



Finance Director
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M E M O

DATE: July 8, 2022
TO: Mike Geisel, City Administrator
FROM: Jeannette Kelly, Finance Director *J. Kelly*
RE: Revenue Options for the City of Chesterfield

As requested during the Finance and Administration Committee meeting on May 23, 2022, I have reviewed the most viable revenue opportunities for the City of Chesterfield. As previously advised by staff, it is our belief that the City of Chesterfield has an unhealthy reliance on sales tax revenue. While sales tax revenues account for only 34% of the General Fund revenues, they are the primary source for the Parks Fund, Capital Projects Fund, and Public Safety Fund.

The current sales tax-focused revenue for the City of Chesterfield is problematic for several reasons. First, sales tax revenues can be difficult to budget for as they are highly volatile seasonally and are subject to economic variation as seen during the Pandemic and the recent inflationary period. Second, we are reliant on sales tax revenues for more than half (55% in 2022) of our budgeted revenues in the four major funds, making the City's operations primarily reliant on sales tax. Finally, the entire retail industry is experiencing a transformational shift causing traditional brick and mortar stores to downsize, while a rapidly increasing proportion of sales are occurring via online channels.

Similar to investing where diversification is accepted as best practice to minimize risk, diversification of revenues is the best practice. This memo outlines a few revenue alternatives outside of current sales tax collections, including:

- Use Tax
- Property Tax
- Business License
- Hotel Tax

Of the revenue alternatives listed, only property tax can be reasonably expected to scale to a level to truly diversify from the current reliance on sales tax revenues. While the other items don't solve the reliance on sales tax individually, in conjunction with one another, they can provide important diversification. It

should be recognized, that Use tax is unique in that it would serve to regain the revenues siphoned off to online sales and to provide a level playing field to protect the brick-and-mortar businesses that are critical to the City's economy.

My recommendation is to focus first on use tax. Although the Prop U initiative failed by a close margin in the April 2022 election, educating our residents on the importance of the use tax would provide revenues to the General Fund without participation in the pool distribution system of St. Louis County. The second focus should be on property taxes as they are reliable, stable, and predictable for budgeting and collection purposes. Care needs to be taken to not overwhelm citizens by pursuing these taxes 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 revenues generated.

Should you have questions or require additional information on this project, please let me know.

Use Tax

A use tax is a tax on the purchase of goods by Missouri residents from out-of-state vendors. Products exempt from the sales tax would be exempt from the use tax. As internet purchases increase, local revenues decrease. Funds generated from the use tax can be used to pay for vital municipal services including public safety and parks. The local use tax rate is the same amount as the sales tax rate (1%).

Pros:

- Fairness / Equity – Creates a level playing field for brick-and-mortar vs. online retailers
- Stability/Growth – As online sales continue to increase, this tax would benefit the City of Chesterfield by capturing online sales not currently captured by the sales tax

Cons:

- Perception – Some consider this a ‘new’ tax, and the public perception may be negative, as more sales are completed online from out of state vendors
- Timeline – It would require a vote of the citizens; following an affirmative vote, the timeline for collection is in the 10-12-month range
- Residents Effect – Residents and local business affected directly

Revenue Generation (estimate):

Per the reported use taxable sales of over \$106,550,000 last year in Chesterfield Taxing Districts (<https://dor.mo.gov/publicreports/taxablesales.php>), the potential for revenue given a 1% use tax is in excess of \$1,065,500 , and can be expected to grow steadily over the coming years.

If instead, we base our assumptions on the 2021 revenues generated by the ½ cent Parks Sales Tax (\$6,907,000) and estimate 15% of Chesterfield sales are from out-of-state vendors, we could expect use tax revenues in excess of \$2,400,000 given a 1% use tax rate.

Property Tax

Property tax (or millage rate) is an ad valorem tax on the value of a property. The tax is levied by the governing authority of the jurisdiction in which the property is located. RSMo 94.060 permits the City to impose a property tax up to \$1 per \$100 of assessed valuation with voter approval.

Pros:

- Used Previously – Chesterfield has used property tax in the past and citizens understand this taxing method. We have not levied a property tax since 2015.
- 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 individuals filing taxes utilizing itemized deductions.
- Revenues can scale greatly – Large tax base means even small tax rates can generate large revenues when needed
- Commercial / Residential Tax choice – This tax can be applied to business and individuals at different tax rates.

Cons:

- Perception – New businesses entering the area may view Chesterfield more negatively if we levy the tax.
- Perception – It would be a new tax and the public perception may be negative.
- Timeline – Requires a vote of the citizens (2/3 majority required)
- Residents Effect – Residents and local business affected 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 the property tax levy would be a council discussion.

Missouri law requires that personal property be assessed at various levels up to 33-1/3% of true value and that real property be assessed at the following percentages of true value:

- | | |
|---|-----|
| • Residential real property | 19% |
| • Agriculture and horticultural real property | 12% |
| • Utility, industrial commercial, railroad
and all other real property | 32% |

- Current assessed valuation per St. Louis County 12/31/2021 is:
 - Residential \$1,447,371,410
 - Commercial \$ 639,364,800
- If utilizing a millage rate of \$0.25 per \$100 of assessed value, the property tax generated would be as follows:
 - Residential: $\$1,447,371,410 / \$100 * \$0.25 =$
 - \$3,618,428
 - Commercial $\$639,364,800 / \$100 * \$0.25 =$
 - \$1,598,412

Business License

Every business planning to operate from a permanent location in the City of Chesterfield, including a home-based business, is required to obtain a business license from the City. The annual fee is currently based on square footage and type of business:

Fee Per Square Foot (Minimum is \$25; Maximum is \$10,000)

- Retail \$0.08
- Service/Office \$0.04
- Manufacturing/Warehouse \$0.02

Pros:

- Impact – The number of businesses and relatively minimal cost of licensing means an increase could be absorbed without a large impact.
- Residents Effect – Residents not directly affected

Cons:

- Perception – Business Licenses can be considered “anti-business”

Revenue Generation:

Business licensing currently generates approximately \$600,000 annually.

Any adjustment to a change in the business license fee structure would require voter approval due to the Hancock Amendment. There are a variety of methods business licensing can be adjusted to increase revenue including a change to the fee per square footage and type of business; a change to the minimum and maximum fees; a change to what the license fee is based on (annual sales instead of square footage). Any of these changes would require additional legal review.

Hotel Tax

Currently the City is barred from levying a hotel tax unless there is another specific statutory grant of authority. RSMo 67.1003 provides such authority for third class cities in St. Louis County having more than 2,500 hotel and motel rooms. If Chesterfield met this requirement (according to CoStar, the City has only 1,959 rooms), the City could impose a ½ cent sales tax on the charges for all sleeping rooms, solely for the purpose of promoting tourism in the City of Chesterfield. This is paid by the transient guests of hotels or motels and requires state legislative authorization and voter approval.

Assuming this becomes an option....

Pros:

- Generally paid by non-residents and travelers to the area
- Supplements existing programs – additional revenue generated from Parks and Recreation events that attract visitors from out of the area
- Not directly a sales tax

Cons:

- Economic Variation – During economic downturns, travel cutbacks are a form of savings for businesses
- Limited/Restricted Use of proceeds
- Nationwide Impression – The St. Louis area is considered one of the highest hotel tax areas in the country; this would add to the negative perception.

Revenue Generation:

Assumptions:

- 2,500 hotel rooms in Chesterfield
- 50% average occupancy rate
- \$118 average hotel room rate

Based on these assumptions there is approximately \$53.8 million in hotel sales which at 0.5% would equate to \$269,000 annual revenue.