**Statutory Authorization:** 24 V.S.A., §§4401, 4403, 4430, 4443
**Type:** NONREGULATORY
**Related Topic Areas:** Bicycle & Pedestrian Facilities; Facilities Management; Impact Fees; Official Map; Roads & Highways

# Capital Improvement Program

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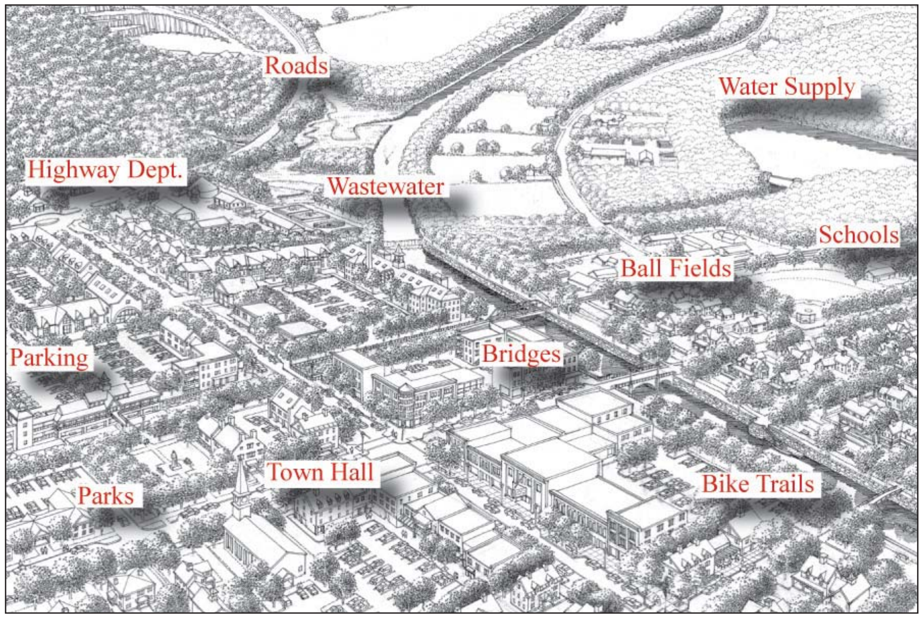
## Overview

Vermont municipalities are regularly faced with decisions regarding where to locate, when to build, and how to pay for major capital investments such as new roads, parks, or public buildings. A capital improvement program is a tool that can help make these decisions. The capital improvement program links a municipality's long-term development plan with its annual budgeting process and can prevent budget and tax rate fluctuations by scheduling expensive capital projects over several years.

The scheduling of capital investments over a number of years is generally referred to as capital improvement programming. A capital improvement program (CIP) typically includes a one-year capital budget for the current fiscal year and a multiyear capital program for subsequent years. This budgeting technique evolved during the 1930s as municipalities, struggling with the impacts of the Great Depression, tried to get the most benefit from limited public dollars. Efficiencies were achieved by eliminating duplication and by avoiding classic errors, such as paving a road and then having to dig it up to install underground utilities.

Capital improvement programs were quickly recognized as an important tool for municipal fiscal management. By the 1950s, capital improvement programming was tied to more comprehensive municipal planning. Comprehensive plans identified the need for new or replacement facilities and where they should be located. The capital improvement program was then used to determine how facilities would be financed and to schedule work accordingly. The preparation of capital improvement programs to implement local plans is now widely practiced throughout the country.




**Capital improvement programs can help communities link the annual budget for new or improved public facilities to the long-term goals of the municipal plan. It can also provide coordination between municipally funded improvements and private sector development activities.**

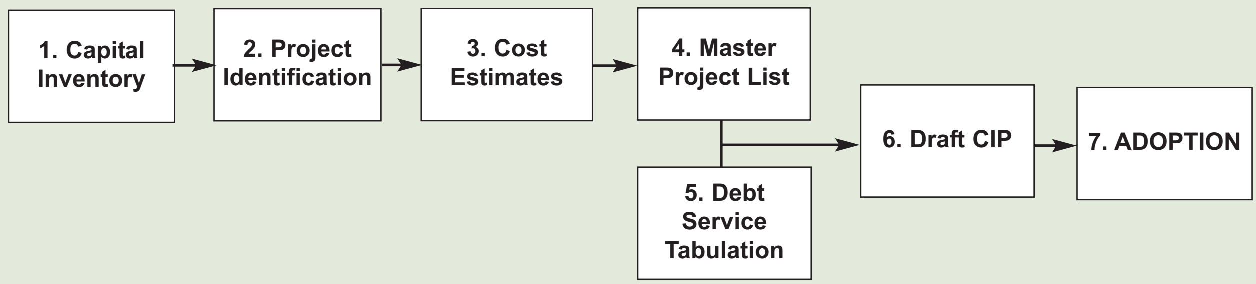
## Application

The creation of a capital budget and program need not be complicated; it can be done by hand on a multicolumn ledger sheet. Use of simple spreadsheet software speeds up the process and facilitates revisions and fine-tuning. Most data required for developing a capital budget and program are available from municipal records and local officials.

The Vermont Planning and Development Act (24 V.S.A., Chapter 117) specifically authorizes municipalities that have duly adopted municipal plans—with utility and facility elements as required under the act—to adopt capital budgets and programs (§§4403, 4443). Chapter 117 also spells out the required content of a capital budget and program (§4430). The capital budget and program is a six-year document: year one is the capital budget for the upcoming fiscal year, and years two through six are the capital program, or schedule of investments, for the following five years. The planning commission, town manager, or other appointed group may take the lead in developing a capital improvement program for consideration by the legislative body. Recommended projects, however, must conform to the municipal plan. The planning commission should review and submit annual project recommendations for inclusion in the CIP.

Section 4430 of Chapter 117 defines a capital project as:

### Typical Process for Capital Programming




- a physical betterment (buildings, furnishings, machinery, apparatus, or equipment);
- land or interests in land;
- preliminary studies related to any betterment, land, or interests in land; or
- any combination of the three.

Many communities supplement this basic definition by specifying certain limits for capital projects, such as a minimum total cost or service life (in years). For example, a capital project may be defined as acquisition of land, a structure, or equipment that costs more than $5,000 and will last more than three years. Once a municipality has specified what constitutes a capital project, the preparation of a capital budget and program can move forward.

The process for creating a capital budget and program typically includes the following steps.

1. **Capital Inventory.** The process generally begins by creating a complete inventory of the municipality's land, buildings, equipment, and so on. This is often based on an annual accounting of capital assets. (The Governmental Accounting Standards Board has issued statement #34 [GASB 34], which encourages municipalities to prepare annual reports in accordance with specified standards, beginning with fiscal year 2003 to 2004. These standards include a statement of all capital assets along with the depreciated value for each.) The inventory should be reviewed and confirmed by all department heads. Once confirmed, this can serve as the baseline for assessing the need for the replacement or expansion of facilities or equipment. Department heads should review the inventory and identify those items that will be up for replacement, renovation, or expansion during the coming six years.
2. **Project Identification.** Once the inventory is established, the next step is to identify potential capital projects to be undertaken during the upcoming six years. Sources for identifying potential projects include the municipal plan, department heads, planning and conservation commissions, and task forces or citizen groups. A typical approach is to develop a standardized capital project form, which has space for various items of information about the project such as:
   - the name of the project;
   - the location of the project;
   - an indication whether it's a replacement, renovation, or expansion;
   - justification for the project;
   - project priority rating;
   - an indication of when the project should be undertaken;
   - an indication of how many years it will take to complete the project;
   - expected life span;
   - anticipated total cost;
   - budgeted annual costs if the project will be undertaken over multiple years;
   - suggested funding sources; and
   - the impact on annual operating expenditures.

   Note that this form can be used to collect information for several subsequent steps in the process.

   The distinction between replacement, renovation, or expansion is particularly important for municipalities that anticipate using impact fees to fund capital projects. Impact fees can be used only to fund capital projects that expand the municipality's capacity to accommodate and serve anticipated growth and development—not to address existing deficiencies. (See related topic paper, Impact Fees.) Defining existing and planned levels of service is very helpful to justify projects needed, in whole or part, to accommodate anticipated growth.
3. **Cost Estimates**. The next step is to prepare and/or verify cost esti-

### Including Schools in CIP

In Vermont, it is typical for school services to be provided by a separate school district. However, it is advisable that the capital improvement program include school capital projects, particularly if it is anticipated that school projects will be funded through impact fees. Including school projects also helps to identify when multiple projects are being scheduled at the same time, potentially resulting in very large annual capital outlays.

mates for identified projects. Department heads are the obvious sources for this information, but it also may be helpful to contact suppliers and professionals, such as engineers, architects, or landscapers, who can help develop accurate cost estimates. As noted above, preliminary studies for larger projects that include cost estimates can be scheduled and budgeted as a separate capital item. In addition to cost estimates, project priorities also should be confirmed.

4. **Initial Master List.** Once cost estimates have been verified, the next step is to include and tabulate all identified projects into a single master list. This often takes the form of a matrix with projects listed in separate rows and the six-year planning period set out in columns across the top. Annual expenditures for the project identified in a particular row are entered into each column for specified years. Annual expenditures can then be totaled for each department or service and for the entire municipality at the bottom of each column. Room for comments can be provided at the right-hand end of each row.

   When this initial list is first prepared, a number of things will become apparent. First, it will clarify how various projects interrelate with each other. There may be a large number of projects scheduled for certain years, while very few are scheduled for other years. One project that should follow another may be scheduled before the first project is completed; for example, a road may be scheduled to be repaved before a sewer line is installed. It's also likely that this first exercise will generate "sticker shock" when annual capital expenditures are added up. Resolving these issues takes place during the remaining steps of the process.

5. **Tabulation of Debt Service.** While the initial list of projects is being prepared, it's also a good time to tabulate the municipality's current long-term debt and associated debt service payments for each year of the six-year planning period. The outstanding balance for each bond or note should be reported, and the annual interest and principal payments for each year should be determined. This information can also be entered in the table. If school projects are included in the capital budget and program, existing school debt and debt service should also be included. When all debt service is listed, the sum of annual debt service payments can be computed for each year of the planning period.

   It's also very helpful to prepare estimates of how much money will be available to fund capital projects for each of the six planning years. This should be based on an examination of past municipal expenditures. By examining annual budget records, it's possible to determine the rate at which total annual expenditures have increased each year and the portion of annual expenditures that have been devoted to capital projects. For planning purposes, an average over three to five years will establish a reasonable basis. By using these averages, it's possible to create simple projections of total annual and capital expenditures over the coming six years. These figures are not expected to be highly accurate, but will provide a reality check when compared to the total annual costs of proposed projects.

6. **Draft CIP.** The next step is to use all this information to prepare a draft six-year capital budget and program of related expenditures, including all expenditures for existing debt service. The list of capital projects should be carefully reviewed. Low-priority projects can be deleted or postponed to future years. The schedule of higher-priority projects should be adjusted so they don't bunch up and result in large fluctuations in total annual capital expenditures. Projects intended to accommodate new development, as set forth in the municipal plan, should be scheduled to be available when growth takes place. Projects can also be redefined to reduce costs or be divided into smaller segments that are scheduled over several more years. Annual payments should be scheduled for projects that will be funded over a period of time, such as through annual allocations to reserve funds or by some form of bond or loan. Ultimately, the total anticipated annual costs of capital projects should approach the level of revenues estimated to be available for capital expenditures, including debt service.

   The actual format of a draft capital improvement program can range from a simple table to complex tables accompanied by written discussions of each project and its justification. A simple table would be similar to the matrix shown above, but would include only the recommended projects and their annual costs. Information, however, should be available regarding funding mechanisms and terms of financing, a project's justification, its role in accommodating anticipated growth and development, and possible impacts on annual

### Capital Plan and Budget Committee

*Example:* ***Town of Randolph***

The Randolph Capital Plan and Capital Budget Committee reviews plans for capital improvements (i.e., major repairs or replacement of infrastructure) and major expenditures (e.g., new fire truck), and makes recommendations to the Board of Selectmen. This committee also makes recommendations on the capital budget based on the capital plan (schedule of projects for each year). Members of this committee are appointed by the Board of Selectmen on a yearly basis. Meetings are once a month and open to the public.

Source: Town website, www.randolphvt.com.

operating expenditures. It's up to the municipality to determine just how much detail it wishes to include. This draft is then presented to the legislative body for final review and refinement. It should be understood that the first year of the six-year plan is the recommended capital budget to be incorporated in the municipality's annual budget deliberations.

7. **Adoption.** The capital budget and program may adopted, amended, or repealed by legislative body following one or more warned public hearings, as specified in Chapter 117 (§4443). A copy of the proposed improvement program must be filed at least fifteen days prior to the first hearing with the municipal clerk and the secretary of the planning commission. The planning commission may submit a report to the legislative body prior to the hearing, but is not required to do so. The capital budget and program is then adopted, amended, or repealed by a resolution of legislative body promptly following the final public hearing.

An adopted capital budget and program represents the community's best thinking regarding recommended and anticipated capital expenditures. The capital budget should be consistent with the capital portion of the current municipal budget. It's important to remember, though, that the adoption of a capital budget and program is advisory to the annual budgeting process and does not mandate that specific projects be included in the budget. The actual capital budget may be adopted as part of the annual budget or as separately warned items.

The capital program should be viewed as a flexible, nonbinding tool. The formal process of creating and adopting annual municipal budgets may or may not result in inclusion of all projects contained in the capital program for specified years. Public opinion may convince the legislative body to deviate from capital program recommendations, or voters may reject a municipal budget or proposed bond to fund a capital project. New information or priorities may also require adjustments to listed projects, particularly those scheduled for later years. For these reasons, the capital improvement program should be reevaluated on a regular basis.

Other than ensuring that the capital budget is considered during annual budget preparations and that the capital program is updated periodically, capital improvement programs require little ongoing administration. Given the information generated when the first capital improvement program is produced, annual updates become a relatively simple matter of deleting the current budget year, extending the planning period to include a new sixth year, and reexamining the recommended set of projects. Some communities choose to do simple updates annually with a major review every five or six years. In any event, the intent is to make sure that present and anticipated capital projects and associated expenditures are systematically evaluated as needed to provide public facilities and services for local residents and businesses.

### Example of a Capital Budget Schedule

| Dates | Tasks |
|---|---|
| October | Departments complete capital budget forms and returned to manager's office. |
| November | Manager transmits draft capital budget to planning commission. |
| November | Commission begins capital budget review. |
| January | Public hearing on capital and operating budgets. |
| January | Select board completes review of capital budget. |
| March | Annual town meeting. |
| March | Vote on budget by Australian ballot. |