Request for City Council Action

Date: March 3, 2015

Agenda Section: General Business No. 6	**Originating Departments:** Finance and City Manager
Item: Discussion of New Revenue Sources for FY 2016 **No.** 6.5	**Approved:**

Background and Summary:

The 5 year budget revenue/expenditure projection estimates contained in the FY 2015 Budget, project a FY 2016 deficit of $782,000. Since the estimates were developed, FY2015 revenues have improved modestly which has also improved the outlook for future years revenues. In addition, several known expense reductions in worker's compensation insurance and Non Bargaining Unit Employee pension rates have reduced projected deficits. Staff has completed the review of 70% of departmental budget requests for FY2016 and thus far there are not any substantial increases or decrease. About $300,000 deficit remains for FY2016 and will require further action.

There is a recent issue that has arisen. Governor Rauner has proposed a 50% cut in Local Government Distributive Fund (LGDF) revenues the City receives from the State on a per capita basis. This includes the State Income Tax and State Use Tax. The Illinois Municipal League reports annual estimates for these taxes and for FY2016 estimates that State Income Tax would provide the City $99 per resident with an additional $19.40 in Use Tax per resident. If the Governor's proposed reduction is approved by the Legislation in July, it would cost the City between $1.4 and $1.5 million. This loss of revenue is not reflected in any of the current projections.

During recent Council meetings the prospect of instituting new taxes and/or increasing existing taxes has been raised. The following is a brief discussion the key elements, issues and impact of three (3) potential new revenue sources for the City that include a Food & Beverage Tax, a Package Liquor Tax or an increase in the Home Rule Sales Tax. At the last Council meeting there was a consensus to use the majority of the revenues from these new resources for needed Capital Improvement Projects (CIP) which the City would not otherwise be able to undertake and to support strategic initiatives such as the Downtown Redevelopment.

Engineering Approval Obtained	Finance Approval Obtained	Legal Approval Obtained	Approval Obtained	Manager's Approval Obtained

Council Action: Motion by: ______________________ 2nd by ______________ To: _________________

Food and Beverage:

A Food & Beverage Tax of 1% would generate approximately $800,000 in additional revenue. This is based on a Standard Industrial Classification (SIC) definition on what items would be taxed and what establishments would subject to the tax. This definition is limited to a “restaurant” environment where items are generally prepared on premises for immediate consumption on premises. Staff has reviewed other communities who levy a Food & Beverage Tax, as well as the City of Carbondale previously enacted Ordinance 82-12, which created a similar tax. What has been seen is a very wide variety of definitions. To enact an ordinance that equitably defines taxable sales will take much more input from the Council and those affected by such an ordinance.

Another factor to be considered is that under the current SIC definition of who will be required to charge this tax, 120 establishments would be involved. The administration (data collection, follow up, and funds collection) will require one additional financial staff member at an estimated annual cost of $40,000 to $50,000 including benefits. As the definition of who this tax will effect broadens, so does the administrative cost.

Packaged Liquor:

A 1% Package Liquor Tax would generate approximately $125,000. This amount does not package liquor sales from grocery stores that would also be subject to the tax but for whom there is not current data available to determine the additional amount of potential tax revenues. All cities who collect a package liquor tax regulate it as part of the licensing for all liquor establishments. Because this is a locally imposed and collected tax, there will be an administrative cost associated with this tax.

Both the Food & Beverage Tax and the Package Liquor Tax can be enacted by the City Council with collections begun within 60-90 days.

Increase in Home Rule Sales Tax:

Another possibility to increase our tax revenue would be to raise our Home Rule Sales Tax. The amount under consideration is ¼ %. This is estimated to increase annual revenue by $1,040,000. Because this tax is collected at the State level, the City will not incur an increase in administrative effort or cost. The State only allows increases in Home Rule Sales Taxes to occur on two dates with any calendar year. To be effective July 1, 2015 an Ordinance must be passed by March 31, 2015 and to effective January 1, 2016 an Ordinance must be passed by September 1, 2015. By meeting the March deadline, the City would be able to collect 10 months of increased revenues. If the September deadline is selected, the City would only collect one month of increased revenues.

One real negative to the addition of a ¼% tax is that it brings the City’s Home Rule Sales Tax rate to 2 ¼% and thereby increasing the overall sales tax rate to 8 ¾ %, which would be the highest in the area. There was some concern expressed that this tax increase would negatively impact overall sales. Also of concern was the idea that the revenues from the increase would be more difficult to set aside to fulfill the intended uses. This is not an issue. The amount designated to be set aside would be placed in the Local Improvement Fund and any desired “special projects” would have to be budgeted for and included in the annual CIP.

Conclusions and Recommendations:

Timing and flexibility are two primary concerns. City staff needs more time to fully investigate the Food & Beverage Tax definition and implementation process and to get input from those impacted by the tax. The Package Liquor Tax is straight forward and easily implemented.

The City Council must adopt a budget by April 30. However, final action on the State of Illinois budget and Governor’s proposed LGDF changes will not be known until July or later. These are two important dates because if the City passes only the Food & Beverage Tax and the Package Liquor Tax in April and the Governor’s proposed cuts to the LGDF become reality, the City will be faced with an overall negative revenue impact and the “special projects” the City Council desires to see implemented will not come to fruition as it will be necessary to use all of the new revenues generated to replace the lost LGDF funds.

Staff has reviewed these options and the desires of the City Council and concludes that the safe and most prudent option is to increase the Home Rule Sales Tax by ¼% with a one year sunset provision. This guarantees two things; first the City insulates itself against any reduction in the LGDF and second it reserves the option for the City Council to implement a Food & Beverage Tax and Package Liquor Tax after the State determines the fate of the LGDF.

If the State does not decrease the LGDF this year, the City Council has the option of sunsetting the ¼% increase in September with an effective date of January 1, 2016.

Recommended Action:

The City Council is requested to hold discussions on creating additional revenues and provide the City Manager with direction on what tax increase documents should be prepared for action by the City Council at the March 24, 2015 meeting.