

# Town of Montgomery, Vermont

Wastewater Implementation - Report of Revenue Options for USDA RD WEP Loan Repayment

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*Prepared By:*

**Hoyle, Tanner**  
& Associates, Inc.

125 College Street, 4<sup>th</sup> Floor  
Burlington, Vermont



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## Executive Summary

The Town of Montgomery, Vermont received the following USDA RD WEP Grant and Loan Funding offer for wastewater implementation in the Village and Center:

USDA RD WEP Loan:	\$4,948,000.00
USDA RD WEP Grant:	\$6,065,000.00
Total	\$11,013,000.00

Repayment of the \$4.948M USDA RD WEP Loan is a significant cost for the Town of Montgomery. This report by Hoyle, Tanner examines five loan repayment options for Montgomery to consider in wastewater implementation decision making.

Hoyle, Tanner & Associates collaborated with Town Stercus Committee members and VT DEC staff during three meetings in January 2020 to develop Town preferred loan repayment options as indicated below:

Funding Source	Approximate Annual Contribution
Add Sewer Bond Charge (Water Rate Increase)	\$60,000
Sewer Benefit Assessment	\$99,376
Local Option Tax	\$35,957
Impact Fee	\$0
Tax Increment Financing	\$0
<b>Total:</b>	<b>\$195,332</b>
<b>Required Annual USDA RD WEP Loan Payment Needed -</b>	
<b>Total:</b>	<b>\$194,854</b>

The Town identified their preferred approach to allocate the entirety of the approximate \$195,000 annual USDA RD WEP Loan payment to be covered by the lower risk Sewer Bond Charge, Sewer Benefit Assessment, and Local Option Tax repayment options.

It is recommended that the Town complete the following:

1. Consult with Town Council regarding integration of the Sewer Bond Charge, Sewer Benefit Assessment and Local Option Tax into the USDA RD WEP Loan repayment plan to ensure that these three potential loan repayment options meet the USDA RD WEP Loan terms and can be legally and practically administered by the Town. Consult with Town Council regarding future integration of the Impact Fee into loan repayment.
2. Consult with the USDA RD WEP Program to ensure the proposed USDA RD WEP Loan repayment options meet the Loan terms.
3. Monitor and contribute to the legislative development of the Project-Based Tax Increment Financing (TIF) program and consult with Town Council regarding integration of the Project-Based TIF into loan repayment in the future.

## 1. Introduction

The Town of Montgomery, Vermont does not currently have a publicly owned wastewater treatment system but is in the preliminary stages of implementing one. The Town received the September 2, 2020 wastewater project funding offer from United States Department of Agriculture Rural Development (USDA RD) Water Environment Program (WEP) including the following:

USDA RD WEP Loan:	\$4,948,000.00
USDA RD WEP Grant:	\$6,065,000.00
PPG Grant	\$30,000.00
Clean Water State Revolving Loan Fund Grant	\$250,000.00
<u>Northern Borders Regional Commission Grant</u>	<u>\$507,000.00</u>
Total	\$11,800,000.00

Repayment of the \$4.948M USDA RD WEP Loan is a significant cost for the Town of Montgomery. This report by Hoyle, Tanner examines some loan repayment options for Montgomery to consider in wastewater implementation decision making.

Based on the USDA RD WEP 30-year loan terms at 1.125% interest compounded annually, this would leave nearly \$195,000 to be paid by Montgomery annually. This Report identifies five potential options for the Town to consider to pay for the \$195,000 annual USDA RD WEP loan cost and the advantages and disadvantages of each option.

Regarding the two questions of "who pays" for the wastewater system bond indebtedness? and can the Town implement a sewer benefit assessment? J. Paul Giuliani, Attorney at Law, Pimmer Piper Egelston & Cramer PC, provided the following May 27, 2020 email response to Charlie Hancock, Montgomery Selectboard Chair:

“Our [VT] statutes dealing with municipal sewer (and water) systems are predicated on user-pay. In return for excluding sewer and water debt from a municipality’s debt limit calculation, the statutes require the municipality to set and collect rates sufficient to pay operation and maintenance costs of the system, pay debt service on its water and sewer bonds, and fund system capital reserves. Water and sewer system revenues can be used for no other purpose. If properly managed, municipal water and sewer systems are self-sufficient, and water and sewer debt is self-liquidating (pun intended).

So, the source of paying for municipal water and sewer systems is system revenue. On the other hand, security for water and sewer bonds and notes is a pledge of the municipality’s full faith and credit. That is, its unlimited taxing authority stands behind the municipality’s general obligation water and sewer system bonds and notes. If, for whatever reason, there should be insufficient system revenue to pay debt service on outstanding water and sewer bonds, the municipality is obligated by law to levy a property tax to cover the deficiency.

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The distinction between source of payment and security for payment is important. Theoretically, improvement bonds secured only by a pledge of water and sewer system revenue could be issued. However, there are only two or three municipal systems in Vermont large enough to support even a modest revenue bond issue.

Regarding the second question, the general statute gives the Selectboard a menu of options in establishing sewer user rates. At one end of the spectrum metered on-premises water consumption is a recognized basis for setting rates. Moving along, water-using fixtures and appliances, square footage, number of bedrooms, and the like are acceptable bases upon which user rates can be imposed. The spectrum also recognizes specifically the impositions of a sewer benefit assessment on all property within the municipality, regardless of whether it is currently hooked into the sewer system, or if there is no possibility that it will ever be connected. The sewer benefit assessment generally is a function of grand list assessed valuation. Imposition of a sewer benefit assessment is a recognition that having wastewater pollution abatement facilities confers upon the municipality at large benefits in the form of, for instance, enhanced property values by virtue of the availability of public sewers.”

The USDA RD WEP Loan will be secured by a General Obligation bond with first lien position in the amount of \$11,700,000. The bond will be fully registered as to both principal and interest in the name of the United States of America, Acting through the United States Department of Agriculture.

The bond and any ordinance or resolution relating thereto must not contain any provision in conflict with the Agency Loan Resolution, applicable regulations, or its authorizing law. In particular, there must be no defeasance or refinancing clause in conflict with the graduation requirements of 7 U.S.C. 1983.

Additional security requirements are contained in RUS Bulletin 1780-12, “Water and Waste System Grant Agreement,” and RUS Bulletin 1780-27, “Loan Resolution (Public Bodies).” A draft of all security instruments, including draft bond resolution, must be reviewed and concurred in by the Agency prior to advertising for bids. The bond resolution and Loan Resolution must be duly adopted and executed prior to loan closing. The Grant Agreement must be fully executed prior to the first disbursement of grant funds.

## **2. Sewer Bond Charge**

### **2.1 Current Drinking Water Charges**

The Town of Montgomery owns and operates a public drinking water system serving 192 accounts as shown in Table 1.

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**Table 1: Number of residential and commercial water accounts**

District	Residential Accounts	Commercial Accounts
Village	46	21
Center	75	38

In addition, there are 11 non-profit accounts (primarily Town buildings) and one school.

System accounts are billed quarterly for water in two components. Water usage is billed using a decreasing block rate structure including a base charge of \$60 for up to 4,000 gallons (\$15/1000 gallons) with additional usage charged at \$7/1000 gallons.

The second component is a fixed charge for bond repayment. The quarterly bond repayment charge for single-family residential users is \$33 in the Center system and \$48 in the Village system. The quarterly bond repayment charge for commercial accounts is \$50 in the Center system and \$61 in the Village system. The non-profit accounts pay \$30 and the school pays \$240 per quarter.

In 2020, Village accounts consumed 4,012,032 gallons and were billed \$40,571 for water usage averaging \$10.11/1000 gallons. Center accounts consumed 6,347,000 gallons and were billed \$64,953 for water usage averaging \$10.23/1000 gallons.

Based on this data, the average water account consumed 148 gpd (gallons per day) in year 2020. Water accounts in the Center system paid about \$680 to \$750 and those in the Village system paid about \$750 to \$800 in 2020.

The bond portion of the rates applies to debt service for three outstanding bonds issued for water system improvements financed through the USDA Rural Development program as summarized in Table 2.

**Table 2: Current Outstanding Water Bonds**

Bond No.	Principal Balance as of 12/31/2020	Semi-Annual Payment	Retirement Year
1	\$117,334.93	\$3,758.00	2041
2	\$294,562.39	\$10,625.00	2041
3	\$287,497.32	\$8,718.00	2047

Currently, about 73% of the apparent debt service of \$46,202 is raised through the water bond repayment charge. The remainder (about \$12,500) is from general Town funds.

## 2.2 Options for Adding Sewer Charges

A system of sewer rates can be a component of the sewer loan repayment plan. The proposed sewer rate schedule would adhere to the same structure as the water rates to be incorporated into the Town’s billing software. The contribution for the sewer bond debt service would be raised

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by a new quarterly sewer bond repayment charge. For purposes of this analysis, the charge would be allocated among the user classes and locations in the same ratios as the current water bond repayment charges. A new sewer user base charge would separately raise the funds needed for annual sewer system operations and maintenance (O&M).

The current proposal is to raise \$60,000 for sewer debt service with the proposed sewer bond repayment charge and \$44,000 for O&M with the proposed sewer user base charge. The resulting combined rates and charges for water and sewer service is shown below in Table 3.

**Table 3: Quarterly sewer rates and rate increases by user type**

User Type	Total Increase in Rates	New Total Quarterly Base User Charge for Water & Sewer	New Quarterly Bond Charge for Water and Sewer	Net Quarterly Increase per Account
Village Residential	232%	\$ 117	\$ 133	\$ 143
Village Commercial	237%	\$ 117	\$ 169	\$ 166
Center Residential	225%	\$ 117	\$ 92	\$ 116
Center Commercial	233%	\$ 117	\$ 139	\$ 146
Non-Profit (Town Facilities)	223%	\$ 117	\$ 83	\$ 111
School	261%	\$ 117	\$ 667	\$ 484
<b>Average:</b>	230%			

### 2.3 Conclusion

Sewer use rates and charges are a reasonable and typical method for contributing to the debt service and O&M expense for the proposed sewer system. These proposed set of sewer rates and charges is designed to be affordable and equitable.

### 2.4 Advantages and Disadvantages

Sewer use rates and charges are paid by those who most directly benefit and utilize the new sewer system. As the system expands and serves new users, additional revenue is raised while the debt service remains fixed. Additionally, the sewer revenue, as proposed, does not depend on actual water consumption; the variable revenue component of the water rates (i.e., charges for water use above the base rate) has not been incorporated into the sewer rate schedule. Therefore, the sewer revenue is considered fixed and reliable. From a rate-making philosophy, a disadvantage of the sewer rates and charges can be that the entire town benefits from having an improved sewer system even if everyone does not tie into it. However, that is why the proposed sewer rate schedule is only one component of the total revenue plan.

## 3. Sewer Benefit Assessment

Revenue generation from a sewer benefit assessment represents a share of the total bond value to be paid by each taxable parcel in Montgomery based upon assessed property value. This



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mandates payments for each property totaling the value needed to pay off the USDA RD WEP Loan. Owners of parcels with greater values would pay more annually than those of lower-valued parcels, with the annual payment dependent on the ratio of each parcel’s value when compared to the Total Municipal Grand List.

Table 4, shown below, identifies the average bond payment per parcel in Montgomery required to meet the annual loan payment. This current proposal is based on a 51% payment share per parcel for the 942 parcels. The other four USDA RD WEP Loan repayment options cannot collectively generate enough revenue to reliably cover the entirety of the USDA RD WEP Loan annual payments, so the sewer benefit assessment percent payment share can be adjusted to ensure that the USDA RD WEP Loan annual payments is met.

**Table 4: Sewer Benefit Assessment total and per-parcel annual payment requirements**

<b>2. Estimate Sewer Benefit Assessment (% Share of Bond Value all taxable parcels will pay)</b>	
Total # of taxable Parcels in Town	942
% share of Annual Bond Payment per parcel	51%
Total of revenue generated from annual Sewer Benefit Assessment	\$99,375.54
Total Municipal Grand List Value	\$1,611,871.43
Annual Sewer Benefit Assessment(per \$100 assessed property value)	\$0.0617
Average Annual Sewer Benefit Assessment revenue per Town parcel	\$105

### 3.1 Conclusion

Unlike the other four USDA RD WEP Loan repayment options, the Sewer Benefit Assessment can be adjusted to ensure that adequate revenue is collected to meet the USDA RD WEP loan cost annually. As a result, it can generate however much income is required by the community and could be adjusted year-by-year to generate revenue needs as they change. In the example shown above, 51% of the annual loan repayment is assigned to the Sewer Benefit Assessment, resulting in nearly \$100,000 of annual revenue generation from a sewer benefit assessment of \$0.0617/\$100 assessed property value.

### 3.2 Advantages and Disadvantages

One advantage of utilizing the Sewer Benefit Assessment as the primary source of revenue generation for repayment of the USDA RD WEP Loan is its malleability. It can be used to produce the needed amount of revenue regardless of how much is produced by the other funding options simply by adjusting the percent share paid by property owners. It is also relatively easy to implement. While the other options would generate revenue by charging users, residents, and nonresidents varying amounts based on external factors including sales, land development growth, and water usage, the Sewer Benefit Assessment would simply charge the owners of all the parcels in Montgomery the exact same amount, \$0.0617/\$100 assessed property value. This simplifies this funding option from an administrative standpoint.

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The Sewer Benefit Assessment is also one of the lower risk funding options of the five options investigated. Since there is low potential variability compared to sales revenue or assuming land development growth, the expected Sewer Benefit Assessment annual revenue generation risk is lower. Another advantage of implementing the Sewer Benefit Assessment is the potential for reduced per-parcel annual payments in the future. Since the annual cost of the sewer benefit assessment for each property is based on the assessed property value, future land development growth within the Town is anticipated to increase the overall Municipal Grand List allowing the Town to reduce the sewer benefit assessment in the future to meet the USDA RD WEP Loan annual cost.

While there are advantages of implementing the Sewer Benefit Assessment, it is not without its disadvantages. The sewer benefit option would generate revenue entirely from existing property owners, including property owners located outside the proposed Village and Center sewer service areas, as opposed to some of the other options which would also generate revenue from nonresidents.

### **4. Local Option Tax**

The State of Vermont allows municipalities to enact a Local Option Tax, or LOT, which applies an additional 1% to state business taxes to generate revenue. The 1% LOT can be added onto the Sales and Use Tax (6%) and Meals and Rooms Tax, which utilizes individual tax rates for Meals (9%), Rooms/Lodging (9%), and Alcohol (10%). The local option tax mandates a 1% tax rate, so communities cannot select an LOT value of, for example, 0.5%. Communities can elect to apply the LOT to any or all of the Sales Tax, Meals and Alcohol Tax, and Rooms/Lodging Tax.

While a 1% tax rate is required, municipalities do not keep the entirety of revenue generated through their local option tax. Instead, 70% of the revenue is returned to the Town, while 30% is funneled to the Vermont Payment in Lieu of Taxes, or PILOT, Fund. The PILOT Fund is designed to compensate municipalities for municipal taxes they are unable to collect on state-owned buildings located in the municipality and its funds are redistributed to municipalities on this basis. In the event of excess PILOT funding, funds are not returned to contributing municipalities but are instead carried forward to the following year, along with any interest generated.

Montgomery tax data from the last 5 years (2015-2019) was used to assess potential revenue generation from the LOT. Refer to Tables 5 and 6, shown below, for a breakdown of annual tax data and estimated annual revenue generation.

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**Table 5:** Annual Sales and Use and Meals and Rooms Tax receipts for Montgomery from 2015 through 2019

	Sales and Use Tax Statistics		Meals and Rooms Tax Statistics		
	Gross Receipts	Retail Receipts	Meals Receipts	Rooms Receipts	Alcohol Receipts
2015	\$11,128,988	\$1,985,259	\$1,321,292	\$665,985	\$587,479
2016	\$11,529,219	\$1,896,349	\$1,321,292	\$646,747	\$587,479
2017	\$10,474,440	\$2,019,601	\$1,595,940	\$606,924	\$587,479
2018	\$10,991,317	\$2,297,698	\$1,756,436	\$754,205	\$587,479
2019	\$12,764,657	\$2,423,299	\$1,585,276	\$608,277	\$587,479

Note: Values in gray cells are assumed to be equal to the 2015 reported values because actual values were not available.

**Table 6:** Annual revenue generated by local option tax based on tax receipt data

	Tax Rate	Total Tax Revenue	PILOT Fund (to State)	LOT Revenue (to Town)
2015	1.00%	\$45,600	\$13,680	\$31,920
2016	1.00%	\$44,519	\$13,356	\$31,163
2017	1.00%	\$48,099	\$14,430	\$33,670
2018	1.00%	\$53,958	\$16,187	\$37,771
2019	1.00%	\$52,043	\$15,613	\$36,430

The Vermont Department of Taxes withholds tax statistics for certain types of sales if there are fewer than 10 reporting accounts. Montgomery had fewer than 10 reporting accounts for meals sales in 2016 and for alcohol sales from 2016 through 2019. Since this data is not available to the public, for the purposes of this analysis, it is assumed that the meals sales in 2016 matched those of 2015 (approximately \$1.3 million) and the alcohol sales from 2016 through 2019 also matched those of 2015 (approximately \$588,000). To estimate the potential future revenue generation from a local option tax in Montgomery, the average revenue generation of the last three complete years for which tax data is available was used. Refer to Table 7 below for a breakdown of annual local option tax revenue generation based on 2017 through 2019.

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**Table 7:** Local option tax average annual revenue generation figures for 2017-2019

Montgomery 2017-2019 Average Annual Net Sales	\$2,246,866
Local Option Sales Tax	1.00%
Local Option Tax Annual Revenue to Town	\$15,728
Total Local Sales Option Tax Annual Revenue	\$22,469
Montgomery 2017-2019 Average Annual Meals	\$1,645,884
Local Option Meals Tax	1.00%
Local Option Tax Annual Revenue to Town	\$11,521
Total Local Meals Option Tax Annual Revenue	\$16,459
Montgomery 2017-2019 Average Annual Lodging	\$656,469
Local Option Lodging Tax	1.00%
Local Option Tax Annual Revenue to Town	\$4,595
Total Local Lodging Option Tax Annual Revenue	\$6,565
Montgomery 2017-2019 Average Annual Alcohol	\$587,479
Local Option Alcohol Tax	1.00%
Local Option Tax Annual Revenue to Town	\$4,112
Total Local Alcohol Option Tax Annual Revenue	\$5,875
<b>2017-2019 Local Option Tax Annual Revenue to Town</b>	<b>\$35,957</b>
<b>2017-2019 Total Local Option Tax Revenue</b>	<b>\$51,367</b>

#### 4.1 Conclusion

Analysis results of the Town sales data during the 5-year period from 2015-2019 indicate that Montgomery can generate approximately \$51,000 per year through the local option tax, retaining approximately \$36,000 (70%) of the revenue while the other \$15,000+ (30%) is allocated to the PILOT Special Fund. While these values represent the average revenue generation based on recent years' data, option tax revenue is wholly dependent on actual sales and could be higher or lower than the 2017-2019 average in future years, presenting an element of risk. This is taken as an 'expected' contribution amount, but given this parameter's potential volatility from year to year it is recommended that the Town consider implementing this option along with lower-risk options for USDA RD WEP Loan repayment.

#### 4.2 Advantages and Disadvantages

Local option tax is one of the most straightforward funding alternatives to implement. The 1% tax on retail sales, rooms, meals, and alcohol is a relatively small increase from a customer's perspective while potentially generating over \$30,000 per year to put towards repaying the USDA RD WEP Loan. Another advantage of the LOT is that a significant portion of the rooms, meals, and alcohol tax burden and much of the retail sales tax burden would be paid by non-residents rather than residents.

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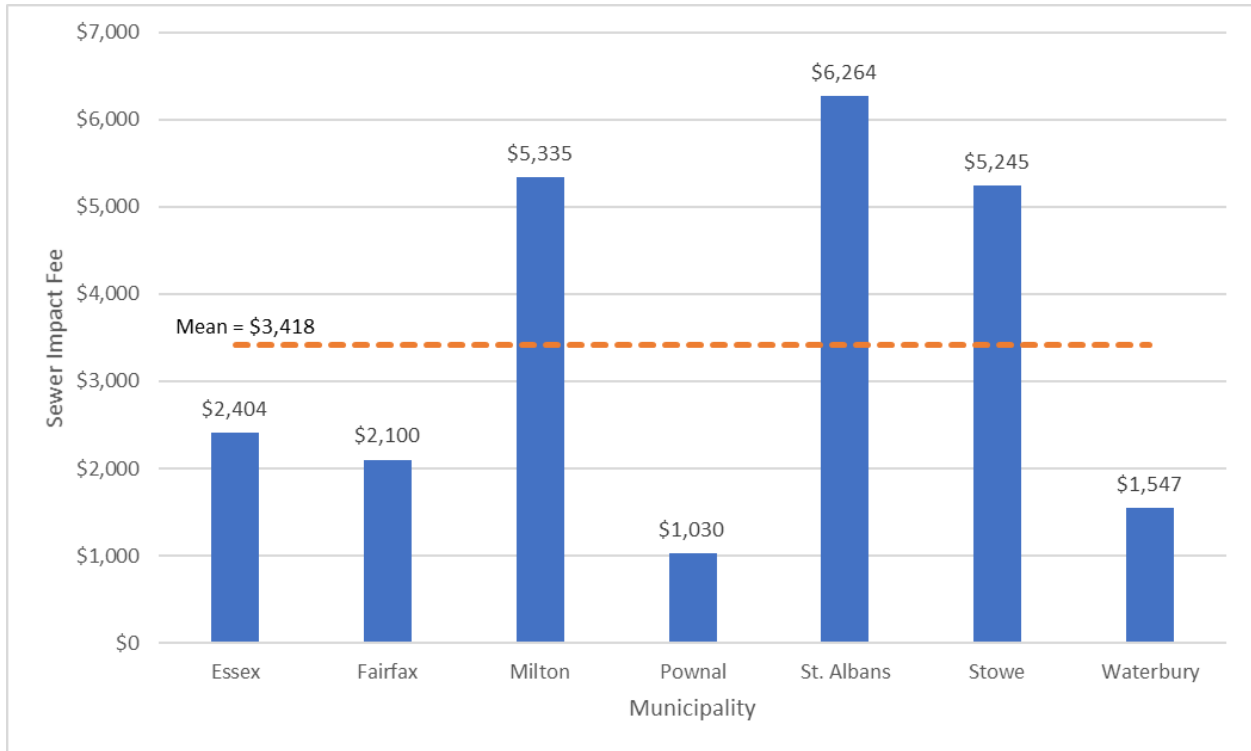
While nonresidents would presumably pay a significant portion of this tax, the messaging approach to residents is important. The structure of the LOT, with 30% of the revenue retained by the state for the PILOT Fund, may be difficult to explain to Town residents. Implementing this tax and only netting 70% while providing the remainder to the state may be an unpopular element of this funding option. Additionally, while the potential revenue generation can contribute to the yearly USDA RD WEP Loan payments, the likely \$30-40,000 revenue generation would still leave around \$160,000 per year which would need to be generated from other revenue sources. The uncertainty of annual revenue generation presents another potential difficulty for this alternative since external factors could influence future tax revenue generation. For example, the COVID-19 pandemic in 2020 has resulted in greatly reduced numbers of people traveling, which leads to reduced spending on rooms, meals, and alcohol, and even retail sales as people order more products online. This presents risk with regard to reliance on any specific amount of revenue generation and would likely require some level of contingency planning. The other potential challenge of implementing a Local Option Tax is the fact that it would need to be approved by Montgomery voters. However, the fact that the brunt of the revenue generation would be on the backs of non-residents should help its popularity among residents.

### **5. Impact Fees**

Impact fees are charges paid by users to establish a new service. They are meant to capture the additional impact levied on a service by the addition of a new user and to effectively reimburse the service for that impact. In the context of wastewater, impact fees are most commonly manifested in the form of connection fees and/or allocation fees. Connection fees charge a user for establishing a new connection, in this case constructing a service lateral between a main and the user's property. Allocation fees allow users to purchase an allocated amount of treatment capacity within a service. For sewer, new customers would pay a fee to contribute a certain amount of wastewater to the publicly-owned treatment system and the treatment system would be expected to effectively treat that contribution.

Vermont communities use different combinations of connection and allocation fees for new sewer users (with some fees using different names). For example, the Town of Essex has a \$1,000 sewer initiation base fee (connection fee) plus a \$5.73/gpd capacity allocation fee, while the Town of Pownal has a \$1,000/EU (equivalent living unit) residential sewer use fee (connection fee) plus a \$30 residential application fee. Refer to Figure 1, shown below, for a breakdown of sewer impact fees for these seven Vermont municipalities in which they have already been implemented: Essex, Fairfax, Milton, Pownal, St. Albans, Stowe, and Waterbury.

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**Figure 1:** Current sewer impact fees in various Vermont municipalities

The sample municipalities were chosen on an arbitrary basis, but Figure 1 indicates sewer impact fees in Vermont are typically somewhere between \$1,000 and \$6,000. The mean impact fee for these seven municipalities is approximately \$3,400 per new user.

For a hypothetical revenue generation analysis the connection fee for new sewer users in Montgomery was set to \$3,500 per connection. See Table 8, shown below, for a breakdown of potential revenue generation through this sewer impact fee.

**Table 8:** Anticipated sewer impact fee revenue generation in Montgomery for next 20 years

Total Wastewater System Capacity (gpd)	75,000
Total existing wastewater need (gpd)	44,000
Potential Wastewater System Capacity for growth	31,000
Mean of 7 VT Town connection fees	\$3,418
Assumed Montgomery Connection Fee	<b>\$3,500</b>
Average Daily Flow per typical home (gpd)	245
Effective connection fee in gpd terms (\$/gpd capacity)	\$14.29
<b>Assumed growth period (years)</b>	
Assumed growth period (years)	20
Total Potential Revenue from available capacity	\$442,857.14
Average annual impact fee revenue	\$22,142.86

## 5.1 Conclusion

Given a \$3,500 connection fee and the assumption that maximum wastewater capacity will be reached in the next 20 years, Montgomery can generate over \$22,000/year to put toward repaying the USDA RD WEP Loan. This is based on a design wastewater system capacity of 75,000 gpd with an existing need for 44,000 gpd. The additional 31,000 gpd of growth capacity is, in simple terms, enough for 124 new homes/connections: 94 in the Center District and 30 in the Village District. Growth could occur as residential or commercial land development, or both. For the purposes of this analysis, it is simply assumed that all of this growth is residential and would occur at a consistent rate in the two-decade period, resulting in a little over 6 new houses per year. This corresponds to the annual revenue generation potential of just over \$22,000 and a total 20-year revenue generation of nearly \$450,000.

While this funding alternative could provide Montgomery some revenue to put towards repaying the USDA RD WEP loan, uncertainty surrounding future growth rate prevents any reliable estimate of future revenue generation and dictates that Montgomery focus on other funding sources.

## 5.2 Advantages and Disadvantages

While new charges are never popular, sewer impact fees would not affect current residents who choose to connect to the new utility soon after its implementation. Instead, this fee would target new residents who would place added stress on the wastewater infrastructure by connecting, therefore providing justification for a fee to be charged. Additionally, the fact that these fees are common across Vermont establishes precedent for their implementation. These fees for new connections are logical since new connections do undeniably impact existing systems, and this may increase support for the new charge among residents.

Although sewer impact fees represent a logical method of revenue generation for infrastructure development in Montgomery, there are major drawbacks to their implementation consistent with those of the Local Option Tax, as discussed in Section 4. Like the Local Option Tax, the expected annual revenue generation has a level of risk. In fact, impact fees have an even higher level of risk than the Local Option Tax since they rely on growth rather than annual sales data (which is likely to be consistent with previous years). While land development can be projected to a certain extent and addition of a wastewater treatment system is expected to catalyze growth, there is still significant uncertainty as to whether anticipated growth rates would actually materialize, and a more conservative growth estimate may be more realistic. While it can be estimated, there is no way to definitively predict how much revenue the Town can generate on an annual basis. Additionally, while any revenue generation is beneficial for repayment of the USDA RD WEP loan, the approximate \$22,000 anticipated annually only represents about 11% of the \$195,000 needed per year for the 30 year USDA RD WEP loan repayment period.

Another disadvantage of implementing impact fees is the potential for discouraging growth. The addition of a publicly-owned wastewater treatment system is expected and hoped to attract new businesses and residents, but it is possible that by requiring payment of an impact fee (especially

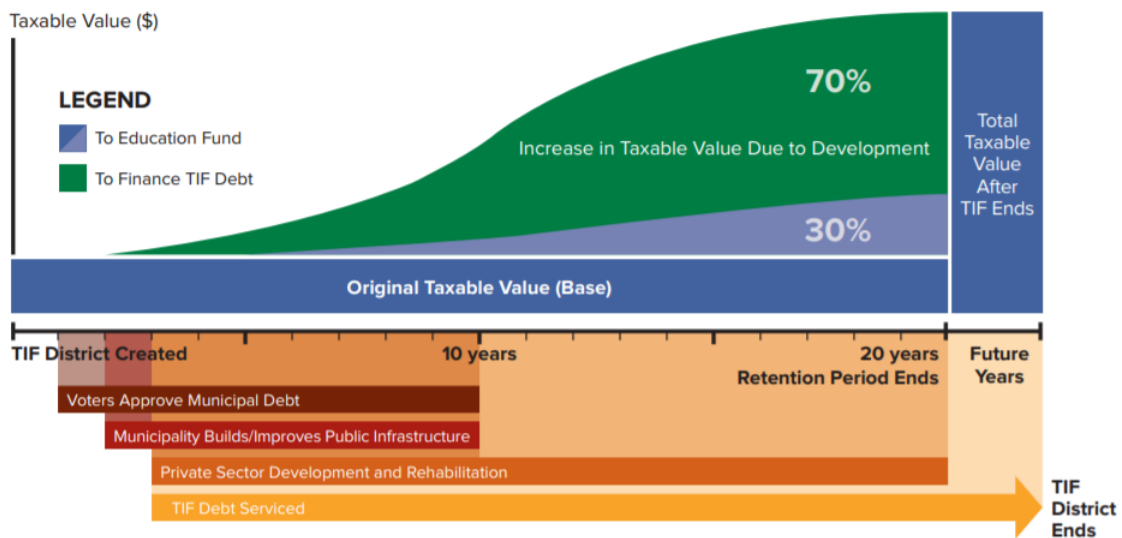
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an excessive one) to connect to the utility, prospective newcomers would choose not to move to Montgomery. Additionally, Montgomery does have a water connection fee which requires new users to retroactively pay bond amounts missed in previous cycles. If this policy is carried over, it could drive up sewer impact fees even more and end up acting as legitimate discouragement for any potential influx of businesses or residences within the community.

### 6. Tax Increment Financing

Tax Increment Financing, commonly referred to as TIF, is a means by which municipalities within Vermont can finance infrastructure development. Municipalities can create a TIF District prior to taking on municipal bonds or other debt to subsidize public infrastructure within the district. This investment is meant to stimulate private development or redevelopment in the district. The private development increases the value of the Total Municipal Grand List and generates increased property tax revenue which can be put towards paying off the municipal debt. Only the revenue from the increase in taxable property value after a TIF District is created can be put towards paying off the municipal debt, not the tax revenue from the total property value.

Municipalities can choose to utilize Education Property Tax revenue for repayment of the municipal debt by seeking approval from the Vermont Economic Progress Council (VEPC). The VEPC may approve no more than six new TIF Districts (limit of two per county). This allows the municipality to gain access to up to 70% of the incremental Education Property Tax revenue for debt repayment while at least 30% is retained by the state. A TIF District can retain funds from Education Property Tax revenue for up to 20 years after its creation, but beyond 20 years the Education Fund receives the entirety of that revenue in perpetuity. The TIF District can be retired when the incurred municipal debt is retired. Figure 2, shown below, illustrates the timeline and revenue distribution of a State-approved TIF District.



**Figure 2:** Timeline and revenue distribution of TIF loan repayment alternative



## Town of Montgomery, Vermont – Wastewater Implementation – Report of Revenue Options for Loan Repayment

If a municipality chooses not to seek VEPC approval, it can still create a TIF District and must pledge at least 85% of incremental municipal property taxes to paying off the TIF debt. Even if the municipality does receive VEPC approval it can still allocate over 85% revenue from the incremental municipal property taxes in addition to the 70% from the Education Property Tax revenue. TIF is credited with assisting in economic expansion in St. Albans and Winooski.

Conventional TIF Districts have been used by some of Vermont's larger communities, like Burlington, South Burlington and St. Albans to fund community projects. However, the existing TIF program requires too much local administrative effort for smaller communities like Montgomery to implement. In the March 27, 2020 news conference, Governor Phil Scott proposed the Project-Based TIF tool to give smaller Towns and Villages an infrastructure financing method to spark economic growth in rural Vermont. Like Conventional TIF, the Project-Based TIF uses increased tax revenue from new land development to pay off the infrastructure project debt with revenue that would not exist without the new land development investment.

The Project-Based TIF concept was proposed in the Vermont legislature in 2020 but did not advance due to the COVID-19 pandemic priorities. It is, however, currently being considered in the 2021 legislative session. The Town should continue to follow the Project-Based TIF legislation as it is considered in the legislature.

### 6.1 Conclusion

Tax Increment Financing is another method allowing municipalities to fund public infrastructure projects. Conventional TIF is typically considered to be too burdensome for small communities like Montgomery to implement. However, the Project-Based TIF, currently being considered in the Vermont Legislature, may provide a simpler TIF-type financing program in the future. Like the Local Option Tax, Project-Based TIF may present an opportunity for Montgomery to generate and collect additional tax revenue to be put towards repaying the USRD WEP Loan for wastewater implementation. Since this is meant to stimulate business development (in addition to residential), it is very difficult to project potential revenue generation from Tax Increment Financing. Much of the potential benefit provided by a TIF could also be realized through implementation of a Sewer Benefit Assessment, which would present a lower level of risk for funding and require less administrative effort. While Conventional TIF may not be the best option for Montgomery, Project-Based TIF may be a good alternative in the future, and it is recommended that the Town monitor its status in the Vermont Legislature for potential future implementation.

### 6.2 Advantages and Disadvantages

A primary benefit of utilizing Tax Increment Financing is its potential to catalyze growth and development within Montgomery and directly reap the rewards of such growth. Business and residential development increase total property value, which leads to increasing property tax revenue generation for use in repayment of the USDA RD WEP Loan. This revenue generation would theoretically increase annually over the lifetime of the TIF District as the Municipal Grand List Total continues to increase over its initial value.

While Tax Increment Financing can be used to fund public infrastructure projects for stimulation of business and residential development, there is no guarantee of any such development, though municipalities will often sign agreements with prospective developers prior to establishment of a TIF District to ensure revenue generation. Additionally, even if Montgomery pursues other funding alternatives, wastewater infrastructure would still be developed, and it is specifically the infrastructure development that would act as the catalyst for that growth. In other words, Montgomery is likely to experience the same growth development whether or not the municipality decides to implement Tax Increment Financing. Another potential drawback to implementing a TIF District is the fact that Montgomery will not be able to receive any funding after 20 years. Given the expected 30-year repayment period, the municipality would not be eligible to receive any Education Property Tax revenue for the final 10 years of the loan, though Montgomery would still be able to generate revenue through municipal property taxes. This would require the community to identify alternative funding sources in the future to make up for the lost revenue generation.

## 7. Conclusions and Recommendations

Five options for USDA RD WEP loan repayment were investigated and potential revenue values, advantages and disadvantages and risks were described. Funding alternatives include the following: Sewer Bond Charge, Sewer Benefit Assessment, Local Option Tax, Impact Fees, and Tax Increment Financing. Based on initial discussions with the Town, the entirety of the approximate \$195,000 annual USDA RD WEP Loan payment can be covered by the Sewer Bond Charge, Sewer Benefit Assessment, and Local Option Tax, as illustrated in Table 9, shown below.

*Table 9: Recommended funding approach for repayment of USDA RD WEP Loan*

Funding Source	Approximate Annual Contribution
Add Sewer Bond Charge (Water Rate Increase)	\$60,000
Sewer Benefit Assessment	\$99,376
Local Option Tax	\$35,957
Impact Fee	\$0
Tax Increment Financing	\$0
<b>Total:</b>	<b>\$195,332</b>
<b>Required Annual USDA RD WEP Loan Payment Needed -</b>	
<b>Total:</b>	<b>\$194,854</b>

This approach would generate revenue from each funding option as is outlined in their respective Report sections. This relies primarily on the Sewer Bond Charge and Sewer Benefit Assessment, both of which are lower-risk funding options. The approach would generate the remainder of the necessary revenue from the Local Option Tax, which, while presenting some risk, is less likely to vary too much in a typical year and is anticipated to gradually increase long-term if wastewater implementation spurs growth in Montgomery. This also does not rely on either the Impact Fees or

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Tax Increment Financing, both of which present higher risk and uncertainty surrounding revenue generation from year-to-year.

It is recommended that the Town complete the following:

1. Consult with Town Council regarding integration of the Sewer Bond Charge, Sewer Benefit Assessment and Local Option Tax into the USDA RD WEP Loan repayment plan to ensure that these three potential loan repayment options meet the USDA RD WEP Loan terms and can be legally and practically administered by the Town. Consult with Town Council regarding future integration of the Impact Fee into loan repayment.
2. Consult with the USDA RD WEP Program to ensure the proposed USDA RD WEP Loan repayment options meet the Loan terms.
3. Monitor and contribute to the legislative development of the Project-Based Tax Increment Financing (TIF) program and consult with Town Council regarding integration of the Project-Based TIF into loan repayment in the future.