



## Understanding In-Town and Out-of-Town Rates

Hillsborough's in-town customers pay nearly half the rate that out-of-town customers do for water and sewer service, but they often have a higher cost of living than their neighbors who live outside the town's limits. About half of Hillsborough's utilities system is outside town limits. Below is information regarding living inside or outside of Hillsborough and the rationale for higher out-of-town water and sewer rates.

### Living in town vs. out of town

Despite a water and sewer rate that is 1.95 times the in-town rate, the cost of living outside Hillsborough's limits often is less expensive than the cost that in-town customers pay in combined property taxes and water and sewer bills.

For neighborhoods with more modest property values, the total cost of services may be less if they were annexed into the town. But for properties with higher values, it generally is less expensive to be outside town limits.



The cost of living within Hillsborough can be more expensive than outside town limits due to municipal property taxes and utility bills. Municipal property taxes help pay for services that also often benefit people living outside but near town limits. Such services include maintenance of town roads.

Over the years, town staff have had conversations with surrounding neighborhoods interested in learning about annexation. These neighborhoods were provided information to help them decide whether it is in their best interest to remain outside of town limits or to become part of the town. Some cost differences include:

#### *Outside town limits —*

- Private trash collection fees if not transporting trash to the landfill on their own.
- Orange Rural Fire District tax

#### *Inside town limits —*

- Municipal property taxes (these help pay for services that include trash collection and fire service)
- Stormwater fee

Annexation's financial attractiveness depends largely on each household's property value and water usage. Anyone wishing to analyze their situation more closely is encouraged to contact the Hillsborough planning staff for assistance with the calculations.

North Carolina law requires voters in an area proposed for annexation to vote in favor of joining the municipality. Annexation of developed neighborhoods is rare in Hillsborough, and the last such annexation was in the 1990s for the first phases of the Cornwallis Hills neighborhood. Most neighborhoods that are annexed are annexed at the request of the developer prior to residents purchasing homes.

### Rationale for higher out-of-town rates

Hillsborough's out-of-town water and sewer fees are higher than in-town fees due to a number of reasons:

#### *Cost of service* —

Customers located farther away from the town's core usually are more expensive to serve on average because of:

- Lower densities — Outlying areas generally are less densely populated than areas within the town, which involves a greater average expense in maintaining and serving the system per foot of pipe.
- Greater distances — The operations, maintenance, pumping of water and sewer, and reading of meters can be more costly in areas outside of town, primarily due to additional distance and travel time from the town's water or wastewater treatment plants.



In-town customers are the owners and operators of the town's water and sewer system, which includes the reservoir. As such, they bear greater investment risks for the system.

National cost-of-service studies generally find that serving out-of-town customers costs 25 to 75% more than serving in-town customers, with typical costs in the range of 45 to 50% more.

#### *Growth management* —

Higher out-of-town charges are a part of managing growth.

When the town provides water and sewer service by request to developments outside of its limits, it loses some of its capacity to attract the type of development that would improve its tax base, help improve the economies of scale in providing services, and potentially ease the tax burden on existing citizens. Charging a higher rate to out-of-town customers is a way to recoup some of the potential lost tax revenue that the town sacrifices by allocating part of its water and sewer resources to outside customers.

Lower in-town fees also can make annexation more desirable in areas that already have water and sewer service. Those in an area annexed would see an increase in their property tax rates to pay for additional in-town services, such as police protection and garbage collection.

#### *Investment risk* —

As Hillsborough residents and the owners of the town's water and sewer system, in-town customers have additional responsibilities not shared by out-of-town customers. They bear more of the investment risks of owning and operating a utility.

For instance, in-town customers assume additional risk when voter-approved general obligation bonds are used to finance large projects, such as the first phase of the town's reservoir. When general obligation bonds are issued, a municipality pledges its full faith and the credit of its taxing power as collateral to ensure the debt will be repaid.

#### *Equity* —

As Hillsborough residents, in-town customers bear more of the burden of financing and facilitating the water and sewer system's operations through their local government, including through paying municipal property taxes.

Out-of-town customers pay nearly double the rates of in-town customers, but in-town customers also pay what amounts to a double share by supporting the town's utility system through water and sewer payments and through municipal property taxes. For instance, in-town customers' water and sewer payments as well as their taxes help pay for positions and resources that support the water and sewer operations, including Human Resources personnel and information technology.

By paying municipal property taxes, in-town customers also subsidize the use of Hillsborough services by out-of-town customers. The town serves about 9,000 people just outside the town's limits with water and sewer service. While they are not a part of the town's population, which numbers about 7,800, out-of-town customers near Hillsborough's corporate limits often use town services that are paid for by in-town customers' tax dollars. These include:

- Police protection when inside town limits.
- Recreation facilities, such as Gold Park, Kings Highway Park and the Riverwalk greenway.
- Streets — Street maintenance is primarily paid for with property taxes and with gas tax proceeds that are distributed based on a formula of population and road miles. Because out-of-town customers are not considered in the population formula, in-town customers partially subsidize the added maintenance costs for streets.

### **Rationale nationally**

Below are additional reasons often cited nationally for charging out-of-town residents more than in-town residents for water and sewer service:

#### *Developable property —*

Out-of-town customers often request municipal water and sewer service to make it possible to build new developments, housing or business. Such requests usually occur where water and sewer service is unavailable or inadequate or where well and septic systems are cost prohibitive or not practical in an area. Access to municipal water and sewer service increases property values because the property becomes more developable, including to a greater density. Developers and homeowners are willing to pay a premium over in-town rates for such benefits.

#### *Lower insurance rates —*

Out-of-town customers often are willing to pay higher rates to be connected to a municipal water system because the service can lower their fire insurance ratings, lowering homeowners insurance rates.