

# CITY COUNCIL COMMUNICATION FORM

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

**THROUGH:** N/A

**DATE:** February 9, 2021

**ITEM:** Fiscal Sustainability- Property Tax Scenarios.

---

DIRECTION  
 INFORMATION  
 ORDINANCE  
 MOTION  
 RESOLUTION  
 PROCLAMATION

---

## **I. REQUEST/ISSUE & BACKGROUND INFORMATION:**

### **Background**

During the last work session on this topic, staff presented City Council with some key questions regarding a potential property tax ballot question in 2021. Council consensus was to move forward with a property tax ballot question come this November.

Council also indicated a preference that the property tax proposal be "revenue positive" versus "revenue neutral". Council did request additional information regarding the future funding needs of the city.

City Council majority also directed staff to limit any property tax increase to a maximum of five (5) mills.

When discussing whether the tax should be dedicated for a specific purpose or project, council did not indicate a strong desire to dedicate the tax revenues and said they would need additional feedback from the community before earmarking the revenues.

Today's discussion will be focusing on funding needs of the city, evaluating different scenarios, and discussion of potential offsets and impacts. Our hope today is that Council will provide direction on moving forward with a five-mil property tax increase, indicate a preferred scenario, and direct staff to draft an ordinance for consideration by Council.

#### Fiscal Sustainability Goal

Following is the City Council's current Fiscal Sustainability Goal from the December 2020 retreat:

*Fiscal Sustainability: Focus on diversification of city revenues; regular monitoring of city revenues and expenses; maintenance of quality of life including attainable housing; economic development, including broadband infrastructure, business retention, expansion and recruitment, and dedicated funding mechanisms.*

#### Problem Statement

City Council has agreed to the following problem statement: *The city is too reliant upon sales tax a primary revenue source.*

Additionally, expectations for levels of service continue to increase as the city grows, and continuing on the current track of service reductions will only lead to the inevitable: improve our revenue picture or negatively impact the quality of life that we all enjoy.

Tackling this issue is consistent with City Council's vision statement to ensure "economic sustainability" for the long-term.

#### **Funding Needs**

For the past decade, the City has been able to adequately fund municipal operations to meet the needs of the community. This has been accomplished in the face of rising costs and a continued increase of service level expectations. Annual personnel costs have increased 5-8% across the entire organization with higher costs in specific departments. Transportation expenditures increased 50% from 2011-2019 with a decrease in service levels due to escalating personnel costs, and Public Safety expenditures increased 54% during the same time period. Additionally, Public Safety is not adequately funded to meet their strategic plan goals related to fire station needs and personnel.

As the community continues to grow in population, so does the level of service expectations with respect to city services and programs. As street lane miles continue to grow (6-mile increase from 2010-2019), so too does the cost of high-quality snowplowing and frequent snow removal the city provides. The city continues to provide high quality recreational facilities and subsidizes many of the recreation and youth programs which continue to grow in popularity. The

high service level expectations continue to put pressure on the department operating budgets and the city's General Fund.

Furthermore, while the City has been able to adequately fund municipal operations with the continued pressure on the General Fund, it has been accomplished at the expense of maintaining the existing city assets, as well as capital investment for future growth. The City maintains over 130 buildings and structures, many of which are reaching the end of their life cycle and are in need of investment. In 2018, the city contracted with EMG to audit 57 facilities and report on current conditions and identify future capital maintenance needs. The report identified over \$2.7M in unbudgeted deferred maintenance needs.

Additionally, a 2016 street pavement analysis determined the City was falling short of annual pavement maintenance and recommended the City increase their annual investment to \$1.5-2.0M. While the City was able to increase the annual pavement maintenance program, the budget was reduced by 50% in 2020, and is short of the recommended amount by roughly \$300K in the next few years.

The Parks, Recreation, Open Space, Trails, and Yampa River Master Plan has identified roughly \$10.4M in deferred maintenance, which is considered by many to be the City's greatest asset.

#### Deferred Maintenance Costs

- Facilities
  - \$2.7M in unbudgeted deferred maintenance needs
- Streets
  - Reduced paving program by 50% (\$800K) in 2020
  - Reduced by \$300K in 2021-2023
- Parks, Recreation, Open Space, Trails, and Yampa River Master Plan
  - \$10.4M in deferred maintenance

With respect to capital investment, the City currently has \$28M in unfunded projects and roughly \$95M in identified needs with no identified funding source. Without these projects, the City is not able to adequately meet the future needs of the community.

#### Capital Improvement Plan

- 6-Year CIP: \$28M in projects unfunded
- Parked Projects: \$95M – identified needs with no funding source

#### Service Level Expectations

As stated above, as the community grows expectations for high levels of service grow with it. Unless we can diversify our revenue sources and mitigate some of the ups and downs of the economic swings resulting from sales tax dependency,

service levels will eventually suffer. Following is a list of services that the city provides and that the community has become accustomed to. Already we have had to reduce some of these services to maintain a balanced budget.

#### Community Level of Service Expectations

- Free Transit
- High Quality Snowplowing
- Frequent Snow Removal
- Subsidized Recreation and Youth Programs
- Substantial Community Support Contributions
- High Quality Recreation Facilities
- High Quality Broadband Access – Location Neutral
- Public Safety – Police, Fire, and EMS

#### **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 they 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 payment, 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.

### **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 finite or permanent?*

The property tax could sunset after a designated amount of time (i.e. 10 years) or could not have any sunset date.

#### Pros:

- Creates accountability in the eyes of the taxpayer, requiring policy makers to demonstrate results and 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 if not replaced by another revenue source.
- Requires future elections which can be costly and adds uncertainty.
- 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.

## **II. SUMMARY AND ALTERNATIVES:**

Per City Council's request, staff has provided several scenarios for Council to consider:

### Scenario 1 - Property Tax Dedicated to Deferred Maintenance

This scenario includes a proposed 5 mill property tax dedicated to Facilities and Public Works deferred maintenance with a 10-year sunset date.

#### Pros:

- Addresses the city's deferred maintenance funding deficiency without decreasing established service levels.
- Sunset date allows Council and citizens evaluate the effectiveness of the tax in 10 years.

#### Cons:

- Doesn't address operational service levels.
- Not a permanent source of funding.

### Scenario 2 - Unrestricted Property Tax

This scenario includes a proposed 5 mill property tax without restriction and without a sunset date.

#### Pros:

- Could be utilized for deferred maintenance, operational funding deficiencies, or capital funding deficiencies.
- Without a sunset date, this creates a long-term fiscal sustainability solution.

#### Cons:

- Unrestricted property tax could be difficult to get approved by the voters.

### Scenario 3 - Property Tax Fully Offset by Reduction in Sales/Use Tax Rate

This scenario includes a proposed 5 mill property tax offset with an equal reduction in the sales and use tax rate. Based on 2019 sales and use tax collections, this reduction would need to be approximately 0.46% taking the city's sales tax rate from 4.5% to 4.04%.

#### Pros:

- Reduces the sales tax, which is considered a regressive tax.
- Provides for revenue diversification.

#### Cons:

- Transfers a portion of tax burden from non-residents to property owners.

Under this scenario staff estimates that there still will be a financial impact to residents and the sales tax reduction will not completely offset the property tax addition for all income levels. The average increase to property tax would be about \$200/year, however the sales tax savings is estimated to be about \$60/year for an average household income.

Scenario 4 - Property Tax Partially Offset by Reduction in Sales/Use Tax Rate

This scenario includes a proposed 5 mill property tax partially offset with a .25% reduction in the sales and use tax rate. This option is revenue positive and it would take the city's sales tax rate from 4.5% to 4.25%.

Pros:

- Reduces the sales tax, which is considered a regressive tax.
- Provides for revenue diversification.

Cons:

- Transfers a portion of tax burden from non-residents to property owners.

**III. STAFF RECOMMENDATION:**

Staff recommends moving forward with a 5 mill property tax on the 2021 ballot. Specifically, staff recommends Scenario 1 that includes dedicating the revenue to deferred maintenance with a 10-year sunset date.

Staff supports a "revenue positive" solution to sustain service level expectations and achieve Council's long-term fiscal sustainability goal.

Staff suggests Council review the Community Survey results in March for further guidance.

**IV. FISCAL IMPACT:**

Five mills of property tax generates approximately **\$3,650,000 per year**, based on current assessed valuation.

**V. LEGAL ISSUES:**

All scenarios will require approval by the electorate.

**VI. CONFLICTS OR ENVIRONMENTAL ISSUES:**

None noted.

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

This effort is consistent with City Council's current fiscal sustainability goals.

**ATTACHMENTS:**

Attachment 1: PowerPoint Presentation.