The Research Bureau

The Case for a Single Tax Rate

Each year, on the third Tuesday of November, the Worcester City Council goes through the ritual of setting the tax rate for the fiscal year that began on the previous July 1. In determining the rate, the Council debates how far to use the "tax classification" system to raise property taxes on businesses so as to minimize the burden on homeowners. Some justify charging higher rates to businesses on the ground that they can afford to pay tax increases more easily than homeowners can. (A skeptic might respond that the real point is that homeowners vote, while businesses don't.) But even when the maximum allowable shift is adopted that is, businesses pay 175% of the single tax rate (total tax levy divided by total assessed value multiplied by one thousand) and homeowners therefore pay the lowest possible rate, the tax bill for homeowners still increases over the previous year. Is tax classification really in the long-term interest of Worcester citizens, including homeowners?

Under Massachusetts General Laws Ch.59, cities and towns are allowed to adopt property tax classification, which permits different classes of property (residential and commercial/industrial) to be taxed at different rates. The City of Worcester adopted this option in FY84, shortly after its enactment. At that time, residential values and commercial/industrial values comprised 65% and 35% of the total tax base, respectively. Today, residential property represents 81% of the total assessed value while commercial/industrial value has shrunk to 19%. In other words, homeowners are now responsible for more of the total tax burden than they were twenty-five years ago. Rather than lowering homeowners' taxes, tax classification has raised them by driving out taxpaying businesses from the City.

As one instance of the effect of tax classification, several years ago, Saint-Gobain decided to build a new plant in Northboro rather than in Worcester, despite having numerous vacant building on its Worcester campus. That decision was followed more recently by a further expansion of its Northboro operations. According to Donald Melville, retired Chairman and CEO of the company, the City's discriminatory tax rate drove the decision. In FY08, Northborough's single tax rate was $13.28 while Worcester's commercial/industrial rate was $26.20, or roughly twice as much.

The latest evidence that the split tax rate matters comes from the Mass High Tech Council's ranking of all 351 Massachusetts cities and towns based on how far they meet the needs of high tech employers and employees. The top variable is tax policy: Is there a split rate? And if so, what is the difference between the two rates? And what is the commercial tax rate? While Shrewsbury and Grafton, both with single tax rates, ranked number 2 and 4, respectively, in the entire state, neighboring Worcester ranked number 240. The accompanying table amply illustrates Worcester's problem and its urgent need to adopt a single tax rate. Why would companies choose to triple their taxes by locating in Worcester rather than in Shrewsbury or Grafton?

Commercial Tax Rate and Mass Track Rank in Nearby Communities

Municipality	2008 Mass Track Rating	FY08 Commercial-Industrial Tax Rate
Shrewsbury	2	$9.14
Grafton	4	$10.05
Douglas	6	$10.11
Boylston	7	$11.44
Leominster	8	$11.25
Uxbridge	10	$10.47
Worcester	240	$26.20

Source: Massachusetts Department of Revenue; Massachusetts High Technology Council

For the past eight years, The Research Bureau has highlighted Worcester's problems that result from tax classification in our annual report "Benchmarking Economic Development in Worcester." To begin the discussions for phasing out the dual tax rate not just in Worcester, but in all 103 municipalities that adopted this local option, The Research Bureau offers a proposal. The Commonwealth should increase local aid to those communities that implement a five-year plan to phase in a single tax rate and meet several performance measures:

- Develop a five-year financial plan for phasing in a single tax rate that is approved by the local legislative body and monitored by the Department of Revenue.
- Increase reserve levels.
- Reduce debt service and establish a cap on borrowing.

- Spend year-end free cash on non-recurring expenditures, or add it to reserves, rather than using it to meet budget deficits. Since free cash varies from year-to-year there is no guarantee that it will be there in successive years to pay for recurring expenses.
- Adhere to a pension funding schedule so that accrued obligations can be paid as employees retire without having to pay for pensions by reducing municipal services.
- Avoid increased pension liabilities by adopting local-option increases such as increasing benefits for public safety employees as has been done in Worcester in the past.
- Reduce health insurance costs for the City by increasing employee contributions and adopting Massachusetts General Laws Ch. 32B Section 18 requiring all municipal retirees to join Medicare rather than remain on conventional plans.

It is time for Worcester to undo a serious mistake made twenty-five years ago that has left the community at a competitive disadvantage.

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