BANKER & TRADESMAN ESTABLISHED IN 1872

Sunday, April 24, 2011, 3:20am

**Law Of The Land**

# Sewer Improvements Pose Taxing Problem For Developers

By Charles N. LeRay

Special To Banker & Tradesman


Charles LeRay

To obtain project approval, the developer of a subdivision, office park, or large commercial building may be required to extend or improve the municipal sewer system.

This may mean constructing an on-site sewer collection system or sewer extension to connect to the municipal system. Or it may involve helping to eliminate existing inflows of storm water or infiltration of groundwater which reduce the municipal system's capacity to receive sewage or contribute to sewer overflows during storms. Negotiations between developers and permitting authorities over the nature and extent of the construction or contribution can be prolonged and contentious.

Two recent Appeals Court decisions establish some parameters for this dialogue.

**North Adams Decision**

In a January 2011 decision, North Adams Apartments Limited Partnership v. North Adams, the Appeals Court addressed what compensation is due when a private sewer system is taken for public use. In 1992, the developer and owner of an apartment complex and residential subdivision spent $136,540 to construct a sewer extension and pump station to connect to the city's sewer system.

In 2005, the North Adams city council took the sewer system by eminent domain, for $10,000. The owner claimed valuation should have been based on a depreciated replacement cost of $271,370 or, using income capitalization, based on $235,000 in estimated sewer tie-in fees from neighboring properties over the next five years.

The Appeals Court held that a private sewer system is no different from any other private property, and cannot be taken without just compensation. However, the court found that this owner had suffered no measurable loss. After the taking, the owner's properties continued to be served by the system, but the owner was relieved of maintenance and repair obligations; future earnings from tie-in fees were speculative.

The court also found that the owner built the system as part of its housing investment, with the costs recouped through apartment rents and the increased value of subdivision homes connected to municipal sewer, rather than to individual Title 5 systems.

Absent particular reasons to retain ownership, such as the need to preserve flexibility for future phases, the likely lack of a significant damages award if the municipality later takes a private sewer system leaves developers with little reason not to seek to transfer ownership – and maintenance obligations – from the start.

**Saugus Decision**

In another January 2011 Appeals Court decision, Denver Street LLC v. Saugus, four developers of multifamily residential projects in Saugus had challenged the town's infiltration and inflow (I/I) reduction contribution charges.

The town's I/I problems had resulted in sewer overflows during storm events since 1986. Saugus entered an administrative consent order with the Department of Environmental Protection in 2005, requiring the town to identify and eliminate I/I sources as a condition of allowing new connections to its sanitary sewer system. In response, Saugus adopted a program under which the town allowed an applicant to purchase the right to connect to the town's sewer system by making an I/I "reduction contribution" based on the project's projected sewer flows.

To determine whether the charge was a permissible fee or an impermissible tax, the Appeals Court applied a three-factor test. A fee must be:

In exchange for a particular governmental service which benefits the party in a manner not shared by other members of society;

Paid by choice, meaning that the fee could be avoided by not utilizing the service; and

Collected to compensate the government entity providing the services, not to raise revenues.

The Appeals Court found that the developers could avoid the charge by abandoning their plans. The court also found that every Saugus inhabitant benefited from infiltration/inflow repairs to the dilapidated sewer system, not just those who paid the "contribution." Furthermore, it said, the I/I charges did not compensate Saugus for expenses incurred in connecting new users, but were used to fix longstanding deficiencies unrelated to the addition of new users.

Therefore, the court held, because Saugus's infiltration/inflow reduction contribution program failed the first and third factors, it was an illegal tax. On March 2, 2011, the Supreme Judicial Court agreed to hear Saugus's appeal of the decision; the town's brief was filed on April 19.

Several other Massachusetts municipalities have I/I programs similar to Saugus. If the SJC also finds that the sewer connection charges imposed under these programs are illegal taxes those communities, like Saugus, may be faced with assessing improvement fees on all sewer users, or imposing moratoria on new sewer connections, or both if they cannot rely on developers to fix municipal problems. Other communities require developers to undertake or fund specific I/I mitigation projects in exchange for being allowed a new sewer connection. Under the three-factor test, these requirements may also be a tax by another name.

Until the deficient municipal sewer systems are improved, developers of larger projects may find that constructing on-site, private wastewater treatment plants is an easier – or the only – way to obtain project approval in those cities and towns.

*Attorney Charles N. LeRay is a founding partner of Brennan, Dain, Le Ray, Weist, Torpy & Garner in Boston. Email: cleray@bdlwtg.com*