Memorandum

Office of the City Administrator

City of Chesterfield

TO: Finance and Administration Committee

FROM: Mike Geisel, City Administrator mg

DATE: June 14, 2018

RE: Revenue Alternatives

Included with your committee packet, is a memorandum from Finance Director Chris DesPlanques which describes various revenue alternatives to be considered by the City. As you know, this information was requested by Council previously and was identified as one of my 2018 Goals & Objectives.

While Chris' analysis is thorough, there are additional questions and strategies that should be considered in conjunction with any proposed increase in revenues. First and foremost, it is important that should the City decide to pursue alternative revenue sources, it is critical that City Officials have a consistent and clear message as to the need and purpose of such revenues.

As has been discussed repeatedly, it is our collective opinion that the City of Chesterfield maintains an unhealthy reliance on sales taxes. There are a variety of reasons for this opinion. Sales tax revenues are volatile, fluctuating wildly not only from month to month, but from year to year. They are both seasonal and dependent on the economic climate. Further, and most importantly, we should all acknowledge that the retail industry is experiencing a fundamental shift from traditional brick and mortar purchases, to on-line purchasing. The traditional big box retail is downsizing significantly and the traditional mall shopping experience is quickly becoming a thing of the past. Sales Taxes comprise roughly half of the City's total revenue stream when considering the General Fund, Parks Fund, Capital Projects Fund, and the Public Safety Fund. The City is highly reliant on a diminishing resource. Sound business planning requires that the City attempt to obtain a more stable, predictable, and growing revenue stream.

If City Council elects to pursue alternative\additional revenue options, a concurrent strategy should be developed to determine the level of revenue sought and the uses of said revenue. One option is to simply pursue an alternative revenue source to diversify the revenue sources and to replace lost revenue experienced in the recent past, such as reduced telephone utility taxes and due to online sales. Another alternative is to pursue additional revenues and associate same with services or transfer of expenses. Obviously, the two strategies require different levels of receipts.

Accordingly, Finance Director Chris DesPlanques memorandum is a starting point for discussion and does not represent a singular choice from several options. We look forward to discussing this with each of you.

City of Chesterfield

Finance Director
636-537-4726

MEMO

DATE: **June 4, 2018**

TO: **Mike Geisel, City Administrator**

FROM: **Chris DesPlanques, Finance Director**

RE: **Revenue Options for Chesterfield**

As you requested, I've reviewed and performed preliminary level research relative to the most viable revenue opportunities for the City of Chesterfield. As staff has repeatedly advised, it is our belief that the City of Chesterfield has an unhealthy reliance on sales taxes. While it is true that sales taxes only make up 1/3 of the General Fund revenues, you must also consider that sales taxes are the primary source of revenue for the Parks Fund, Capital Projects Fund, and the newly created Public Safety fund. The current sales tax focused revenue for the City of Chesterfield is problematic for multiple reasons. First, sales taxes can be difficult to budget for as they are highly volatile seasonally and are subject to economic variation. Secondly, we are reliant on sales taxes for more than half of our budgeted revenues; Chesterfield's operations are primarily reliant on sales tax. Finally, the entire retail industry is experiencing a transformational Industry shift causing traditional brick and mortar stores to downsize or shutter, while a rapidly increasing proportion of sales are occurring via on-line channels.

Analogous to investing, diversification of revenues is an intelligent choice. I have presented a few options that provide revenue alternatives outside of the current sales tax collections.

The Revenue Options presented are:

1) Property Tax
   a. commercial
   b. residential
   c. combined
2) Use Tax
3) Utility Tax
4) Hotel Tax
5) Business License

Of the revenue option presented, only one can be reasonable expected to scale to a level to make a meaningful dent in the problematic sales tax to total revenue ratio, and that is property tax. The other items can be used in conjunction with one another. While they don't solve the reliance on sales tax individually, they can provide important diversification, and varying amount of hedge on economic reliance on sales tax. It should also be recognized, that while it is a sales tax at its core, the Use Tax is unique in that it would serve to partially sustain those sales tax revenues that are shifting to on-line sales, but it also is an important component in providing a fair playing field to protect the brick and mortar businesses that are critical to the City's economy.

My recommendation is to focus first on property tax. It is the best hedge against the current sales tax variation, and can scale in amount if needed. In most cases it provides a tax deductible expense to individuals, which lessens the impact to the property owners, when compared to a utility tax that effects the same group of people, but would likely not be deductible for most people. Property Taxes are reliable, stable and predictable for budgeting and collection purposes.

While the other options here are worthwhile in that each could provide between $250,000 and $1,000,000, care needs to be taken to not overwhelm citizens by pursuing them concurrently, as that could create a large impact if pursued all at once.

In any event, should the City elect to pursue any of the described additional revenue sources, we should be prepared to clearly explain the purpose, need, and use of the additional revenue generated.

Revenue Options for Chesterfield

Property Tax

Pros:

Known - Chesterfield has used property tax in the past, people understand this taxing method. It is not new or exotic.

Stability - Not subject to seasonal or economic changes in the short term. Assessments lag changes in values and are only adjusted bi-annually. Property Values would increase/decrease on a longer time horizon giving Council time to react.

Predictability - Assessments are a known amount and only change every two years. Collectability is high. Once calculated, there is very little change from budget to collection.

Deductible expense - Property taxes are generally tax deductible for business, and most individuals.

Revenues can scale greatly - large tax base means even small tax rates can generate large revenues when needed.

Commercial/Residential Tax choice - can be applied to business and individual at different rates

Cons:

Perception - Chesterfield, for business comparison purposes, may be viewed more negatively.

Perception - It would be a "New" Tax, and the public perception may be negative

Residents Effect - Residents and local business effected directly

Revenue Generation:

Below is an example to illustrate scale and provide an easy to use calculation and is not a suggestion; the actual amount of property tax would be a council discussion.

Current Valuation: Residential $1,202,432,310/100 = $12,024,323 *.10

=$1,202,432 per .10/100 of assessed value

Commercial $574,337,420 /100 = $5,743,374 *.10

=$574,337 per .10/100 of assessed value

Revenue Options for Chesterfield

Use Tax

Pros:

Fairness/Equity-creates more level playing field with in the online vs "brick and mortar"

Stability/Growth-While just like sales tax there is seasonality and economic condition variability; online sales not currently subject to a use tax, that would benefit the City of Chesterfield, are growing by all national indicators.

Cons:

Perception-It would be a "New" Tax, and the public perception may be negative, as more sales are done online

Timeline-It would require a vote of the citizens, following an affirmative vote; the timeline for collection is in the 10-12 month range.

Effectiveness-To be most effective a use tax should be done on a regional basis. A small pocket of use tax in one city could be easily overlooked, by even well-meaning out of state businesses.

Taxable-Not a deduction like some revenue options (residential and in most cases)

Residents Effect-Residents and local business effected directly

Revenue Generation:

Per the reported use taxable sales of over $31,000,000 last year in Chesterfield Taxing Districts the potential for revenue given a 1% use tax is in excess of $310,000, and can be expected to grow steadily over the coming years.

https://dor.mo.gov/publicreports/taxablesales.php

13600	CHESTERFIELD	14,137,842.93	16,115,424.01	0.00	0.00	30,253,266.94
13601	CHESTERFIELD (X1)	34,391.16	16,590.66	0.00	0.00	50,981.82
13602	CHESTERFIELD (T1)	154,607.24	165.14	0.00	0.00	154,772.38
13603	CHESTERFIELD (T2)	3,741.66	3,741.66	0.00	0.00	7,483.32
13604	CHESTERFIELD (T3)	406,970.34	460,234.52	0.00	0.00	867,204.86

Revenue Options for Chesterfield.

Utility Tax

Pros:

Growth-increasing utility rates would provide built in increase mechanism.

Revenues can scale greatly- large tax base means even small tax rates can generate large revenues when needed.

Commercial/Residential Tax choice-can be applied to business and individual at different rates

Need for an increase in the utility tax correlates directly with the experienced loss of City revenues. E.g., the City's utility tax revenues have decreased $2 million

Cons:

Variability- Weather and Seasonality can make budgeting for this item accurately, more difficult. It is slightly less reliable a source of revenue than some options.

Growth- As a landlocked city, growth would be primarily from existing business expansion, and would be offset by general conservation and energy efficiency improvements that are becoming more and more affordable.

Economic Variation – utility cutbacks are the easiest to make in an economic downturn

Taxable-Not a deduction like some revenue options (residential and in most cases)

Residents Effect-Residents and local business effected directly

Revenue Generation:

Below is an example to illustrate scale and provide an easy to use calculation and is not a suggestion; the actual amount of utility tax would be a council discussion

Residential $718,000 per additional 1% (at 2017 utilization)

Commercial $392,000 per additional 1% (at 2017 utilization)

Revenue Options for Chesterfield

Hotel Tax

Pros:

Generally paid by non-residents and travelers to the area.

Supplements existing programs – additional revenue from Parks and Recreation events that bring in visitors from out of the area.

Not directly a sales tax

Cons:

Economic Variation – travel cutbacks are a business savings target in economic downturn

Nationwide Impression – The St Louis Area consistently makes the news as one of the highest hotel tax areas in the country, this would add to that negative perception

Requires State legislative approval

Revenue Generation:

Currently there are approximately 46,000,000 in annual hotel sales, which would equate to $461,000 at a one percent hotel tax. (the unknown here is what portion of the those sales are from food or presentation room rental, or other non-hotel taxable amounts)

Revenue Options for Chesterfield

Business License

Pros:

Impact-The number of businesses and the currently fairly minimal cost of licensing, mean this can be absorbed without a large impact.

Residents Effect-Residents not directly effected

Cons:

Perception-Business Licenses can come off as "anti-business"

Revenue Generation:

Business Licensing currently generates approximately $600,000.

There are a variety of methods business licensing can be adjusted to increase revenue. Currently the practical limit of rate increases before a vote will be required is estimated to yield an additional $600,000. A larger overhaul of the system could yield up to an additional $1,000,000, but would be subject to additional legal review. Any change to business licensing before modifying a fee would require Handcock Amendment analysis.