CITY OF SALEM

555 Liberty St SE
Salem, OR 97301

Staff Report

File #: 19-315
Version: 1

Date: 7/8/2019
Item #:

TO: Mayor and City Council

THROUGH: Steve Powers, City Manager

FROM: Robert Barron, Chief Financial Officer

SUBJECT:

Revenue Options for the General Fund

Ward(s): All Wards
Councilor(s): All Councilors
Neighborhood(s): All Neighborhoods
Result Area(s): Good Governance; Natural Environment Stewardship; Safe Community; Safe, Reliable, and Efficient Infrastructure; Strong and Diverse Economy; Welcoming and Livable Community

ISSUE:

Shall City Council direct the City Manager to prepare two ordinances for Council's consideration to enact an operating fee and an employee-paid payroll tax to support ongoing services in the General Fund?

RECOMMENDATION:

Direct the City Manager to prepare an ordinance for Council's consideration to enact an operating fee to support General Fund services with the following components:

1. Target revenue amount of $8.2 million
2. Monthly rate at $10.00 for residential utility accounts, $8.00 per multi-family unit, and $30.00 for non-residential accounts
3. Ratio of 1:3 for residential to non-residential rates
4. Low-income discount of $10.00 per month for qualified residential account holders

Direct the City Manager to prepare an ordinance for Council's consideration to enact an employee-paid payroll tax to support ongoing General Fund services with the following components:

1. Target revenue amount of $8 million
2. Rate at 0.3 percent of gross wages
3. Tax applies to employees working within Salem city limits

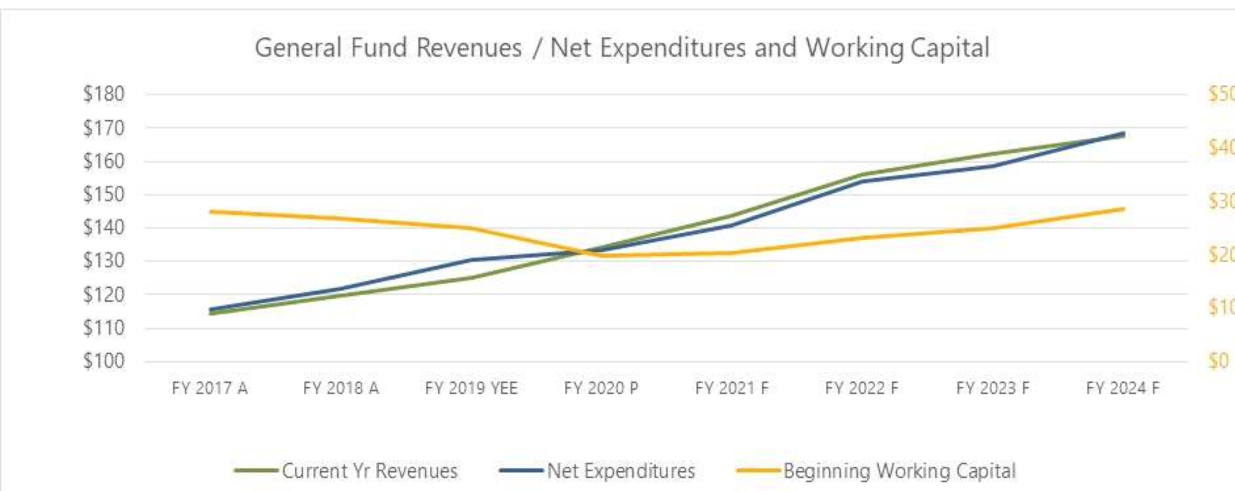
SUMMARY:

There is a structural imbalance in the City's General Fund. Current revenues are insufficient to fund current services. The gap between revenues and expenditures worsens with the increasing demand for services as Salem's population grows and as the City's expenses increase.

The City has used working capital, or our savings account, to close the gap between recurring revenues and the cost of services. Working capital is a finite resource. Continued use of working capital to balance ongoing expenses will cause almost full depletion of savings by FY 2022. Without additional revenue, reductions to services would be required for the City to adopt a balanced FY 2022 budget in compliance with Oregon budget law.

To correct the structural imbalance, the City Manager recommends that City Council consider proceeding with both a City operating fee and an employee-paid payroll tax that would generate approximately $16.2 million by FY 2022[1].

The recommendation combines the stabilizing, flat operating fee that provides immediate, short-term relief for the General Fund with an employee-paid payroll tax that is dynamic and more likely to keep pace with future increases in General Fund expenditures. The combination of the operating fee and payroll tax displayed below aligns revenues with expenses during the forecast period and provides funding to consider capacity increases to meet rising demand.



[1] Total revenue of $16.2 million is offset by estimated annual administration costs of $100,000 for the operating fee billing system support and customer service and $650,000 for the Oregon Department of Revenue administration and collection of the employee-paid payroll tax. The total revenue and offsetting expenses are included in the graph on this page.

FACTS AND FINDINGS:

During the June 17, 2019, work session, City Council discussed the City Manager's recommendation to enact an operating fee and an employee-paid payroll tax to support ongoing services in the General Fund. At the work session, members of Council requested staff provide additional information, primarily focusing on issues of equity, for both recommended revenue sources.

City Operating Fee

The City Manager's recommendation includes monthly fees for single family residential ($10.00), multifamily ($8.00), and non-residential ($30.00) utility account holders. Staff was asked to provide a rate structure mirroring the proportionate rate between residential and non-residential customers found in the City's streetlight fee of 1:4.82. Using this ratio and keeping the monthly residential rate at $10.00, the non-residential rate would be $48.20 per month, generating $600,000 more revenue each year. This rate structure and corresponding revenue is detailed in Attachment 1.

Additionally, Council members requested staff provide more information on how a low-income discount program could be applied to a City operating fee. The Utility Rate Relief Program currently serves approximately 160 elderly or disabled utility account holders who reside in Salem. Staff is working with Mid-Willamette Valley Community Action Agency to expand participation in the program.

With a planned expansion of the program, current research indicates qualifying account holders could increase substantially in the near term. Assistance recipients could automatically qualify to receive a $10.00 monthly discount for the operating fee on the utility bill. For every 100 participants in the program, the General Fund would forego $12,000 of annual revenue. As an example, if program participation increased to 600, the revenue collected would be reduced by $72,000 annually.

Employee-Paid Payroll Tax

Council asked staff for more information on two options to address equity concerns with the employee-paid payroll tax.

One idea was an exemption from the payroll tax for employees that make $20,000 or less per year. Staff increased the exemption threshold to full-time minimum wage, which equates to $11.25 per hour or $23,400 annually, because the recommendation is based on wage rate and not annual income. To maintain the revenue target of $8M with this exemption, the proposed tax rate would need to increase from 0.3 percent to 0.332 percent. This estimate is based on census data of individual incomes in Salem and varies from the table depicting household income that was used for the June 17 Work Session. More detail is available in Attachment 2.

A progressive rate structure for the payroll tax was also requested, with a focus on the structure Eugene recently enacted. The tax rate structure in Eugene's employee-paid payroll tax has two tiers. Employees earning more than minimum wage up to $15.00 per hour will pay a rate of 0.3 percent. Employees earning more than $15.00 per hour will pay a rate of 0.44 percent. Employees earning minimum wage are exempt from the payroll tax.

Following Eugene's employee-paid payroll tax model, including an exemption for minimum wage earners, Salem could adopt tiered rates lower than the Eugene model and still realize revenue of $8M. One example that maintains the revenue target is 0.2 percent for employees earning more than minimum wage up to $15.00 per hour and 0.35 percent for those that earn more than $15.00 per hour. Attachment 2 provides more information on this progressive rate structure.

Staff has continued conversation with the Department of Revenue (DOR) regarding a proposed employee-paid payroll tax in Salem. With competing priorities and current workload demands, the DOR has not committed to a specific timeframe for beginning work on a Salem tax. While administration costs and implementation timing are not yet finalized, the DOR indicates a minimum 12 month implementation period. DOR staff recommend aligning Salem's ordinance with State statute, maintaining a single rate tax structure, and a strong communication plan to educate businesses about the tax to lower administration costs and increase the rate of compliance.

Timing Considerations

If approved, staff would prepare an ordinance for the operating fee and return to Council in August. An ordinance for the employee-paid payroll tax could come before Council as soon as September.

If Council decides to refer either option to voters for approval for the election in May 2020, second reading of an ordinance and adoption of a resolution would need to occur at the very latest by February 24, 2020 to meet election requirements.

Staff will provide material for public outreach and engage in a robust information initiative following Council action on July 8.

Attachments:

1. Operating Fee with increased ratio
2. Payroll Tax - low-income exemption and progressive rate structure
3. June 17, 2019 Work Session materials