



KENAI PENINSULA BOROUGH

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DAVID R. CAREY
BOROUGH MAYOR

MEMORANDUM

TO: Milli Martin, Assembly President
Members, Kenai Peninsula Borough Assembly

FROM: *David R. Carey* David R. Carey, Borough Mayor

DATE: October 1, 2009

SUBJECT: Ordinance 2009- 49, Suspension of the Borough's 3% sales tax on vehicle fuel for the period January 1, 2010 to May 31, 2010

The Borough's General Fund, fund balance is now anticipated to come in higher than projected for the fiscal year ended June 30, 2009, due to the receipt of unbudgeted funds from the Federal Government for the PILT and Forestry receipt programs, under expenditure of department budgets, and interest earnings in excess of budgeted amounts. Spendable fund balance at June 30, 2009, is estimated to be \$24,604,294; the projected amount per the FY2010 budget was \$23,290,828, a difference of \$1,313,466.

Through this ordinance, I am proposing that a portion of this increase be used to reduce the future public tax burden.

The administration has looked at a number of options on how best to do this, some of which include the following: suspension of the borough's sales tax rate on fuel for motor vehicles during the period January 1, 2010 to May 31, 2010; changing to a flat tax of \$.05 per gallon of fuel versus the current 3% sales tax; and a rebate to the FY2011 property tax bills equal to approximately .15 mills. Below are comments regarding each of these options:

1. Suspension of the borough's sales tax on fuel for motor vehicles during the period January 1, 2010 to May 31, 2010.

One of the challenges with estimating the fiscal impact of this option is that the borough does not have exact sales tax revenue amounts that are generated from sales of fuel. Vendors within the borough are not required to disclose the amount of fuel they sell separately from other items sold. The borough's finance department has made an estimate of the fiscal impact based upon sales information that was received from some businesses in the borough that sell fuel. The reduction in sales tax revenue from suspending the borough's 3% sales tax on fuel during the period January 1, 2010 to May 31, 2010 is estimated to be between \$1,000,000 and \$1,400,000.

2. Changing to a flat tax of \$.05 per gallons versus the current 3 percent sales tax.

As mentioned in the previous option, the borough does not have exact sales tax revenue that is generated from fuel sales in the borough. The current estimate of sales tax revenue that is generated on fuel sales on an annual basis from the borough's 3 percent sales tax is between \$3.8 million to \$4.2 million. Using these same estimates, if the borough changed to a flat tax of \$.05 per gallon, the revenue estimate is between \$2.0 million and \$2.5 million, a reduction of around \$1.5 million.

There are a number of legal and practical concerns with this option. Variances in implementation and interpretation could cause the tax to be considered a new sales tax, a use tax or an excise tax. A new sales and use tax or an increase in the rate of levy is not effective until ratified by a majority of voters at an election. The earliest a vote could occur without a special election would be **October 2010**. Further a use tax rate must equal the sales tax rate. If the tax were collected at the pump it would almost certainly be considered a sales tax. The state and federal governments impose a flat tax on refined motor fuel on a per gallon basis as contemplated here. These taxes are collected at the wholesale level. The Borough does not currently collect any taxes at the wholesale level and this process may present a **practical** challenge. While an excise tax, which **taxes** the importation or manufacture of the product **within** the borough would not require ratification by a vote, the state has restricted certain taxes on refined fuel. Depending on how the tax is implemented and interpreted, state restrictions could present a legal obstacle.

3. A rebate on the FY2011 property tax bills equal to approximately .15 mills.

Another option considered is to provide a property tax credit equal to .15 mills on the FY2011 assessed values, for owners of record as of January 1, 2010. This credit would be based upon the FY2010 general fund taxable assessed values, be recognized in FY2010 and would equate to a credit of \$952,159 in property taxes and applied to the FY2011 tax bills. For financial purposes, the borough would recognize this credit in the current fiscal year, FY2010. The tax credit would be applied on total taxable assessed value of property subject to tax in the general fund in such a manner that the tax bill for each property is reduced by an amount that is the same percentage of the total taxable assessed value of the property.

This third option also presents legal concerns. These include running afoul of the public purpose doctrine, whether or not the borough has the authority to provide the credit.

The ordinance is being submitted using the reduction in sales tax on motor vehicle fuels for the period January 1, 2010 to May 31, 2010. If either of the other two options are considered, changes to the ordinance would be required. Below are the changes that would need to be made to the proposed ordinance for each option.

Changing to a flat tax of \$.05 per gallons would require the following changes:

- Replacement of the 3rd whereas and creation of a new 4th whereas:

WHEREAS, it is estimated that the Borough currently collects between \$3.8 million and \$4.2 million in sales tax revenue on an annual basis from the 3% sales tax on motor vehicle fuel; and

WHEREAS, it is estimated that if the Borough changed from a 3% sales tax to a flat tax of \$.05 per gallon, the estimated sales tax revenue on motor vehicle fuel would be in the range of \$2.0 million and \$2.5 million.

- Section 1 would need to be replaced with the following:

SECTION 1. That KPB 5.18.100(A) is hereby amended as follows:

A. Except as provided below [T]there is levied by the borough a consumer's sales tax of up to 3 percent maximum rate on all retail sales, on all rents, and on all services made or rendered within the borough, measured by the gross sales price of the seller. Any future increase to the sales tax maximum rate, as provided in this section, shall not take effect until ratified by at least 60 percent of voters at a regular borough election. There is also levied by the borough a sales tax of up to \$.05 per gallon on all wholesale sales of fuel made or rendered within the borough.

- Add a new Section 2 as follows:

SECTION 2. That the following proposition shall be placed on the ballot for the regular municipal election to be held October 5, 2010:

“Shall a flat tax of 5 cents per gallon be imposed on the wholesale sale of fuel sold within the boundaries of the borough?”

- Add a new Section 3 as follows:

SECTION 3. That if a majority of the voters voting on the question favor the proposition, then section one of this ordinance shall become effective immediately upon verification of the election by the assembly.

Changing the ordinance to provide a rebate on taxes would require the following changes:

- Replacement of the 3rd whereas with the following

WHEREAS, a property tax credit equal to .15 mills on the FY2010 taxable assessed values would reduce property tax revenue by \$952,159 and would be recognized in FY2010. The tax credit would be applied to the FY2011 tax bills on total taxable assessed value of property subject to tax in the general fund in such a manner that the tax bill for each property is reduced by an amount that is the same percentage of the total taxable assessed value of the property.

- Section 1 would need to be replaced with the following

SECTION 1. That the Borough will issue a tax credit on the FY2011 tax bills equal to the taxable assessed value of .15 mill of the FY2010 taxable value in the general fund. The tax credit will be recognized in the Borough's General Fund in FY2010.