

DURHAM



1869
CITY OF MEDICINE

CITY OF DURHAM | NORTH CAROLINA

DATE: March 3, 2008

TO: Patrick Baker, City Manager

FROM: Bertha T. Johnson, Interim Director of Budget & Management Services

RE: Interlocal Agreement for the Distribution of Sales Tax between the City of Durham and Durham County

EXECUTIVE SUMMARY

The current interlocal agreement for the distribution of sales tax between the City of Durham and Durham County expires on June 30, 2008. By state statute, every April counties can change the method of distributing local option sales tax revenues within the county: from *per capita* to *ad valorem* or vice versa. The method chosen by the county board of commissioners determines the division of money among the county and municipal governments for the next year.

In lieu of the Board of County Commissioners changing the method of distribution of Sales Tax from *per capita* method of distribution to the *ad valorem* method of distribution Durham County has offered to renew the interlocal with the City of Durham with the following terms:

1. The sales tax will continue to be distributed on a per capita basis between the County of Durham and the City of Durham.
2. The distribution ratio will change to 41/59% for the County.
3. This new agreement will remain in effect for five years - FY 2008-09 through FY 2013-14.

RECOMMENDATION

The Administration recommends that the City Council;

1. Authorize the City Manager to enter into an interlocal agreement with the County of Durham regarding the distribution of sales tax and;
2. Authorize the City Manager to modify the interlocal agreement before execution, provided that modifications do not decrease the anticipated revenues to the City of Durham.

BACKGROUND

Durham County has a sales tax rate of 6.75% sales tax on the purchase of most goods. This is split as follows:

- o 4.25% is retained by the state

- 2.5% is distributed to the local governments
- The 2.5% Local Government Share is made up of:
 - Article 39: 1%; returned to county of collection
 - Article 40: ½%; distributed to counties statewide on a per capita basis
 - Article 42: ½%; distributed to counties statewide on a per capita basis statewide
 - Article 44: ½% of which ¼ is distributed to counties statewide on a per capita basis and ¼% is returned to the county of collection

In July 2007 the state budget included the following provisions for “Medicaid Relief” (H1473) for counties. The Medicaid Relief Components are:

- Effective 07/01/2008 the State will assume 50% of county Medicaid expenses and effective 07/01/09 the State will assume 100% of county Medicaid costs.
- To help the state absorb this cost:
 - Effective 10/1/08, the state will retain ¼ cent of the Article 44 sales tax for counties and cities.
 - Effective 10/1/09, the state will retain all of the Article 44 sales tax for counties and cities.
 - Cities will be “held harmless”, with an allowance for the natural growth of sales tax. Cities will receive 50% of Article 40 collections and 25% of Article 39 collections in place of Article 44 sales tax.

Durham County will lose sales tax revenue, as well as some state support of school construction, but will gain “Medicaid relief” funding. Legislation was also approved to authorize counties to seek voter approval to enact a 0.4% land transfer tax or an additional ¼ sales tax (excluding food). The estimated revenue for the County in FY 2008-09 from these new taxes:

¼%	sales tax	\$ 9,844,589
0.4%	land transfer tax	\$11,614,155

Ten counties pursued the land transfer tax option in November, but none were successful. Voters in five counties passed local-option sales tax referendums. Five counties put both options on the ballot (sales and land transfer tax) and voters rejected both in all five counties. There is no requirement in the legislation for distribution of any of the proceeds for any of these taxes to cities. There are also no earmarks on the proceeds. The Administration requested that Durham County include a provision in the agreement that will allow the City of Durham to share in the above “new” revenues.

The current interlocal agreement between the City of Durham and Durham County for distribution of sales tax is effective through June 30, 2008. This agreement provides for a *per capita* split of 43.14% for the City and 56.86% for the County.

The County is authorized to choose the allocation of local option sales tax (*per capita* vs. *ad valorem*) in April of each year. The new formula is effective from the beginning of the next fiscal year.

Durham County is proposing the terms of the agreement be modified as follows:

1. The current agreement on the *per capita* split between the City and County of 43.14% for the City and 56.86% for the County will change to 41.00% to 59.00% respectively. (The sales tax will continue to be distributed on a per capita basis.)
2. Because the City receives more from the Article 44 sales tax than it lost in state reimbursements, the City will provide the County with 50% of its net gain, after the 41.00%/59.00% split.
3. This agreement will remain in effect for five years (FY 2008-09 through FY 2013-14) in order to provide both governments with some stability in our revenue streams.

ALTERNATIVES

The City Council could elect to reject the term modifications offered by Durham County. However, the County has stated that if the terms of the agreement are not accepted the County will adopt a resolution choosing the *ad valorem* method of distribution which would result in a loss of \$5.8 million to the City's General Fund. The City Council could elect to raise property taxes to bridge the gap in funding.

FINANCIAL IMPACT

If the City Council chooses to accept the terms offered by Durham County, the City's General Fund will suffer a loss of \$3.6 million in FY09. However, if the City does not accept the terms and the County chooses *ad valorem* as the sales tax distribution method, the City will suffer a loss of \$5.8 million.

Impact on Revenue (based on FY08 Budget of \$42,214,634):

1. Straight Per Capita	4,543,525
2. Current Inter-local	(782,968)
3. New Inter-local (59/41)	(3,060,719)
4. Ad Valorem	(5,860,309)

SDBE

Due to the nature of this item, SDBE review is not applicable.

ATTACHMENTS

- Attachment 1: Letter from Michael Ruffin outlining the County's offer.
Attachment 2: Sales Tax Distribution Comparisons.