

# CITY COUNCIL COMMUNICATION FORM

**FROM:** Gary Suiter, City Manager  
Kim Weber, Finance Director

**THROUGH:** N/A

**DATE:** December 8, 2020

**ITEM:** Long Term Sustainable Funding.

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<input checked="" type="checkbox"/>	DIRECTION
<input checked="" type="checkbox"/>	INFORMATION
<input type="checkbox"/>	ORDINANCE
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## **I. REQUEST/ISSUE & BACKGROUND INFORMATION:**

On November 10<sup>th</sup>, staff presented City Council with multiple options to address City Council's long-standing goal of fiscal sustainability. Options included property tax, sales tax, lodging or accommodations tax, "lift" tax, "sin" tax, timeshare tax, paid parking, impact fees, forming a stormwater utility, and establishing new special districts.

Following are Council's fiscal sustainability goals:

Previous years: *Develop a long-term fiscal sustainability plan for the City, which incorporates revenue diversification, cost recovery, asset performance for facilities, and community education and outreach.*

Current 2019-20 goal: *Sustainable Funding- consider destination marketing funding; lift tax; Howelsen Hill; community support; mental health.*

City Council considered and agreed to the following problem statement: *The city is too reliant upon sales tax a primary revenue source.* This overdependency on sales tax makes the city and its services subject to external factors beyond the city's control such as tourism, weather, wildfires, special events, retail sales, airline travel, pandemics, and economic recession.

Tackling this issue of financial instability will create consistency with City Council's vision statement to ensure "economic sustainability" for the long-term.

Following extensive discussion and deliberation, City Council directed staff to proceed with a more detailed evaluation of two options: *property tax and lodging (accommodations) tax.* This work session will focus on those two options. Per City Council's request, staff has conducted research for other comparable communities and provided a spreadsheet showing types of tax, tax rates, restricted uses, and diversity of revenue sources.

City Council also leaned toward submitting a ballot question(s) to the electors in November 2021. With that in mind, it is important we strategize now, evaluate options, and select a path forward. Following are more detailed evaluations of each form of tax:

## **Property Tax**

### Pros:

- The property tax is a more stable and reliable revenue source than other taxes.
  - Property values are usually less susceptible to short-term economic fluctuations than other major revenue sources, including sales tax.
- Ensures non-resident homeowners are paying for the services they receive.
  - Many part-time residents benefit from city services but contribute only minor amounts of sales tax to cover the costs of providing these services.
- Property tax is very difficult to avoid or evade.
  - Since property taxes can be secured by the property, they are difficult to evade which ensures that a broad segment of the population shares in the costs of government services.
- Property tax systems are more open and visible than those for other taxes.
  - Property owners can examine their assessments and those of nearby properties and can appeal the assessment.
  - Property owners are provided with a statement that shows their entire liability, which makes the full magnitude of the tax obvious.

This is not the case with taxes that are collected in small amounts as part of a purchase price (sales tax).

Cons:

- There is often a misunderstanding of the relationship between the actual value, assessed value, and mill levy. This can be viewed as a disadvantage when compared to fixed-rate taxes, such as sales tax.
- Due to Gallagher, commercial properties have historically paid a much higher property tax rate than residential properties (about 4x). With the recent defeat of the Gallagher Amendment, the disparity between commercial and residential property tax rates will ease over time, thereby providing some relief to commercial property owners. Tax rates may decrease but cannot be increased without a vote of the people.
- Increases the cost of housing and commercial lease rates.
  - Property taxes can result in higher monthly rental payments adding to the cost of living. For commercial properties, the property tax is typically paid by the tenant, so a higher tax could result in higher lease rates.

One mill of property tax generates approximately **\$730,000 per year**, based on current assessed valuation.

Property Tax and Sales Tax

Since property tax tends to be a more stable revenue source, it provides insulation during economic downturns (see attached comparison between sales tax and property tax). It also diffuses arguments about new construction and new homeowners not paying “their fair share”.

Property values are usually less susceptible to short-term economic fluctuations than sales tax. It should be noted that sales tax on groceries and utilities are relatively stable and not as susceptible to economic downturns as sales tax on general merchandise. These two items constitute nearly a quarter of the city’s annual sales tax revenues. Eliminating sales tax on groceries and utilities would make sales tax as a revenue source even less stable. This is the primary reason most comparable cities researched tax both utilities and groceries.

In addition to City Council’s goal of long-term sustainable funding, City Council has determined that service level expectations from residents often exceed the city’s current revenue sources, which is why lowering the sales tax rate to an amount equal to a levied property tax would be considered “revenue neutral” and would shift a significant portion of the tax burden from visitors to residents. While this might provide more revenue stability, it would still fall short of providing the revenue needed to meet service level expectations.

### Proposed Definition of City Services

City staff suggests designating a property tax to fund only “Central Governmental Services”, as described below. You will note that “transit” has been moved to the “Non-Central” category.

#### “Central Governmental Services”:

- Police
- Fire/EMS
- Public Works (streets, engineering, airport)
- Planning
- Municipal Court
- Facilities Maintenance
- Administrative Services (financial services, city clerk, administration, human resources, procurement, IT, etc.)

#### “Non-Central Governmental Services”:

- Transit (SST)
- Affordable housing
- Parks, open space, and trails
- Recreation programs and facilities
- Community support
- Destination marketing
- Howelsen Hill operations
- Educational programs
- Economic development
- Special events
- Other

Non-central governmental services would be subject to the fluctuations of the sales tax revenue source and consequently the tourism sector of the local economy.

### **Lodging (Accommodations) Tax**

#### Pros:

- Shifts a portion of the local tax burden to visitors.
- This tax is often appealing to local voters.
- The practical application of lodging tax is to market to future customers that will occupy hotel rooms and similar lodging accommodations.

Cons:

- The lodging industry often voices concerns that they could see a reduction in overnight guests.
- A concern expressed by the lodging industry in Steamboat Springs is that they already carry a disproportionate tax burden.
- This tax is subject to many of the same external factors mentioned above.
- Can add to the cost of lodging and accommodations.

Currently, a 1% city-wide lodging tax generates approximately **\$1,100,000 per year** in the City of Steamboat Springs. This lodging tax is often referred to as "2A Trails" funds. The monies are restricted until 2023, primarily for multi-use trails. After 2023, the restrictions are lifted, and it reverts to the original 1986 ballot language designated for "tourist amenities".

It should be noted a Local Marketing District (LMD) was created by City Council Ordinance in September 2004. There are five board members appointed by City Council which effectively operate as a separate governmental entity. The boundaries are smaller than the city limits (mountain area and along Highway 40).

In 2005, the electors approved a 2% accommodations tax within the LMD. These funds are dedicated for airline revenue guarantees. The annual revenue generated is approximately **\$1,800,000 - \$2,000,000**. Total lodging tax within the district is currently 3%.

City Council has several options pertaining to a lodging tax:

(A) Maintain the existing 1% lodging tax for tourist amenities (no change).

Pros:

- Would not require any action by City Council.
- Funds could be used for any tourist amenity consistent with original ballot language.

Cons:

- Does not address Council's goal of dedicated funding for destination marketing.
- Maintenance funding is not included which continues to stress the city's general fund.

(B) Re-purpose the existing 1% lodging tax from tourist amenities to destination marketing.

Pros:

- Identifies dedicated funding for destination marketing.

Cons:

- Would require an election.
- Stakeholder groups may oppose as they would prefer to see money dedicated to actual projects.

(C) Submit a new 1% lodging tax to the voters which would create a total of 4% total lodging tax within the LMD boundaries.

Pros:

- Identifies dedicated funding for destination marketing or the general fund for tourist-related projects.

Cons:

- Additional tax would be opposed by lodging community.
- Subject to many of the same external factors mentioned earlier.
- Can add to the cost of lodging and accommodations.

Consistent with City Council's goal, approval of a lodging tax dedicated to destination marketing will provide a long-term stable funding source for this specific purpose.

### **Other Considerations**

There are other considerations that City Council must evaluate when placing tax questions on the ballot. Following are some of those considerations/questions:

*Should the tax be dedicated to specific government functions?*

Pros:

- Can be viewed favorably by the voters
- Creates more accountability as to where the tax dollars go
- Provides guidance to future City Councils

Cons:

- Can tie the hands of future City Councils
- Limits flexibility for changing economic conditions
- Policy makers and citizens may disagree on how the funds are allocated

*Should the tax be finite or indefinite?*

Pros:

- Creates accountability in the eyes of the taxpayer, requiring policy makers to justify the tax when facing expiration

- Perceived as a definitive tax with a sunset, versus an indefinite, forever tax
- Finite taxes are generally more popular with voters

Cons:

- The tax could be eliminated by voters in future years, creating financial difficulty for city government
- Requires future elections which can be costly
- Would typically require an accompanying campaign, spearheaded by a citizen's committee, which can be difficult to initiate and organize
- Future city councils could allow the tax to expire, adversely affecting city services

*What tax rate is appropriate?*

City Council needs to consider the amount of tax being requested and the amount of stability that it will provide in future years. Going for small incremental tax increases has proved ineffective at stabilizing the city's revenue sources.

City Council should also consider the likelihood of generating voter support for various tax rates. A tax rate perceived as too high could jeopardize its chances of passing at the polls.

**II. SUMMARY AND ALTERNATIVES:**

City Council has the opportunity to address their longstanding goal of fiscal sustainability. Staff has been directed to initially evaluate two options: property tax and lodging tax. Alternatives include:

1. Direct staff to plan on placing a 5-10 mill property tax question on the fall ballot in 2021.
2. Select another property tax mill levy rate for consideration by the voters.
3. Do not pursue a property tax.
4. Repurpose the current 1% lodging tax from tourist amenities to destination marketing for a term of 10 years – 2021 election.
5. Submit to the voters an additional 1% lodging tax (2% City + 2% LMD).
6. Maintain 1% lodging tax for tourist amenities (no change).
7. Direct staff to evaluate other forms of taxation.

**III. STAFF RECOMMENDATION:**

Staff recommends option 1 above, submitting a property tax question to the electors in 2021 of 5 to 10 mills, designated for central government services, as a perpetual tax.

Staff also recommends option 4 above, submitting a lodging tax question to the electors in 2021 repurposing the 2A funds from tourist amenities to destination marketing, as a finite tax with an expiration date in 10 years.

**IV. FISCAL IMPACT:**

Currently, a 1% lodging tax generates approximately **\$1,100,000 per year** in the City of Steamboat Springs.

One mil of property tax generates approximately **\$730,000 per year**, based on current assessed valuation.

**V. LEGAL ISSUES:**

Both tax options will require approval by the electorate.

**VI. CONFLICTS OR ENVIRONMENTAL ISSUES:**

Not applicable.

**VII. CONSISTENCY WITH COUNCIL GOALS AND POLICIES:**

This effort is consistent with City Council's long-standing fiscal sustainability goals:

*Previous years: Develop a long-term fiscal sustainability plan for the City, which incorporates revenue diversification, cost recovery, asset performance for facilities, and community education and outreach.*

*Current 2019-20 goal: Sustainable Funding: Consider destination marketing funding; lift tax; Howelsen Hill; community support; mental health.*

**ATTACHMENTS:**

Attachment 1: PowerPoint Presentation.

Attachment 2: Comparable Cities table.