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**Objectives of Residential Exemptions**

The committee’s explicit charge reads: “Preserving affordability for residents is the Board's top financial goal. This ad-hoc committee will continue the work of a fact finding working group formed to study the Residential Exemption and analyze if adopting the exemption could help reduce the property tax burden and make it easier for residents to remain in their homes. The ad-hoc committee will focus on identifying policy questions and will make recommendations to the Selectmen regarding the residential exemption.”

A challenge for the committee was how to evaluate the impact of a Residential Exemption. On the one hand, the committee needed to focus specifically on the language of the charge, and in particular evaluating the phrase “if adopting the exemption could help reduce the property tax burden and make it easier for residents to remain in their homes”. At the same time, it was clear that the committee is also charged with estimating the effects of adopting a Residential Exemption.

In early deliberation, it was clear that one person could use the term “fairness” to describe something which another perspective might believe is undermining community objectives. To resolve perspective issues, the committee adopted the terminology “goals” to describe potential objectives or evaluation criteria for a Residential Exemption, without validating that all community members would agree with these goals. The purpose of stating the goals is to identify possible evaluation criteria and then this report can discuss the impact of various types of Residential Exemptions on these goals. However, it remains for the body politic to determine which goals merit actions such as a Residential Exemption.

The following sections outline objectives or criteria by which one might evaluate a Residential Exemption.

**Goals from the Charge**

The phrase “make it easier for residents to remain” led to discussion of two aspects: migratory and psychological.

**Migration Goal**

If residents find it easier to remain in their homes, then evaluation criteria would be whether creating a Residential Exemption would impact migration patterns. It is commonly articulated that high property taxes “force” some residents to leave Lexington and sell their homes. Would lowering the property tax burden in fact change decisions to leave Lexington? If these households are in fact forced by high property taxes to depart, is there evidence that lower property taxes would impact their decision to migrate?

Questions were asked of brokers and housing economists about the impact of property taxes on buyers and sellers, and data from the housing survey was used to better understand current migration patterns and the relationship between property taxes and migration.

**Psychological and Cost Burden Goal**

While migration is a specific response to high property taxes, it is also possible that some residents do not find it “easy” to remain in their homes. Perhaps they experience high housing stress, or have to make difficult choices about food, entertainment or home maintenance when they balance a fixed budget against high property taxes. Could a Residential Exemption ease psychological and cost burden while in the home, and make it “easier” for residents to remain in their homes?

The committee used the housing survey to ask residents about housing stress, and connect those stress levels to income, age, home value, time in Lexington, property tax level, owning and renting, and monthly rent or housing costs. This data would then be a basis for understanding whether high property taxes are significantly correlated with housing stress, and whether a Residential Exemption is a targeted tool for reducing the strain of remaining in one’s home.

**Equity Goals**

An objective of taxation is typically to collect taxes from those able to pay. This concept underpins the property tax system which taxes residents proportionally to the value of their real estate investment.

A possible lens to evaluate a Residential Exemption is whether it succeeds in increasing the relationship between ability to pay and taxation. Although non-linear taxation may be unconstitutional in Massachusetts (see below), from an equity perspective some would judge a system more equitable if one can show it causes taxation to bear a stronger relationship to ability to pay.

**Equity Goal: Proportionate Property Taxation**

The Massachusetts Constitution adopted in 1780 permits “proportional and reasonable assessments, rates and taxes”[[1]](#footnote-0), a clause which has in numerous court cases been used to strike down progressive and disproportionate taxation. Recent proponents of progressive taxation have sought amendment to the state constitution to work around court cases in this area.[[2]](#footnote-1)

Although Massachusetts provides for a Residential Exemption, it is not clear that this tax provision is consistent with the proportional taxation requirement in the Massachusetts Constitution. Moreover, as pointed out by Peter Enrich at the housing panel, it is also not clear that the residency requirement provision present in the Means-Tested Residential Exemptions is consistent with the Federal Constitution.

The basis for property taxation in general is that owners of more property are better positioned to support the public good than owners of less. [cite Lincoln Land Institute?] On the one hand, the owner of a $1,000,000 property is only being asked to contribute about 1.4% to the public good each year, which is not substantially disproportionate than some investments such as managed mutual funds, while public services are being simultaneously rendered. Moreover, while some residents in such properties may feel strained for cash flow, a number of financial vehicles exist to allow residents to leverage their property to provide cash flow. Among these instruments are reverse mortgages, home equity loans, and tax deferrals. And when the resident passes and the house moves into estate, the home is now protected in most cases from federal estate taxes, and passes on to its heirs with a possible lien for a tax deferral but typically at a lower value than the home appreciation which has occurred in similar years.

Some have asked whether some residents should subsidize the heirs of those who live in homes today? Does it contribute to the public good that a home should pass free-and-clear to the next of kin without a tax lien for deferred (unpaid) property taxes?

**Most Efficient Uses of Property and Housing Crisis**

Due to the housing crisis in the Boston area, a coalition of Boston area leaders have committed to creating 185,000 new housing units by 2030.[[3]](#footnote-2) These units are one step in the direction of 435,000 new units needed in Eastern Massachusetts by 2040.

Although it may be inconvenient to those who seek to remain in their homes, the present free market system theoretically ensures the best use of housing. Thus, a resident may leave their home and capture appreciated home value which can be used in lower cost units for a smaller home size or deployed for assisted living. A new family which requires additional space can renovate or tear down an existing home, creating the space they need for their family.

Residential Exemptions attempt to tweak the present system, and some critics argue they prevent housing from reaching optimal use. Does Lexington want to support a system which is convenient for its homeowners, but keeps residents in their existing properties longer than makes sense for their family size? Would it be more strategic to authorize building of homes for seniors to downsize to, and encourage small households to migrate to space efficient, single floor, low maintenance units suitable for a senior population?

**Ownership versus Renting**

Typically the class of owners in American society have more assets than the class of renters. Therefore, a Residential Exemption favors owners who live in their residence over asset holders (and their renters) who do not own in residences they occupy. Like the federal mortgage tax deduction, policies such as Residential Exemptions may support those who have the benefit of owning more property over those who own less.

Based on US Census data:

“The median net worth of all Americans is $68,828. The median net worth excluding equity is $16,942 - which means equity is 75.39% of total net worth.”[[4]](#footnote-3)

Americans without equity have insignificant levels of net worth especially compared with a Lexington home with an assessed value typically closer to $800,000.

With student debt levels surpassing $1.5 trillion dollars, and the average student debt per graduate at $37,172[[5]](#footnote-4), one has to ask whether tomorrow’s graduates will be impacted in their access to home ownership. Should Lexington adopt a tax policy which explicitly favors owners over renters, at the same time many residents favor progressive values around financial equity? Local tax policy may persist for generations; is favoring ownership over renting something which Lexington would favor in the long term?

Lexington has a growing rental population with the expansion of Avalon in Lexington, and the units at Kathadin Woods. A Residential Exemption favors owner occupied condominiums over rental units. Would Lexington benefit if owners of these properties conceived a manner in which to convert some or all units to condominiums to reduce a Residential Exemption tax shift, and in so doing displaced rental residents for those able to afford condominiums?

At the population ages, policy makers should also consider what communities will be created for seniors. At the fall 2018 town meeting, Lexington supporting a zoning change so two for-profit senior care facilities could be created. Moreover, the non-profit Brookhaven facility exists in Lexington, which pays a Payment in Lieu of Taxes (PILOT) to Lexington for property taxes? Should Lexington support a Residential Exemption which specifically penalizes these group homes in favor of single family homes and owner occupied condominiums?

**State Residency and Taxation**

States compete with one another in offering services and opportunities to residents in exchange for public taxation. Some residents own properties in multiple states, and if snow-birding or otherwise shifting residence among multiple jurisdictions, may declare their state of residency for tax benefits. For example, a resident may prefer to declare Florida a state of residence to avoid Massachusetts property taxes and estate taxes.[[6]](#footnote-5) Part-time residents declaring residency elsewhere not only deprive the state of taxation on passive income, but also deprive Lexington of motor vehicle excise taxes.

A Residential Exemption may have sufficient value to motivate part-time residents to declare their residency in Massachusetts, thereby returning income taxes to Massachusetts and excise taxes to Lexington. For those who receive more financial benefit keeping their state of residence elsewhere, a Residential Exemption absorbs additional taxes locally which offset a portion of the savings the household may be making on income and excise taxes. To the extent a Residential Exemption policy comples those unfairly escaping taxation to pay into the local system, it may be judged more fair.

However, a Residential Exemption may increase taxes sufficiently for non-owner occupied homes to instead motivate homeowners to sell those properties. This may have the effect of substituting a new buyer who is a net detractor from local revenues (see below) for a part-time resident who has few economic costs for the town. Conversely, encouraging the multi-home resident to sell one of their properties may ease the housing crisis, and constitute desirable housing policy.

**Use of Public Services**

Sometimes argued from a political economic perspective and at other times from a fairness perspective, one case for a Residential Exemption is that beneficiaries are net contributors to the town and they would deserve a property tax cost reduction.

Some residents are net contributors. For example, an owner of a $1,000,000 property who contributes $14,300 in residential taxes, but has no children in school, probably pays in the current year more for town services than they themselves directly consume. (Of course, some argue they may once have had a child in school, or themselves benefitted as a child from public schooling, or benefit from high property values associated with a high quality school districts.) This taxpayer is a “net contributor” and the town budget should prefer having as many net contributors as these taxpayers provide net benefits to the town which keeps the necessary property tax rate low.

Conversely, another taxpayer living in the same property may have three children in school. While contributing $14,300 in residential taxes, their school children alone consume an average of more than $45,000 in educational costs, and their family may also consume fire, police, waste, recreation and other services. These taxpayers are “net detractors” from the town budget, and addition of more of these taxpayers increases the necessary tax rate for the town.

A political economic perspective argues that a goal of the town is to identify how policies can favor retention or attraction of net contributor residents and discourage net detractors. Favoring net contributors eases tax burdens, and therefore has a total effect on the town budget. Policies with this impact are not zero-sum, as any policy which shifts the balance between net contributors and net detractors impacts the total town budget, and thus the taxes all residents must bear. (Note: One can observe that Lexington’s taxation always at the levy limit might suggest that services are being routinely curtailed or that Selectmen are taxing above the “necessary” rate and the argument above is not supported. However, as Lexington has use excess levy to create reserves and as a result request less money from debt exclusions, as occurred in 2017, there is evidence that the “necessary” tax rate has consequences for Lexington’s ability to fund capital items and the resulting tax rate.)

The fairness argument around consumption of public services proceeds in a similar manner, but results in a more polarized understanding. Some argue that taxpayers should contribute in some proportion to current consumption. This line of argument suggests that public schools should become partly governed by user fees, as tax breakers are provided to households without children in school, and those with children in school are asked to pay more. When one cannot institute a user fee directly, a proxy such as age is then substituted to characterize whether a household is likely a net detractor from the town budget. Some open response survey respondents advocated that seniors deserve tax reductions due to their net contributor status.

An opposed argument to this fairness argument identifies that Lexington has never asked current families with school children to fully fund the public education system. Instead, public education is a public good owned by the community, and underwritten by many families without children for the good of Lexington’s households, but often more specifically those families with public school attending children. Even for those who have never had a family member attend the Lexington public schools, few are those who have not traced their own benefit to use of public schools at some point in their ancestry. While one could argue for fairness in terms of current public school attendance, it is almost directly contrary to the foundation and purpose of public schools.

1. Charles Bullock, “The Taxation of Property and Income in Massachusetts”, *The Quarterly Journal of Economics*, 31:1, Nov 1916. <https://www.jstor.org/stable/pdf/1885988.pdf> [↑](#footnote-ref-0)
2. “Massachusetts High Court Strikes Down Millionaire’s Tax”, Bloomberg News, <https://www.bna.com/massachusetts-high-court-n73014476606/> [↑](#footnote-ref-1)
3. <https://www.mapc.org/news/metro-boston-mayors-region-must-produce-185k-new-housing-units-to-keep-up-with-economic-population-growth/> [↑](#footnote-ref-2)
4. <https://www.businessinsider.com/heres-the-average-net-worth-of-americans-at-every-age-2017-6> [↑](#footnote-ref-3)
5. <https://www.studentdebtrelief.us/student-loans/student-debt-statistics/> [↑](#footnote-ref-4)
6. <https://www.cushingdolan.com/Articles-by-Our-Attorneys/Domicile-Avoiding-the-Massachusetts-Estate-Tax-and-Moving-To-Florida.shtml> [↑](#footnote-ref-5)