

League of Women Voters of Amherst

Understanding Municipal Finance

Part I: Overview

October 18, 2007

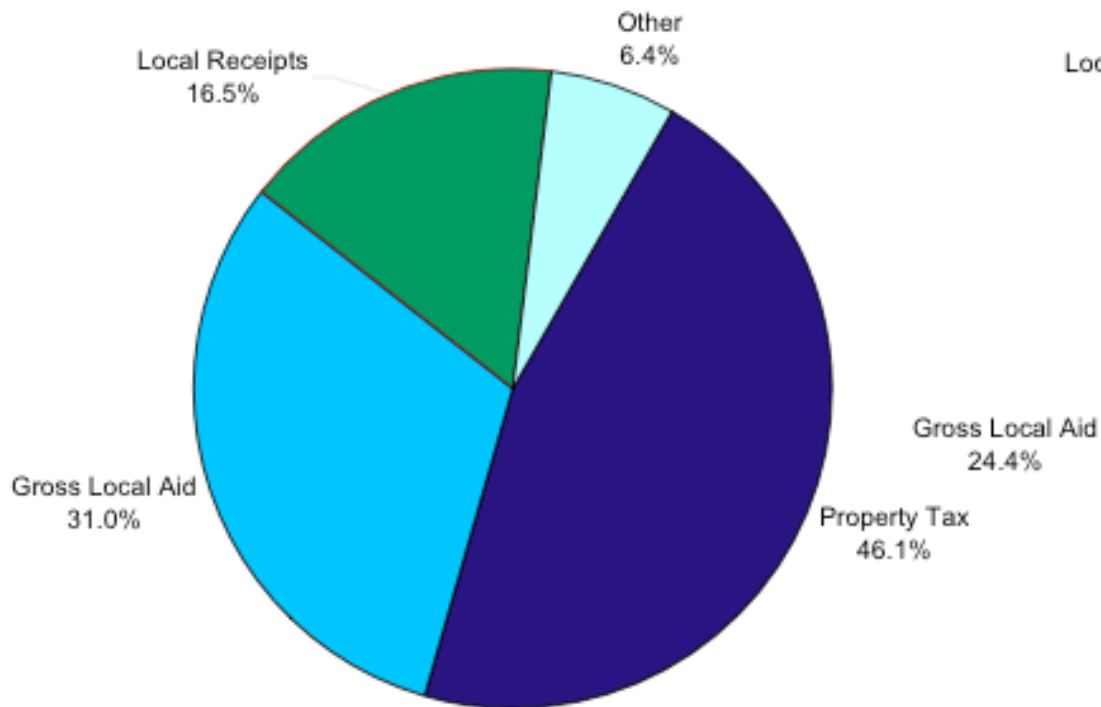
Sources of Municipal Revenue

Cities and towns in Massachusetts obtain their revenue from local property and excise taxes, fees, and local aid from the state (also referred to as state aid). In recent years, state aid has not kept up with inflation and property taxes support a larger share of municipal budgets. Local property taxes are restricted by Proposition 2 1/2 .

Municipal Revenue Sources

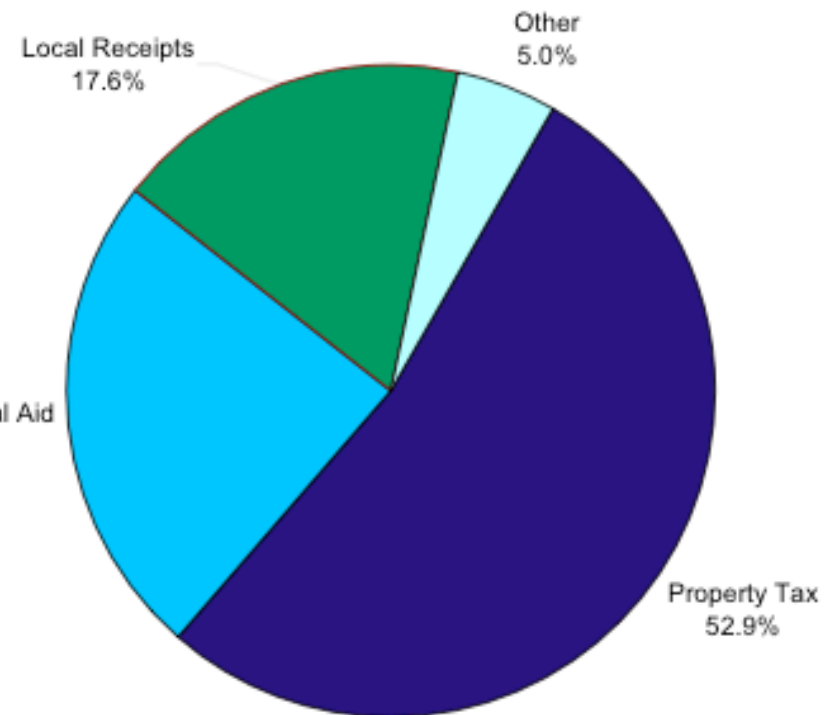
FY 1988

Chart 2.1
Fiscal 1988 Municipal Revenue Sources
Peak Local Aid Year
Constant Dollars, Per Capita



FY 2004

Chart 2.2
Fiscal 2004 Municipal Revenue Sources
Most Recent Year
Constant Dollars, Per Capita



Source: Municipal Finance Task Force (Hamill Report) 2005

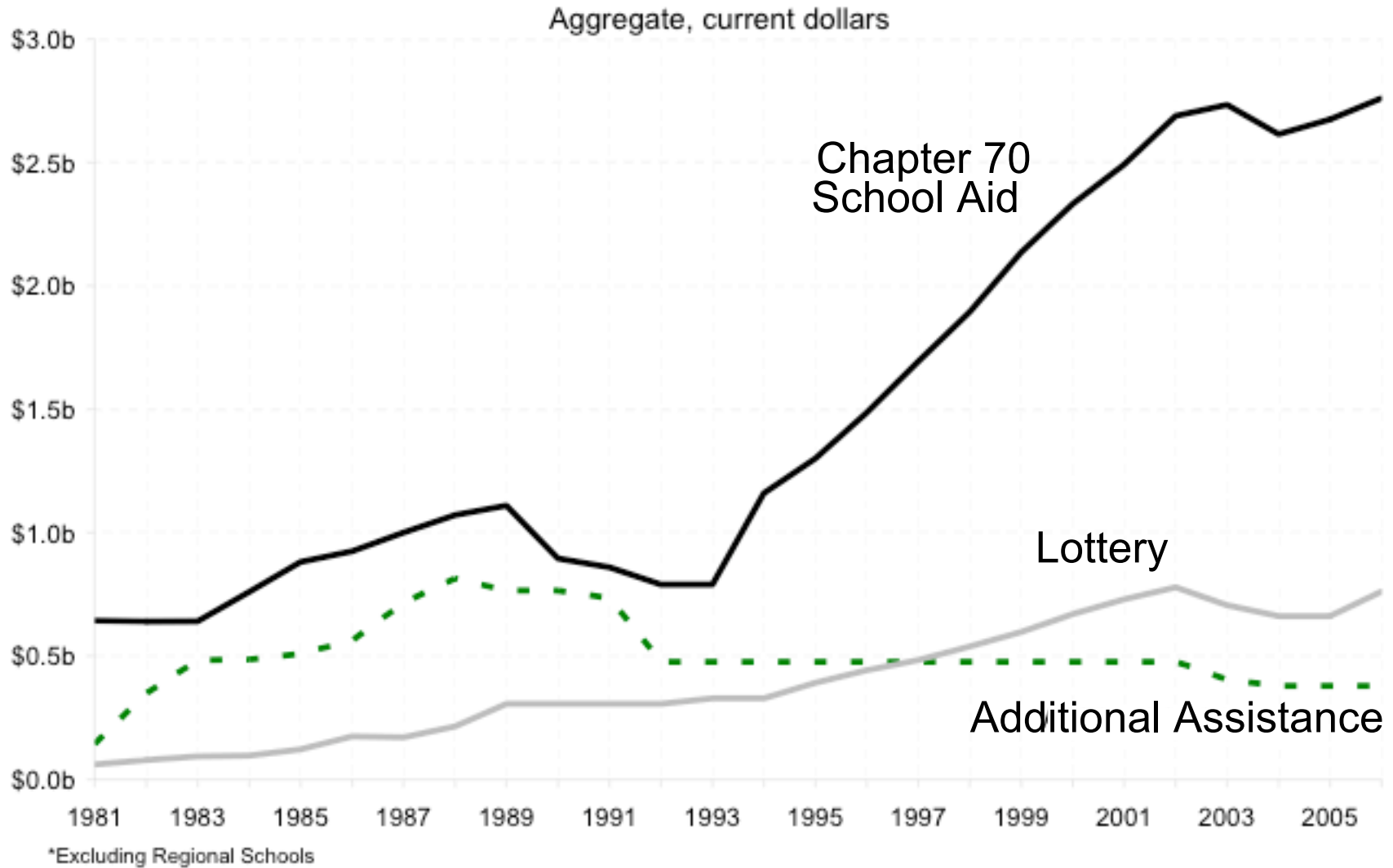
Main Components of Local Aid

Local aid comes to cities and towns on the so-called Cherry Sheets, which show the various payments to municipalities and the assessments that must be paid to the state. Local aid includes Chapter 70 funding for public schools, lottery aid, and additional assistance, both of which provide support for general government services. Additional assistance was initiated to help even out disparities among municipalities, but has been decreasing. Since the Education Reform Act of 1993, Chap. 70 school aid has become the major component of local aid.

Lottery Aid

Voters approved the state lottery in 1971, with net lottery proceeds to be distributed to cities and towns as unrestricted local aid. However, the lottery distribution must be voted by the Legislature each year. During economic downturns, lottery funds have been diverted from municipalities to the state's General Fund. Lottery aid is therefore dependent on lottery revenue and the vote of the State Legislature.

Main Components of Local Aid 1981 - 2005



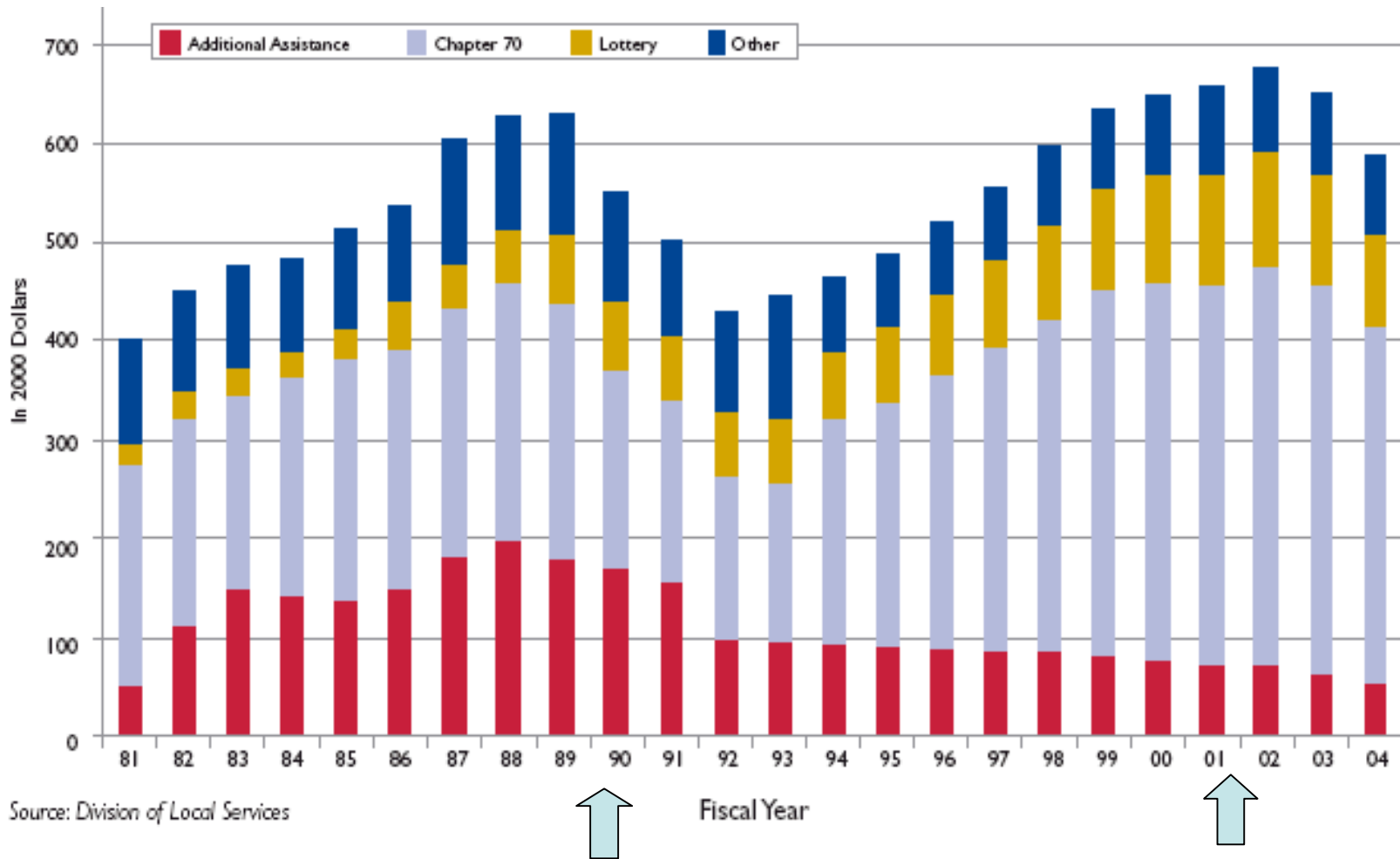
Source: Municipal Finance Task Force (Hamill Report) 2005

Trends in State (Local) Aid

The trends reflect the financial health of the Commonwealth. The recession in 1990 - 1991 led to a drop in state (local) aid, primarily Additional Assistance. The 2001 - 2002 economic downturn led to cutbacks in all categories of state aid the next budget year. That is, state aid gets cut at the very time when municipalities need it most. After cutbacks, it takes years for aid to return to former levels; meanwhile, expenses continue to rise.

Long term fluctuation in state aid

Figure from Bluestone Report



Relationship: State government and municipalities

- Massachusetts municipalities are **limited in ability to raise own revenues**
- Despite home rule, **do not have fiscal autonomy**, unlike many other states
- Thus, municipalities must **rely on local property taxes** as their main revenue source

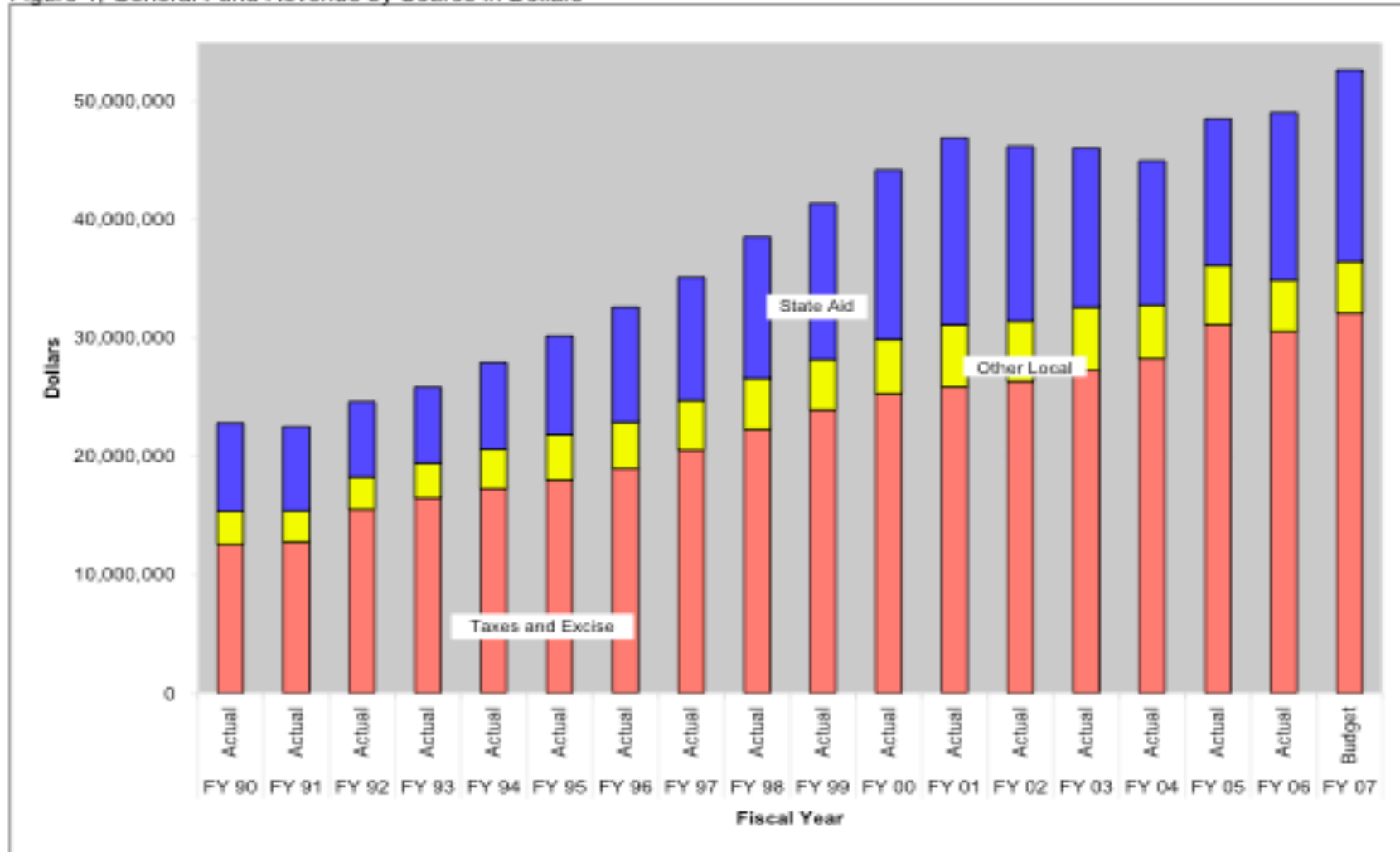
Overview of Amherst's Financial Picture

These state-wide trends are evident in Amherst's budget picture. Property taxes are the main source of revenue (48% in FY2007), with state aid providing about 24%. The decrease in state aid in 2004 was partially offset by use of the Town's reserve funds. These reserves are now spent down and are no longer available.

Over 60% of the budget was spent on education in FY2007, about 35% for Town operations, and 4% for the libraries. (Note: these numbers do not include about \$1.4 million for debt service)

Amherst General Fund Revenue 1990 - 2007

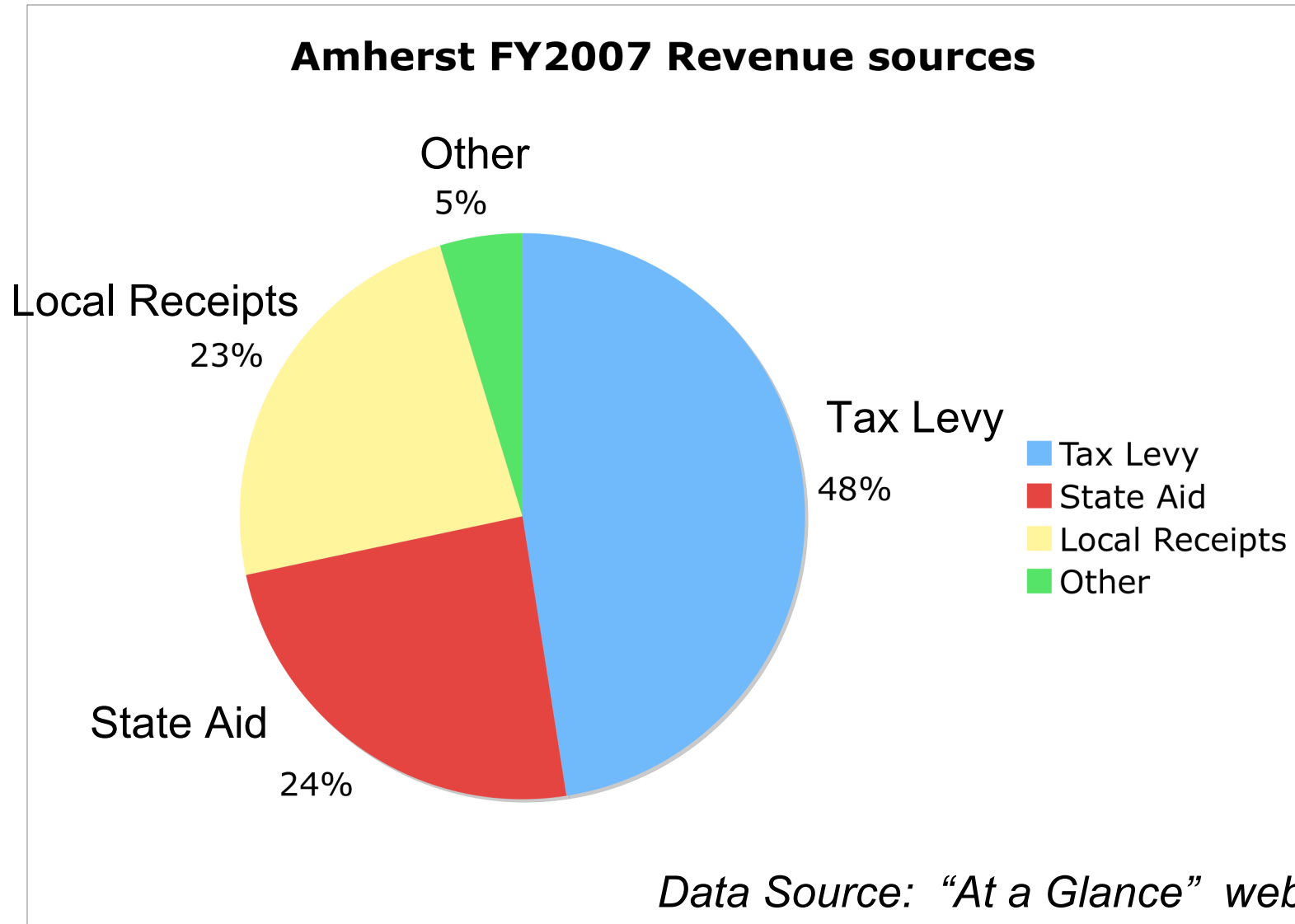
Figure 1, General Fund Revenue by Source in Dollars



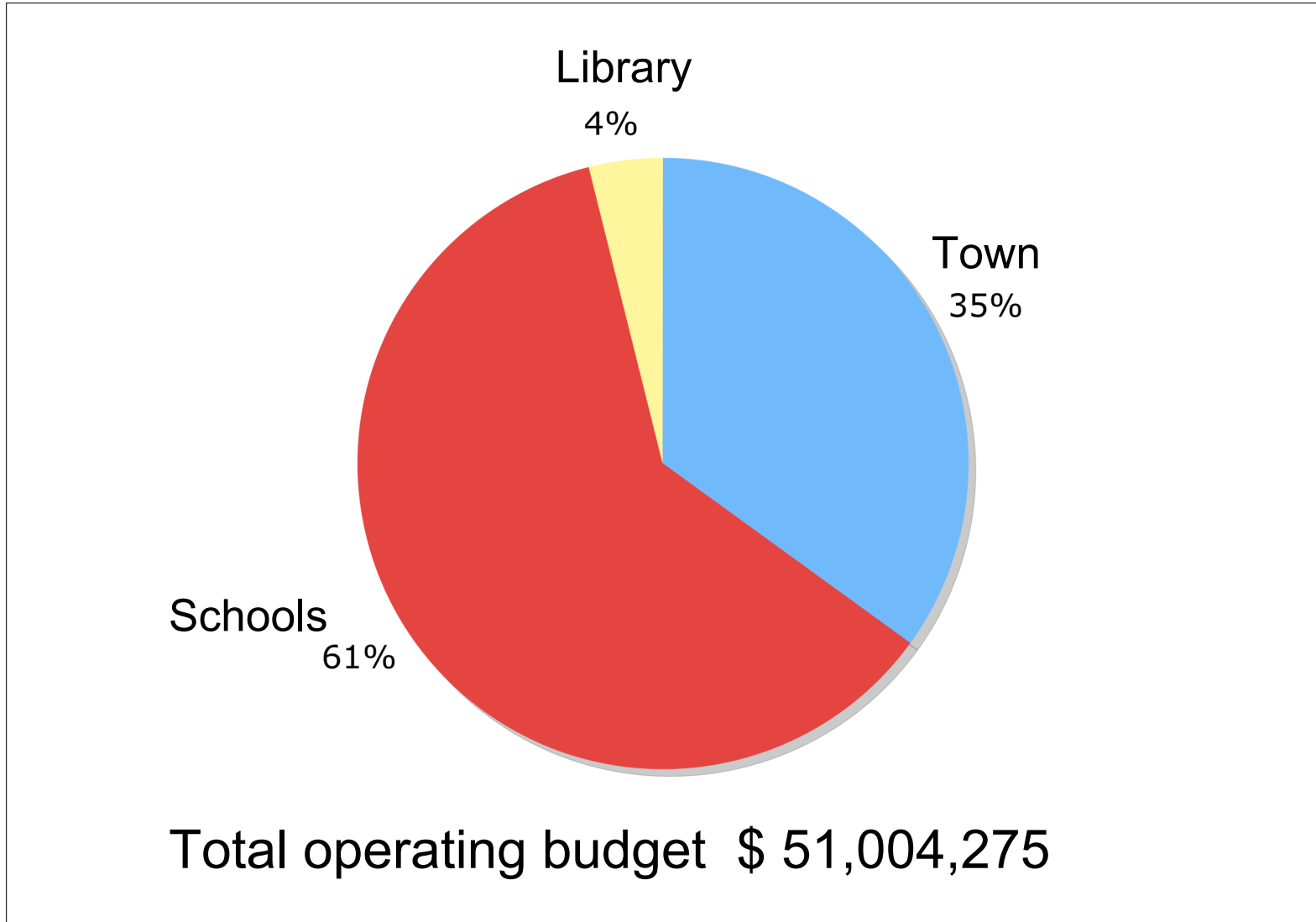
Source: Amherst Finance Committee Report

Exceptional increases in energy and health insurance costs contributed to the structural deficit on the spending side, as did various new or expanded state and federal requirements for which we must pay.

Amherst FY2007 Revenue Sources



Amherst Expenditures FY 2007 Budget



Data Source: Town Finance Director

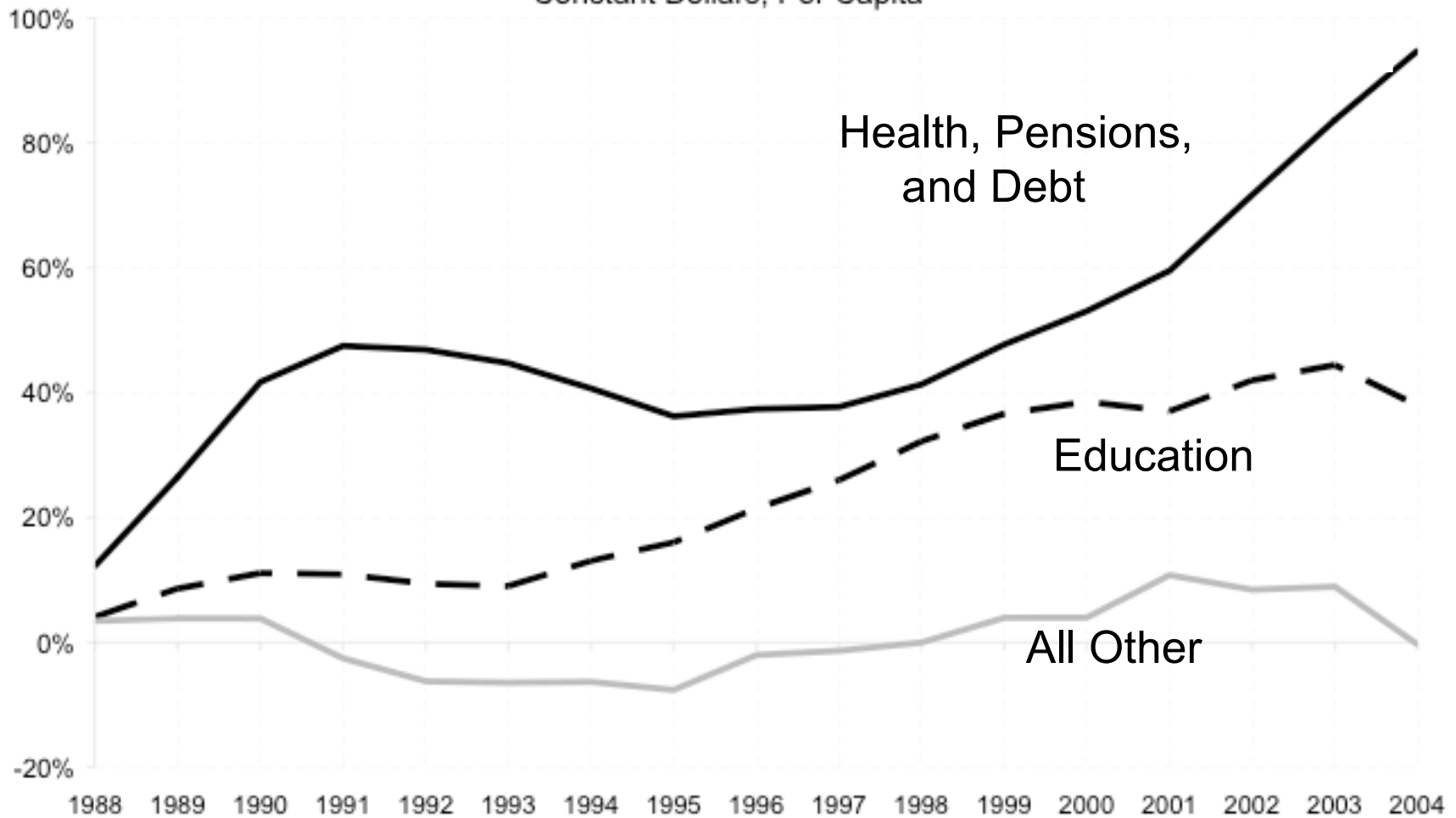
Areas of Expenditure Pressure

Certain costs are rising statewide more rapidly than the overall increase in municipal budgets. These include health insurance, pensions, debt service, and education, particularly special education. Spending on these items that are beyond the control of municipalities makes less money available to support other town services.

Statewide Areas of Expenditure Pressure

FY 1987 - 2004

Cumulative Annual Percentage Change
Fiscal 1987 - 2004
Constant Dollars, Per Capita



Source: Municipal Finance Task Force (Hamill Report) 2005

Limiting Factors Affecting Municipalities

In summary, municipalities are caught between rising costs and limited revenue sources:

- *Proposition 2 1/2*
- *Cap on MA income tax*
- *Cuts in local (state) aid*
- *Rising health insurance and pension costs*
- *Increasing Special Education expenses*
- *Escalating fuel and utility costs*
- *Inflation*

Our presentation describes how these factors affect the town, school, and library budgets