Municipal Corner – Long Term Debt

In October of 2013 Moody's provided the Town of Stowe a bond rating of Aa3 (which in Moody's language means "high quality and very low credit risk". For perspective, the State Bond Bank's is Aa2 – one grade above ours). The Town's strengths are its stable tax base, the above average income and wealth level of its residents and a moderate debt to total assets ratio. According to Moody's our most noteworthy challenge is our exposure to unanticipated expenditures. We do not, as a policy, carry an undesignated fund balance. Stowe has historically used its available surplus carry over from the previous fiscal year to buffer taxes in the following year. Some municipalities maintain a reserve fund set at a consistent percentage of the total budget for unanticipated expenditures and to help smooth out the tax rate over time. The risk of using the entire surplus as a revenue stream in one year is that if it's not available in the next, the resulting tax rate increase is disproportionate to the spending increase.

According to the book, *Capital Budgeting and Finance: A Guide for Local Governments"* For most local governments, the rating agencies consider debt service to be high when it is between 15 and 20 percent of general fund spending or revenues. When debt takes 15 to 20 percent of a local government's operating budget, this can crowd other spending needs." In FY'15 debt equals $1,283,094 of the $11,149,133 of General Fund Expenditures, which equals 11.5%", not yet of concern, but to be watched.

Stowe used to bond more frequently for smaller amounts of money. In recent years, the Town has moved towards funding lower dollar value projects through pay-as-you-go financing (primarily with annual Local Option Tax revenues) and bonding only for larger dollar value projects ($500,000 +). The use of long term debt insures that the beneficiaries of these large scale projects are the ones who pay for them. The downside of long term debt is that it inherently reduces the ability to lower expenses in the future. This is most often felt during times of economic downturn or years where unexpected expenses are high. These are the age old challenge for municipalities as well as individuals as we strive for balance between the use of long term debt and pay-as-you-go capital spending.

There are no laws capping the amount of long term debt a community can obligate itself to. At the end-of-the-day the amount of long term debt a community takes on is up to the community and its voters. As well, Moody's does not tell us that we must have a reserve fund, but they do suggest that it may wise. This sentiment is echoed by our auditors. The Selectboard has discussed the idea of creating an unallocated operating reserve fund. However, funding such a reserve fund as part of the upcoming budget will be a challenge due to the anticipated reduction in available surplus carry forward. If we do ever have a surplus carry forward greater than the previous year and/or the community thinks we have the fiscal capacity, the community should consider starting to build up a reserve fund (aka "rainy day fund").

If you have any questions on this article or have topic you would like me to consider addressing in a future municipal corner, please email me at csafford@townofstowevermont.org or stop by the Town Offices to discuss in person.