

REQUEST FOR CITY COUNCIL CONSIDERATION

Meeting Date: March 5, 2007

Agenda Item: 7B	Prepared By: A. William Moss, City Manager Date: February 27, 2007
Agenda Section: Business: Discussion	
Subject: STRP Financing Option - \$10,000 CAP And Property Tax	Department: City Council

Chairwoman DiSciullo seeks Council agreement to discuss another option to finance the Septic Tank Replacement Program. This option will provide for a \$10,000 assessment for all properties in the Septic Tank Replacement Program with the balance to be funded by the issuance of General Obligation Bonds with repayments through revenues derived from the property tax.

EXECUTIVE SUMMARY:

The proposed option will limit the STRP assessment to \$10,000 per property (ERC). The balance of the STRP will be funded by the issuance of a General Obligation Bonds in the amount of \$88.6 million. A General Obligation Bond issue requires approval of the electorate by referendum. The electorate may also need to approve an exception to the spending cap provisions of the City Charter in the same referendum.

The STRP payment options for property owners will be as previously established. The \$10,000 is the cash payment, the assessment may be paid in equal installments over 20 years (about \$930 per year), or payments may be deferred for 20 years or upon transfer of ownership.

A property tax increase of \$0.522 per \$1,000 of assessed value is required to pay the annual General Obligation Bond principle and interest over 25 years. The tax increase for a property with a taxable value of \$500,000 is \$261 per year.

Alternative STRP options discussed to date anticipate an increase in the water and sewer General Rate Base (month bills for all utility customers) of about 16%. For a single-family residential property with a water consumption of 25,000 gallons per month, the annual bill for water and sewer will increase by \$291.

For many property owners, the proposed increase in the property tax is a less expensive alternative than the proposed increases in the utility rate base.

If approved by Resolution on March 19th or April 9th, a mail ballot election may be scheduled near the end of June.

The referendum will not determine whether to proceed with the Septic Tank Replacement Program. The Program will proceed. The referendum will determine whether a specific financing option will be used to reduce the assessments to properties subject to the STRP while distributing the balance of the cost to all property owners.

BACKGROUND:

City Council established the STRP to provide sanitary sewer lines to the unsewered areas of the City. The Program provides for the recovery of the cost to provide sanitary sewer lines and expand the capacity of the Wastewater Treatment Plant through a special assessment to property owners receiving the new service. The first two assessment areas were established in 2005 with completion of construction at the end of 2006. The next five assessment areas for Year 2 of the Program were established in September of 2006. Contracts for Year 2 construction have been awarded with construction to begin after April 9, 2007. City Council adopted the Preliminary Assessment Resolutions for two additional districts for Year 3 of the Program on February 20, 2007.

Over the past year City Council has modified the STRP seeking to lower the assessment to property owners or to otherwise provide favorable attributes. These policy decisions are summarized as follows:

- Commitment to apply anticipated grants of \$5 million to the STRP to reduce assessment costs. This reduced assessments by about \$1,000.
- By Ordinance No. 06-16 dated November 6, 2006, City Council increased the sewer impact fee to \$4,610 so that all new development will pay the same impact fee as the capacity cost portion of the assessment for each existing property in the assessment areas. This action reduced assessments by about \$700.
- On October 9, 2006 City Council agreed to remove the cost of street resurfacing associated with the new sewer line construction. The cost of street resurfacing was shifted to the Utility Base Rate (monthly utility bills) with the resulting increase of 8% in the Utility Base Rate over four years. The first phase of this increase was approved on January 22, 2007 by Resolution No. 07-04. The reduction in assessments to property owners is \$1,500 on average.
- On September 5, 2006, by Resolution No. 06-46 City Council established a Voluntary Assessment Program. The program enabled property owners to lock in the 2006 estimated sewer construction cost in order to be protected from future construction cost increases that may be associated with their assessment area. In December 2006 letters were sent to 4,000 property owners to offer the Voluntary Assessment Program option. Approximately 1,200 property owners expressed an interest in participation.
- On February 20, 2007, by Resolution No. 07-08, City Council approved the form of contract necessary to implement the Voluntary Assessment Program for each property owner. Mail out of the contracts to the 1,200 property owners is delayed pending a decision on the proposed financing option described below.
- On February 14, 2007 City Council met in a workshop session to discuss the possibility of removing costs of wastewater system upgrades from the Septic Tank Replacement Program. The purpose of the meeting was to consider ways to allow monthly bills of the new customers in the STRP to avoid funding Wastewater Treatment Plant upgrades through the monthly utility bill. Staff was asked by the Chair to provide funding alternatives to meet debt service requirements. City Council was presented alternatives that included increasing the Utility Rate Base, implementation of a 5% Public Service Tax, and implementation of an ad valorem tax at the rate of .225 mils to replace the \$4,610 capacity assessment. As options were considered, City Council focused on the net present value of the portion of the monthly utility bill that could be attributed to the sewer plant upgrades. Using this methodology, Council reached a consensus that \$2,758 be removed from the STRP assessment to offset the cost of wastewater system upgrades. In order to offset the revenue reduction, the Utility

Rate Base would need to increase by approximately 8%. City Council agreed to consider formal adoption of this policy at a future meeting with the subsequent approval of a Utility Base Rate increase following the required public hearing.

Presented for City Council consideration is another STRP financing option. The proposed option is to:

- Cap the sewer assessment to every property at \$10,000.
- Shift the balance of the cost for sanitary sewer line construction to the property tax paid by all City property owners.
- Hold a mail ballot referendum in June seeking voter approval to issue \$88.6 million in General Obligation Bonds (and amending the Spending Cap provisions of the City Charter, if required) to fund the balance of the sanitary sewer line construction.

Acceptance of this proposal would place the above referenced Voluntary Assessment Program on hold until after the referendum. If the referendum is approved, there is no need to have the Voluntary Assessment Program since STRP property owners will pay only \$10,000, regardless of the actual construction costs. If the referendum proposal is accepted by City Council, the 1,200 property owners who have expressed interest in the Voluntary Assessment Program will be notified by letter that the option is placed on hold pending the result of the referendum.

Furthermore, there is no need to allocate the street resurfacing cost from the sewer construction assessment to the General Utility Rate Base (8% increase to monthly utility bills); although the first phased increase at 2% is in effect. And, if the referendum is approved, there is no reason to implement another 8% General Utility Base Rate increase to offset the cost of the upgrades to the existing Wastewater Treatment Plant.

This proposal, if approved by the electorate, will increase property taxes for all property owners while eliminating proposed increases in monthly utility bills to fund the STRP. The payment options for the \$10,000 assessment would remain the same [\$10,000 cash payment, payment over 20 years in equal annual installments, (about \$920 per year), or deferral of all payments for 20 years or upon transfer of property ownership, based on a \$10,636 assessment that includes financing costs].

A spreadsheet was developed (see Exhibit "A") to determine the amount of the required General Obligation Bonds. The assumptions used to calculate the estimated construction costs are critical to this analysis.

The Project Engineer, Boyle and Associates, generally used the unit prices submitted by DN Higgins for the recently awarded contracts for the North Barfield, North Marco, and the Old Marco/Port Marco Assessment Areas. They were asked to calculate an inflation index of 3% for future assessment areas.

The required bond issue to fund the balance of the STRP through the property tax will vary significantly, based on the assumption used to calculate the construction costs for future districts. The 3% inflation index may be too low. It is well below recent annual increases in construction costs. If future construction exceeds the construction estimates shown on Exhibit "A," the balance must be recovered through an increase in the Utility Rate Base. Using a higher inflation index, of course, increases the required amount of the bond issue and subsequent property tax. A more conservative approach would be to use a 6% inflation index.

After the payment of \$10,000 for each of the 5,653 lots in the STRP, and adding required bond issuance costs and bond reserve, the estimated General Obligation Bond issue is \$86 million, based on 3% inflationary index.

To determine the increase in property tax, one may apply the rate of \$0.522 for each \$1,000 of assessed value. The estimated annual property tax required to pay the bond principal and interest on a 25-year General Obligation Bond is as follows:

\$ 300,000 assessed value	\$157
500,000 assessed Value	\$261
750,000 assessed value	\$392
1,000,000 assessed value	\$522

Pending options to this property tax proposal may increase the Utility Rate Base by approximately 16%. While it was not anticipated that the full 16% would be applicable throughout a 25-year period, for the purpose of this illustration, it is assumed that the increase will remain in place for 25 years. The increase in annual utility bills under the option discussed on February 14th is as follows:

20,000 Gal. Water Usage/Month	\$20.82 = \$250 year
25,000 Gal. Water Usage/Month	\$24.27 = \$291 year
30,000 Gal. Water Usage/Month	\$27.96 = \$336 year
50,000 Gal. Water Usage/Month	\$47.18 = \$566 year

Single-family residence water and sewer bill, Tier 1 lot size – up to 9,000 square feet.

For single-family residential property owners with a taxable assessed value of \$500,000 or less, the property tax increase is more likely a better option than a utility rate increase of 16%. This may also be the case with higher valued properties depending on water consumption.

Reasons that one may support this proposal include the following:

- STRP properties will pay a flat rate of \$10,000 for their assessment.
- STRP properties will pay the same impact fee/capacity cost (\$4,610) as other properties that are not within the STRP. The balance (\$5,390) will be used to fund construction of the sanitary sewer lines in the assessment areas.
- The balance of costs for sanitary sewer line construction will be paid by all City property owners, including those in the STRP.
- Anticipated Utility Base Rate increase paid by all utility customers will be eliminated.
- General Obligation Bonds may attain a lower interest rate because of the pledge of the full faith and credit of the City. Furthermore, a state revolving loan at even lower interest rates may be possible.
- All registered voters will have the opportunity to voice their support or objection to the proposal through a mail ballot referendum.
- The assessment payment options (reduction for cash payment, equal payments over 20 years, deferral for 20 years) may continue.
- The entire community is contributing to a policy designed to ensure protection of water quality in and around Marco Island.
- The anticipated \$5 million in grants will be used to offset the costs of the STRP.
- The \$10,000 assessment may gain greater acceptance by those property owners subject to the STRP.

- Property taxes may be used as a federal tax deduction, while utility bills generally cannot be deducted.

Disadvantages to the proposal include the following:

- Property owners may perceive that they are paying higher taxes to subsidize other property owners who have no investment in the sewer collection system.
- Property owners currently connected to the central collection system may believe that they have paid their fair share and should not be required to pay higher taxes to offset the cost for other property owners.
- Two properties may have the same size lot and the same size structure. However, because of the “Save our Homes” provision, one property owner could pay substantially more in property taxes than the other property owner, while receiving exactly the same benefit.
- Property owners who have heretofore remained uninvolved in the STRP policy process may now oppose the STRP if they have to share the costs through an increase in property taxes.
- Opponents may frame the referendum to their advantage while confusing the question and purpose.

City Council should adopt a “Plan B” in the event that the referendum fails. Plan B could be the February 14th policy discussed by City Council that would further lower assessments by about \$2,758, keeping other reductions in tact, and increasing the Utility Rate Base by about 16%. This option is also included in this Agenda.

The Voluntary Assessment Program will be put on hold until this decision is made.

Should City council elect to pursue the referendum option, consideration should include:

- Whether City Council is committed to the option. Without Council leadership, it is highly probable that other organized efforts will take the initiative to defeat the proposal. A divided Council will convey a contradictory message to the electorate.
- The cost of a mail ballot referendum is about \$30,000. At least another \$20 - 30,000 should be planned for public education.
- A majority of your management’s time over the next three months will be dedicated to this initiative.
- Rather than bringing the community together, this initiative may result in a backlash among the many who thus far have been uninvolved.

Staff has observed that some citizens are urging a citywide assessment program that would equally assess all properties. The purported purpose is to resolve inequities in the property tax system. Staff and legal counsel agree that a citywide assessment program for the STRP would not meet the fair apportionment test.

RECOMMENDED ACTION:

Discussion and further direction.

Reviewed by Department Director

Reviewed by City Manager

Council Action: Motion by:

Second by: