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**CITY COUNCIL AGENDA ITEM**

**ACTION REQUESTED:**

Receive the May 2021 Financial Report

**DEPARTMENT:** Finance Department

**SUBMITTED BY:** Rachel Mayer, Finance Director

**BOARD/COMMISSION REVIEW:**

N/A

**BACKGROUND:**

Developed in response to the unprecedented economic impacts resulting from the COVID-19 pandemic, the monthly financial report provides timely information and data related to the City’s financial position and the local economy. This report is intended to assist the City Council in making strategic financial decisions when necessary.

**DISCUSSION:**

*Recent Actions & Trends*

Response to the pandemic continues to constantly evolve, and staff is monitoring national, state, and local changes that may impact the local economy.

Recent events include:

- 1. Transition to Bridge Phase:** On May 6, Governor JB Pritzker announced that improving public health metrics allow the entire state to move to the Bridge Phase of the Restore Illinois plan on May 14. The Bridge Phase allows for increased capacity at most indoor and outdoor settings, including restaurants, offices, and entertainment venues. This is a positive economic development as several revenue streams have shown improvement during periods of less stringent mitigation efforts.

**2. Vaccination Progress:** The Illinois Department of Public Health (IDPH) reports full vaccination of 41% of DuPage County’s population and 33% of Will County’s population as of May 9. DuPage County continues to lead the Chicago metropolitan area in percent of population vaccinated. Public health officials continue to point to mass vaccination as a critical component of the transition to Phase 5 of the Restore Illinois Plan.

*Economic Indicators*

City staff monitors various revenue streams, particularly those that are more economically sensitive, as indicators of the health of the local economy. In the early months of the pandemic, staff identified five state-collected revenues and four City-collected revenues that serve as the best indicators of economic activity. This group of revenues provides insight into the local economy as most are driven by consumer behavior at the local level. Revenues disbursed by the state on a per capita basis, such as income, motor fuel, and use taxes, are indicators of the broader statewide economy.

**State Collected Revenues:** Revenues collected by the state continued to show positive trends in April, exceeding budget projections by 11.4%. Monthly projections are based on the historical timing of when the City receives revenue throughout the year as some categories fluctuate more than others from month to month. Because of the State’s disbursement schedule, some of these revenues are received three full months after the tax is collected at the point of sale; April’s figures represent revenues from January. Monthly projections have become increasingly unreliable in 2021 as several revenues have recovered more quickly than anticipated and revenue is shifting among categories.

Tax	Description	Total	Above/Below Projections	Analysis
<b>State Sales Tax</b>	Collected on retail sale of all goods sold within the City, including automobiles. The City receives 1% of the total 7% tax applied to purchases.	\$2.7M	Above by 14.6%	Outperformance largely attributable to the inclusion of sales tax dollars for online purchases that were previously recorded as use tax and shared on a per capita basis.
<b>State Income Tax</b>	City’s share of personal and corporate income taxes paid to the state and disbursed to municipalities through the Local Government Distributive Fund (LGDF). Shared on per capita basis.	\$1.8M	Above by 39.3%	Significant outperformance continues due to better-than-expected economic conditions and full LGDF remittance by the state.
<b>Home Rule Sales Tax (HRST)</b>	Additional 0.75% tax collected on retail sales. Rate set by City. Not applicable to certain purchases, including auto sales, groceries and healthcare items.	\$1.0M	Below by 0.2%	This is a significant improvement over the prior three months due to the addition of tax dollars tied to online purchases.

<b>Motor Fuel Tax (MFT)</b>	State tax collected on fuel sales. Shared on per capita basis. Includes transportation renewal funds (TRF), which is portion of 2019 MFT increase being shared with City.	\$417,476	Below by 3.4%	Improved by 3.6% from prior month. Recovery continues to lag as regular commuting patterns have not resumed.
<b>Local Use Tax</b>	State tax applied to purchases made outside of Illinois for use within the state - largely online purchases.	\$430,059	Below by 30.4%	Legislative changes began shifting some of this revenue to the sales tax category, which is why this fell short of projections. Revenue 2% higher than same period in 2020.

**April State Collected Revenues**

Revenue	Projection (\$)	Actual (\$)	Difference (\$)	Difference (%)
Sales Tax	2,352,457	2,696,303	343,846	14.6%
State Income Tax	1,304,295	1,816,337	512,042	39.3%
Home Rule Sales Tax	1,007,753	1,005,784	(1,969)	-0.2%
Motor Fuel Tax/TRF	432,109	417,476	(14,634)	-3.4%
Local Use Tax	618,028	430,059	(187,969)	-30.4%
<b>Totals</b>	<b>5,714,643</b>	<b>6,365,959</b>	<b>651,315</b>	<b>11.4%</b>

Better than expected returns in sales tax, income tax, and local use tax continues to drive positive revenue trends. These three General Fund revenues are already \$2.7 million ahead of budget projections for this point in the year and all HRST funds remain allocated to capital and debt service. In total, the State collected revenues are exceeding budget projections by 8.0% through April.

**YTD State Collected Revenues through April**

Revenue	Projection (\$)	Actual (\$)	Difference (\$)	Difference (%)
Sales Tax	11,016,262	11,725,689	709,427	6.4%
State Income Tax	4,641,929	6,171,696	1,529,767	33.0%
Home Rule Sales Tax	4,942,814	4,351,046	(591,769)	-12.0%
Motor Fuel Tax/TRF	1,885,537	1,736,526	(149,011)	-7.9%
Local Use Tax	2,058,007	2,512,156	454,150	22.1%
<b>Totals</b>	<b>24,544,549</b>	<b>26,497,113</b>	<b>1,952,564</b>	<b>8.0%</b>

**Locally Collected Revenues:** Staff monitors four locally collected revenues for signs of economic recovery. The second table below details taxable sales reported on submitted returns and not the actual tax revenue received. Taxable sales provide a clearer picture of economic trends as the receipt of actual revenue can be delayed at times. Returns submitted in April are for March sales.

Tax	Description	Taxable Sales	Change from last month	Analysis
<b>Food and Beverage Taxes</b>	1% citywide tax and 0.75% downtown tax on prepared food and beverages, most commonly restaurant and bar sales	\$36.8M	Increased by 31%	Comparison to March 2019 shows food and beverage sales for current period down by less than 7%
<b>Local Gas Tax</b>	\$0.04 City tax on each gallon of motor fuel sold in the City	\$4.0M	Declined by 1.6%	Sales have held steady around \$4M for three months; still down from pre-pandemic as normal commuting activity has not resumed
<b>Hotel/ Motel Tax</b>	5.5% tax on hotel/motel room occupancies; most collected quarterly	\$5.0M	Increased by 14% from Q4 2020	Most impacted of all revenues; first notable improvement in three quarters
<b>Real Estate Transfer Tax</b>	Transfer tax on sale of real estate in City; rate of \$1.50 per \$500 in sale price	\$153.9M	Increased by 105%	Improvement from sharp drop in February sales - possibly due to fewer business days in month and timing of closing of sales around the holidays

The table below provides monthly taxable sales for 2021 and the fourth quarter of 2020.

Month	Food & Beverage	Hotel/Motel	Local Gas	Real Estate
October	31.80	4.39	4.60	191.77
November	24.28	0.20	3.78	133.49
December	28.22	4.39	3.76	148.18
January	26.22	0.27	4.23	145.21
February	28.10	0.47	4.10	75.03
March	36.78	5.00	4.04	153.87
<b>YTD Totals</b>	<b>91.09</b>	<b>5.74</b>	<b>12.38</b>	<b>374.11</b>
<b>\$ in millions</b>				

*Online Sales Tax Revenue*

In 2018, a U.S. Supreme Court decision (South Dakota v. Wayfair) opened the door for state and local sales taxes to be applied to out-of-state purchases when the seller has no physical presence within a state. In response, Illinois adopted substantial changes to sales tax laws in 2019 to create a level playing field, from a tax perspective, for brick and mortar and e-commerce retailers. Under the new legislation, taxes are destination-based and may include both sales tax and HRST. These changes took full effect on January 1, 2021.

The Illinois Municipal League (IML) noted the change should benefit municipalities in two ways. First, taxes shift from the per capita based use tax category to the location-based sales tax category. This

should be of benefit to communities where residents with higher personal income, such as Naperville, spend more. Second, HRST will apply to most e-commerce purchases for the first time, creating new revenue for municipalities.

Staff accounted for the increase to HRST in the 2021 budget by adding 3% growth for the year, equaling nearly \$400,000. That increase comes after the downward revenue adjustment made due to the ongoing pandemic. At the suggestion of IML, staff made no revisions to sales tax revenue for 2021 as it was impossible to forecast the shift between use tax and sales tax revenue.

April marks the first month in which revenue data is reflective of the tax law changes. Analysis of April sales tax, use tax, and HRST provides early confirmation of the assumed revenue impacts. The table below shows a year-over-year comparison for April. April 2020 numbers represent January 2020 sales, before the pandemic began impacting revenues.

	April 2020	April 2021	Change
Sales Tax	2,510,865	2,696,303	7.4%
Home Rule Sales Tax	992,131	1,005,784	1.4%
Local Use Tax	421,774	430,774	2.0%

All three categories increased year-over-year. In contrast, a year-over-year comparison of the prior three months shows an average decline of 6.3% in sales tax and 13.3% in HRST, while use tax was up an average of 35.7% in that timeframe. It is difficult to say how much of the monthly increase is attributable to shifting revenues versus improvement in the pandemic economy. However, individual sales data includes revenue from recognizable e-commerce retailers, indicating that online sales played a significant role in improving revenues. The Illinois Department of Revenue informed staff that many e-commerce retailers are not clear on the new laws and revenues are likely to experience some minor turbulence while IDOR provides guidance and sellers submit amended returns.

*Local Economic Support*

The Temporary Utility Assistance Program continues to aid customers seeking assistance with the payment of their utility bills. While requests for residential assistance have maintained a consistent pace, small business requests are nearly unchanged from last month’s report. Utility disconnections resumed on May 4 with electric service to 60 residential accounts being shut off. Past due balances totaled \$214,000 for those accounts of which \$100,000 was collected to restore electric service. A total of 26 payment plans were initiated and 10 utility accounts remain disconnected with no payments being made. The Finance Department experienced no significant customer service impacts as the disconnection process resumed.

Below is a summary of assistance program activity through May 7.

Program	Customers Approved	Amount Disbursed	Funds Remaining
Residential	152	\$40,677	\$229,323
Small Business	51	\$46,024	\$153,976
<b>Total</b>	<b>203</b>	<b>\$86,701</b>	<b>\$383,299</b>

*American Rescue Plan Act Update*

Earlier this year the \$1.9 trillion American Rescue Plan Act (ARPA), which included \$350 billion in aid to state and local governments, passed into law. Over the past few months, the U.S. Treasury has been working to determine exact final allocations and develop further guidance on the use of funds.

Staff recently received word that Naperville’s final allocation is \$13.3 million, which will be given to the City in two disbursements. The first half, totaling \$6.65 million, should be received within days; the second half will be provided one year from now. All funds must be used by Dec. 31, 2024, and use can be spread out over this time period for financial stability.

This significant one-time infusion of dollars to the City has the potential to be highly transformative with a long-term impact. While additional parameters on uses may be imposed by the federal government, the following are current use/non-use stipulations:

Eligible Uses	Restrictions
Respond to or mitigate the COVID-19 public health emergency or its negative economic impacts	Cannot offset tax reductions or delay tax increase by states or territories
Cover costs incurred as a result of such emergency	Cannot be used for pension funding
Replace revenue that was lost, delayed, or decreased as a result of such emergency	
Address the negative economic impacts of such emergency	

### Funding Goals and Considerations

Staff previously introduced potential funding goals for these dollars to Council as a starting point for future decision making. In reviewing the goals of ARPA and additional guidance, staff has modified this framework to the following:

- Using funds and partnerships to drive transformative, innovative and long-term economic re-investment to our local economy’s business sector
- Providing direct financial assistance to businesses and/or residents
- Supporting the health and well-being of our community through our non-profits and partners
- Solidifying the City’s financial position through the replenishment of City funds

Additionally, in light of the many ways ARPA provides direct assistance to certain heavily-impacted sectors of the economy, an additional goal is:

- Allocating funding in a way that maximizes support for unique efforts and economic sectors not already covered by existing ARPA assistance channels

Although early in the process, there are some additional considerations to keep in mind as discussions begin around these dollars:

- **One-time versus recurring investment:** As mentioned previously, this is a one-time infusion of dollars to state and local governments; the viability of additional assistance in coming months and years is speculative at best. Using these dollars to create new programs or enhance existing programs that will require ongoing annual funding can create a funding gap

down the road that will require new revenue sources to fill.

While investments in water, sewer, and broadband infrastructure are specifically called out as permitted uses, other capital projects may be achievable. Capital projects provide a long-term value for a one-time investment, keeping in mind ongoing maintenance associated with the capital investment.

- **Comprehensive economic impacts:** The backbone of services the City provides - public safety, roadways, etc. - are the framework for our world-class quality of life that is accentuated through the work of our intergovernmental partners, educational institutions, and not-for-profits. Partnerships with organizations on transformative ideas that have a generational impact and, in turn, grow our economic base through revitalization and improvements that bring more people to live, work, and play in Naperville can be a use of these dollars.
- **Other direct ARPA assistance to certain economic sectors:** Certain hard-hit sectors of the economy are accounted for in ARPA separately through direct assistance programs. For example, the Restaurant Revitalization Fund is providing restaurants with funding equal to their pandemic-related revenue loss up to \$10 million per business and no more than \$5 million per physical location.

Staff is compiling recommendations internally for projects that may meet the above-mentioned parameters for Council consideration. As the U.S. Treasury provides additional guidance on the use of ARPA funding, staff will bring recommendations to Council for additional discussion.

### **Next Steps**

Staff will continue bringing monthly reports before the Council at the second meeting of each month. These reports will focus on the state of economic recovery and include relevant topics for discussion, such as areas of current or future years' budgets that require additional attention as information becomes available.

### **FISCAL IMPACT:**

N/A