

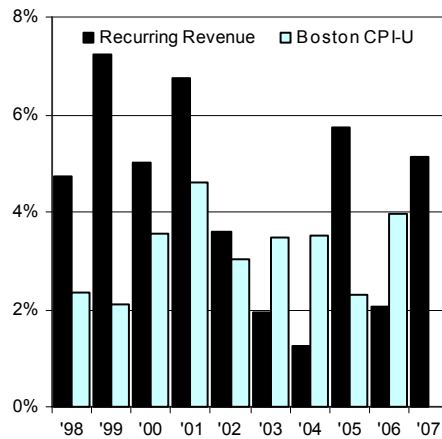
Revenue Estimates and Analysis

OVERVIEW

The FY07 Budget is supported with \$2.129 billion in recurring revenue, an increase of \$95.9 million, or 4.7%, from the FY06 Budget. The budget also includes \$5.3 million in non-recurring revenue and \$8.0 million from budgetary fund balance, yielding total revenue of \$2.142 billion, an increase of \$80.0 million, or 3.9% from FY06.

FY07 will likely represent a third year of real increase to recurring revenue growth after less than or only inflationary growth in FY03 and FY04 (Figure 1). Note that FY05 revenues increased substantially as the economy recovered during that year and that the FY06 Budget is likely conservative as a result. The FY07 Budget incorporates growth expected to be achieved in FY06.

The largest portion of the FY07 increase is attributable to growth in the Property Tax. None of the major revenue categories are projected to be less than budgeted for in FY06.



Annual Change in City Revenues and Boston CPI-U
FY98 - FY07 Recurring Revenue

Figure 1

This chapter begins with a review of national and state economic trends that have and will continue to impact Boston in FY07 and beyond. It is

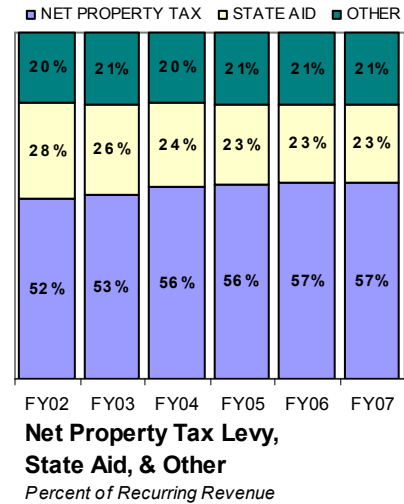


Figure 2

followed by an analysis of recent state budget trends and state aid, the City's second largest revenue source. Finally, a detailed discussion of the property tax levy, the City's largest revenue source, is presented along with other City revenues. Net property tax and state aid together make up 80% of total City revenues with the share of property tax increasing steadily and state aid decreasing steadily. Their stability is of critical importance in determining the City's ability to deliver quality services while maintaining overall fiscal stability and a balanced budget (Figure 2).

THE NATION

The Nation has dealt with considerable adversity over the past year, with the ongoing conflict in the Middle East, escalating energy prices, and hurricanes which have devastated the Gulf Coast. However, according to recent statements by the Board of Governors of the Federal Reserve System, the Nation's economy has weathered these challenges as exhibited by steady growth in Gross Domestic Product, employment, and labor productivity.

Concerns regarding price level pressures and wages have continued to drive interest rate increases in 2006. Additionally, while the housing market, a source of stability over the past several years, continued to grow in 2005, there have been recent signs of softening which are likely to continue in the months ahead.

While the economic outlook remains positive, the combination of on-going volatility in the energy markets, fears of escalating inflation, a softening housing market, and the continuance of large federal budget deficits will continue to threaten higher levels of economic growth.

Currently, the Federal Reserve continues to tighten monetary policy through the Federal Funds rate, from the June 2003, 41 year low of 1.00% to the current rate of 5.25%. Starting in June 2004, the Federal Reserve has increased the federal funds rate by 25 basis points at each of 16 intervals (Figure 3). Even with these increases, "real" or inflation-adjusted short-term interest rates are still historically accommodative. The Federal Reserve will continue to use monetary policy to maintain its dual charges of price stability and economic growth as the economy expands.

Interest rates can speed or slow the economy. An example of the stimulatory effect of monetary policy can be seen in the use of recent historically low interest rates (and its Aa1 bond rating) by the City to refinance nearly half of its outstanding debt. This action resulted in considerable savings that could be used elsewhere in the budget. *(Please refer to the Financial Management Chapter for more detail.)*

Mortgage rates remain historically low despite an increasing Federal Funds rate. The monthly average conventional 30-year fixed-rate mortgage has risen from 5.40% in March 2005 to 6.65% in June 2006. Mortgage rates are expected to rise throughout the remainder of 2006 and into 2007 as the full effect of interest rate changes come to bear.

The housing market is likely to slow as mortgage rates rise. As a result, consumer spending on big-ticket durable goods should also experience a slowdown. However, a sharp decline in housing values, as was experienced during the early 1990s is not likely as the housing market is expected to

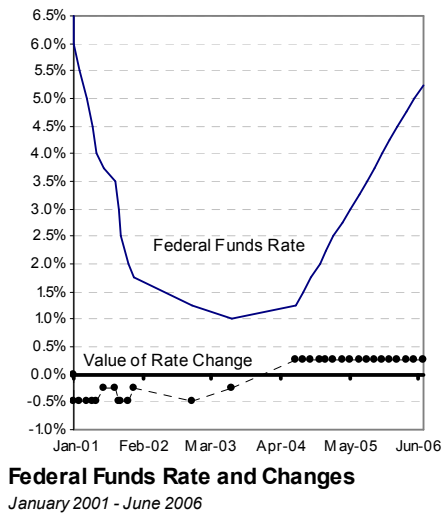


Figure 3

be supported by employment and income gains and therefore should remain relatively healthy, but with lower annual rates of appreciation for the foreseeable future.

Overall economic growth as measured through Real Gross Domestic Product (GDP) grew at 2.5% in the second quarter of 2006, down from the 3.3% GDP growth a year earlier and less than half that of the previous quarter's 5.6%. Real GDP growth is expected to steady over the course of 2006, with the Federal Reserve estimating growth of 3.5% for 2006, largely unchanged from actual 2005 GDP growth.

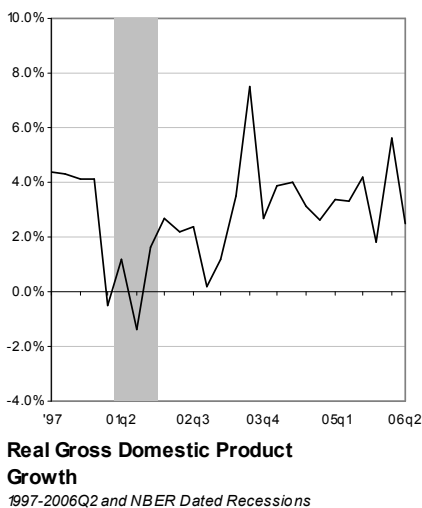


Figure 4

The seasonally adjusted unemployment rate in the U.S. was 4.6% in June 2006, down from 5.0% in June of 2005 (Figure 5). Given the current economic environment the unemployment rate is expected to remain in the range of 4.5% to 5.0% through the end of 2006.

The U.S. consumer price index for all urban consumers (CPI-U) rose 4.3% in the year ending June 2006, up from 2.5% for the year ending June 2005, while the “core” rate of inflation, all items less food and fuel, increased by 2.7% between June 2005 and 2006. Fuel prices, the main driver of overall inflation, saw an increase of 11.2% over the same period.

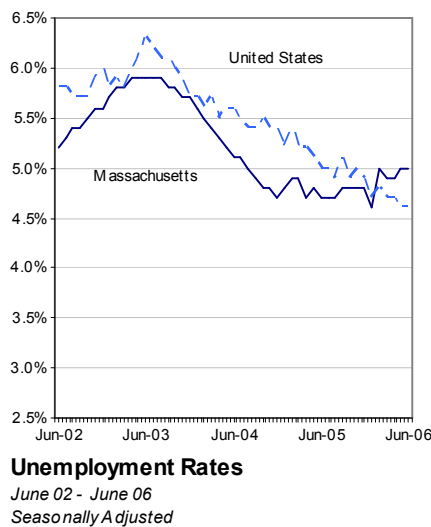


Figure 5

Even with the improving health of the national economy, federal budget deficits are expected to grow due to tax cuts, entitlement cost pressures and military action in Iraq. Given this and ambiguous projections of when balanced budgets will return, it is not expected that the states will see substantial increases in federal funds during the coming year.

THE COMMONWEALTH

The rate of growth in the Massachusetts economy boomed in 2000, declined slightly in 2002, and has recently begun to recover, however slower than in the nation overall.

According to the Bureau of Economic Analysis (BEA), Massachusetts’ real Gross State Product (GSP) increased in 2000 by 7.7% from 1999. By 2001, annual Massachusetts real GSP growth had

slowed to 0.6% and by 2002, had declined by -0.6%. In 2003, real GSP growth estimates ranked Massachusetts at a dismal 49th out of the 50 states, with only Illinois and the District of Columbia ranking lower. But by 2005 the state’s economy had improved, growing 9.1% in the three years since 2002, but Massachusetts still only ranks 30th among all 50 states in growth.

The decline in economic growth and state tax revenues during this recent recession was substantial. Massachusetts lost the highest percentage of jobs in the nation, at one point losing more than 200,000 jobs or 6.0%.

Simultaneously the bursting of the internet-stock market bubble greatly affected Massachusetts’ income tax collections. For example, collections from wage and salary withholding taxes fell \$600 million in FY02, while overall income tax from all sources fell nearly \$2 billion. This demonstrates that not only did taxable incomes fall as a result of job losses, but also due to massive losses in investment income as well. It should be noted that several income related state tax cuts were still phasing in during this period, further exacerbating the decline in revenue. Further detail on state tax cuts is provided in this chapter.

Employment and tax revenue in Massachusetts have been slowly increasing. Massachusetts added 25,700 new jobs between June 2005 and 2006, with 8,600 new jobs in April alone, the largest single monthly job gain in a year. While the number of jobs has grown, the state’s unemployment rate has remained largely unchanged, increasing slightly over the past year from 4.7% to 5.0%, higher than the national rate of 4.6% in June 2006. Personal income taxes are expected to increase 6.1% in 2006, after 7.1% growth in 2005.

The employment outlook is mixed for the coming year, the Massachusetts Taxpayers Foundation estimates job growth of just 0.7 percent over the next two years, with the State’s economy adding only 27,000 jobs in 2007.

Massachusetts’ seasonally adjusted total personal income grew by 5.2% between the quarters ending March 2005 and March 2006. Earnings growth by industry over this period was strongest in state and local government, information as well as administrative and waste services. Earnings in non-durable goods manufacturing, military, and

federal civilian employment exhibited the weakest growth during the same period.

(See *Boston's People & Economy* section of Volume I for detail on Boston's economy.).

THE COMMONWEALTH BUDGET

The Governor's FY07 budget, totaling \$26.9 billion, placed an increased focus on local aid. By removing the cap placed on lottery proceeds and proposing changes to the distribution of Chapter 70 education aid, the Governor's budget took some positive steps towards helping municipalities recover from the cuts of the recent past.

The most recent recession and the corresponding drop in state tax revenues left the state in need of making program reductions, drawing on reserves, increasing taxes and reducing local aid in order to balance the state budget. Most municipalities, including Boston, have yet to recover from these sudden and drastic aid reductions.

Following these fiscal hardships the Commonwealth has tended to build its budgets cautiously the last several years by being relatively conservative in its revenue estimates. This caution had been rewarded by the accumulation of reserves that have allowed the state more options in dealing with recent revenue shortfalls than in the past. The state had nearly exhausted those reserves by the close of FY03 and has now largely rebuilt them. The administration projects that the State's stabilization fund will grow to \$2.6 billion by the end of FY06.

The following discussion details some fiscal decisions made by the Commonwealth over the past several years.

With the Commonwealth running large budget surpluses in the 1990's, tax cuts occurred in rapid succession. In July 1998, the Legislature and the Governor worked out a tax cut that included a doubling of the personal exemption and a reduction in the unearned income tax rate from 12% to 5.95%. In the FY00 Budget, the Governor signed into law a reduction of the earned income tax rate from 5.95% to 5.75% over three tax years. The Governor's FY01 Budget recommended a reduction in the tax rate on earned income and the interest and dividend components of unearned income to 5.0% over three tax years, which was later passed by referendum in November of 2000.

The FY02 Budget included the above rate cut and some smaller targeted tax cuts taking effect in tax year 2001. The tax cuts included a refundable local property tax credit for low income senior citizens, an increase in the residential rental deduction, a new deduction for charitable donations, and a credit for developers of low income housing. The Governor's FY03 Budget included the continuation of the voter-approved income tax rate reduction to 5.0% valued at \$452 million in FY03.

In FY03, the legislature, instead of continuing tax cuts, voted to accept a tax increase package. Valued at \$1.14 billion by the Massachusetts Taxpayers Foundation, the package included a freeze of the income tax rate at 5.3% (\$215 million), reducing the personal exemption by 25% (\$240 million), repeal of the charitable donations deduction (\$190 million), an increase in capital gains taxes (\$275 million), and a \$0.75 increase in the cigarette tax (\$220 million) along with other increases to fees for various licenses. The Governor vetoed these tax increases but the legislature overrode those vetoes.

Even with the enacted tax increases, the FY03 budget was reduced several times during the course of the year as revenues failed to meet estimates. Most early reductions fell on executive branch agencies or grant accounts where the governor has the power to cut unilaterally. In January 2003, the new governor sought from the legislature temporary power to reduce local aid accounts normally under legislative control. The legislature granted that temporary power and local aid for FY03 was reduced statewide. The FY04 Budget then further reduced major local aid accounts. The FY05 and FY06 budgets, while not further reducing local aid, did not increase revenues enough to mitigate any of the serious operating challenges facing municipalities.

Beyond the recent reductions in and level-funding of local aid accounts, the City sees the ongoing need to modernize the property tax and seek a more diversified mix of revenue sources. To that end, the City has proposed several state legislative changes to shore up the property tax and to allow municipalities to generate more "own-source" revenue.

Specifically, the Mayor has filed legislation to close property tax loopholes that allow private businesses on tax exempt land to avoid taxes and that allow exemptions for certain equipment or corporate structures in the telecommunications industry.

In addition, the Mayor has filed legislation to enact a 1% local option tax on prepared food and beverages sold in municipalities in addition to the 5% state tax already in place. If the Legislature were to enact this legislation and the City Council adopted it, the City could recover an estimated \$17 million annually. A meals tax is a good fit for the strong tourist and travel economy in Boston. It would provide revenue growth at a nominal rate without a heavy burden on residents, tourists or travelers with the total rate of taxation remaining one of the lowest of any major city.

At the same time, the Mayor has filed legislation to enact a local option tax on parking in commercial parking lots. The City, like other regional employment centers, expends considerable resources on traffic control and street maintenance in support of this employment. But unlike other cities, Boston does not have any taxing authority to recover those costs. This local option tax could generate approximately \$19 million annually.

STATE LOCAL AID

The FY07 local aid estimate assumes growth in Education and Lottery aid. The City received local aid (after adjusting for an accounting change in the treatment of Charter School Tuition) from the Commonwealth totaling \$476.6 million in FY03, \$459.8 million in FY04 and \$461.1 million in FY05.

The City expects to receive \$469.6 million in local aid in FY06 and is budgeting \$482.2 million in FY07.

Local aid refers primarily to distributions from the Commonwealth to municipal general revenue for Chapter 70 education aid, additional assistance and lottery aid. The amount of these funds to be distributed is listed on each community's cherry sheet (a listing of a city or town's local aid that was formerly printed on cherry-colored paper) along with other relatively smaller Commonwealth programs such as library aid, school construction, transportation and other reimbursements, and highway funds.

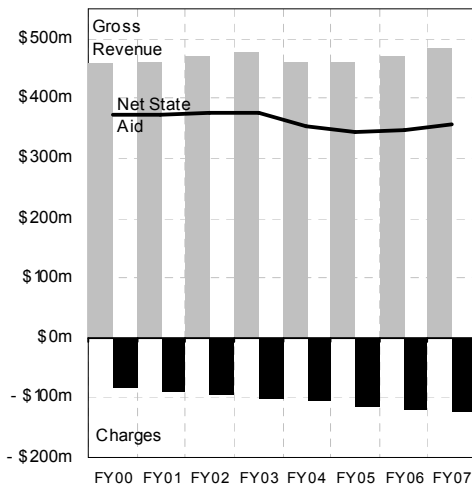
In the decade prior to FY03, Commonwealth officials, driven by practical considerations and availability of resources, reinstated increases in local aid in the form of aid earmarked for education. This period of increases followed three years of significant local aid reductions, which played a key role in the Commonwealth's return to a balanced budget after the last economic recession during the early 1990s. The Commonwealth's annual expenditure for direct local aid statewide has increased from \$2.32 billion in FY92 to \$5.02 billion in FY03, an increase of 116%.

At the same time, Boston's share of local aid (net of reimbursement for teacher's pensions) increased 36.9%. The remainder of this section looks at Boston's experience with local aid in more detail.

Net state aid, gross state aid revenue minus assessments or "charges", was largely flat from FY00 through FY03 when aid was reduced. After those reductions, net state aid has again remained flat from FY04 through FY07. The rapid annual increases in the Charter School Tuition assessment combined with very low growth in education and lottery aid serve to keep the City's net state aid at a virtual standstill. Without even inflationary increases in net state aid, any small increase in annual aid can translate into an inflation-adjusted reduction (Figure 6). Even with marginal increases in net state aid for FY07, Boston still remains \$72.2 million below its FY02 level of net state aid of \$429.2 million.

Net state aid amounted to \$353.3 million in FY04 and \$349.4 million in FY05. FY06 budgeted net state aid totals \$349.0 million and the FY07 Budget assumes only minor growth to \$357.1 million.

Since FY82, there have been three distinct phases in state local aid funding policy. From FY82 through FY89, local aid policy was essentially a revenue sharing response to Proposition 2 ½, the statewide cap on local property tax rates and levies. A reasonable annual increase in local aid became an essential component in the financial planning for municipalities. The distribution between municipalities was based upon a relative measure of balance between local needs and local resources, and the revenue was distributed both in the Chapter 70 and Additional Assistance line items.



Net State Aid (net of Teacher's Pension)
 FY00 - FY07 Estimated

Figure 6

During the FY90, FY91 and FY92 budgets the Governor and the Legislature sharply reduced state revenue sharing with cities, towns, and regional school districts in order to help balance the state budget. Between FY89 and FY92, statewide cherry sheet aid declined \$639 million or 21.5% while all other state spending increased by \$1.5 billion or 15%.

Education Aid

Beginning in 1993 with the passage of the FY94 state budget, the Commonwealth embarked upon a multi-year commitment to increase and equalize funding for local education in its local aid distributions. During this period, Chapter 70 increased and additional assistance remained frozen. In general, state local aid during the FY94-FY03 period has been less favorable for Boston than the revenue sharing arrangement during the FY83-FY89 period. To illustrate, the City's total state aid between FY92 and FY03 grew \$121 million or 36.9%, while its total state aid between FY82 and FY89 increased by \$215 million or 111%.

The City received Chapter 70 education aid totaling \$205.6 million in FY02 and FY03. The City received \$200.5 million in FY04 and FY05 and expects to receive \$203.6 million in FY06 and \$207.0 in FY07.

FY00 was the last year of the statutorily established funding schedule for education reform. There has yet to be established a post-

FY00 funding schedule. A vital component in the City's delivery of quality public education in the near-term is strong financial support from the Commonwealth.

A key component of the Commonwealth's education reform effort is charter schools. The current educational aid is delivered in tandem with state-mandated costs for charter schools. Charter schools, which are granted charters by the State Board of Education, are publicly funded schools administered independently from local school committees and teacher union rules and regulations. There are two kinds of charter schools, the Commonwealth charter school and the Horace Mann charter school. The former is a school outside the local public school system and the latter is part or all of a school in the public school system. Unlike a Commonwealth charter school, Horace Mann charter school budgets remain part of the public school budget. In addition to the Board of Education, the local school committee and local bargaining agent must approve Horace Mann charter schools.

There are currently both Commonwealth charter schools and Horace Mann charter schools available to Boston resident students. There were approximately 4,253 Boston resident students attending Commonwealth charter schools in FY06. The City expects that number to increase to 4,697 in FY07.

Before FY99, all charter school tuition was drawn directly from the City's Chapter 70 aid. This draw on the City's education aid totaled \$10.9 million in FY98. Under amendments to the charter school law, the Commonwealth, subject to appropriation, is required to pay to the City as reimbursement for Chapter 70 aid reductions 100% of tuition for new charter school students the first year, followed by 60% of tuition and tuition increases the second year, 40% of tuition and tuition increases the third year and 0% thereafter.

In FY03, the Commonwealth failed to appropriate funding for the charter school reimbursement, therefore the City paid the full tuition cost of \$32.1 million in that year. The net cost to the City of charter schools in FY04 was \$33.6 million. In FY06, the City budgeted a \$13.9 million reimbursement on a \$50.6 million tuition assessment for a net impact of \$36.8 million. In

FY07 the city has budgeted a \$13.3 million reimbursement against a \$53.7 million tuition cost, yielding a net impact of \$40.4 million.

Lottery Aid

Lottery aid for the City, as for most municipalities, had grown steadily over the last few years as a result of a state decision to phase-out an earlier imposed lottery cap and return to the practice of returning all lottery profits to cities and towns. The City's lottery aid was \$71.0 million in FY01, and \$63.5 million in FY02. Lottery aid was then level funded in the state's FY03 budget and then later reduced to \$57.6 million after the Governor effectively capped Lottery aid to cities and towns, diverting the excess funds to the state. In FY04, Lottery aid was further reduced to \$54.0 million and remained at that level through FY05. The City will receive \$60.54 million in FY06 and \$70.6 million in FY07 once the lottery cap is lifted.

Under normal circumstances, the lottery formula is not favorable to the City because it distributes lottery aid increases based inversely upon each municipality's relative per capita property wealth. The City receives a smaller percentage share of lottery aid than its share of the state population, and dramatically less than the share of lottery proceeds derived from sales in Boston.

Nevertheless, lottery aid has been an important source of revenue growth, aiding the City's efforts to sustain adequate municipal services. Beginning in FY01, growth in the City's lottery distribution reflected only profit growth in the lottery and not the removal of the state cap on lottery aid that had been in effect the five years prior to FY01. The Governors FY07 budget proposed an end to the diversion of lottery funds.

Additional Assistance

Additional Assistance, as mentioned above, had been frozen since FY94, with most local aid increases coming through Chapter 70 education aid instead. Its purpose and usefulness came into question during the FY03 state budget process when the Governor vetoed \$31 million from the statewide appropriation and the legislature failed to override that veto. Subsequently, the new Governor, using his temporary local aid reduction powers, reduced additional assistance yet again in January 2002 by \$73 million. As Boston receives

over 40% of the statewide distribution of additional assistance, these reductions fell disproportionately on the City. The City received \$206.6 million in additional assistance in FY02 and adjusted additional assistance of \$175.1 million in FY03. The City received \$164.2 million in FY04 and FY05 and expects the same in FY06 and FY07. Additional assistance has been important to Boston in supporting schools, public safety, and other basic services. Its continued reduction would seriously risk the City's ability to provide those services to residents and visitors alike.

PROPERTY TAX LEVY

The property tax levy has been the City's largest and most dependable source of revenue growth over the past 22 years. In FY06, the net property tax levy is \$1.17 billion, providing 57.7% of recurring revenue, with an increase to \$1.22 billion expected in FY07. According to current estimates, the net property tax levy will account for 57.3% of recurring revenue in FY07.

The increases in the gross property tax levy have been steady and consistent from FY85 to FY06, ranging from \$28 million to \$63 million. However, because of the increasing property tax levy base, the \$29.9 million increase in FY85 represented an 8.9% increase, while the budgeted \$57.3 million rise in FY06 represents 5.0% growth. It is important for the financial health of the City that the property tax levy continues to grow, but its future growth, as explained in more detail below,

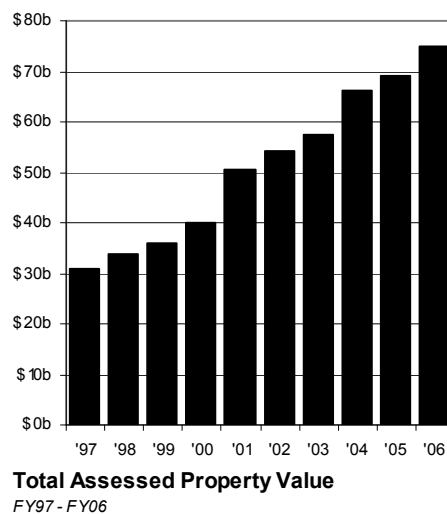


Figure 8

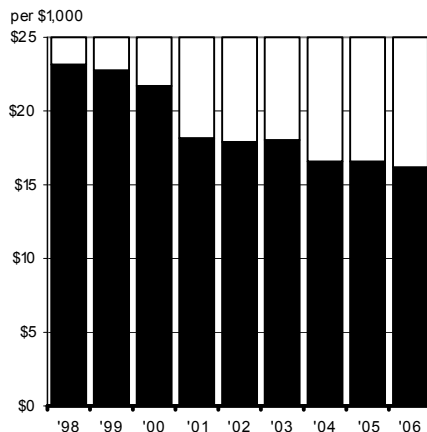
is not guaranteed.

The difference between the Gross and Net property tax levies is due to a required “overlay reserve”. The overlay reserve is a portion of the gross levy set aside to pay for abatements of tax bills that are contested. Until FY04, the City was required by Chapter 717 of the Acts of 1957 to reserve between 5% and 6% of the levy for this purpose. In FY04, the City petitioned the state legislature to repeal the act and allow the state Department of Revenue to approve the City’s reserve annually as it does with every other city or town in the Commonwealth. The act was repealed and the City reserved 4% of the levy in FY04 and FY05. This 1% lower reserve amount added approximately \$10 million in recurring revenue to the operating budget starting in FY04. The level of needed reserve is determined by the City Assessor each year according to the projected need to satisfy abatements. In FY07, the reserve has been set at 3.5%.

Proposition 2 1/2 has been the overwhelming factor affecting the City’s property tax levy since being passed in 1980. Proposition 2 1/2 limits the property tax levy in a city or town to no more than 2.5% of the total fair cash value of all taxable real and personal property. It also limits the total property tax levy to no more than a 2.5% increase over the prior year’s total levy with certain provisions for new growth and construction. Finally, Proposition 2 ½ provides for local overrides of the levy limit and a local option to exclude certain debt from the limit. The City of Boston, however, has not voted to either override the levy limitations or exclude any debt from the limit.

Proposition 2 ½, as amended in 1991, allows growth in the levy beyond the 2.5% limit for any new properties and any increases in property valuations that are not related to municipal-wide revaluations. This limitation is more flexible than the original limitations on allowable new growth and has helped to strengthen revenue growth in a budget that does not have a diversified revenue base.

In each year since FY85, the City has increased its levy by the allowable 2.5%. These increases have grown as the levy has grown, beginning in FY85 at \$8.4 million and reaching \$27.3 million in FY05.



Overall Property Tax Rate & Space Below Levy Ceiling
FY98 -FY06

Figure 7

During these same years, the levy has also been positively impacted by taxable new value, especially from new construction that has added to the tax base. The amount levied from taxable new value in FY06 was \$29.8 million and is estimated at \$23.0 million in FY07. The combined effect of the allowable 2.5% increase and the taxable new value is an average annual levy increase from FY98 through FY06 of \$50.8 million or 5.4%, and a projected increase in FY07 of \$53.2 million or 4.4%.

As real estate values decreased in the early 1990s, the City continued each year to maximize the allowable levy increase under Proposition 2 ½. Between FY90 and FY94, the levy increased each year by an average of 6.4%. The dramatic decrease in values brought the effective tax rate (levy / taxable value) from its healthy low point of 1.4% in FY89 to 2.47% in FY94, dangerously close to the Proposition 2 ½ tax rate ceiling of 2.5%. Reaching the 2.5% cap would have resulted in a very limited increase in allowable annual levy growth.

However, due to several years of strong taxable value increases, the City now has some space between its FY06 net effective tax rate of 1.62% and the tax rate ceiling (Figure 7).

Should the real estate market depreciate, the City’s lack of proximity to the 2.5% property tax rate threshold should insulate revenues from an immediate shock but could, if values are depressed long enough, impair the growth of the property tax. This would have serious implications for the City’s ability to maintain services.

Excises

The Commonwealth imposes an excise on the registration of motor vehicles, the proceeds of which are received by the municipality where the vehicle is principally kept. The excise is a uniform rate of \$25 per \$1,000 of vehicle valuation. Valuations are determined by a statutory depreciation schedule based on the manufacturer’s list price and the year of manufacture.

Having reached the peak of automobile sales in 2000, the City expected the market to soften or plateau, eroding revenues through the depreciation schedule mentioned above. Motor vehicle excise revenue totaled \$33.1 million in FY04 and \$44.7 million in FY05. The City expects motor vehicle excise revenue to exceed the midyear projection of \$40.0 million in FY06 and then decrease to \$40.0 million in FY07.

The local room occupancy excise amounts to 4.0% of the total amount of rent for each hotel or motel room occupied. Another 5.7% excise is directed to the state general fund, and another 2.75% to the state’s convention center fund. The City divides its 4.0% excise into “Base,” from the pre-July 1, 1997

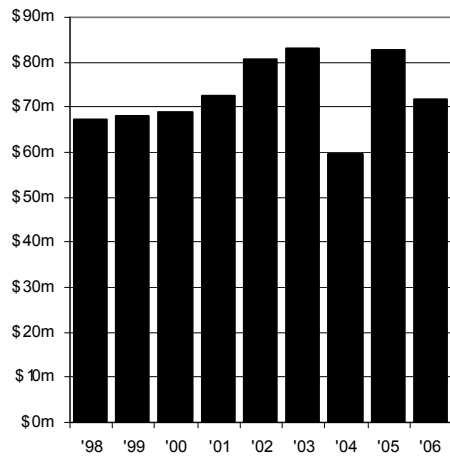


Figure 9

hotels, targeted to the general fund, and “New,” from the post-July 1, 1997 hotels, targeted to the City’s convention center fund.

Boston’s occupancy and average daily room rates are usually among the highest in the nation, but this market was strongly affected by the events of September 11, 2001 and the national recession. Recently, receipts have stabilized and are growing as occupancy and room rates have increased.

Base room occupancy excise revenue (a portion of this revenue is sometimes retained in the convention center fund) totaled \$19.8 million in FY04 (\$17.0 million went to the general fund) and \$21.9 million in FY05 (\$18.0 million went to the general fund). The City’s base room occupancy excise tax receipts are expected to exceed the midyear budget estimate of \$19.0 million in FY06, and are projected to increase to \$23.0 million in FY07.

A significant number of new hotel rooms are planned, already in construction, or were recently constructed. This will benefit the City’s convention center fund and pay for a significant portion of the City’s debt for the new Boston Convention and Exhibition Center. The debt is scheduled to be fully paid in FY2027. Therefore, for the foreseeable future, growth in room occupancy excise in the general fund depends upon increases in room rates and room occupancy in the 1997 base of hotel rooms.

The excise on the sale of jet fuel is 5% of the sales price, but not less than five cents per gallon. Jet fuel excise tax collections were severely impacted by the events of September 11 and the national recession, as travel and cargo shipping slowed sharply. The City expected jet fuel excise collections to reach bottom in FY04 and recover as the economy strengthened and travel returned in FY05. Jet-fuel excise revenue in FY04 totaled \$8.5 million (which was missing the first FY04 payment of \$3.2 million) and \$18.4 million in FY05 (which had an extra payment from FY04). The City expects this revenue source to exceed the midyear projection of \$14.0 million in FY06 due to sharp price increases related to hurricane Katrina in the fall of 2005 and projects an increase to \$15.0 million in FY07 (Figure 9).

Fines

Over the last three years, the City has issued an average of approximately 1.63 million parking tickets per year and has maintained a high rate of collection on its tickets for several years, collecting approximately 82.0% of tickets in the first six-months after issuance and over 87.7% within a year. The major factors contributing to the City’s successful collection rate include non-renewal of violator’s registrations and licenses by the Registry of Motor Vehicles until penalties are paid, booting and towing of vehicles, increased

ability to recover fine payments from rental agencies, and systematic collection of fines for company cars and leased vehicles.

The City collected parking fine revenue of \$63.1 million in FY04 and \$62.2 million in FY05. Parking fine revenue is expected to exceed the mid-year budget estimate of \$61.3 million in FY06. The FY07 projection of \$64.2 million is based upon full staffing of Parking Enforcement Officer positions and an increase in the fine related to street cleaning.

Interest on Investments

In general, the City's level of investment income is a function of the level of prevailing short term interest rates and daily cash balances. Investment income peaked at \$26.1 million in FY01 driven by rising cash balances and high interest rates. Interest rates have now risen from their recent 41-year lows and as cash balances have improved, earnings have increased. Investment income totaled \$7.8 million in FY04, and \$17.8 million in FY05. As the Federal Reserve has been increasing interest rates steadily since the end of 2004 while balancing economic growth and inflation, the City expects better cash balances and projects interest income will increase to \$22.8 million in FY06 and \$24.0 million in FY07 as a result.

Payments In Lieu of Taxes

Payments in lieu of taxes (PILOTs) are payments made by tax-exempt institutions located in the City, including hospitals, universities and cultural institutions. These are voluntary contributions for municipal services such as police and fire protection and snow removal.

Growth in PILOTs comes from new PILOT agreements, contract escalations that adjust the payments for inflation, or re-negotiation of a current contract. The Massachusetts Port Authority (MassPort) recently renegotiated its agreement with the City and now provides more than half of the PILOT revenue the City receives annually.

Payments in lieu of taxes totaled \$22.3 million in FY04 and \$23.4 million in FY05. The City expects this revenue source to meet the midyear budget estimate of \$26.8 million for FY06 (due to payment of a balance owed by MassPort) and has projected

\$27.3 million for FY07 exclusive of any new agreements expected to result from negotiations.

Urban Redevelopment Chapter 121A

Chapter 121A legislation allows local governments to suspend the imposition of property taxes at their normal levels in order to encourage redevelopment. In recent years, the City used this mechanism to encourage development of the Seaport Hotel and the World Trade Center office buildings. Chapter 121A revenues are based on two separate sections of the law as described below.

The Urban Redevelopment Corporation excise is a municipal excise in-lieu-of-income tax for which the Commonwealth acts as the collector and distributor. In most cases, the formula for the 121A, Section 10 excise in-lieu-of-tax is \$10 per \$1,000 of the current fair cash value plus 5% of current gross income. In FY04 and FY05, the City received Chapter 121A, Section 10 distributions of \$34.7 million and \$36.1 million, respectively. In FY06 and FY07, Chapter 121A Section 10 revenues are budgeted at \$33.5 million and \$34.3 million, respectively.

In addition to the Section 10 payments collected by the Commonwealth described above, most 121A corporations have individual Section 6A agreements with the City that result in additional payments made directly to the City. These Section 6A agreements are complex, with actual amounts owed dependent on a formula that varies widely among the 121As. The City collected Section 6A payments of \$18.7 million in FY04 and \$17.7 million in FY05. The City expects FY06 Section 6A collections to exceed the midyear budget estimate of \$18.5 million and has a budget of \$19.0 million for FY07.

Miscellaneous Department Revenue

This category contains several large accounts and many more small accounts. The largest revenue source in this revenue category is municipal medicaid reimbursements for school health services. This federal reimbursement, administered by the state, began in FY94. The City received \$11.6 million in FY04 and \$14.2 million in FY05. Municipal medicaid reimbursement is expected to reach the midyear budget estimate of \$11.5 million in FY06, and is budgeted at \$12.0 million in FY07. One other account in this revenue

category is projected to exceed \$5.0 million in FY07 - Other Miscellaneous Department Revenue, which consists of miscellaneous fees for services, rents, and reimbursements, is projected at \$9.6 million.

Licenses and Permits

The level of economic activity largely determines the amount of licensing and permitting done by City agencies. This category is dominated by building permit revenue, from which the City received \$22.7 million and \$23.2 million in FY04 and FY05 respectively. Building permit revenue should exceed the midyear budget estimate of \$17.0 million in FY06 due to strong residential construction and continuing commercial projects. The City expects to receive \$20.0 million in building permit revenue in FY07.

The next highest license and permit revenue is the cable television license fee from which the City received \$4.2 million in FY04 and \$3.1 million in FY05. The City has a budget of \$3.0 million for FY06 and \$4.0 million for FY07.

Alcoholic beverage licensing is the only other revenue source in this category that regularly exceeds \$2 million in annual revenue. Alcoholic beverage licenses are budgeted at \$2.3 million and \$2.4 million, in FY06 and FY07, respectively.

Penalties and Interest

Taxpayers are assessed both a penalty and interest for late payments of property tax bills and motor vehicle excise bills. The recent trend has been down for these revenues as the City excels in collection of receivables, but when the economy suffers and unemployment increases, more taxpayers are late in making payments, temporarily increasing revenues. The City collected \$9.8 million in such penalties and interest in both FY04 and FY05. Actual penalty and interest collections for FY06 will reach the current midyear budget estimate of \$8.3 million. The City expects to collect \$8.6 million in penalty and interest revenue in FY07.

Available Funds

Available funds are linked to a separate category of expenditure appropriation - those supported by immediately available fund transfers. Most of the City's general fund budget is supported by the revenues that are estimated to come in during the course of the fiscal year. This includes the

property tax levy, excises, state aid and the various other categories of revenues described above.

The only two significant available funds that the City budgets each year are parking meter revenues to support the Transportation Department, and cemetery trust monies which are used to support the City's maintenance of its public cemeteries. The City transferred a total of \$2.9 million and \$5.5 million from these two sources combined in FY04 and FY05 respectively. The City expects to transfer \$10.0 million from the Parking Meter Fund to the General Fund in both FY06 and FY07. The City also plans to transfer \$2.1 million from the Cemetery Trust Fund to the General Fund in FY06 and \$2.2 million in FY07. These monies were available at the beginning of FY06 and will also be available at the beginning of FY07.

Both of these special funds have fees collected during the course of the year. By transferring out less than what is collected over the years, the City has built up the balances of these funds. Trust fund balances also benefit from the opportunity to invest in securities offering a higher return than short-term fixed-income investments (see *Financial Management* section of Volume I for detail).

Teachers' Pension Reimbursement

Boston's cherry sheet includes an item unique to the City, the teachers' pension reimbursement for pension charges to the City. The pensions paid to retired teachers in all other cities and towns in Massachusetts come directly from the Commonwealth via the State-Teachers Retirement System.

In a singular arrangement mandated by general law, pensions paid to retired Boston teachers are paid by the State-Boston Retirement System, which charges the City of Boston for this cost as part of its annual pension funding. The City is then reimbursed by the Commonwealth through the cherry sheet. In short, the Boston teachers' pension payroll is administered locally, but, as with all other teachers' pensions in Massachusetts, is the financial responsibility of the Commonwealth. The teachers' pension reimbursement totaled \$61.4 million in FY04, \$76.5 million in FY05, and is budgeted to be \$76.5 million in FY06. The teacher's pension reimbursement is estimated at \$85.2 million in FY07.

Non-recurring Revenue

Included in the FY07 Budget is \$5.3 million in non-recurring revenue to be transferred from the surplus property disposition fund. In maintaining its policy of not supporting recurring operating costs with non-recurring revenue, the City limits this transfer to an amount not greater than \$1.0 million for the Risk Retention Reserve plus \$4.3 million for the Mayor's "Leading the Way" housing initiative.

Budgetary Fund Balance

Fund Balance can be appropriated for use during the fiscal year. Fund Balance, or Budgetary Fund Balance, is more commonly referred to as "Free Cash" when used this way. This item is most simply described as the portion of available reserves, generated to a considerable degree by annual operating surpluses, which the City can responsibly appropriate for spending.

The law governing the calculation and availability of budgetary fund balance for cities and towns is Chapter 59, section 23 of Massachusetts General Law, and is administered by the Massachusetts Department of Revenue. On January 12, 2005, the Director of Accounts certified that the amount of funds available for appropriation ("free cash"), as of July 1, 2004, was \$56,291,000. The FY05 Budget employed the use of a \$20.0 million appropriation from that amount, but due to strong growth in local revenues the amount was not needed at the close of the fiscal year. On March 1, 2006, the Director of Accounts certified free cash, as of July 1, 2005, was \$54,416,841. For FY06 a \$20.0 million appropriation has been made and for FY07 \$8.0 million is assumed to be appropriated. (See *Financial Management* section of Volume I for more detail on this revenue source.)

CITY OF BOSTON REVENUE DETAIL

		FY04 Actual	FY05 Actual	FY06 Budget	FY07 Budget
PROPERTY TAX LEVY OVERLAY RESERVE		1,094,149,616	1,150,589,723	1,207,619,855	1,260,810,351
		(42,082,678)	(44,253,451)	(40,837,386)	(42,636,099)
Subtotal		1,052,066,938	1,106,336,272	1,166,782,469	1,218,174,252
EXCISES					
Motor Vehicle Excise		33,137,120	44,697,767	38,500,000	40,000,000
40129	Room Occupancy Excise	17,000,000	18,000,000	19,000,000	23,000,000
40130	Jet Fuel Excise	8,524,273	18,403,579	14,000,000	15,000,000
40140	Condominium Conversion Excise	834,500	1,347,500	400,000	600,000
	Boat Excise	69,943	65,771	50,000	50,000
Subtotal		59,565,837	82,514,616	71,950,000	78,650,000
FINES					
Parking Fines		63,097,196	62,207,762	61,300,000	64,200,000
45104	Code Enforcement - Trash	286,393	309,669	300,000	300,000
	Other Fines	3,280,474	3,095,702	3,175,000	3,285,000
Subtotal		66,664,063	65,613,133	64,775,000	67,785,000
47151	INTEREST ON INVESTMENTS	7,791,729	17,787,353	22,806,289	24,000,000
40169	Massport	11,017,226	11,128,435	14,753,000	15,000,000
	Other Payments In Lieu of Taxes	11,250,958	12,319,365	12,026,912	12,341,631
Subtotal		22,268,184	23,447,800	26,779,912	27,341,631
URBAN REDEVELOPMENT CHAPTER 121A					
	Urban Redev. Chap. 121B Sec. 16	1,448,872	1,049,853	1,534,500	1,500,000
	Urban Redev. Chap. 121A Sec. 6A	18,655,871	17,720,143	18,500,000	18,962,500
41013	Urban Redev. Chap. 121A Sec. 10	34,702,694	36,142,426	33,500,000	34,337,500
Subtotal		54,807,437	54,912,421	53,534,500	54,800,000
MISC. DEPARTMENT REVENUE					
43105	Registry - Vital Statistics	1,661,742	1,647,714	1,500,000	1,600,000
43109	Liens	934,725	844,675	800,000	800,000
43120	City Clerk - Fees	534,994	748,353	535,000	750,000
43137	Municipal Medicaid Reimbursement	11,571,725	14,150,466	11,500,000	12,000,000
43202	Police Services	826,938	982,032	650,000	825,000
43211	Fire Services	2,702,822	2,763,405	2,700,000	2,700,000
43301	Parking Facilities	1,520,418	1,444,229	1,450,000	1,250,000
43311	PWD - Street & Sidewalk Occupancy Fees	2,309,062	1,987,005	2,000,000	2,025,000
43797	PWD - Fiber Optic Rental Fees	207,215	1,470,199	200,000	300,000
44002	Tuition & Transportation - Schools	395,581	785,981	400,000	450,000
47119	Settlements	455,733	633,610	450,000	465,000
47131	Pensions & Annuities	3,003,110	2,961,575	2,250,000	3,000,000
47132	Fringe Benefit & Indirect	0	0	0	0
47155	Prior Years Reimbursements	754,660	448,446	235,160	129,318
48000	Detail, 10% Admin. Fee	2,379,810	2,002,980	2,000,000	2,300,000
	Other Misc. Department Revenue	11,547,867	10,186,798	5,858,260	9,630,000
Subtotal		40,806,401	43,057,468	32,528,420	38,224,318

CITY OF BOSTON REVENUE DETAIL

		FY04 Actual	FY05 Actual	FY06 Budget	FY07 Budget
LICENSES & PERMITS					
40211	Building Permits	22,724,810	23,213,600	17,000,000	20,000,000
40213	Weights & Measures	235,081	238,835	230,000	235,000
40215	BTD - Street & Sidewalk Permits	1,804,755	1,327,803	1,300,000	1,500,000
40221	Health Inspections	1,182,989	1,228,258	1,100,000	1,200,000
40222	Alcoholic Beverage Licenses	2,361,597	2,360,181	2,300,000	2,350,000
40224	Entertainment Licenses	1,383,232	1,431,551	1,350,000	1,400,000
40229	Other Business Licenses and Permits	127,358	100,564	100,000	115,000
40235	Cable Television	4,203,714	3,050,569	3,000,000	4,000,000
	Other Licenses and Permits	796,732	869,716	800,000	815,000
	Subtotal	34,820,267	33,821,076	27,180,000	31,615,000
PENALTIES & INTEREST					
40133	Penalties & Interest - Property Tax	1,768,406	2,008,769	1,675,000	1,850,000
40134	Penalties & Interest - Motor Vehicle Excise	2,909,603	3,113,460	2,850,000	3,000,000
40136	Penalties & Interest - Tax Titles	5,145,195	4,627,377	3,750,000	3,750,000
40139	Penalties & Interest - 121A	123	92	0	0
	Other Penalties & Interest	7,823	1,280	10,000	10,000
	Subtotal	9,831,151	9,750,978	8,285,000	8,610,000
AVAILABLE FUNDS					
42502	Cemetery Trustee	1,932,385	2,029,004	2,110,000	2,220,500
42503	Parking Meters	1,000,000	3,500,000	10,000,000	10,000,000
	Subtotal	2,932,385	5,529,004	12,110,000	12,220,500
STATE AID					
41015	State Owned Land	170,686	266,810	340,116	226,372
41101	R.E. Abatements - Veterans/S.S./Blind	464,028	201,595	468,191	463,894
41104	Elderly Exemptions	454,310	617,460	617,460	570,272
41111	State Lottery Local Aid	53,968,473	53,968,473	60,545,688	70,589,023
41114	Veterans Services	1,618,085	1,783,305	1,932,574	2,056,250
41116	Additional Assistance	164,211,152	164,211,152	164,211,152	164,211,152
41119	Racing Taxes	722,801	735,583	630,000	609,000
41301	School Construction	17,555,199	16,144,882	15,463,685	13,815,487
41305	Charter Schools Reimbursement	3,085,155	7,089,219	10,359,141	9,654,809
41306	Chapter 70 Education Aid	200,498,366	200,498,366	203,634,716	207,044,706
41307	Charter Schools Capital Reimbursement	0	3,135,364	3,501,507	3,656,896
41311	School Transportation	9,152,359	0	0	0
41117	Police Career Incentive	7,941,863	7,846,979	7,937,515	9,315,000
41121	Municipal Relief	0	4,635,129	0	0
	Subtotal	459,842,477	461,134,319	469,641,745	482,212,861
41115	TEACHERS PENSION REIMBURSEMENT	61,389,720	76,520,673	76,520,673	85,164,054
	RECURRING REVENUE TOTAL	1,872,786,589	1,980,425,115	2,032,894,008	2,128,797,616
NON-RECURRING REVENUE					
42500	Budgetary Fund Balance	20,000,000	0	20,000,000	8,000,000
42501	Surplus Property	0	0	9,226,000	5,331,000
	GRAND TOTAL	1,892,786,589	1,980,425,115	2,062,120,008	2,142,128,616