWN OF SHREWSBURY'S (MA) $6.1 MILLION GENERAL OBLIGATION BOND ANTICIPATION NOTES

Aa3 RATING AFFIRMED; AFFECTS $72.65 MILLION IN OUTSTANDING LONG-TERM DEBT

Municipality
MA

Moody's Rating

ISSUE	RATING
Bond Anticipation Notes, Unlimited Tax	MIG 1

Sale Amount	$6,100,000
Expected Sale Date	11/09/06
Rating Description	Bond Anticipation Notes, Unlimited Tax

Opinion

NEW YORK, Nov 8, 2006 -- Moody's Investors Service has assigned a MIG 1 rating to the Town of Shrewsbury's $6.1 million General Obligation Bond Anticipation Notes. At this time, Moody's has affirmed the Aa3 rating assigned to the town's $72.65 million outstanding long-term general obligation debt. The notes (dated November 22, 2006 and payable November 21, 2007) are secured by the town's general obligation unlimited tax pledge, as debt service has been voted exempt from the levy limits of Proposition 2 1/2. Proceeds will refund maturing notes. The MIG1 rating reflects demonstrated market access and the town's above-average underlying credit profile, which includes a financial position that is expected to be augmented in fiscal 2006 following anticipated declines in reserves in fiscal 2004 and 2005, a rapidly growing and wealthy tax base reflective of the location of the community between Worcester (rated A3) and Boston (rated Aa1/stable outlook), and a manageable debt burden with moderate borrowing plans.

DEMONSTRATED MARKET ACCESS

Moody's believes that Shrewsbury will maintain sufficient access to capital markets based on the town's favorable history. The town received six bids on its most recent note sale, dated September 15, 2006, seven bids on its sale dated August 12, 2005 and six bids on its prior note sale dated November 24, 2004. Proceeds will renew maturing notes originally issued to fund the acquisition of a 60-acre parcel of commercially-zoned land, the former Allen Farm, which is intended to be resold to a developer. The state has extended the period of time in which the notes may remain outstanding to ten years as the town intends to repay the notes with proceeds from the resale of this land. However, the notes are ultimately secured by the town's general obligation pledge and could be refinanced with long term debt in the event the sale is delayed beyond this time frame.

SLIM FINANCIAL POSITION EXPECTED TO IMPROVE

Moody's anticipates that the town's financial position will begin to stabilize after several years of reserve declines. Shrewsbury's operating budget has faced pressure from unanticipated weather-related expenses, rising pension, health insurance and reductions in state aid other than education funding. As a result the town's available reserve (combined unreserved general fund and stabilization fund) position has declined to very slim levels, with the fiscal 2005 available reserve of $5.3 million representing 7% of general fund revenues, significantly lower than the $8.4 million (12.9% of revenues) recorded in fiscal 2003, a level that is inconsistent with medians for the current rating level. Favorably, preliminary fiscal 2006 projections indicate significant replenishment of reserves after tight expenditure management, reduced free cash appropriations and conservative revenue forecasting, as well as limited one-time revenue receipts, are expected to generate an increase in undesignated general fund balance to a healthier $4.7 million (5.8% of revenues) from a very narrow $2.1 million (2.8%) in fiscal 2005. Pro-forma projections for available reserves improve to $7.99 million or 9.8% of revenues, despite a net draw on the stabilization fund to offset debt service expenditures. However, management expects operating budgets for fiscal 2007 and future years to remain pressured and reserve replenishment to be limited as revenue growth from state aid and expected tax base expansion may not outpace salary-related expenses and residents' demands for restored services. Despite the failure of override votes for fiscal 2005 and 2006, town officials are considering an operating override in the spring of

2007 to augment tax levy capacity in fiscal 2008. Future rating actions will incorporate the town's ability to maintain structural balance and to replenish reserves to levels consistent with similarly-rated communities.

GROWTH IN RESIDENTIAL AND COMMERCIAL SECTORS MAY BE LIMITED BY WATER AND SEWER CAPACITY

Located in Worcester County near the Route 495 corridor, Shrewsbury has been a high-growth community over the past decade. Its population grew 31% from 1990 to 2000, and equalized valuation has increased a substantial 13.3% annually since 2001. The town, which is 88% residential, has added $2.1 billion in assessed valuation in the past five years alone. Although the majority of new growth in prior years has been within the residential sector, the town is beginning to see a shift to more commercial construction. Management reports new commercial development in properties adjacent to the industrial park, and a continuing increase in assessed commercial values, reversing the trend of declines in commercial assessments in the last few years. Although new single-family housing development has slowed, multi-family residential development continues and is expected to add $96 million in taxable value in fiscal 2007. Future residential growth may be limited as the town is beginning to reach water and wastewater system capacity; the town has recently reserved 75% of its remaining wastewater treatment capacity for future commercial development. The value of the average single-family home has increased to $380,000 in fiscal 2006, a healthy 11% increase from fiscal 2005. The town's socioeconomic indices continue to strengthen, now exceeding state medians and further reflected in the solid $127,864 equalized value per capita.

FAVORABLE DEBT PROFILE SUPPORTED BY UTILITY REVENUES AND STATE GRANTS

Moody's anticipates that the town's average 2.0% overall (unadjusted) debt burden will remain manageable, given an average retirement of principal (67.4% within 10 years), and significant state school building aid (64%). After adjusting for commonwealth reimbursement, the town's debt burden drops to a more modest 1.1% of equalized valuation. Town officials began receiving state payments for construction of the high school in 2004, and for the middle school project in August 2005. With the large middle school and high school projects largely behind them, town officials expect more moderate debt issuance going forward. Voters recently extended Shrewsbury's solid track record of capital project approvals by excluding debt service for $7.4 million in fire station construction and renovations from Proposition 2 ½. Future projects are expected to include a $10 million library expansion, for which a 33% state grant is expected, a renovation and expansion of the middle school, ongoing water and sewer improvements and a new police station. The town plans to issue up to $4 million in short-term notes in fiscal 2007 to finance the first phase of the fire station project and two new water tanks. Water and wastewater debt service is expected to be fully covered by system revenues and recent rate increases in each system of up to 15% are expected to generate sufficient revenue in the medium term for ongoing capital projects. The library project is expected to be funded by a state grant of approximately $4 million and private fund raising. The town's second middle school project has been postponed pending updated enrollment projections and revised eligibility guidelines for the commonwealth's school construction reimbursement program.

KEY STATISTICS

2000 Population: 31,640

2007 Equalized Valuation (proposed): $5 billion

2007 Equalized Value per capita: $152,046

Average Annual Growth, Equalized Valuation (2001-2007): 13.3%

Overall debt burden: 1.6% of equalized valuation

Adjusted debt burden: 1.1% of equalized valuation

Amortization of principal (10 years): 67.4%

Per Capita Income: $31,570 (121.6% of commonwealth, 146.2% of US)

Median Family Income: $77,675 (126.0% of commonwealth, 155.2% of US)

Fiscal 2005 General Fund balance: $9.7 million (12.6% of revenues)

Fiscal 2005 Available Reserve balance: $5.38 million (7% of revenues)

Long-Term Debt Outstanding: $72.65 million

Exhibit 8.2

School Enrollment Projections

	k	1	2	3	4	5	k- 5	6	7	8	6-8	9	10	11	12	9-12	TOTAL*	preschool	
		1.152	1.030	1.004	1.036	1.004		1.005	1.010	1.004		0.938	1.001	0.971	0.998				
1994	346	316	329	327	308	281	1907	247	286	321	854	263	268	194	202	927	3688	76	3764
1995	339	366	329	327	324	318	2003	280	257	275	812	268	256	265	189	978	3793	87	3880
1996	342	381	375	340	341	323	2102	321	288	252	861	243	255	254	249	1001	3964	76	4040
1997	330	365	400	389	348	359	2191	330	331	291	952	196	225	264	239	924	4067	105	4172
1998	403	381	365	408	395	354	2306	356	328	338	1022	241	198	226	254	919	4247	134	4381
1999	359	466	395	391	424	394	2429	352	356	328	1036	266	234	202	219	921	4386	126	4512
2000	393	420	471	402	399	433	2518	389	361	367	1117	290	280	245	213	1028	4663	135	4798
2001	385	475	444	469	424	419	2616	427	400	364	1191	324	296	283	236	1139	4946	131	5077
2002	407	442	483	442	488	428	2690	423	426	395	1244	343	330	287	274	1234	5168	150	5318
2003	398	484	464	480	464	494	2784	436	438	437	1311	356	343	324	289	1312	5407	157	5564
2004	384	449	489	464	504	463	2753	492	444	441	1377	413	360	334	320	1427	5557	174	5731
2005	394	452	466	502	466	502	2782	461	486	443	1390	425	402	345	344	1516	5688	188	5876
2006	378	440	468	452	507	462	2707	488	449	501	1438	408	436	388	351	1583	5728	173	5901
2007	410	435	453	470	468	509	2746	464	493	451	1408	470	408	423	387	1689	5843		
2008	373	472	448	455	487	470	2706	512	469	495	1475	423	470	396	423	1712	5894		
2009	395	430	486	450	471	489	2722	473	517	471	1460	464	423	457	396	1740	5922		
2010	359	455	443	488	467	473	2685	491	477	519	1487	442	465	411	456	1773	5945		
2011	384	414	469	444	506	468	2685	476	496	479	1451	487	442	451	410	1790	5926		
2012	384	442	426	471	460	508	2691	471	480	498	1449	450	487	429	450	1816	5957		
2013	384	473	487	428	488	462	2721	511	475	482	1468	467	450	473	428	1819	6008		
2014	384	442	487	489	443	489	2735	464	516	477	1457	453	468	437	472	1829	6022		
2015	384	442	456	489	507	445	2722	492	469	518	1479	448	478	454	436	1816	6017		

Births		k		b-k
1997	441	2002	407	0.923
1998	460	2003	398	0.865
1999	458	2004	385	0.841
2000	460	2005	394	0.857
2001	453	2006	378	0.834
			5 Year Ave =	0.864
		Projections		
2002	474	2007	410	0.864
2003	432	2008	373	0.864
2004	457	2009	395	0.864
2005	415	2010	359	0.864
	445			
Assumed				
2006	445	2011	384	0.864
2007	445	2012	384	0.864
2008	445	2013	384	0.864
2009	445	2014	384	0.864
2010	445	2015	384	0.864

survivals	k-1	1 - 2	2 - 3	3 - 4	4 - 5	5 - 6	6 - 7	7 - 8	8 - 9	9 - 10	10 - 11	11 - 12
2001-02	1.148	1.017	0.995	1.041	1.009	1.010	0.998	0.988	0.942	1.019	0.970	0.968
2002-03	1.189	1.050	0.994	1.050	1.012	1.019	1.035	1.026	0.901	1.000	0.982	1.007
2003-04	1.128	1.010	1.000	1.050	0.998	0.996	1.018	1.007	0.945	1.011	0.974	0.988
2004-05	1.177	1.038	1.027	1.004	0.996	0.996	0.988	0.998	0.964	0.973	0.958	1.030
2005-06	1.117	1.035	0.970	1.010	0.991	0.972	0.974	1.031	0.921	1.026	0.965	1.017
ave	1.152	1.030	1.004	1.036	1.004	1.005	1.010	1.004	0.938	1.001	0.971	0.998

Notes:

- 1994-2006 are actual enrollments
- Projections were calculated by taking a 5 year average of the birth to kindergarden survival for years 1997-2006 and multiplying the average survival factor by the births recorded in 2002-2005
- Assumed births for 2006-10 were calculated taking the average of the previous four years of recorded births

Shaded areas indicate projections based on assumed births

2006

Town Manager's Office
10/16/2006