

# City of Alexandria, Virginia

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## MEMORANDUM

DATE: MARCH 10, 2011

TO: THE HONORABLE MAYOR AND MEMBERS OF CITY COUNCIL

FROM: JAMES K. HARTMANN, CITY MANAGER 

SUBJECT: BUDGET MEMO # 14 : ALTERNATIVE BUSINESS LICENSE (BPOL) RATE REDUCTION OPTIONS

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As part of the transportation add-on tax proposal, a companion reduction in business license (BPOL) taxes for small business was proposed. The tax relief, which would cost \$1.625 million, and when combined with a \$0.375 million increase in funding for destination marketing and group meetings solicitation by ACVA, brings the total business benefits package to \$2.0 million. Since the proposal of the BPOL tax relief a month ago, a number of alternative tax relief ideas have been suggested by members of the business community. Staff encouraged the articulation of new options and offered to cost out options that might be proposed, so that Council had a broad menu of choices when it came time to make the BPOL reduction choice. It should be noted that any additional BPOL tax relief costs represent reduced General Fund revenues or increased general real estate taxes on all property owners which would otherwise be used to support the City's general governmental (such as Police and Fire) and public school expenses.

### **Base Proposal (initial BPOL reduction option proposed in the budget):**

- Increase the threshold for paying the BPOL tax from \$100,000 to \$350,000. This would benefit 1,440 businesses with an average relief of \$626 per year and cost \$0.9 million.
- Reduce the BPOL rates by 50% for those businesses with gross receipts between \$350,000 and \$750,000. This would benefit 807 businesses with an average relief of \$898 per year and cost \$0.725 million.
- The total amount of relief would annually benefit 2,247 small businesses and cost \$1.625 million. The average relief would be \$723. This is some 45% of businesses who currently pay BPOL on a gross receipts basis.
- These businesses would pay the \$50 business license fee that businesses which gross \$100,000 or less now pay.
- This tax relief would substantially, if not fully offset the cost of transportation add on tax for many of these small businesses. (See Budget Memo #4 for details.)
- This tax relief would not apply to those who rent commercial or residential properties, nor would it apply to public utilities and telecom firms.

- This tax relief would be effective starting on January 1, 2011 (as BPOL is a calendar year tax usually paid on March 1 of each year).

The following new options have been costed out and would apply to all businesses other than those listed in the above last bullet.

**Option 1: Add a 25% additional tax relief category between \$750,000 and \$1.0 million to the current proposal:**

- In addition to the base proposal, add a new category of tax relief between \$750,000 and \$1.0 million in gross receipts and reduce the current business license tax rates by 25%.
- This would create a smoother transition from the 50% tax relief category to the no tax relief category and reduce the incentive to restructure one's business receipts into the 50% category.
- The cost of this tax relief which would be additive to the base proposal cost of \$1.625 million and would be \$0.212 million and would benefit 273 businesses with an average relief of \$777 per year.
- The total cost of BPOL relief would rise to \$1.837 million with 2,520 businesses benefiting.

**Option 2: Add a 25% additional tax relief category between \$750,000 and \$1,250,000 to the current proposal:**

- In addition to the base proposal, add a new category of tax relief between \$750,000 and \$1.25 million in gross receipts and reduce the current business license tax rates by 25%.
- This would create a broader, smoother transition from the 50% tax relief category to the no relief tax category and reduce the incentive to game one's business into the 50% category.
- The cost of this tax relief, which would be additive to the base proposal cost of \$1.625 million would be \$0.402 and would benefit 472 businesses with an average relief of \$852.
- The total cost of BPOL relief would rise to \$2.027 million with 2,719 businesses benefiting.

**Option 3: Allow all businesses to deduct \$250,000 from their gross receipts calculations before applying the BPOL tax rates:**

- Currently, the BPOL tax rates apply to all gross receipts of a business with no deductions allowed.
- This proposal would keep all BPOL tax rates unchanged and allow businesses who file on a gross receipts basis to deduct \$250,000 from their gross receipts before applying the tax rates.
- This proposal would benefit large and small businesses with an equal dollar amount of tax relief (i.e., equal within each BPOL rate category).
- The cost of this relief would be \$3.570 million with 5,000 businesses benefiting.
- Since this relief option would be in lieu of the base proposal, the net new cost would be \$1.945 million (\$3.570 million less \$1.625 million in the base proposal equals \$1.945 million).

**Option 4: Allow all businesses to deduct \$350,000 from their gross receipts calculations before applying BPOL tax rates:**

- Currently, the BPOL tax rates apply to all gross receipts of a business with no deductions allowed.
- This proposal would keep all BPOL tax rates unchanged and allow businesses who file on a gross receipts basis to deduct \$350,000 from their gross receipts before applying the tax rates.
- This proposal would benefit large and small businesses with an equal dollar amount of tax relief (i.e., equal within each BPOL tax rate category).
- The cost of this relief would be \$4.7 million with 5,000 businesses benefiting.
- Since this relief would be in lieu of the base proposal, the net new cost would be \$3.1 million (\$4.7 million less \$1.625 million in the base proposal equals \$3.1 million).

**Option 5: Apply the \$1.625 in budgeted BPOL tax relief to an across-the-board reduction in business license tax rates:**

- This proposal would take the \$1.625 million in budgeted business license tax relief and use it to reduce BPOL rates across the board.
- This would provide a small benefit to all 5,000 businesses that currently pay the business license tax on a gross receipts basis.
- Since it is estimated that BPOL would raise some \$31.6 million before any tax relief, a \$1.625 tax relief amount represents a 5.14% rate reduction.
- The rate reductions have been rounded to 1, 2 or 3 cents (depending on the current rate) with the professional category, which currently pays the highest BPOL rate, receiving the largest rate reduction of 3 cents.
- No change in the 5-cent wholesaler’s BPOL rate is proposed since a 5.14% reduction is less than a 0.25 cent rate reduction.
- When the 5.14% rate reduction percentage is applied and the results rounded, the following new rates are derived:

<b>Category</b>	<b>Current Rate*</b>	<b>Option 5 Rate</b>	<b>Rate Reduction*</b>
Professional Services/Occupations	.58¢	.55¢	-.03¢
Financial Services	.35¢	.33¢	-.02¢
Personal Services	.35¢	.33¢	-.02¢
Repair Services	.35¢	.33¢	-.02¢
Retail Merchants (excluding restaurants)	.20¢	.19¢	-.01¢
Restaurants	.20¢	.19¢	-.01¢
Contractors/builders/developers	.16¢	.15¢	-.01¢
Wholesalers	.05¢	.05¢	NC

\*All rates = Per \$100 gross receipts

**Option 6: Establish a 6.3 cent commercial add-on tax rate, cut BPOL taxes by \$6.0 million and increase the base real estate tax rate on all properties in the City by 2.8 cents:**

- This proposal would set the add-on tax rate at 6.3 cents which is about 50% of the proposed 12.5 cent rate.
- This 6.2 cent add-on tax rate reduction would reduce FY 2011 add-on tax revenues by \$3.0 million, and FY 2012 revenues by \$6.1 million, for a total loss of \$9.1 million.
- BPOL taxes under this proposal would be reduced by \$6.0 million (which is \$4.4 million more than set aside in the FY 2012 budget for BPOL tax relief).
- Since it is estimated that BPOL would raise some \$31.6 million before any tax relief, a \$6.0 million tax relief amount represents at 19% rate reduction.
- When the 19% rate reduction is applied, the following new rates are derived:

Category	Current Rate*	Option 6 Rate*	Rate Reduction*
Professional Services/Occupations	.58¢	.47¢	-.11¢
Financial Services	.35¢	.28¢	-.07¢
Personal Services	.35¢	.28¢	-.07¢
Repair Services	.35¢	.28¢	-.07¢
Retail Merchants (excluding restaurants)	.20¢	.16¢	-.04¢
Restaurants	.20¢	.16¢	-.04¢
Contractors/builders/developers	.16¢	.13¢	-.03¢
Wholesalers	.05¢	.04¢	-.01¢

\*All rates = Per \$100 gross receipts

- In order to finance the \$9.1 million in lost add-on tax revenues and the \$4.4 million in added BPOL tax relief, some \$13.5 million from the base real estate tax rate would be needed.
- Under this option, this \$13.5 million would be financed by a 2.8 cent increase in the general real estate tax rate that would apply to all taxable real property in the City for CY 2012. For CY 2013, the real estate tax rate would need to be increased by another 0.9 cents to 3.7 cents to raise an equivalent amount of tax revenues.

**Option 7: In lieu of adopting the add-on tax, increase the real estate tax rate on all properties by 3.8 cents to raise a similar amount of funds:**

- Under this option the general real estate tax rate on all properties would be increased by 3.8 cents per \$100 of valuation.
- This is an equivalent 4.0% additional increase in the taxes levied on all property owners
- Approximately 6% of these property owners representing 30% of the tax base would have been otherwise subject to the add on tax, and 94% of these property owners representing 70% of the tax base would not have been subject to this tax.
- In order to effect this option, Council will have to decide to advertise this 3.8 cent increase in the real estate tax rate above the base proposed 97.3 cent rate on March 12.
- This 3.8 cents would raise some \$18.2 million for FY 2012 (including the June 2012 payment) and then about \$12.1 million in future fiscal years.

**Option 8: Apply the \$1.625 million in budgeted tax relief towards priority transportation projects:**

- In the event that Council decides not to adopt the commercial add on tax for transportation purposes, the BPOL tax relief partial offset to the add-on tax is no longer needed.
- The \$1.625 million budgeted for BPOL tax relief then could be directed towards partially funding part of one of the identified priority transportation projects, or other Council priorities.
- This action could be accomplished through increasing the cash capital transfer to the City's cash capital projects fund.

If Council or the business community wishes additional options to be calculated, staff can undertake these calculations and provide that information to assist with the tax reduction decision making.

Attached is a summary chart comparing the base proposal with these eight options.

Attachment

**SUMMARY OF BPOL RATE REDUCTIONS OPTIONS**  
(in Millions)

<b>Option</b>	<b>Title</b>	<b>Net New Business Tax Relief Above Base<sup>1</sup></b>	<b>Total Business Tax Relief<sup>1</sup></b>
<b>Base Proposal</b>		<b>N/A</b>	<b>\$1.625</b>
<b>1</b>	<b>Add a 25% additional tax relief category between \$750,000 and \$1.0 million to the current proposal</b>	<b>\$0.212</b>	<b>\$1.837</b>
<b>2</b>	<b>Add a 25% additional tax relief category between \$750,000 and \$1,250,000 to the current proposal</b>	<b>\$0.402</b>	<b>\$2.027</b>
<b>3</b>	<b>Allow all businesses to deduct \$250,000 from their gross receipts calculations before applying the BPOL tax rates</b>	<b>\$1.945</b>	<b>\$3.570</b>
<b>4</b>	<b>Allow all businesses to deduct \$350,000 from their gross receipts calculations before applying BPOL tax rates</b>	<b>\$3.098</b>	<b>\$4.723</b>
<b>5</b>	<b>Apply the \$1.625 in budgeted BPOL tax relief to an across-the-board reduction in business license tax rates</b>	<b>-0-</b>	<b>\$1.625</b>
<b>6</b>	<b>Establish a 6.3 cent commercial add-on tax rate, cut BPOL taxes by \$6.0 million and increase the base real estate tax rate on all properties in the City by 2.8 cents</b>	<b>\$13.500</b>	<b>\$15.125</b>
<b>7</b>	<b>In lieu of adopting the add-on tax, increase the real estate tax rate on all properties by 3.8 cents to raise a similar amount of funds</b>	<b>\$18.200</b>	<b>\$18.200</b>
<b>8</b>	<b>Apply the \$1.625 million in budgeted tax relief towards priority transportation projects or other Council priorities</b>	<b>-\$1.625</b>	<b>-0-</b>

<sup>1</sup> Reflects FY 2012 budget impact compared to base proposal of a 12.5 cent add-on tax and \$1.625 in BPOL tax relief.