



Q&A

1. What is the income tax credit?

The City's current tax structure grants people that live in Kent but work outside of Kent a 100% credit on their income tax. That means if you work in a city that has a 2% income tax or higher you pay no income tax to Kent. Or if the City where you work has a 1% income tax you pay 1% to them and 1% to the City (for a total of 2%). Twenty years ago few neighboring cities had a 2% income tax but today many do which means the City has lost about \$500,000 a year that used to come in to Kent but is now going to those other cities. Losing this funding is particularly hard since residents typically consume services where they live (in Kent) not where they work yet they are paying less than .10 cents on the dollar of what it costs to provide those services in Kent.

2. Why is City Council looking at changing the income tax credit?

Back in 2006 the City Council asked a Panel of 6 local investment managers, bankers and accountants for their advice on how to solve the City's worsening financial condition. At that time the City had just ended 2005 \$1.5 million in the red with revenues failing to keep pace with expenses for the third straight year. If something didn't change the City would run out of money in 2-3 years. After 8 months of study the Panel members recommended a list of changes to City Council including a reduction in the income tax credit. The Council took the Panel's recommendations out to the community in a series of neighborhood meetings in 2006 and 2007 to get public input. Then in 2007 Council adopted the first item, a \$5 change in the vehicle license fee. Now in 2008 Council is considering adopting a second item, a 25% reduction in the income tax credit.

3. Why can't the City just cut expenses?

We can and we have. Over the last five years the City has cut jobs and reduced the work force by about 8% saving over \$1 million a year. The City has also cut contracts, supplies and materials saving another \$1 million. But that wasn't enough so the City put a 3-year (2005, 06, 07) hiring freeze into effect which has added a total of \$2.6 million to the City's savings. These cuts and freezes made it possible to build up our reserves again - which is important -- but the cuts have not spurred an economic recovery so the most we can say we've accomplished by cutting has been to delay when we run out of money.

4. Why can't we just make all the cuts permanent?

The cuts are permanent and the frozen positions could be made permanent but that gets to a bigger question of what kind of community we want to live in. We've worked hard to stretch resources the best we could but the more cuts we make the lower the levels of service we can provide. If we want to try to cut our way out of this problem we'll have to accept the fact that further cuts will mean fewer employees and less City services. Less service will mean longer delays, fewer potholes patched, and fewer sidewalks repaired. It will mean fewer people available to wait on customers, return calls, and answer questions. It will mean less time to study, plan and anticipate future needs. We can cut services but surveys of residents and City Council consistently indicate that they want more services not less.

5. How about cutting back on City projects?

We did that in 2007, delaying almost all of our major capital projects, but that didn't fix the problem either, it just helped buy us some time. To cut our way out of this we need to cut City services, e.g., streets, police, fire, planning, etc., that are funded in the operating budget. The money used for projects is one-time money that comes from the City's capital budget which is a separate pot of money altogether. So deferring capital projects may provide a little extra cash for one year but once you spend that capital cash it's gone; meanwhile the operating deficit will be right back the next year. And remember, you can only defer projects so long before things start to really break down which in the end drives the cost of repair higher than it would have been if you took care of it when it first needed attention.

6. So why change the income tax credit?

The Panel was very sensitive to the issue of spreading any new tax burden fairly across all segments of the community so they presented Council with 6 different steps to do that. Reducing the income tax credit was one step that the Panel thought should be taken in order to get a fair share of taxes from residents that live in Kent but work outside of Kent. It turns out that those residents enjoy the benefit of City services but because they get full credit for the income taxes they pay in the city where they work they contribute less than 10 cents on the dollar for the services they get in Kent. The Panel noted that it seemed unfair to the residents that live and work in Kent to subsidize the services for those residents at a rate of 90 cents on the dollar so they recommended reducing the credit from 100% to 75%. Of the steps proposed by the Panel the change in the income tax credit is something that Council can put into effect immediately so they are starting there but discussions are underway about the remaining items as well so that any new tax costs are shared as fairly as possible.

7. But I hear we've got money in reserves we could spend?

After 3 years of running in the red (2003, 04, 05) the writing was on the wall – if the City didn't take drastic measures the reserve fund was in jeopardy of being depleted in 2-3 years which would mean the City ran the risk of going bankrupt. That's why the City put into effect all of the cuts and freezes that we could starting in 2006. And it has worked. We reversed the trend in 2006 and 2007 bringing the reserve balance back up to where it was in 2004-05. That was critically important because the reserves are the City's safety net to use during hard times and it is also a source of investment funds that we can use to try to be a catalyst for an economic recovery. The trouble is the reserve funds are one-time dollars that are gone once you spend them so they buy you temporary relief but they don't fix the problem. The City could go back to relying on these savings to balance the budget for a couple of years but then we'd be right back where we were in 2005 and we would have no funds to invest in stimulating an economic recovery which is the best solution.

8. I feel like I'm being punished for working outside of the City.

Certainly this change in the tax credit impacts the amount of money that people that work elsewhere pay to the City. For example, if you make \$50,000 working in another city that has a 2% income tax rate, you're paying that other city \$1,000 a year and \$0 dollars to the City of Kent in income tax. If the credit was reduced to 75%, you would still pay the other city \$1,000 but you would then pay the City of Kent \$250 a year or roughly \$20 a month to support the Kent City services that you receive.

Understandably if you're a person working outside of Kent it's frustrating to be asked to pay more. But the Panel presented this issue to Council as a fairness question: Is it fair to ask people that use services where they live to pay their fair share? Is it fair for people that live and work in Kent to subsidize their neighbors who choose to work outside of Kent at a 90:10 split? Even if this income tax reduction is put into effect the people that work outside of Kent would still only be paying for roughly 35% of the cost of the services that they receive.

In states that use sales taxes to support government services they advocate the importance of buying goods and services in their community so that tax dollars stay where they are used. Likewise, in states like Ohio that rely on income tax we have to advocate working in the City where you live to keep tax dollars here. I'm not judging whether that's right or wrong, it is just a product of the state tax structure. Reducing the tax credit begins to align the City's financial policies with the reality of the state tax system, creating an incentive to work where you live and contribute taxes where you use the services those taxes pay for.
