Review of the Fiscal Impact Analysis for Proposed Trappe East Development

Prepared for Friends of Trappe

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Overview

This is a review of the study, ***The Fiscal, Economic and Capital Asset Impact of the Proposed Trappe East Project on the Town of Trappe, Maryland***, by Urban Analytics, Inc. of Alexandria, Virginia (August 2004). The review was conducted on behalf of Friends of Trappe in order to evaluate the validity of the study's findings regarding the fiscal impacts of the proposed Trappe East development.

The Trappe Fiscal Impact Analysis (FIA) included analysis of three impact areas, labeled in the study as follows:

1. Fiscal Impact
2. Economic Impact
3. Capital Asset Impact

Typically, #1 (fiscal impact) and #3 (capital asset impact) are both part of the fiscal impacts on the public sector (local government and taxpayers) and are considered together in a fiscal impact analysis. The second area, economic impact, is an evaluation of private sector impacts (spending, wages and jobs) and is not technically part of a fiscal impact study. While fiscal impacts are the primary concern of this review, a brief evaluation of the economic impact section is included at the end.

The proposed action considered in the Trappe East FIA is the development of 858 acres of land (newly annexed to the Town of Trappe) with 2,262 housing units and 245,000 square feet of commercial construction. The development would result in an estimated increase in town population of 5,384 people (from 1,150 to 6,534 people).

The Trappe East FIA concludes that this development will result in a net surplus (fiscal benefit) to the Town of $196,000 per year. This is a relatively slim margin of benefit, given the $3 million in costs estimated. If costs end up being just 6.5% higher than predicted in the analysis, benefits will disappear.

Under "capital asset impact" the study finds that the Town will need to spend $6,245,000 for additional capital assets (public facilities) to serve the new population. If these costs are distributed among just the 2,262 new residential units, the cost would average only $2,761 per unit. This figure appears to be far too low to accurately reflect the full cost of providing a modern level of urban services to residential development. For example, the cost of providing new sewer mains and sewage treatment facilities alone could cost more than $2,500 per new dwelling unit.

The Relationship between Growth and Taxes

The study mentions two relationships between urban growth and local taxes and services. First, there is an "economy of scale" associated with growth whereby a city can provide service more economically to a larger population than a smaller population. Second, there is an increasing level of complexity involved in serving larger populations, as more varied services are required and level-of-service standards are upgraded. These two effects work against each other, one decreasing cost of services on a per capita basis, and the other increasing it. A third relationship in urban growth is the increasing cost of land and labor associated with larger and faster growing cities. And finally, new growth creates a demand for new and expanded public facilities that would otherwise not be needed.

Since these relationships are complex, it is helpful to look at empirical studies that have examined the overall effect of urban growth on local taxes and services for cities and counties around the country. Numerous studies have shown that residential development tends to represent a net fiscal drain to the local government.[1] [2] [3] [4] [5] [6] [7] [8] [9] [10] [11] Studies that looked at the correlation between urban growth and local taxes found the following relationships:

1. Local population growth tends to increase the residential tax burden (measured as a percent of residential personal income).[12] [13]
2. Areas with the most rapid growth have the greatest tax increases.[14] [15] [16]
3. Fast-growing areas that do not increase taxes will tend to see a reduction in public services.[17]
4. Bigger cities tend to have higher taxes than smaller cities.[18]

These studies indicate that cities are unlikely to see real net fiscal benefits from growth. Instead, the likely outcome will be higher costs, resulting in either higher taxes or reduced services or both. Furthermore, these outcomes are likely to be amplified by the rapid pace and large scale of the proposed Trappe East development.

The best explanation for the negative fiscal impacts from urban growth is high cost of the capital facilities and infrastructure new growth requires. As stated by former Maryland Governor Parris Glendening in 1997, ***"Every new classroom costs $90,000. Every mile of new sewer line costs roughly $200,000. And every single lane-mile of new road costs at least $4 million."***[19]

The findings from the Trappe East FIA study (that the proposed development will generate a net fiscal surplus) are inconsistent with the research literature. This raises questions as to whether the methodology adequately evaluated impacts, and in particular, costs associated with the proposed development.

What are Fiscal Impacts?

A fiscal impact analysis evaluates the financial costs and benefits of a particular action or decision to a local government, or to the public sector in general. The Trappe FIA looked only at the impacts on the Town of Trappe's government. In so doing, the study excluded impacts to other local government entities, such as the county and state. This is often the case with fiscal impact studies commissioned by a single government entity. However, the broader public policy question is: How will this action or decision affect local taxpayers? This broader question allows elected officials to determine whether the proposed action will affect local tax rates or the quality of local services. This question tends to be the one of most interest to local voters and the public in general. The question is also identified as an issue in the town's "Public Services" element of the Trappe 2002 Comprehensive Plan.

Assessment of Costs Associated with Trappe East

While the tax revenues from new development can be estimated in a fairly straightforward manner, it is more difficult to calculate the costs. This disparity plagues fiscal impact studies and often results in accurately stated revenues, but understated costs. This appears to be the case in the Trappe East FIA.

In order to estimate the fiscal impacts of proposed growth, the study uses averaged revenues and averaged costs based on five towns in Talbot County. This method does not accurately reflect the growth-related costs of the planned Trappe East development for a number of reasons discussed below.

- **Average Town Costs do not Reflect Growth Costs**

The impacts of Trappe East development are estimated in the FIA by using an aggregated average of five local towns (Trappe, St. Michael's, Oxford, Denton, and Easton). While it might be appropriate to compare the balance sheets of these towns for some purposes, it is not the correct method for estimating growth-related fiscal impacts.

A town's revenues and expenses are derived from the entire town, not just the growing portions of the town. Therefore it is incorrect to simply directly apply data from the five towns to predict the impacts of growth in Trappe. New growth creates certain unique costs that are different than those of the established development and are usually much higher. In particular, new growth requires costly new public infrastructure, including streets, sewer capacity, water supply, stormwater system, schools, libraries, police and fire protection facilities, etcetera (see Table 1).

Table 1
Growth-Related Capital Costs for
Public Facilities/Infrastructure

- School Facilities (K-12)
- Sanitary Sewer System
- Storm Drainage System
- Transportation System
- Water Service Facilities
- Fire Protection Facilities
- Parkland, Open Space & Recreation Facilities
- Library Facilities
- Police Facilities
- Corrections and Jail Facilities
- General Government Facilities
- Electric Power Generation and Distribution
- Natural Gas Distribution System
- Solid Waste Disposal Facilities
- Cable and Telecommunications Systems

- **The Proposed Growth of Trappe will Greatly Exceed that of Local Towns**

It is not reasonable to use the fiscal cash flows of slow-growing towns to estimate the fiscal impacts of growth on a fast-growing town. As mentioned above, growth creates unique costs. The more growth a town has, the more of these costs it will incur. The proposed Trappe East development will cause the town to grow by 568 percent. If this growth is assumed to occur over the next 10 years, it will result in an annual growth rate in Trappe of 19% per year. As shown in Table 2, towns in Talbot County have been growing at an average rate of about 1.8% per year. Under the proposed development, Trappe would grow 10 times faster than the average for towns in the county and will experience extraordinarily high growth-related costs that are not accurately represented in the Trappe FIA study.

Table 2
Average Growth Rates of Talbot County Towns, 1990 to 2000

	1990 Pop	2000 Pop	Average Annual Growth Rate	Period Growth Rate
Talbot County Population	30,549	33,812	1.02%	10.68%
Town of Easton	9,379	11,699	2.24%	24.74%
Town of St. Michaels	1,314	1,183	-1.04%	-9.91%
Town of Oxford	703	778	1.02%	10.68%
Town of Trappe	978	1,150	1.63%	17.60%
Town of Queen Anne (pt)	122	68	-5.75%	-44.66%
Total Incorporated Towns	**12,464**	**14,911**	**1.81%**	**19.63%**
Unincorporated Area of County	18,085	18,901	0.44%	4.51%

Source: Calculated from ***Talbot County Comprehensive Plan*** (February 2005)

- **Historic Costs do not Accurately Reflect Current Costs**

To determine the costs for new public facilities to serve the Trappe East development, the Trappe East FIA uses historic and depreciated costs for existing facilities in five local towns. These values represent the actual historic costs paid when the facilities were built, less depreciation. This method leads to an extreme understatement of the cost of building new facilities today. The proper value to use is the cost to build these same facilities today, or the full "replacement value" of the facilities.

The Trappe FIA calculates that the proposed Trappe East development will require about $6 million in infrastructure. The fact that this is unrealistically low is illustrated by the $60 million in infrastructure construction bonding currently being proposed by the Town to serve the development.

- **Enterprise Funds were not Included in Study**

The study failed to include many of the development-related costs by specifically excluding public facilities and services that are managed as "enterprise funds." An enterprise fund is a self-sustaining service category where the revenues are set to match the expenses. In Trappe, these include the water system and sewer system.

The rationale used in the study to exclude enterprise funds is that these funds are self-supporting and therefore will create no net impacts on the town. But this rationale fails to reflect the increases in user fees and connection charges that will likely result from the Trappe East development. Higher charges would be passed on to established residents and businesses. The enterprise fund is essentially an accounting tool to set service rates. The facilities and services in enterprise funds should be treated the same as other town facilities and services. A fiscal impact results from the higher rates the town must charge to meet increased expenses, just as taxes must be increased to cover other new costs the town incurs.

- **Value of Existing System Capacity not Considered**

The Town of Trappe appears to have excess capacity in some of its service areas, notably sewage treatment and parkland. This excess capacity will be consumed by new growth. Excess system capacity has a real value that has been paid for by the taxpayers of the town. This value is approximately equal to the cost of providing an equivalent amount of new or replacement capacity. The Trappe FIA failed to calculate the cost of excess capacity that will be consumed by the new development.

- **Level-of-Service Standards were not Evaluated**

Existing levels of service in Trappe and surrounding towns were used to calculate requirements for new development. This is appropriate when LOS is adequate and meets the standards expected by new development. However, it appears in the case of Trappe, that levels of service are quite low and would not be adequate for large scale, new development. Since Trappe would grow six fold under the proposed development plan, it would essentially become a new town. As such, it would need to meet today's service expectations in all areas. A higher level of service will require more expense for the facilities and services necessary to serve the new development.

- **Costs for Non-Town Services were Excluded**

The study looked only at costs and revenues affecting town government. This approach excludes public facilities and services that are provided by other public agencies. For example, the cost to provide new school facilities for the new children moving in to Trappe East will be funded through the Talbot County school system. Because these costs will be borne by Talbot County, they are not included as a fiscal impact in the Trappe East FIA, even though Trappe taxpayers will pay a share of these costs. The Trappe FIA also did not include impacts to the county and state for new roads and highways that are not funded by the town. These non-town costs will have significant impacts on local taxpayers.

- **Higher Taxes are not Counted as a Fiscal Impact**

The Trappe East FIA assumes that the taxes and fees generated by the town will increase dramatically (almost triple) under the development scenario, but fails to count these increases as a fiscal impact. The study states that revenues from town taxes and fees will increase from the current $174 per capita, to $501 per capita. This represents a $327 per year average cost to each resident of Trappe, amounting to $376,050 per year in additional cost to the 1,150 existing residents of Trappe (see Table 3). Including $47,995 in higher taxes on commercial uses, the total cost to existing residents and businesses would be $424,045 per year. Since the costs for the Trappe East development have been understated (as discussed above), the costs to local taxpayers are likely to be significantly higher than shown in Table 3.

Table 3
Higher Taxes in Trappe (from Trappe East FIA)

Revenues	Current Rate	Rate with Trappe East Development	Difference With Trappe East Devel.	Annual Cost to Existing Residents and Businesses*
Per Capita	$174	$501	$327	$376,050
Per Job	$150	$295	$145	$47,995
Total:				**$424,045**

* Total additional cost based on the 1150 residents and 331 jobs currently in Trappe (per Trappe East FIA)

Conclusions

The Trappe East FIA uses an economic analysis methodology that does not accurately reflect the fiscal impacts of new development. Each of the issues raised above contributes to the underestimate of likely costs. As a result, the study has substantially understated the likely public sector (and taxpayer) costs associated with the proposed Trappe East development. Given the typical magnitude of these additional costs, the Trappe East development is likely to generate far greater costs than revenues, resulting in a negative fiscal impact on the town and its taxpayers.

In the time since the Trappe East FIA was completed in August of 2004, the development plan has changed. Proposed residential units have been increased from 2,262 to 2,501 units and the 245,000 square feet of commercial development has been eliminated. Since residential development typically has a higher demand for services and facilities (such as schools, parks and social services) than commercial development, this will tend to exacerbate the negative fiscal impacts of the development.

Economic Impact Analysis

The Economic Impact Analysis (EIA) portion of the Trappe East FIA study looked at private sector impacts from the proposed Trappe East development on Talbot County (rather than the fiscal, public sector impacts). The study looked at the county instead of the town because economic data was not available at the town level. The EIA projected benefits to Talbot County in the form of gross economic spending on construction totaling $416 million and job creation resulting from the construction spending totaling 3,465 jobs.

The EIA significantly overstates the actual benefits of the proposed development for the following reasons.

- **Economic Costs were not Considered**

The analysis tabulated gross economic benefits, while including no economic costs. Economic costs to the private sector resulting from significant growth include:

1. Increased land costs
2. Increase housing costs
3. Increased traffic congestion and delays
4. Increased taxes
5. Increased utility rates and connection charges

- **Expenditures are Incorrectly Assumed to Stay in the County**

The EIA assumes that 100% of the $396 million in spending for construction, including materials and supplies, will stay in Talbot County. However, construction materials such as lumber, cement, appliances, cabinets, flooring, plumbing fixtures, lighting, doors, windows, plaster and paint are obtained through a national and international supply network. It is highly unlikely that a significant portion of these construction materials will be produced within the county. Therefore, most of this spending will quickly leave the county.

The EIA also assumes that other construction-related spending (design, engineering, construction labor) will stay in Talbot County. However, the design firms and construction companies that are capable of this scale of development are likely to be large companies located out of the area, or out of state. Most of the expenditures to firms and employees based out of the area will leave Talbot County.

Use of "multiplier effects" is a common practice in economic analysis. It is used in the EIA to show how money can be recycled in a community or region and

can significantly inflate the apparent economic benefits. In contrast, empirical studies show that local growth does not result in real benefits to the community in terms of increased per-capita income.[20] Therefore, it must be assumed that much of the direct and indirect economic activity flows out of the community and does not significantly benefit local residents. In this case, "multiplier effects" are likely to be offset by national builders, national building materials suppliers, and non-local workers who will take much of the money out of the community.

- **Job Creation Benefits are Greatly Exaggerated**

The EIA estimates creation of 3,465 new jobs resulting from the total of $391 million in construction spending. However, it appears that this employment figure is based on the construction occurring in a single year. If the construction occurs over 10 years, the annual employment will be 346 jobs.

The EIA counted jobs as benefits, regardless of whether or not the jobs go to local residents of the town or to people who move in to take the jobs. Studies show that most new jobs in a town end up going to people who did not live there before the job was created.[21] Many of the new jobs will be filled by out-of-county and out-of-state workers, and therefore do not represent benefits to current Trappe or Talbot County residents. Only new jobs going to existing residents of Talbot County who are unemployed or underemployed can be counted as benefiting the county.

Furthermore, these construction-related jobs are temporary employment that will disappear when construction is completed. The eventual loss of these jobs will create a financial hardship for the county similar to the closing of a major manufacturing plant or industry in the area.

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