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COMMENTARY

Special Assessment Bonds Key to Financing Local Infrastructure

By William F. Griffin Jr.

THE MASSACHUSETTS LEGISLATURE CURRENTLY has before it the opportunity to provide municipalities with a local option to approve "special assessment financing" of public infrastructure needed to support private development and to upgrade existing public works facilities. A bill creating Chapter 40T of the General Laws, which I participated in drafting, has recently been reported out favorably by the Joint Committee on Community Development and Small Business, and has received the support of officials in Gov. Deval Patrick's administration, as well as business and community leaders.

Massachusetts communities face difficulties in financing needed public infrastructure and efforts are under way to find a solution to this problem. Chapter 40T would provide the "missing link" enabling our communities to tap into a robust, multibillion-dollar market for investment capital for public infrastructure without placing further stress on scarce municipal resources.

Many desirable private or community development projects must be supported by public infrastructure improvements, such as streets, lighting, storm drainage, water and sewer systems, public transit improvements, public parking, parks and recreational facilities. Municipal resources, however, are limited, and municipalities often are unwilling or unable to allocate scarce tax revenues or increase municipal debt burdens to finance public infrastructure for worthy projects.

Massachusetts has attempted to deal with this problem through a variety of programs, including direct state grants, state tax credits, and the pledging of expected increases in state or local tax revenues to finance bonds for infrastructure improvements. The common thread of all of these programs is that either the state or its municipalities ultimately uses its resources to support private development.

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Chapter 40T is different: it is the "developer pays" option. Experience in dozens of other states has proven that developers are willing to pay for local infrastructure if the terms of financing are favorable enough.

Under Chapter 40T, private developers or community groups may file a petition with the municipality for the establishment of a "development zone" within the municipality. Petitions must have the consent of the owners of 80 percent of the acreage, and 80 percent of the tax parcels, within the development zone, and must include a detailed improvement plan and an estimated budget and timetable for the completion of the public improvements. The petition may or may not seek the establishment of a "local improvement district," a public entity that would construct, finance and maintain the public infrastructure improvements.

The municipality must hold a public hearing on the petition. If the petition is approved by the municipal governing body, then the municipality, MassDevelopment or the local improvement district, as designated in the petition, would adopt an "assessment plan" to impose special betterment assessments on privately owned property within the development zone. These special assessments provide the revenues to support tax-exempt bonds sold to finance the construction of the improvements. MassDevelopment or the local improvement district may issue special assessment bonds to finance the construction of the improvements. Public improvements in a development zone may be owned only by a public entity.

The great benefit of the Chapter 40T program is that, unlike other methods of financing public infrastructure, the entire cost of construction, financing and maintaining the improvements is borne by the property owners in the development zone, not by the municipality or the state.

There is nothing novel or experimental about special assessment financing. It has been employed for years in more than 35 states, including California, Florida, Illinois and Maryland. The 2002 U.S. Census identifies some 35,000 special district governments in the nation. According to The Bond Buyer newspaper, Florida has sold $14.8 billion in special assessment bonds in the last five years and California has sold $6.3 billion in the same period. Banc of America Securities estimates that it will underwrite some $3 billion in special assessment bonds this year alone.

Special assessment financing allows the issuance of tax-exempt revenue bonds to finance infrastructure improvements that are paid by special betterment assessments on privately owned real estate in the development zone. Because these bonds are secured by tax liens on the property, they are high-

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credit, tax-exempt long-term securities and are very attractive to investors. Developers like special assessment bonds because they provide a long-term, low-interest source of funding for pre-construction expenditures, which does not interfere with construction or permanent project financing. The municipality benefits, of course, from enhanced property tax revenues from the project without a reduction of its scarce tax revenues or an increase in its municipal debt burden.

Fueling Growth

The benefits of Chapter 40T include the following:

• Chapter 40T is a local option, not an entitlement – Chapter 40T does not create an entitlement for developers. Under Chapter 40T, it is entirely optional with the municipality, which may elect at its sole discretion whether to take advantage of its provisions in any given case, and to condition its approval of a special assessment project as it deems appropriate.

• Chapter 40T does not add debt burdens to municipalities – Under Chapter 40T, the property owners in the development zone, not the municipality, have the obligation to construct the new public infrastructure improvements. The costs of the infrastructure, and the debt service on the associated bonds, are paid by special betterment assessments on the privately owned real property in the development zone. By law, the state and its municipalities have no liability on the special assessment bonds, which are "revenue bonds" secured only by the special assessments on the property in the development zone. In the case of a default on the bonds, the bondholders, not the state or the municipality, bear the entire risk of the investment.

• Chapter 40T enhances municipal tax revenues – The municipality in which a development zone is created benefits from enhanced tax revenues from new construction added to the municipal tax base. Of course, new development is not costless, and may increase municipal expenses, including fire and police protection and, for residential developments, costs of public education. However, these are all factors that a municipality can evaluate in deciding whether to approve an improvement project.

• Chapter 40T does not affect zoning or land-use regulation – Private development in a Chapter 40T development zone is subject to all zoning and land-use regulations applicable to conventional development projects.

• Chapter 40T can be used to finance municipal improvement projects – Chapter 40T may be used to finance community development projects as well as to support private development. For example, neighborhoods needing upgrades to sewage disposal systems, roads or other public works may petition the municipality to fund the improvements by special assessments under Chapter 40T rather than by municipal tax revenues or general obligation bonds. Or business owners in a city with a downtown area with inadequate parking can petition the municipality to construct a new parking garage financed by assessments against the downtown property owners.

• Special assessment bonds may be used only for public infrastructure – Under Chapter 40T, all proceeds of special assessment bonds must be used for public infrastructure improvements and costs of issuance. Under Chapter 40T, and under Federal income tax rules as well, all project infrastructure must be owned by public entities and bond proceeds may not provide property used for private activities.

Chapter 40T embodies a proven financing program which has been successfully used in many other states to attract billions of dollars of investment capital for public infrastructure. It is a local option, not an entitlement, which allows each municipality to choose the rate of economic growth which best fits its needs. No state or local general tax revenues or credit are involved. Chapter 40T promises to be the rocket fuel needed to propel economic growth in Massachusetts. ■