ONGOING FALLOUT FROM BOSTON'S EMPTY OFFICES

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THE CENTER FOR STATE POLICY ANALYSIS

BOSTON POLICY INSTITUTE

EXECUTIVE SUMMARY

Empty offices continue to threaten Boston's fiscal future, as once-attractive buildings sell for half their former value and property tax collections weaken faster than anticipated.

Just last year, the Boston Policy Institute partnered with the Center for State Policy Analysis to assess Boston's vulnerability, but those findings now look outdated and overly optimistic. A lack of decisive action, combined with a faster-than-expected decline in tax assessments, has further darkened the outlook.

Working with the latest available information, we find that:

- Office values are likely to fall 35-45 percent from their 2024 levels, a drop that reflects recent sales data and weak FY 2025 collections. This is far more than the 20-30 percent decline we previously anticipated.
- The city's budget shortfall will widen, expanding from $135 million this year to over $550 million in FY 2029 and totaling $1.7 billion over five years.
- Rather than adjust spending or reduce revenue expectations, Boston chose to offset its FY 2025 shortfall by increasing property tax rates. Continuing this approach through 2029 will require tax rates for homeowners to rise 25 percent above their 2024 level.
- Given the uncertainty behind our central projection, we are presenting two alternatives. In our "turnaround" scenario, office values find a quicker floor, limiting the city's five-year revenue shortfall to $1.4 billion. By contrast, our "spillover" scenario shows how tax increases weigh on residential and retail properties, causing the shortfall to exceed $2.1 billion.

While there is little Boston can do to prevent office values from continuing their decline, city leaders must decide whether to: a) fill revenue shortfalls by raising property tax rates, particularly for homeowners, or b) maintain stable tax rates and budget for the new reality of reduced revenues.

What follows is a fuller exploration of our updated findings, along with basic background on Boston's tax system, an overview of the challenges afflicting commercial real estate, and a discussion of the risks posed by the deteriorating economic climate.

BOSTON'S UNUSUAL BUDGET

While the collapse in commercial real estate affects cities everywhere, it hits Boston particularly hard. That's because Boston is unusually dependent on commercial property taxes to fund everything from schools and public parks to emergency services and road repair.

Commercial properties are the single biggest source of revenue for core city services, providing more direct support than homeowners, the state, or the federal government.

There are several reasons for Boston's outsize dependence on commercial properties. One is that they pay a much higher tax rate, more than double the rate for homes. Second, residents can claim a range of exclusions and tax exemptions that are unavailable to businesses. And third, Massachusetts law prevents Boston from diversifying its tax system by introducing a local sales or income levy.

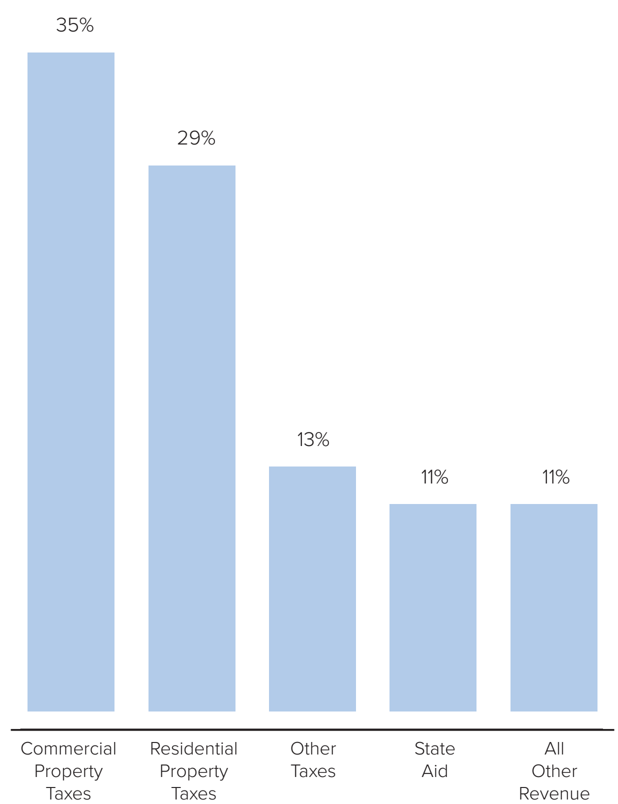
As a result, Boston's budget looks nothing like the budgets of other large American cities. Whereas the typical city draws roughly 10 percent of its total revenue from commercial property taxes, Boston hinges a third of its entire budget on this one source.

This arrangement definitely has its virtues. Property taxes are very stable, which has helped Boston weather economic storms. And charging commercial properties a higher rate has allowed the city to shelter homeowners without dampening the economic dynamism of recent decades.

But times change. And in the current economic environment, Boston's unusual tax structure has ceased to be a source of resilience and has become a liability.

FIGURE 1

Commercial property taxes are Boston's largest revenue source



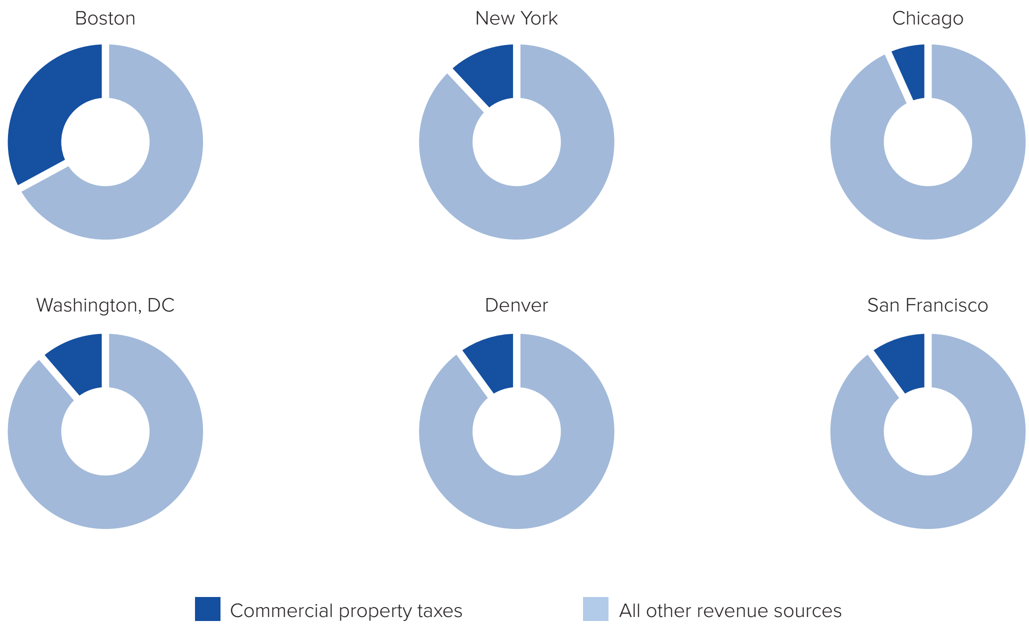
Source: Annual Comprehensive Financial Report, 2024

THE WORSENING OFFICE CRISIS

Until recently, it was hard to accurately assess the real value of Boston's office buildings. Sales were rare. Vacancy rates were rising, but there was lots of unused space still technically under long-term lease. And while folks fretted about foreclosure, banks didn't really want to take ownership of office buildings, so they loosened lending terms as part of a can-kicking strategy sometimes called extend and pretend.

FIGURE 2

No peer city is as reliant on commercial property taxes



Source: Tax Policy Center

Over the last year, however, more high-profile Boston office buildings have begun to trade hands, which finally allows us to put hard numbers to the toll. Buildings at 101 Arch Street, 400 Atlantic Avenue, 179 Lincoln Street, and elsewhere are selling at discounts of 50-70 percent, compared to prior (inflation-adjusted) prices. And it's not clear these declines represent the true floor. Consider the steeply-discounted foreclosure auction at 1 Lincoln Street, where the property was ultimately purchased by one of the building's creditors, suggesting that finding an independent buyer may have required an even bigger loss.

Meanwhile, office vacancy rates remain very high, having climbed from 8 percent in 2019 to nearly 24 percent today.

Behind this continuing weakness lie two main forces: hybrid work, which has become the new normal across the region, and mortgage rates, which remain elevated. Add the tariff-spiking cost of obtaining parts for building maintenance and there's no reason to expect a near-term turnaround in the value or profitability of office spaces.

Which is not to say that things are uniformly bleak. There are still bright stars in Boston's commercial landscape, including Back Bay's mix of office, retail, and residential and the relative strength of properties in the Seaport.

But the sky has darkened quickly. The total assessed value of all office properties in Boston fell 9 percent in FY 2025 (in real terms), a one-year decline comparable only to the financial crisis and the bursting of the dot-com bubble. And while those earlier, recession-induced drops were short-lived, today's slump seems more durable.

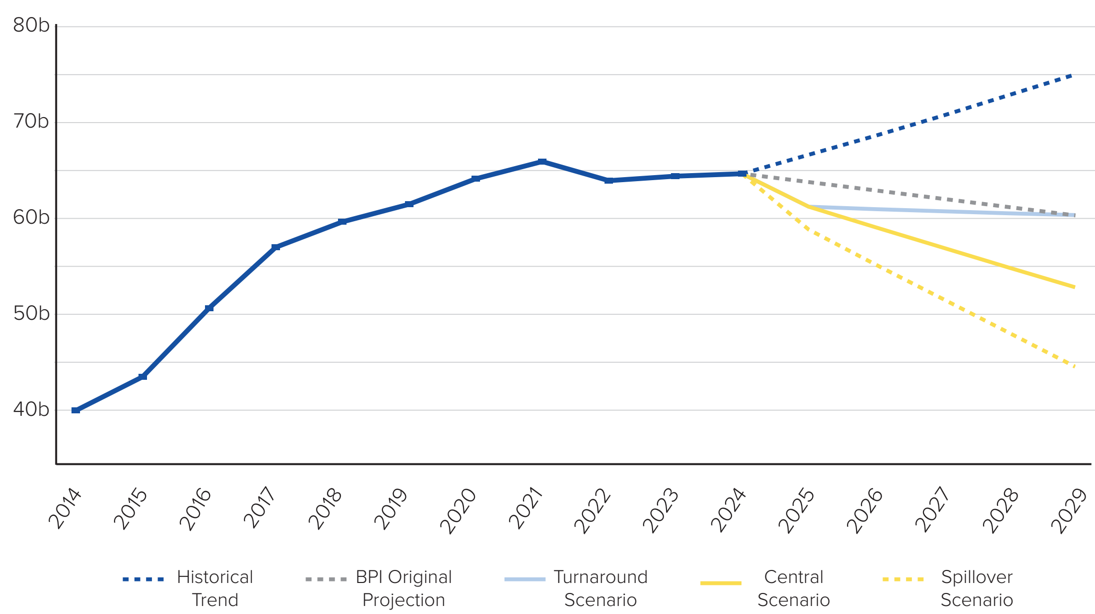
BOSTON'S WORRISOME FUTURE

Looking ahead five years, there is essentially no hope of a complete turnaround. Even the best case involves a durable decline in office values with serious implications for Boston's budget. And the worst case is devastating for the city's future.

We present three scenarios. First is a "central" scenario that reflects our best estimate of future office values and tax revenues. Alongside that, we include two alternatives: a "turnaround" scenario where office values find a faster floor and a "spillover" scenario where tax increases weigh on property values.

FIGURE 3

Commercial property values already falling, poised to fall further



Source: cSPA Calculations, real 2025 dollars
Note: Spillover scenario also reflects declining residential and industrial values

All three scenarios show marked declines from the historical trend. Between 2002 and 2024, real commercial property values in Boston grew 3 percent per year, a pace that would likely have continued without the changes wrought by remote work and higher interest rates.

CENTRAL SCENARIO

Our best estimate is that real (inflation-adjusted) office assessments will fall 35-45 percent from their 2024 levels.

This core assumption is supported by several features of the current landscape. First, the fact that major office buildings in the city are already selling at nearly half their 2024 assessed values. Second, that the 9 percent (inflation-adjusted) decline in 2025 is consistent with a 35-45 percent dropoff over five years.

If office assessments do decline 35-45 percent through 2029, it would create a $1.7 billion hole in Boston's budget, meaning that the city would collect $1.7 billion less over five years than could reasonably be expected from historical trends. Year by year, this budget shortfall would grow from $135 million in 2025 to over $550 million in 2029.

To address this growing gap, Boston could increase taxes, reduce revenue expectations, or attempt some combination of both.

Relying on tax increases alone — which is the path the city chose for 2025 — would require the tax rate for homeowners to rise from 1.09 percent in 2024 to 1.34 percent in 2029, an increase of nearly 25 percent. Tax increases for commercial and industrial properties would be far smaller, with rates rising from 2.53 percent to 2.65 percent over that same timeframe.

The tax rates we estimate here — and in our alternate scenarios — reflect the twin constraints of Proposition 2½ (which sets a limit on total tax collections) and the 175 percent tax split between commercial and residential property (which prevents the city from meaningfully raising commercial rates as office values collapse, unless the state legislature approves a larger shift).

TURNAROUND SCENARIO

Even in the most optimistic case, Boston faces a 20-30 percent decline in real office values through 2029 — akin to the already challenging outlook we described in our initial report last year.

Given that valuations fell 9 percent in FY 2025 alone, finding a 20-30 percent floor would require quick braking. But there are a few ways this could happen.

A decline in interest rates would make it easier for building owners to extend mortgages and finance operations. Alternatively, the arrival of new buyers — possibly lured by shifts in global asset markets — could firm up office values.

If Boston does limit the damage, a 20-30 percent fall in office values would create a slightly smaller 5-year budget shortfall of $1.4 billion, culminating in a $415 million gap in 2029. Filling this hole entirely through property tax increases would require a 1.27 percent rate for homeowners.

SPILLOVER SCENARIO

Both the "central" and "turnaround" scenarios assume that the decline in office values is narrowly contained, without risk of bleeding into the rest of the city budget. But this is unlikely, particularly if Boston continues to offset falling valuations by raising tax rates.

A weak but well-established economic relationship connects tax rates and property values. When rates go up, values go down (a little). And the rationale is fairly straightforward: higher property tax rates make it a little more expensive to own a home, which then makes home ownership a little less desirable.

So if Boston's continued response to empty offices involves higher tax rates for residents and other businesses, that will somewhat reduce the value of homes, retail shops, industrial buildings, and beyond.

Accounting for these broader effects raises the city's fiscal shortfall to $2.1 billion over five years, culminating in a $660 million gap in 2029.

And note there's a potential feedback loop. Filling a $2.1 billion gap requires residential property tax rates of at least 1.38 percent — but this rate would put additional downward pressure on home values, further reducing property tax collections, widening the budget shortfall, and requiring ever-higher rates.

SCENARIO	KEY ASSUMPTION	5-YEAR REVENUE SHORTFALL	RESIDENTIAL RATE TO CLOSE GAP
Central	Office values decline 35-45 percent	$1.7 billion	1.34%
Turnaround	Office values decline 20-30 percent	$1.4 billion	1.27%
Spillover	Tax increases depress property values	$2.1 billion	>1.38%

THE CHOICES AHEAD

Boston's leaders aren't responsible for this collapse in office values. Broad changes in the way we work combined with increases in the cost of borrowing have made office space less desirable and undermined the city's otherwise stable financial base.

Nevertheless, the city, the state, and local civic leaders have to deal with this change of fortune by forging a new path to budgetary stability and long-term growth.

Boston's leaders sometimes imply that their budget is self-healing, that shortfalls cannot happen, and that the city can always collect the maximum amount of revenue allowable under Massachusetts law.

But there's no magic here. The way shortfalls get filled, in the current budget process, is through automatic tax rate increases. And while that may be fine when the increases are small, large rate hikes carry substantial economic and political risk.

Already we can see that Boston's leaders are uncomfortable relying on automatic tax increases. Last year, the mayor and her team invested substantial political capital in a failed effort to block the automatic tax increase on homeowners and shift more of the burden onto commercial properties.

If the city continues to target the maximum allowable revenue, it will trigger years of steadily-rising tax rates on homeowners. And persisting with the plan to shift these tax increases to commercial properties risks deeper damage:

- Shifting more of the tax burden onto commercial properties will only worsen the already-severe problems in the office sector. These buildings are not in a position to absorb the cost of new taxes.
- As office values fall, retail spaces — which include a lot of local Boston businesses — will make up a growing share of commercial property values. So shifting the tax burden to commercial will increasingly affect retail properties.
- Perhaps most fundamentally, pressing for tax shifts while defaulting to maximal revenue targets undermines honest debate about how much the city should raise and spend.

Given the scale of the challenge facing Boston, nearly all viable solutions require a new approach to taxing and budgeting.

Which is not to say that other efforts to revivify the downtown are irrelevant. Converting offices to residential buildings, for example, can expand housing opportunities and ensure downtown dynamism. But for now, there are only a few projects moving through this pipeline. And even successful conversions don't actually improve the city's budget, since the new residential buildings often receive tax credits and only pay the lower residential tax rate.

What's needed is a city budget based on consistent and affordable property tax rates for homeowners and businesses, even if it means collecting less revenue than allowed under Massachusetts law. This is the surest way to re-ground Boston's finances and boost confidence among vital partners, like state legislators considering additional aid, local non-profits negotiating PILOT payments, or rating agencies tracking the city's fiscal picture.

Absent a new budgetary approach, the same fights that shaped city politics last year will return, only with rising stakes and higher tax rates.

A RECESSIONARY WRINKLE

Even as office values in Boston have steadily fallen, the local economy remains relatively strong. And our projections — including all three scenarios described above — assume continuing economic health.

But the odds of an economic slowdown or nationwide recession are climbing. And Boston may be more vulnerable than in past downturns, for at least two reasons:

1. Some of the economic buffers that have protected the city — like the stability of higher education and the health care industry — are being directly targeted by federal lawmakers, potentially turning these traditional shock absorbers into accelerants of economic distress.

2. Contra sound policy and long precedent, the administration in Washington may decide to steer economic assistance to its favored locales, while limiting aid in places like Boston that have drawn presidential ire for their status as sanctuary cities.

A recession in 2025 or 2026 would have all manner of baleful effects for families and businesses in Boston. But one likely result would be an uptick in bankruptcies, foreclosures, and office building defaults, which would make it even harder for the city to balance its budget through property tax increases.

One potential upside is that economic slowdowns generally lower interest rates, which would alleviate some of the pressure on office buildings. But even that silver lining may melt away this time, as the ongoing trade war and rising national debt are poised to keep rates elevated.

CONCLUSION

In the year since our initial report highlighted the risk of falling commercial property values in Boston, reality has not only confirmed but actually outrun our earlier expectation.

Assessments have fallen faster than anticipated, and we now expect the city to face a $1.7 billion budget hole between FY 2025 and FY 2029.

In FY 2025, Boston lawmakers chose to fill this hole chiefly by raising taxes on homeowners. And while they may be able to continue this strategy, it would require annual ratcheting rate hikes and a growing risk of dampening home values.

Yet the city does have other options, provided it's willing to choose appropriate tax revenue targets rather than simply collecting the maximum allowable amount each year.

Shrinking demand for office space is not a short-term problem that the city can hope to simply wait out. It requires a durable, transparent rethinking of budgetary priorities in order to sustain and support Boston's economic future.

METHODOLOGICAL NOTES

Details about Boston's tax system were chiefly drawn from the Massachusetts Division of Local Services. Finding the assessed value of specific properties, and calculating the share of total value tied to office spaces, involved parcel-level data from the city's Analyze Boston dashboard.

Values were adjusted for inflation using the Consumer Price Index, accessed through the St. Louis Federal Reserve's FRED platform.

Projections from 2026 to 2029 involved a number of assumptions. We assumed that residential values, non-office commercial values, industrial values, personal property values, and new growth would continue rising at the same real, annual rate as they had (individually) grown from 2002 to 2024. And we projected inflation to grow at 2.5 percent per year.

To measure the budget shortfall, we combine the actual data for FY 2025 with projections for FY 2026 through FY 2029 — and compare these projections against a counterfactual where office values grow at their historic rate (2002 to 2024). Our counterfactual further assumes that residential and commercial tax rates remain at their FY 2024 level.

For our "spillover" scenario, we assume a residential elasticity of .2 and a commercial elasticity of .4.