

Impact of Development on Property Taxes

By **Claude R. Pellegrino, Chairman of the Sprague Board of Finance**

I presented this report to the Sprague Board of Finance at our November 17, 2005 meeting. The basis for my report was to show the difficulty that the Board and the Town faces in keeping property taxes from increasing. I explained to the Board that as a small town, Sprague cannot achieve property tax reduction or stabilization with any degree of permanency and remain principally a residential community. By using straightforward examples, I showed that the required type, frequency, and size of development make it highly unlikely that it can be done.

First, I will provide you with the same background statistics on development that I gave to the Board. Many studies have been done across the United States with the goal of determining the dollar cost of development. These costs of community services studies, as they are called, have shown that residential development costs a town between \$1.15 and \$1.50 per dollar of revenue received. This, of course, means that residential development results in higher taxes. Furthermore, this was the outcome in each and every study with no exceptions.

Commercial & industrial development costs a town between 35 and 65 cents per dollar of revenue received and, therefore, has the potential to decrease taxes. Likewise farmland & open space which costs a town between 30 and 50 cents has the potential to decrease taxes as well.

Clearly, residential development, with costs uniformly above a dollar for each dollar of revenue, can be ruled out as way to lower taxes. Commercial & industrial development (or simply referred to here as commercial development) would seem to be an answer for lower taxes. My report does not support this conclusion as the necessary frequency and size of the commercial development make it difficult to attain and sustain. I can explain this best by a series of examples.

The first example determines the amount of the grand list that produces one mill's worth of revenue. This is found by dividing the grand list by the mill rate. In Sprague for fiscal year 2005-06, each \$8.5 million of grand list produces one mill's worth of revenues. This calculation should provide you with a sense of scale to the changes in the grand list necessary to have a noticeable impact on the mill rate.

A slightly different example calculates the change in the grand list necessary to produce a one mill reduction in property taxes assuming no change in the Town's revenue requirements and no change in its expense needs as well. It takes an \$8.9 million increase in the grand list's assessed value (or a \$12.7 million increase in property market value) to reduce the mill rate by one with other factors remaining the same.

Assuming no expenses though is unrealistic. As studies have shown, it takes on average 50 cents of municipal expenses to support a dollar of revenues from commercial development. For Sprague, it will take an increase of \$17.8 million of assessed value in the grand list from commercial development (or \$25.4 million of market value) to reduce the mill rate by one assuming 50 cents of expense per dollar of revenue and other factors remaining the same.

This past spring the Norwich Bulletin reported that the Lowe's Regional Distribution Center (RDC) in Plainfield had an assessed value of \$36 million. This facility is approximately 1.3 million-square-feet which is the equivalent of 28 football fields under one roof and is built on a 215-acre site. Next year, due to tax concessions, the assessed value for tax purposes will be 60% of that or \$21.6 million. In Sprague, an enterprise the size of a Lowe's RDC and under similar tax concessions would impact the tax base by roughly one mill.

For the next example, instead of solving for the change in the grand list, we compute the change in the mill rate and provide the other necessary information. In Sprague, if 20 new commercial enterprises are added, say, to the Baltic Village and each added \$300,000 to the market value of its property, plus the town added a trooper at the cost of \$90,000 to increase security in the Village, then the net effect on the mill rate is essentially zero. This shows that the tax revenues from small scale commercial development are easily offset by relatively small changes in the expense base. The 50 cents on average expense versus a dollar of tax revenue can easily jump to a dollar or more of expense thus negating any tax benefits.

As an economically "distressed community", one of Sprague's issues is having a large component of its revenue source as grant money. Since grant monies from the State, such as the education cost sharing (ECS), are growing at neither the rate of need nor the rate of inflation, financial pressure is put on us via increased taxes to fund the gap.

In Sprague, education expenditures are currently running 72% of the Town's total expenditures with general government expenditures at 28%. On the revenue side, grants contribute 35%, taxes 60%, with local and other revenues of 5%. If education costs continue to grow faster than inflation, say 5%, and all other revenues and expenses grow at the rate of inflation, say 3%, except for State grants, say 2%, then the net effect is nearly a 6% increase in taxes! Consequently, there is an approximately 1.4 mills per year increase built into Sprague's revenue and expense structure! This would require adding \$25.3 million of commercial development (assuming 50 cents of expense per dollar of revenue) just to keep taxes flat for one year!

To keep taxes flat year after year the amount of commercial development must grow from \$25.3 million year after year. At some point with all that commercial development (if it were achievable), home valuations probably would stop keeping pace with comparable homes in more residential communities. This would make keeping taxes flat even more problematic.

From the examples presented above, it should be clear that reducing property taxes or holding them flat is very difficult indeed. As has been shown, the size and frequency of the required commercial development makes it impractical for Sprague to achieve property tax reduction or stabilization. Only large scale development can have a reductive impact on property taxes, but once on the grand list property taxes will go up from there while property valuations may go down from there.

The effects of commercial development must be carefully thought through, planned for, and measured against desired results. Only then can Sprague have a chance of achieving for its residents the economic benefits of commerce while retaining the financial benefits of higher property valuations and paced property tax increases.