

CITY OF UNALASKA
UNALASKA, ALASKA

ORDINANCE 2021-11

AN ORDINANCE AMENDING UNALASKA CODE OF ORDINANCES CHAPTER 6.40, SALES TAX, TO INCREASE THE RATE OF THE SALES TAX LEVY FROM THREE PERCENT (3%) TO FOUR PERCENT (4%) FOR THE PURPOSE OF CREATING A UTILITY INFRASTRUCTURE FUND TO SUPPLEMENT THE UTILITY PROPRIETARY FUNDS

WHEREAS, the City of Unalaska determined, through a detailed rate study for each public utility, that customer rate increases were necessary to achieve a Debt Service Coverage Ratio beyond 1.25 for each Utility Proprietary Fund and to continue operations at the current level of service; and

WHEREAS, the Unalaska City Council authorized rate increases for each utility, to be phased in over four years, through Resolutions 2021-26 and 2021-35, adopted on May 10 and May 25, 2021, respectively, and Ordinance 2021-10, the FY22 Schedule of Fees, adopted on June 22, 2021; and

WHEREAS, these utility rate increases do not meet the full revenue requirement identified in the rate study for each utility; and

WHEREAS, the Unalaska City Council has determined it is necessary to increase the sales tax levy and use the increased sales tax revenue to create a Utility Infrastructure Fund to supplement the Utility Proprietary Funds to be used for utility operational and infrastructure needs.

NOW THEREFORE, BE IT ENACTED BY THE UNALASKA CITY COUNCIL:

Section 1: Classification. This ordinance is a code ordinance.

Section 2: Amendment of UCO §6.40.020. Section 6.40.020, Levy of Tax, is hereby amended to read as follows: [new language is underlined, deleted language is overstruck]:

§ 6.40.020 LEVY OF TAX

A sales tax is levied on all sales, rents and services made in the City at the rate of ~~three percent (3%)~~ four percent (4%) of the selling price. The burden of this tax rests upon the consumer. This tax shall not be levied on raw seafood products taxed pursuant to Chapter 6.44. The tax on services shall not include salaries or wages received by an employee from an employer, but shall include consideration for furnishing labor and materials for accomplishing a specific result.

Section 3: Amendment of UCO §6.40.025. Section 6.40.025, Tax Schedule, is hereby amended to read as follows: [new language is underlined, deleted language is overstruck]:

§ 6.40.025 TAX SCHEDULE

The amount of tax to be added to the lease, rental, transfer or assignment of any right, title or interest in any goods, personal property of any kind, real property and any provision of labor or services for a consideration subject to levy under § 6.40.020 shall be in accordance with the following schedule:

<u>Price</u>	<u>Tax</u>
\$0.01 - \$0.30	\$0.01
\$0.31 - \$0.60	\$0.02
\$0.61 - \$1.00	\$0.03
<u>\$0.01 - \$0.25</u>	<u>\$0.01</u>
<u>\$0.26 - \$0.50</u>	<u>\$0.02</u>
<u>\$0.51 - \$0.75</u>	<u>\$0.03</u>
<u>\$0.76 - \$1.00</u>	<u>\$0.04</u>

Section 4: Use of Sales Tax Increase. Section 6.40 is hereby amended by adding a new section 6.40.150, as follows:

§ 6.40.150 Application of Tax Revenues. Subject to annual appropriation by the City Council, the difference in sales tax revenues generated by a 4% rate instead of a 3% rate shall be deposited in a newly created Utility Infrastructure Fund to use for utility operational and infrastructure needs.

Section 5: Authorization of Election. The City of Unalaska, at the October 5, 2021 municipal election, shall conduct an election on the question of whether there should be an increase of the sales tax rate by placing before qualified voters a proposition for approval or rejection. The City Clerk is directed to take all action necessary to arrange for this election. The proposition must receive a majority vote of those qualified voters actually voting on the question in order to be approved by the voters. The proposition shall be presented printed on a ballot substantially in the following form:

Should the City of Unalaska increase the rate of Sales Tax from three percent (3%) to four percent (4%) for the purpose of creating a Utility Infrastructure Fund to supplement the Utility Proprietary Funds, to be used for utility operational and infrastructure needs?

Yes No

Section 6: Effective Date. This ordinance shall become effective January 1, 2022, following certification of the election by the City of Unalaska, showing ratification by a majority of the qualified voters of the City of Unalaska voting at the election.

PASSED AND ADOPTED by a duly constituted quorum of the Unalaska City Council on August 10, 2021.

 Vincent M. Tutiakoff, Sr.
 Mayor

ATTEST:

 Marjie Veeder, CMC
 City Clerk

MEMORANDUM TO COUNCIL

To: Mayor and City Council Members
From: Marjie Veeder, City Clerk and Dan Winters, Director of Public Utilities
Through: Erin Reinders, City Manager
Date: July 27, 2021
Re: Ordinance 2021-11: Amending UCO Chapter 6.40, Sales Tax, to increase the rate of the sales tax levy from 3% to 4% for the purpose of creating a Utility Infrastructure Fund to supplement the Utility Proprietary Funds

SUMMARY: This ordinance is presented in response to Council's directive issued on May 25, 2021. The directive was issued following a recommendation in the utility rate studies to increase sales tax by 1% to create a Utility Infrastructure Fund (UIF) because utility rate increases recently authorized by Council will not fully meet revenue requirements for the public utilities. Staff recommends approval.

PREVIOUS COUNCIL ACTION: In 1988, the sales tax levy was increased from 2% to 3%, and was ratified by Unalaska's voters. The revenue generated by the 1% increase was dedicated to fund capital improvement projects. This fund is still in existence today.

In 1996, council adopted Ordinance 1996-14 increasing the sales tax levy from 3% to 4% with increased revenue dedicated to the existing special revenue fund for capital improvements. This tax increase was not ratified by voters.

Council last addressed the sales tax levy with Ordinance 2017-14, amending Title 6 to increase sales tax on alcohol, tobacco and marijuana by 3%, thereby taxing those particular products at the rate of 6%. This proposition was not ratified by Unalaska's voters, with 263 yes votes and 298 no votes.

BACKGROUND: Council heard numerous presentations about utility rates starting in February 2021, and authorized rate increases for each utility to be phased in over four years, through Resolutions 2021-26 and 2021-35, adopted on May 10 and May 25, 2021, respectively, and Ordinance 2021-10, the FY22 Schedule of Fees and Services, adopted on June 22, 2021.

The recent rate increases were necessary to achieve a Debt Service Coverage Ratio beyond 1.25 for each Utility Proprietary Fund and to continue operations at the current level of service. These utility rate increases do not meet the full revenue requirements identified in the rate study for each utility.

To address this revenue shortfall, Council directed staff to prepare an ordinance to increase the sales tax levy by 1% and create a Utility Infrastructure Fund for the purpose of supplementing the Utility Proprietary Funds.

The table below shows the complete picture of the revenue shortfalls for each utility proprietary fund, both before and after the recent rate increases. The combined revenue shortfall for all the utilities is (\$4,448,032) -- after the rate increases.

**REVENUE REQUIREMENT SHORTFALL
Before and After Rate Increases**

	Electric 6.1% Rate Inc.	Water 3.6% Rate Inc.	Solid Waste 33% Rate Inc.	Wastewtaer 40% Rate Inc.	Totals For All Utilities
Current Revenue Requirement	\$ 9,762,823	\$ 3,530,573	\$ 4,102,820	\$ 4,319,505	\$21,715,721
Current Revenue	\$ 7,248,373	\$ 2,616,686	\$ 2,562,531	\$ 2,468,212	\$14,895,802
Current Revenue Shortfall	\$ (2,514,450)	\$ (913,887)	\$ (1,540,289)	\$ (1,851,293)	\$ (6,819,919)
Revenue from Rate Inc.	\$ 444,436	\$ 94,532	\$ 845,635	\$ 987,284	\$ 2,371,887
Revenue Shortfall After Rate Inc.	\$ (2,070,014)	\$ (819,355)	\$ (694,654)	\$ (864,009)	\$ (4,448,032)

DISCUSSION: Ordinance 2021-11 (a) increases the sales tax levy from 3% to 4%; (b) includes language specifically dedicating the increased revenue to a Utility Infrastructure Fund to be used for utility operational and infrastructure expenses; and (c) outlines the proposition language for the ballot and an effective date should the proposition receive voter approval.

DEDICATION OF REVENUE

The dedication language in the ordinance is prefaced with the phrase “Subject to annual appropriation by the City Council ...” All expenditures of City funds are “subject to appropriation” in that the City cannot spend money that has not been authorized to be spent by the Council.

The phrase “subject to appropriation” also means that Council could not be forced to make a specific appropriation to the UIF based on the dedication language and Council has the freedom to appropriate the funds elsewhere without violating this section of code.

If the phrase “subject to appropriation” is removed, it would not impact the validity of the remaining language of the dedication, and transfers to the UIF would be required as set out in the dedication language.

Ordinances ratified by voter approval, as is required for increases in the sales tax levy, cannot be changed by City Council for a period of two years. If the phrase “subject to appropriation” is removed from the ordinance, the result is that council cannot appropriate these funds elsewhere for a minimum of two years.

VOTER RATIFICATION

Any increase in the sales tax levy must be approved by voters. As drafted, the ordinance sets the question for the October 5, 2021 general municipal election, which will be certified by Council no later than October 12, 2021. The effective date for the sales tax increase is January 1, 2022 to allow time for City staff to prepare for the increased tax rate and to inform sales tax collectors of the new rate; to allow time for collectors to implement the new levy; and to set the new rate at the beginning of a reporting quarter.

FINANCIAL IMPLICATIONS: The increased sales tax revenue will be dedicated to the UIF to provide cash flow to supplement the utility proprietary funds, both for operational and infrastructure needs.

There was some discussion at previous council meetings of increasing the sales tax levy beyond the 1% increase recommended by Aldrich, at either 1.5% or 2%.

The following table shows sales tax revenue for the last four years, using actuals for FY18-20, and unaudited revenue received for FY21. (FY21 sales tax revenue is down compared to prior years and it is believed to be due to the coronavirus pandemic and resulting decrease in sales in some business sectors.)

3% Sales Tax Revenue	
FY18	\$ 10,568,302
FY19	\$ 10,928,892
FY20	\$ 10,639,924
FY21 (unaudited)	\$ 9,480,045
Four Year Average	\$ 10,404,291

The four-year average sales tax revenue is \$10,404,291. Using the four year average, we calculated estimated sales tax revenue based on increases to the sales tax levy at 1%, 1.25%, 1.5% and 2%. We also calculated the resulting amounts to be funneled to the UIF (the portion above the existing 3% levy); and the revenue requirement shortfall (the needed \$4,448,032 less the portion dedicated to the UIF):

Sales Tax Rate Increase	Estimated Total Sales Tax Revenue	Portion to UIF	Revenue Requirement Shortfall
1% increase - 4% Tax	\$ 13,872,388	\$ 3,468,097	\$ (979,935)
1.25% increase - 4.25% Tax	\$ 14,739,412	\$ 4,335,121	\$ (112,911)
1.5% increase - 4.5% Tax	\$ 15,606,436	\$ 5,202,145	\$ 754,113
2% increase - 5% Tax	\$ 17,340,485	\$ 6,936,194	\$ 2,488,162

As you can see, a 1% sales tax increase does not fully cover the combined revenue shortfall for all utilities of \$4,448,032 and misses the mark by \$979,935. An increase of 1.25% misses the mark by \$112,911; and a 1.5% increase exceeds the goal by \$754,113.

The Department of Public Utilities will continue their efforts to increase efficiencies and trim the budget in order to further reduce this shortfall through cost savings, just as was done for the FY22 budget.

Presently, revenue shortfalls are covered by the unrestricted net assets for each utility, and this practice would continue if the UIF cannot cover the full revenue requirements of the utilities. It should be noted that additional sales tax revenue due to an increase in the sales tax levy will not be received until after the first quarter of 2022 as the ordinance is presently written.

Additionally, the CMMP shows multiple capital improvements for the utility proprietary funds, and continued depletion of the unrestricted net assets will impede our ability to pay for capital project improvements for the utilities.

ALTERNATIVES: City Council may approve the ordinance as presented or not; and can amend the ordinance, including the rate of the proposed increase in the sales tax levy or the dedication language, before public hearing and final approval, which is presently scheduled for August 10, 2021.

If council chooses to amend the ordinance, staff provides language for proposed motions, as follows:

To change the sales tax levy: “I move to amend Ordinance 2021-11 as necessary to reflect an increase in the sales tax levy from 3% to _____%” inserting the desired rate in the blank.

To remove the phrase “subject to appropriation” in the dedication: “I move to amend Section 4 of Ordinance 2021-11 to strike the phrase ‘Subject to annual appropriation by the City Council’.”

The ordinance will then be amended and presented to council on August 10 for public hearing, second reading and potential adoption. In order to be included on the October ballot, the ordinance must be approved no later than the second meeting in August, which is August 24, 2021.

LEGAL: This ordinance has been developed with the assistance of the City Attorney.

STAFF RECOMMENDATION: This ordinance, showing a 1% increase to the sales tax levy, is presented in accord with the council’s directive. Staff recommends approval of Ordinance 2021-11 increasing the sales tax levy from 3% to 4%, and the creation of a UIF. It is Council’s decision as to the amount of the sales tax increase.

PROPOSED MOTION: I move to schedule Ordinance 2021-11 for public hearing, second reading and adoption on August 10, 2021.

CITY MANAGER COMMENTS: This ordinance has been developed based on council’s directive. I support adoption of Ordinance 2021-11 in order to meet revenue requirements for continued operation of the public utilities.