

Rational for Borrowing to Fund Specific Capital Requests

2024 Montague Annual Town Meeting

Capital Projects and Town Capital Stabilization

Montague has made tremendous financial strides in recent years, allowing it to execute numerous timely and often overdue capital projects and equipment purchases. Capital project funding in particular has been enhanced by new revenue associated with the Cannabis Excise Tax, Sandy Lane solar lease, and one-time windfalls due to excess Free Cash and the release of \$800,000 in Assessor's Overlay funds following settlement of 5 years of contested assessments with FirstLight Power in 2019.

As one-time or potentially time-limited sources, the above sources have been channeled into the Town's Capital Stabilization (TCS) Fund resulting in rapid accumulation. At the same time the Town has leveraged federal ARPA and grant funds to address numerous Town capital project and equipment needs, while largely avoiding use of the TCS Fund. Thoughtful management has resulted in an historically robust TCS Fund balance of \$2,237,446 as we arrive at the May 4, 2024 Town Meeting.

As currently proposed, the ATM motions suggest use of TCS funding for two articles, totaling \$228,500 (the Library Design Study and the Sewer Manhole/Pipe Lining Project). If funded, the TCS balance would be \$2,008,946. There are three other General Fund capital requests on the warrant totaling \$836,500 that are proposed for borrowing (below) and there has been discussion as to whether they should instead be funded by TCS. This is a viable option and would leave the TSC Fund balance at \$1,172,446, but it may not be a sustainable long-term capital funding strategy.

Project	Cost	Suggested Financing Term
Town Hall Parking Lot	296,000	
10-Wheel Dump Truck	365,000	10-15 years
Hillcrest Paving/Sidewalks	175,500	
Total	\$836,500	

While Town finances remain on solid footing, cannabis revenues are on a steep decline and ARPA funds are near wholly allocated. The Six-Year capital plan shows substantial ongoing capital needs and even without implementing all required investments a "pay as you go" (PAYGO) approach would quickly erode the TCS Fund balance, which will likely have a replenishment rate between \$200,000 and \$280,000 per year, including its annual allocation from taxation (\$46,761 in FY25). Post-ARPA, the Town will still win grants, but many project types are not readily grant eligible or as flexible as ARPA.

How Do We Become More Sustainable?

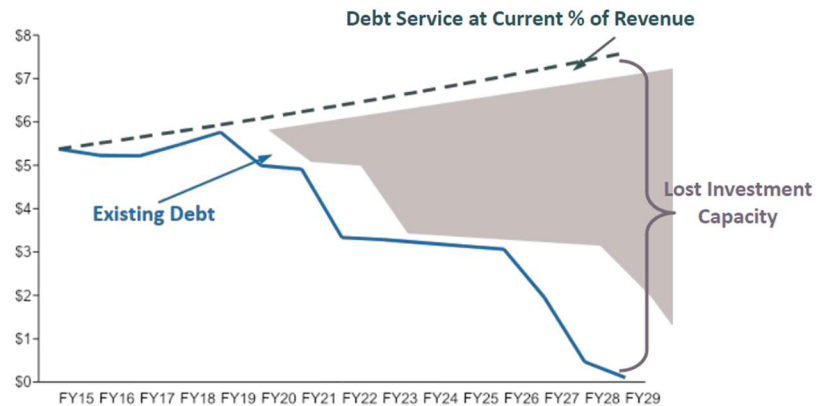
Town facilities, infrastructure, and equipment are in many ways just as important as the people who manage, plan, and provide services; but we have generally only accounted for their related capital costs through Excluded Debt, reserved for major building renovation or replacement projects (DPW, Police, TFHS). The General Fund makes very little use of non-excluded debt, so when the excluded debt is retired, the associated taxation goes away, leaving no funding for ongoing capital needs.

To support adequate capital investment, the MA Division of Local Services recommends establishing a predictable level of debt in the operating budget as a [best practice in municipal budgeting](#).

Maintain a Steady Balance of Capital Investment

- Because of critical nature and large financial obligation, municipalities should re-use debt service runoff
 - Don't use it for "operating budget relief"
 - Maintain debt service as a constant percent of revenue

- Lack of reinvestment leads to lost capacity



Montague's Town financial policies – developed with expert technical assistance – recommend we maintain 4% to 6% of the prior year's gross operating revenues (PYGOR) to fund non-excluded debt-financed projects. As these bond issues would often be shorter than those for major building projects, they would "run off" the books more quickly, ultimately resulting in a steady available balance for capital investment.

Once non-excluded debt is built into the budget, through multiple bond issues over several years, there would be an ongoing opportunity to fund new projects with runoff debt capacity. Viewed realistically, 4% of Montague's PYGOR would be \$935,000 in FY25, so this would need to be accomplished incrementally - but progress is achievable over time.

What Happens if We Borrow Now as the Motions Recommend?

As noted above, it's taken several years, favorable circumstances, and financial discipline to position the TCS Fund (and other reserves) as it is today. Borrowing now protects the TCS balance, which provides important long-term financial flexibility. It would require first that the Treasurer issues a Bond Anticipation Note – short term financing on which we pay interest only until we have amassed sufficient borrowing (in excess of \$1M, ideally \$2M+). Initial estimates suggest the carrying cost of the BAN for \$836,500 would be \$40,000 beginning in FY26.

Knowing that the Clean Water Facility is poised to borrow \$283,000 for the Montague Center Pump Station Rehabilitation Project and the Town's [FY24-FY29 Capital Improvement Plan](#) anticipates additional projects in FY26, it is likely that we will be in position to bond by FY27. Staying with the proposed \$836,500 of projects for General Fund borrowing, the cost of carrying that debt for an additional 8 years (retiring it in FY35) would be around \$150,000. These figures reflect conservative estimates of interest rates in the current municipal borrowing environment.

What Happens if We Choose to Use Town Capital Stabilization for these Articles?

The projects would be directly funded, the capital needs of the moment would be met, and – beneficially – we would avoid bonding and interest costs, which can be substantial even when discounting for inflation. This approach is not necessarily a problem today; but it delays progression toward a long-term strategy that leverages debt to create a more sustainable long-term capital funding strategy. A strategy that could continue to pursue PAYGO projects, but would now pair that strategy with dedicated space in our operating budget for non-excluded debt.

The substantial burden of capital articles on TCS developed late in the budget cycle, as the need to purchase the 10-wheel dump truck emerged during the winter and it had been assumed that improvements to the Town Hall parking lot would be grant (CDBG) eligible. With those substantial additions emerging in March, staff felt compelled to accelerate this conversation for the FY25 budget, and the strategy was endorsed by most members of the Finance Committee and Selectboard.

Understanding that this is a somewhat new concept for many, we hope the borrowing motions as written are seriously considered, but also acknowledge that Montague is in a fortunate moment, having some choice now before it commits to this new course, if Town Meeting so decides.

Referenced Links:

DLS Best Practices in Municipal Management:

<https://www.mma.org/resource/municipal-finance-101-budgeting-best-practices/>

Town of Montague Financial Policies (see policy A-2 Capital Planning):

https://montague-ma.gov/files/Montague_Financial_Policies_revision_04-30-24.pdf

Town of Montague Capital Improvements Plan FY24-FY29:

https://montague-ma.gov/files/Capital_Improvement_Plan_FY24_Final.pdf