City of Salem
Revenue Task Force

PRE-READ PACKET
JANUARY 2024

Welcome to the Task Force!

Thank you for your interest in and commitment to solving the City of Salem's forthcoming revenue challenge. City leadership and staff are extremely grateful for your passion and stewardship. The efforts of dedicated community members like you are vital for ensuring the City can continue to provide excellent services to the Salem community in the years to come.

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I. WHAT IS THE CHALLENGE?

Salem is facing a significant budget shortfall, and the City's projected revenues will soon not be enough to pay for the services we provide today through the General Fund. These services include police, fire, public safety, parks and recreation, library, land use planning and zoning, enforcement of codes or rules to maintain neighborhood livability, social services that help those in need, municipal court, and other services that provide a general citywide benefit.

As more people live in our community, the demand for and cost of services increase each year, but the revenue to provide those services grows at a slower rate. As a result, the cost of providing General Fund services is projected to be $15 million greater than revenues collected by June 2026.

For years, the City has relied on reducing costs and services, deferring on-going needs, and foregoing long-term investments to maintain compliance with financial policies and fiscally responsible operations. Additionally, implementing the City operations fee provided significant revenue. Even with these efforts and the one-time infusion of federal funds during the pandemic, the costs to provide ongoing services are greater than the revenues received to support those services, and costs continue to escalate faster than revenues.

Solving this General Fund deficit, or structural imbalance, is critical to maintaining City services and staffing levels. Closing this immediate funding gap will not increase community services or add staffing.

The Salem Revenue Task Force has two main responsibilities:

- Understanding the City's needs, evaluating different revenue scenarios, and reviewing information from City Council, the Budget Committee, and staff.
- Recommending to City council the **<u>means</u>** through which the City will pursue revenue. In other words, what new fees or taxes will the City attempt to collect?

If the City is unable to resolve the budget shortfall with additional revenue, then services will need to be reduced to adopt a balanced budget. In addition to the Task Force's work to identify new potential sources of revenue, the Budget Committee and City Council will develop options to reduce City services in conversation with our community. Ultimately, a balanced budget will likely result from both increased revenue and decreased services. To give a sense of scale, a $15 million reduction to services in the General Fund would be the equivalent of decreasing services by 65 police officers (about 20%); six fire stations ($2.3 million each); or all park maintenance ($9.3 million) and all Library services ($6 million).

This packet is intended to provide the necessary background information for Task Force members to understand the tax law that contributed to the budget shortfall and that continues to affect possible solutions, and the nature and scale of the revenue problem. This packet will also describe the possible revenue options that currently exist and introduce strategies that similar cities have pursued.

WHY A TASK FORCE?

The purpose of the revenue Task Force is to explore new, additional revenue sources and adjustment to fees to sustain services that do not have a dedicated revenue stream. Community Task Forces are a common tool used by cities to make strategic decisions that greatly affect residents. These short-term advisory committees are usually a group of representative stakeholders who are selected to develop a specific policy recommendation. Considerable care is taken to select the committee members. The Task Force will prepare a recommendation to the City Council, who will make the final decision.

HOW DID WE GET HERE? 1990'S OREGON TAX MEASURES

In the 1990s, Oregon voters passed two initiatives that restricted the amount of property tax that could be collected: Measure 5 and Measure 50. While these measures immediately reduced government revenues to a limited extent, they also set the stage for major structural deficits and severe revenue shortfalls for cities across the state.

Measure 5: Total Limits Across All Governments

Measure 5 limited the total amount of general property tax that could be collected. For general governments, this was limited to $10 per $1,000 of real market value for a property. So, for example, the property tax for a $100,000 home was limited to $1,000. This limit is a total limit across all general governments, so the total tax levied against one household by all local jurisdictions (e.g., city, county) cannot exceed that amount. So, in this example, the maximum of $1,000 is not just for the City of Salem. This $1,000 would have to be split between Salem, Marion or Polk County, and any special districts where the home is located, such as the Marion County Extension & 4-H Service District.

Measure 50: Permanent Rates, Assessed Value, Growth Limits

Permanent Rates: Measure 50 restricted property tax rates (percentages) to the rates they were in 1997. This means that cities like Salem cannot set property tax rates higher than this limit, though voters can temporarily increase these limits through a local option levy—which we will talk about later.

Assessed Value: Measure 50 also separated property tax from a property's real market value—the dollar value that a home or parcel of land would be sold for to another party in the free market—by creating a new concept called **assessed value**, an amount at which properties would be taxed that is *artificially lower* than real market value. As a result of Measure 50, **properties in Oregon are not taxed at their actual market value.**

Measure 50 set the initial assessed value of all properties to 90% of their value in 1997. So, our example home bought at $100,000 would have an assessed value of $90,000. Because of the $10 tax limit per $1,000 of value from Measure 5, this home could now only have a maximum property tax of $900 across all governments.

Market value of an example home purchased in 1997	$100,000
Maximum property tax before Measure 50	$1,000 Restricted by Measure 5
"Assessed Value" of Home after Measure 50	$90,000
Maximum property tax *after* Measure 50	$900

Growth Limits: Finally, and most importantly, Measure 50 **limited the maximum annual growth of assessed value to 3%**, even if the property value increased by far more. If our $100,000 home increased 15% in value to $115,000 the next year, its assessed value would be $92,700—only 3% greater than its assessed value the previous year.

EXAMPLE OF THE TAX IMPACT OF MEASURE 50 IN A SINGLE YEAR

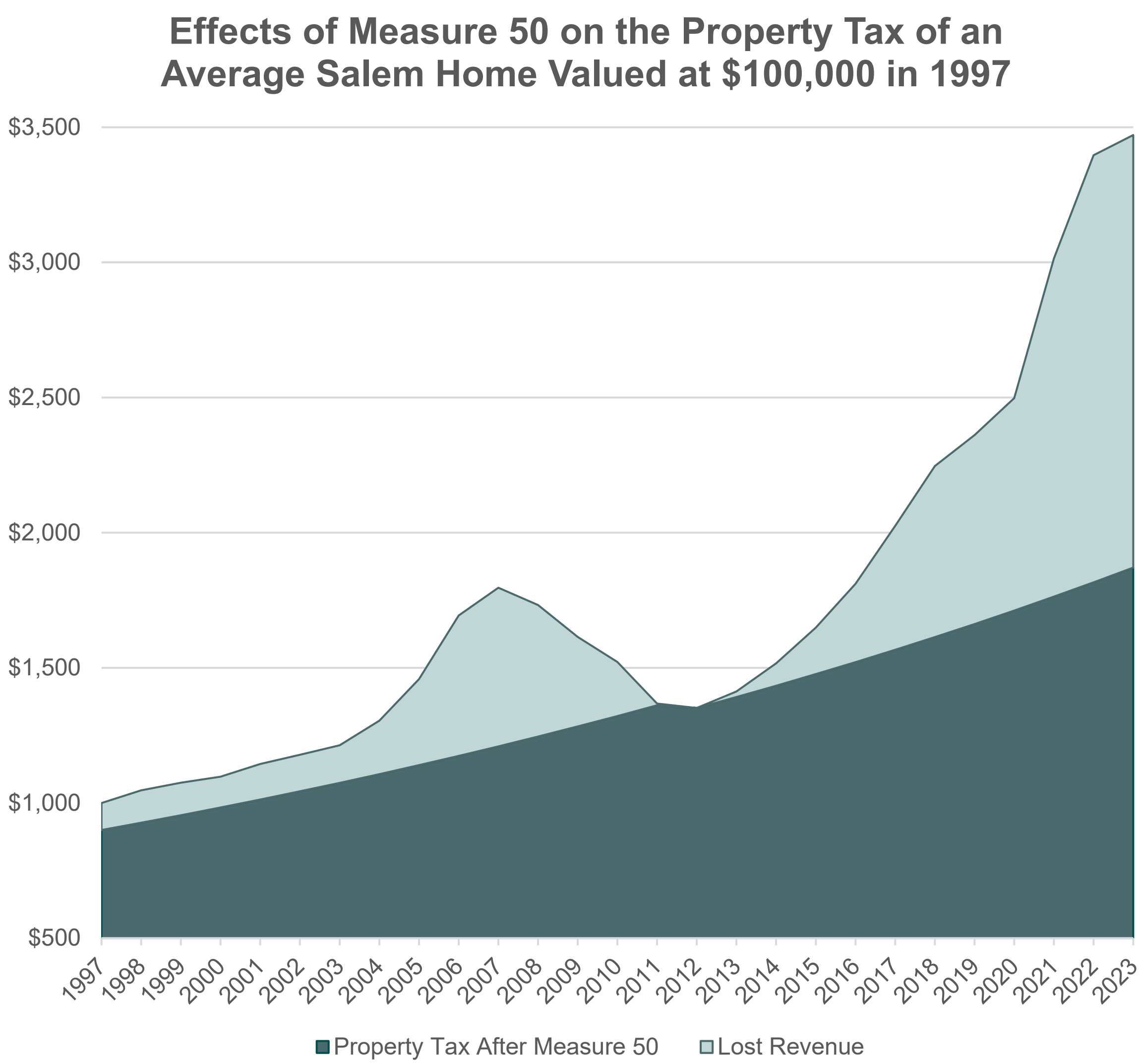
PRIOR TO MEASURE 50			
Market Value of House	Prior Year Property Tax	Increase in Market Value of House	New Year Property Tax
$100,000	$1,000	+15% → $115,000	$1,150
AFTER MEASURE 50			
"Assessed Value" of House	Prior Year Property Tax	Increase in Assessed Value of House	New Year Property Tax
$90,000	$900	+3% → $92,700	$927

These limits on the growth of assessed value meant that small amounts of lost revenue for cities in 1997 gradually got bigger and bigger over time. Average home values in Salem have increased 247% since 1997. Before Measure 50, property tax revenues would have gone up by approximately 247%. However, the average assessed value for all Salem homes is only 108% greater than 1997, meaning property tax values are about half as much as they would be prior to Measure 50. Our example house worth $100,000 in 1997 would provide local governments with nearly double the amount of revenue if Measure 50 was not passed (see table below). These lower levels of property tax, repeated across thousands and thousands of properties across Oregon, have decimated municipal government revenues throughout the state.

It's important to remember that Measure 5's cap on property taxes means that even this lower level on property tax is *shared between all local governments*. The City of Salem alone would not receive this artificially low property tax amount of $1,870 in our example. This lower amount is shared between Salem, Polk/Marion County, and any special district governments that the property is within.

EXAMPLE OF THE TAX IMPACT OF MEASURE 50 THROUGH 2023

PRIOR TO MEASURE 50			
Market Value of House	**1997 Property Tax**	**Increase in Market Value of House 1997 → 2023**	**2023 Property Tax**
$100,000	$1,000	+247% → $347,000	$3,470
AFTER MEASURE 50			
"Assessed Value" of House	**1997 Property Tax**	**Increase in Assessed Value of House 1997 → 2023**	**2023 Property Tax**
$90,000	$900	+108% → $187,071	$1,870



WHY ARE THESE PROPERTY TAX LIMITS SUCH A BIG ISSUE?

1. Property taxes are the lifeblood of local governments in the western United States. Property taxes constitute the majority of General Fund revenue in cities across the State of Oregon.
2. The costs of providing city government services have increased much more quickly than the growth in revenues. **This is true for city governments across the state**, not just Salem.
    - Inflation *alone* has been about 90% since 1997. In inflation-adjusted dollars, our example house's $1,870 of property taxes is only worth $984 in 1997 dollars, only 9% greater than three decades ago.
    - Local government services predominantly involve **people** and **physical infrastructure.** The costs of both of these things have increased by much *more* than inflation.[1] Even if Oregon cities provided the *exact* services at the *exact* same levels as in 1997, there would not be enough property tax money to provide them.
    - Residents *expect more* from city governments than they did in the 1990's. Residents expect both *more types* of services and *greater levels* of service. For example, in the 1990s, Salem did not fund community policing, homeless services, or a climate response.
3. There are a limited number of additional revenue options available to cities. Oregon law restricts both the type and size of taxes that local governments can impose.
4. New taxes or fees can face public resistance. Multiple Oregon city tax ballot measures failed in 2023.
    - However, this creates a situation where residents are demanding more and better services from cities, but do not provide city governments with the financial resources to provide these services. This is called a *structural deficit* and is unsustainable.

WHY DOES THIS MATTER *RIGHT NOW*?

Cities across Oregon are at a point of crisis. Although this crisis point was delayed for Oregon cities using extra federal COVID assistance dollars, this temporary funding is ending. City governments, faced with fewer resources, have been providing *more* to residents with *less*. Many cities, including Salem, have not maintained service levels with population growth—and in fact have decreased the levels of service through layoffs and other reductions.

Even at these lower levels of service, costs will continue to outpace revenues. Without new revenues, Oregon cities will soon have to eliminate or reduce services beyond what most residents would consider acceptable. There are no easy cuts—balancing Oregon city budgets solely through expense reductions would drastically reduce or eliminate basic government services.

[1] Public administration wages have increased 127% and construction wages (a proxy for public works) have increased by 111% since 1997. Road construction costs have increased by 196% since 2003. You can learn more by visiting the websites of the Bureau of Labor Statistics or the National Highway Construction Cost Index.

II. WHAT ARE THE AVAILABLE REVENUE OPTIONS?

REVENUE OPTIONS: TYPES

Oregon state law limits the type and amount of revenues (taxes) that local governments can impose. There are three main options that have previously been identified by the City's previous revenue task force and by city staff—which are detailed below. Additional revenue options will be considered as part of the Task Force's work.

Revenue Option 1: Increase City Operations Fee

- City Council enacted the City operations fee, an additional flat dollar charge placed on the monthly bills of utility customers. The fee amount varies by customer type (i.e., residential, commercial, industrial).
- Over 30 cities in Oregon implement such utility operations fees.
- Salem already has an operations fee in place and could raise more revenue by increasing the amount of this fee.
- An increase could be implemented through either council action or ballot approval, depending on what task force members and city councilors believe is the best path forward.

Revenue Option 2: Local Option Levies

- A local option levy temporarily increases the rate of property tax that the City of Salem can collect.
- Must be implemented through ballot approval. Extremely common across Oregon.
- Provides additional revenues for operations for the following 5 years. Must be renewed every 5 years to maintain funding levels.
- Because of Measure 5's total property tax limit of $10 per $1,000 of assessed value, local option levies may not collect the total amount approved by voters. If multiple governments have their own property taxes on a given parcel, once the tax hits this limit, governments do not get more revenues from raising property tax rates. Instead, the property taxes of the various governments get compressed to still meet this $10 limit.
- For Salem, this compression is already an issue in Marion County. And compression could become further of an issue over the life of such a tax if other governments pass their own levies or if a recession makes real market values decline.

Revenue Option 3: Payroll Tax

- Payroll taxes consist of a percentage-based tax on gross wages. This is similar in structure to the Social Security and Medicare taxes you pay.
- Payroll taxes can be structured three main ways: employee-paid, employer-paid, and jointly paid.
    - Employee-paid payroll taxes are solely paid on gross wages *received by* the employee.
    - Employer-paid payroll taxes are solely paid on gross wages *paid by* the employer.
    - Jointly paid payroll taxes are paid *both* by the employee on gross wages *received by* the employee <u>and</u> gross wages *paid by* the employer.

- An employee-paid payroll tax failed drastically in the November 2023 election (82% No, 18% Yes).
- A payroll tax *could* be implemented through a ballot measure or through council action. Based on the results of the previous election, however, popular sentiment would likely require passing such a revenue by ballot measure.

REVENUE OPTIONS: CUSTOMIZABILITY

For all revenue options, including the ones highlighted above and all others that may be identified later, the City has the flexibility to customize these taxes to address and public desires. These aspects of customizability include:

- **Number of additional revenues:** The City does not have to choose *just one* option. Generally, a wider variety of revenue sources improve government resiliency.
- **Size:** How much tax is collected by each revenue measure?
- **Branding & Spending Restrictions:** Tax measures can be *branded*, associating these taxes with certain city services. For example, a local option levy could be dedicated to public safety so that voters could be motivated to vote for the increase in taxes, knowing that the funding would go to fire services and police services.
    - If desired, funds could be legally *restricted* to certain purposes. In the example above, the spending of local option levy funds on public safety could be legally mandated to only be spent on fire or police. This could provide more assurance to voters who worry that the City will spend these additional funds on other services. Restricting the funds would mean new revenue would be spent on the specified services, while some existing funds supporting those services would be reallocated to support other programs in the General Fund.

III. WHAT ARE OTHER CITIES DOING?

Salem is not alone in its current efforts to find revenues. Cities across Oregon, and mid-sized cities in particular, are dealing with sharp budget deficits and exploring new revenue options as a result. These cities include but are not limited to Bend, Corvallis, Eugene, Gresham, Hillsboro, Medford, and Springfield.

City staff, Councilors, and residents from these cities are also currently engaged with solving similar revenue issues as the Task Force. The information below summarizes the current available status on the efforts of other cities.

Eugene

- $15 million structural deficit, with $5 million of additional priorities desired from council.
- The city has undergone significant reductions in recent years to help close the gap:
    - $16.5M in annual, ongoing service reductions
    - $4.3M of one-time reductions
- A minimum of $8.3M of additional revenue needed.
- Eugene already has a payroll tax.
- Eugene already has multiple local option levies in place. These local option levies must be renewed by vote in the coming years to continue current funding levels.
- Eugene is exploring a city operations fee (utility fee).

Gresham

- Gresham's deficit is projected to be $11 million in 2025 and $15 million in 2026.
- Gresham voters <u>rejected</u> a public safety local option levy in November 2023.
- Gresham City Council supports pursuing a new local option levy in a future election.
- Gresham is also exploring an increase to its city operations fee (utility fee).

Bend

- Bend's annual deficit is approximately $7.9 million.
- Bend voters recently approved an increase in the Fire/EMS services local option levy, ensuring that Fire and EMS services are provided at a consistent level for the next few years.
- Bend is seeking to increase the amount collected by its operations fee.
- Bend is not using city funds to support the homeless shelter facilities that it purchased in recent years.

Corvallis

- The current deficit for Corvallis is about $9.6 million.
- This deficit is deceptively small, as the City is using and depleting its remaining $1.7M ARPA funds.
- Corvallis recently increased its city operations fees.

- In November, Corvallis voters passed a local option levy dedicated to Parks and Library services.

Springfield

- Springfield's general fund shows a relatively small deficit now of $1.2 million, though it is relying on the continued use of federal COVID funds to keep its deficit at this level.
- Over the next few years, this deficit will gradually increase to $4.8 million.
- If trends continue, the city expects that it will be unable to adopt a budget in 2028.
- Springfield is currently exploring revenue options and expense reduction scenarios with consultants from the Center for Public Service at Portland State University.

Hillsboro

- Hillsboro's deficit is comparatively moderate in the next two years, between $1.6 and $3.2 million. However, these smaller deficits rely on the use of federal and other one-time funds.
- Hillsboro is in a unique situation in which its property tax (+$9M) and local option tax (+$4.5M) will increase in the next few years as the city's 2005 Strategic Investment Program is moving out of abatement.
- Hillsboro must renew two local option levies to maintain current funding levels: one in 2026 and the other in 2028. If these are not renewed, deficits will increase sharply.
- The City is also reliant on Washington County's library local option levy that provides funding to nine cities in the county.