County of Fairfax, Virginia

MEMORANDUM

DATE: April 27, 2016

TO: Members, Board of Supervisors

FROM: Edward L. Long, Jr., County Executive

SUBJECT: CORRECTED – Update on Meals Tax Information

Note: This memorandum corrects and replaces the prior Update on Meals Tax Information memorandum dated April 26, 2016 in order to properly attribute Attachment D, Fairfax County Proposed Food Tax: Foodservice Industry White Paper to the Restaurant Association of Metropolitan Washington; Virginia Restaurant, Lodging, and Travel Association; National Restaurant Association; and the NOVA Chamber of Commerce.

This memorandum is in response to the Board Matter adopted by the Board of Supervisors at the March 1, 2016 meeting to provide an informational update on a number of issues related to a possible meals tax referendum, alcohol tax levy, and Business, Professional and Occupational License (BPOL) rates, pending Board direction.

<u>Meals Tax:</u>
The information, including the Meals Tax in Fairfax County white paper (Attachment A), has been updated to reflect current revenue estimates, projected out-of-county restaurant customers, surrounding jurisdictions that have enacted or put a meals tax to referendum, recent Virginia meals tax referendum results, and a list of the Virginia jurisdictions with a meals tax. Staff prepared a timeline (Attachment B) for the required steps and their likely deadlines, should the Board decide to pursue a meals tax referendum to be held on the November 8, 2016 general election. Should a meals tax question be put to referendum and be approved by the voters in the November 2016 general election, the Department of Tax Administration (DTA) has reviewed the meals tax process and could be ready for internal implementation in the County by the time the Board adopted an ordinance authorizing a meals tax. DTA is prepared in that event to initiate immediate communication with affected businesses to inform them of the new requirements. Staff anticipates that actual implementation of a meals tax could occur by July 1, 2017.

- The Board asked for a legal analysis of how the Board can ensure that the County keeps 100% of the revenue generated by the tax. Under current law, the state has neither the authority nor the mechanism to take any of the revenue. Only localities have the authority to impose a meals tax. Va. Code

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Ann. § 58.1-3833 allows counties (subject to approval by referendum) to impose a meals tax. Va. Code Ann. § 58.1-3840 allows cities and towns to impose meals tax. As with real estate taxes and Business, Professional, and Occupational License taxes, counties have the power not only to levy and administer a meals tax, but also to receive directly the revenues the tax generates. The businesses that collect the tax will remit the tax revenues directly to the County's Department of Tax Administration. Since meals tax revenues do not pass through state hands at any time, the state has no current mechanism to retain part of the revenues.

Alcoholic Beverage Tax:
With respect to a potential tax on alcoholic beverages, the Board does not have the authority to enact such a tax. Va. Code Ann. § 4.1-128 prohibits localities from imposing any sales or excise tax on alcoholic beverages, other than the general sales tax or a meals tax. The county meals tax enabling legislation, § 58.1-3833 allows the Board (subject to approval by referendum) to impose a tax on "food and beverages sold, for human consumption, by a restaurant." The term "beverage" means "alcoholic beverages . . . and nonalcoholic beverages served as part of a meal." There is an Attorney General opinion holding that the phrase "served as part of a meal" modifies both alcoholic and nonalcoholic beverages. (1997 Va. Op. Atty. Gen. 186; *see also* 1990 Va. Op. Atty. Gen. 233.) Based on that opinion, the Board has authority to tax alcoholic beverages only when they are sold as part of a meal.

Cigarette Tax:
With respect to a potential increase in the cigarette tax, the Board does not have the authority to increase the existing rate of 30 cents per pack. Va. Code Ann. § 58.1-3831 permits the Board to enact a local tax on cigarettes at a maximum rate of 5 cents per pack, or the amount levied under state law, whichever is greater. Pursuant to VA Code Ann. § 58.1-1001, adopted in 2004, the state levied a cigarette tax of 30 cents per pack starting in 2005. In 2004, the Board adopted Section 4-11-3 to the Fairfax County Code of Ordinances which raised the local cigarette tax rate to the state maximum of 30 cents per pack starting in 2005. Any additional increase in the local cigarette tax rate would require legislative change at the state level. If Fairfax had the authority to raise the cigarette tax rate to 75 cents per pack, the rate of both the Town of Vienna and the City of Falls Church, the County would have approximately $10 million more in revenue.

BPOL Taxes:
The LOBs Q&A regarding the history and explanation of the various, existing BPOL rates has been attached (Attachment C).

Other:
Outreach to the hospitality industry on the impacts of a potential meals tax is ongoing. The Restaurant Association of Metropolitan Washington; Virginia Restaurant, Lodging, and Travel Association; National Restaurant Association; and the NOVA Chamber of

Commerce prepared a foodservice industry white paper on the potential impact of a meals tax (Attachment D).

As directed by the Board on April 19, 2016, the above items will be discussed at the Board's May 3rd Budget Committee meeting.

Further information on revenue sources may be found in the Fairfax County revenue book located at: http://www.fairfaxcounty.gov/dmb/revenue-book-january-2016.pdf.

If you have any questions or desire additional information, please give me a call.

Attachments:

Attachment A: Meals Tax in Fairfax County – Updated April 2016
Attachment B: Possible Schedule of Events for Board-Initiated Petition For Meals Tax Referendum on November 8, 2015
Attachment C: Response to Questions on the 2016 LOBs – Provide Information Regarding the Business, Professional and Occupational License (BPOL) Tax
Attachment D: CORRECTED – Fairfax County Proposed Food Tax: Foodservice Industry White Paper

cc: Joseph M. Mondoro, CFO, Director, Department of Management and Budget
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Meals Tax in Fairfax County

Updated April 2016

Description

> **To what kind of items does the meals tax apply?**
> - A tax on prepared food and beverages (ready-to-eat) at restaurants, lunchrooms, cafeterias, coffee shops, cafes, taverns, delis, push cart operations and hot dog stands
> - Includes alcoholic and non-alcoholic beverages served with a meal
> - Does not apply to groceries - grocery and convenience stores only collect the tax on ready to eat foods - such as the deli or salad bar
> - Does not apply to vending machines

The meals tax is a tax imposed on the purchase of all prepared and ready to eat food and beverages. All restaurants as well as grocery stores and convenience stores selling prepared foods at a delicatessen counter must collect this tax from their customers if a locality levies the tax. As authorized by §58.1-3833 of the *Code of Virginia*, counties may levy the tax if approved in a voter referendum. The voter referendum may be initiated either by a resolution of the Board of Supervisors or on the filing of a petition signed by 10 percent of the voters registered in the County. Cities and towns may impose a meals tax without holding a referendum. In addition, several counties have been exempted from the voter referendum requirement provided that a public hearing is held before adoption and the governing body, by unanimous vote, adopts the tax by local ordinance. The counties that have been granted an exemption to the voter referendum requirement are Arlington County, Roanoke County, Rockbridge County, Frederick County, and Montgomery County.

Meals Tax in Other Jurisdictions

While Fairfax County does not levy the meals tax, the Town of Vienna levies a 3.0 percent meals tax and the Town of Herndon imposes the meals tax at 2.5 percent. Other Northern Virginia localities that tax meals are: Alexandria, Arlington, Fairfax City, Falls Church, Manassas, and Manassas Park. Each of these jurisdictions levies the meals tax at 4.0 percent. The tax is in addition to the state's sales tax. According to the publication, *2014 Tax Rates: Virginia's Cities, Counties and Selected Towns Rates*, all 38 cities levy the meal tax. In addition, 47 counties, and 107 of the reporting towns in

Virginia levied a meals tax during tax year 2014. The State of Maryland, Montgomery County, and Prince George's County do not levy a meals tax. Maryland's sales tax is 6.0 percent.

The table below shows the meals tax rates and revenue for surrounding jurisdictions that levy a meals tax.

Meals Tax Rates and Revenue Generated

Locality	FY 2016 Sales Tax Rate Paid on Meals	FY 2016 Meals Tax Rate	FY 2016 Estimated Meals Tax Revenue (millions)
Northern Virginia			
Alexandria	6.0%	4.0%	$17.8
Arlington	6.0%	4.0%	$37.1
Falls Church	6.0%	4.0%	$2.9
Fairfax City	6.0%	4.0%	$6.0
Herndon	6.0%	2.5%	$2.1
Vienna[1]	6.0%	3.0%	$2.5
District of Columbia[2]	0.0%	10.0%	$378.9

[1] The revenue for the meals tax in Vienna also includes the lodging tax.

[2] The revenue shown for the meals tax in DC represents FY 2015 data.

Revenue Estimate

Based on calendar year 2015 taxable sales at Food and Drink Places in Fairfax County, a 1.0 percent meals tax is estimated to generate approximately $24.0 million in revenue in FY 2016. At the maximum 4.0 percent rate, a County meals tax would generate annual revenue of approximately $96.0 million.

What effect would the meals tax have on an average resident at a 4.0% tax rate?

- On a $5 "fast food" meal, tax would be 20 cents
- On a $50 meal at a "nice restaurant," tax would be $2.00

Tax Limitations

Counties in Virginia are limited to a rate of up to 4.0 percent and must gain voter approval in a referendum before levying the tax. There are no restrictions on the use of the tax revenue generated by the meals tax. However, some localities that levy the meals tax earmark a portion or all the revenue to a specific purpose. For example, Vienna's meals tax revenue goes entirely to the debt service fund. Herndon dedicates approximately 1.0 percentage point of the 2.5 percent tax rate to economic development initiatives and capital improvement projects. Some counties that have asked voters in recent years to approve the meals tax had planned on dedicating at least a portion of the revenue to a specific purpose such as schools operating expenditures or new school construction.

Under state law, a county meals tax does not apply within the limits of a town that has its own meals tax. Since Herndon and Vienna levy their own meals tax, a Fairfax County meals tax would not apply within their limits. The Town of Clifton currently does not have a meals tax. State law also provides that a county meals tax would apply in a town without a meals tax only if the town's governing body approves. Therefore, a Fairfax County meals tax would not apply to Clifton unless the Town Council allowed it to apply within the town.

Issues

Who would pay the meals tax?

- County residents who choose to dine out
- Commuters, travelers and tourists who pass through Fairfax County

- A meals tax would further diversify the County's revenue base. **A 4.0 percent meals tax is equivalent to over 4 cents on the FY 2016 Real Estate Tax rate.** When the County increases the real estate tax, this applies to all property-owning County residents, regardless of their ability to pay. If the County imposed a meals tax, it would apply to tourists, commuters and travelers, as well as residents who choose to dine out.

Tourist Spending in Fairfax County

- 2014 total tourist spending in Fairfax County: $2,852 million*
- Estimated tourist spending on eating out in Fairfax County: $570.4 million
- Estimated 4.0% meals tax revenue generated from tourists: $22.8 million

* *Source: Virginia Tourism Corporation*

- Based on visitor spending data from the Virginia Tourism Corporation, it is estimated that approximately 28.0 percent of meals expenditures in Fairfax County are generated by non-County residents.

- The Fairfax County restaurant customer base is comprised of many non-residents. For example, **355,301 individuals commute into Fairfax County** on a daily basis, almost three times more than into Arlington County.

Commuting Patterns in the Northern Virginia Region

	Fairfax County	Arlington County	Prince William County	Loudoun County
People who live and work in the area	245,465	19,780	47,105	55,042
In-Commuters	355,301	123,929	65,824	87,297
Out-Commuters	270,591	92,518	148,756	122,809
Net In-Commuters (In-Commuters minus Out-Commuters)	**84,710**	**31,411**	**-82,932**	**-35,512**

Source: "Virginia Workforce Connection – Community Profiles, March 2016"

- Demand for restaurant meals is relatively inelastic and therefore a meals tax would likely have minimal impact on the price or quantity of sales. The decision to eat out is not entirely an economic one but to a large extent is driven by convenience, adjacency, food selection, ambience, and other non-economic factors. For example, when Arlington instituted a meals tax in 1991, the County saw restaurant revenues increase in the year after its meals tax was implemented. The National Restaurant Association reports having no research that shows an overall negative impact on restaurant sales of a restaurant meals tax. Restaurant sales are more heavily impacted by other cyclical economic trends. From 2006 to 2015, restaurant sales in Fairfax County increased 51.5 percent, or an average annual growth of 4.7 percent. During the economic recession, restaurant sales in the County fell 0.6 percent between 2008 and 2009.

- Sales tax on unprepared food is considered a regressive tax since lower-income households tend to spend larger fractions of their incomes on necessities such as food and clothing. This is why it is typical for unprepared foods to be taxed at a lower tax rate than other items or even to be exempt from sales taxes altogether. Restaurant meals are not necessities and, based on the Bureau of Labor Statistics Consumer Expenditure Survey, higher-income households tend to spend a larger share of their food budget on eating out.

Administering the Meals Tax

Typically, in localities that levy the meals tax, the Commissioner of the Revenue is responsible for administering the tax. All restaurants and other places that sell food and drinks in a form ready for consumption, on or off their premises, must collect this tax from their customers when the charge for the food and beverages is paid. They are then required, within a specified period, to prepare and file monthly reports and to remit to the Commissioner of the Revenue the taxes collected in the previous month. For the purpose of compensating their collection efforts and timely filing and remittance of the tax, localities may allow businesses to deduct a commission or a dealer's discount, the size of which varies by locality. For example, Falls Church allows a 2 percent commission, Fairfax City and Vienna – 3 percent, and Herndon – 6 percent. Alexandria and Arlington do not provide a commission.

Steps to Initiate Meals Tax Referendum

- The process requires approximately a 4-month lead time
- Board of Supervisors (BOS) approves, by majority vote, a resolution to initiate a referendum
- Office of the County Attorney writes a petition to the Circuit Court asking for an order for a special election on the meals tax question. The petition would include a certified copy of the BOS resolution and a draft order for the court to enter
- Absentee ballots must be available 45 days before the election

For a November ballot, the resolution by the Board of Supervisors would need to be approved by the end of June to early July. This is the same time frame used for a bond referendum.

Recent Meals Tax Voter Referendum History

- A Fairfax County meals tax was put to voter referendum in April 1992, but was defeated 58 percent to 42 percent with approximately 102,000 votes cast, representing about 25 percent of total registered voters in 1992.
- In 2004, legislation was introduced to exempt Fairfax County from the voter referendum requirement. The legislation was passed by the Senate but failed in the House.
- Loudoun County held a referendum for a meals tax in November 2008 but it failed by a vote of 70 percent to 30 percent. The new tax would have funded new school construction.
- Henrico, Chesterfield and Middlesex Counties held meals tax referendums in November 2013. Henrico's 4.0 percent meals tax was approved 51.5 percent to 48.5 percent with 102,274 votes casted. Henrico's tax is dedicated to Henrico's schools. It should be noted that Henrico County mounted a strong public awareness campaign for the meals tax including a website and numerous public discussions. Middlesex County also approved a 4.0 percent meals tax (55.8 percent to 44.2 percent, 3,816 votes casted). The revenue in Middlesex County is used to fund emergency services and capital improvements for the county and schools. The referendum for a 2.0 percent meals tax failed in Chesterfield County, 56.1 percent to 43.9 percent with 103,214 total votes.

The table below shows recent meals tax voter referendum results in Virginia.

RECENT MEALS TAX VOTER REFERENDUM RESULTS IN VIRGINIA

County	Year	Result	Earmarked	Purpose	Tax Rate
Pittsylvania	2007	yes	no	General Fund	4.0%
King William	2008	yes	no	offset real estate tax increases	4.0%
Fauquier	2008	no	yes	capital projects	--
Loudoun	2008	no	yes	school construction	--
Culpeper	2008	no	no	offset real estate tax increases	--
Rockingham	2009	yes	yes	schools	4.0%
Southampton	2009	yes	yes	county and schools capital projects	4.0%
Bath	2009	yes	no	offset real estate tax increases	4.0%
Sussex	2009	no	no	General Fund	--
Accomack	2010	no	yes	schools	--
Halifax	2011	yes	yes	schools	4.0%
Louisa	2011	yes	yes	schools and public safety CIP projects	4.0%
Campbell	2012	no	yes	schools	--
Buckingham	2012	no	no	General Fund	--
Brunswick	2012	no	no	General Fund	--
Smyth	2013	no	no	General Fund	--
Middlesex	2013	yes	yes	emergency services & capital projects	4.0%
Chesterfield	2013	no	yes	capital projects for public safety and schools	--
Henrico	2013	yes	yes	schools - operations and capital projects	4.0%
Patrick	2014	no	no	General Fund	--
Matthews	2014	no	no	General Fund	--
Dickenson	2014	no	no	offset real estate tax increases	--

Note: The State Code was amended in 2001 to allow the ballot question to include information regarding the purpose for which the revenue would be used. This information is not required.

The table below shows the meals taxes in Northern Virginia.

MEALS TAXES IN NORTHERN VIRGINIA

Local Jurisdiction	Year Enacted	Requirements for Levying the Meals Tax	Current Rate	Collector's Commission/ Discount	Designated for Specific Purpose
Arlington	1991	Exempted from referendum requirement. Adopted by unanimous vote.	4.0%	None	No
Alexandria	1975	Has authority to levy without referendum	4.0%	None	No
Fairfax City	1985	Has authority to levy without referendum	4.0%	3.0%	No
Falls Church	1977	Has authority to levy without referendum	4.0%	2.0%	No
Herndon	2003	Has authority to levy without referendum	2.5%	6.0%	1.5% rate to General Fund / 1% rate to CIP & Economic Development
Manassas City	1988	Has authority to levy without referendum	4.0%	3.0%	No
Manassas Park	at least since 1995	Has authority to levy without referendum	4.0%	2.0%	No
Vienna	1989	Has authority to levy without referendum	3.0%	3.0%	Debt Service
Fairfax County	Not levied	Referendum required. Referendum failed in 1992	--	--	--
Loudoun	Not levied	Referendum required. Referendums failed in 1992, 1998 and 2008	--	--	The 2008 referendum would have been used for school construction
Prince William	Not levied	Referendum required. Referendum failed in 1995	--	--	--

Meals Tax Levied by Virginia's Localities

Locality	Meals (Restaurant) Tax (%)
Cities	
Alexandria	4.0
Bristol	6.0
Buena Vista	6.0
Charlottesville	4.0
Chesapeake	5.5
Colonial Heights	6.0
Covington	7.5
Danville	6.0
Emporia	6.5
Fairfax	4.0
Falls Church	4.0
Franklin	6.5
Fredericksburg	6.0
Galax	7.0
Hampton	7.5
Harrisonburg	6.5
Hopewell	5.5
Lexington	5.0
Lynchburg	6.5
Manassas	4.0
Manassas Park	4.0
Martinsville	6.5
Newport News	7.5
Norfolk	6.5
Norton	7.0
Petersburg	6.0
Poquoson	6.0
Portsmouth	6.5
Radford	5.5
Richmond	6.0
Roanoke	5.0
Salem	6.0
Staunton	6.0
Suffolk	6.5
Virginia Beach	5.5
Waynesboro	6.0
Williamsburg	5.0
Winchester	5.0

Locality	Meals (Restaurant) Tax (%)
Towns	
Abingdon	7.0
Altavista	5.5
Amherst	4.0
Appalachia	3.0
Appomattox	8.0
Ashland	5.0
Berryville	2.0
Big Stone Gap	6.0
Blacksburg	6.0
Blackstone	6.5
Bluefield	5.0
Boones Mill	5.0
Boydton	4.0
Bridgewater	6.0
Broadway	4.0
Brookneal	5.0
Buchanan	4.0
Cape Charles	5.0
Cedar Bluff	6.0
Charlotte Court House	5.0
Chase City	5.0
Chatham	5.0
Chilhowie	5.5
Christiansburg	7.5
Clarksville	5.0
Clifton Forge	4.5
Clintwood	6.0
Colonial Beach	5.0
Crewe	5.0
Culpeper	6.0
Damascus	7.0
Dayton	5.0
Dublin	4.0
Duffield	3.5
Dumfries	4.0
Edinburg	5.0
Farmville	7.0
Fincastle	4.0

Meals Tax Levied by Virginia's Localities

Locality	Meals (Restaurant) Tax (%)
Towns continued	
Floyd	5.0
Front Royal	4.0
Gate City	3.5
Glade Spring	5.0
Glen Lyn	N/A
Gordonsville	5.5
Gretna	5.0
Grottoes	5.0
Grundy	5.0
Halifax	3.0
Hamilton	4.0
Haymarket	4.0
Haysi	5.0
Herndon	2.5
Hillsville	8.0
Honaker	7.0
Independence	5.0
Irvington	N/A
Kenbridge	5.0
Keysville	5.0
Kilmarnock	5.0
Lacrosse	4.0
Lawrenceville	5.0
Lebanon	6.0
Leesburg	3.5
Louisa	5.5
Lovettsville	3.0
Luray	4.0
Madison	4.0
Marion	7.0
Mineral	5.0
Narrows	4.0
Nassawadox	4.0
New Market	5.0
Occoquan	2.0
Onancock	4.0
Orange	8.0
Pearisburg	4.0
Pembroke	4.0
Pennington Gap	5.0

Locality	Meals (Restaurant) Tax (%)
Towns continued	
Pound	4.0
Pulaski	6.0
Purcellville	5.0
Rocky Mount	5.0
Rural Retreat	5.0
Saint Paul	5.0
Saltville	6.0
Scottsville	4.0
Smithfield	6.0
South Boston	4.0
South Hill	5.5
Stanley	4.0
Strasburg	5.0
Surry	3.0
Tappahannock	4.0
Tazewell	7.0
Timberville	5.0
Urbanna	5.0
Victoria	4.0
Vienna	3.0
Vinton	5.0
Wachapreague	N/A
Wakefield	5.0
Warrenton	4.0
Warsaw	4.0
Waverly	5.0
West Point	4.0
White Stone	N/A
Windsor	5.0
Wise	6.0
Woodstock	5.0
Wytheville	6.0

Meals Tax Levied by Virginia's Localities

Locality	Meals (Restaurant) Tax (%)
Counties	
Accomack	N/A
Albemarle	4.0
Alleghany	4.0
Amherst	4.0
Appomattox	N/A
Arlington	4.0
Augusta	4.0
Bath	4.0
Bedford	4.0
Bland	4.0
Botetourt	4.0
Brunswick	N/A
Buchanan	N/A
Buckingham	N/A
Campbell	N/A
Caroline	4.0
Carroll	4.0
Chesterfield	N/A
Clarke	N/A
Craig	4.0
Culpeper	N/A
Dickenson	2.0
Dinwiddie	4.0
Fairfax	N/A
Fauquier	N/A
Floyd	N/A
Franklin	4.0
Frederick	4.0
Giles	N/A
Gloucester	4.0
Goochland	N/A
Grayson	N/A
Greene	4.0
Greensville	4.0
Halifax	4.0
Hanover	N/A
Henrico	4.0
Henry	4.0
Highland	N/A
Isle of Wight	4.0

Locality	Meals (Restaurant) Tax (%)
Counties (continued)	
James City	4.0
King George	4.0
King William	4.0
Lee	N/A
Loudoun	N/A
Louisa	4.0
Madison	4.0
Mecklenburg	N/A
Middlesex	4.0
Montgomery	4.0
Nelson	4.0
New Kent	4.0
Northampton	4.0
Nottoway	N/A
Orange	4.0
Page	4.0
Patrick	N/A
Pittsylvania	4.0
Prince George	4.0
Prince William	N/A
Pulaski	4.0
Rappahannock	4.0
Roanoke	4.0
Rockbridge	4.0
Rockingham	4.0
Russell	N/A
Scott	N/A
Shenandoah	N/A
Smyth	N/A
Southampton	4.0
Spotsylvania	4.0
Stafford	4.0
Sussex	N/A
Tazewell	N/A
Warren	4.0
Washington	N/A
Wise	N/A
Wythe	4.0
York	4.0

ATTACHMENT B

POSSIBLE SCHEDULE OF EVENTS FOR BOARD-INITIATED PETITION FOR MEALS TAX REFERENDUM ON NOVEMBER 8, 2016

Date	Event
June 7, 2016, **June 21, 2016** or **July 12, 2016** [July 26, 2016, leaves the minimum time to obtain a court order.]	Board adopts a Resolution that sets forth the ballot question, directs the County Attorney to file a Petition with the Circuit Court, and asks the Circuit Court to order an election on November 8, 2016, on the question as set forth in the Resolution.
June or July 2016	County Attorney files Petition with Circuit Court.
August 19, 2016	Last date on which Circuit Court may order referendum election to be held on November 8, 2016. The Court Order will set forth the question to appear on the ballot as it is stated in the Resolution.
September 20, 2016	Optional: Board approval of a "Plain English" statement that sets out the ballot question and a neutral explanation of not more than 500 words on the proposed question.
September 23, 2016	Deadline by which the General Registrar must make printed ballots available for absentee voting.
September - October 2016	The clerk of the circuit court publishes notice of the election in a newspaper of general circulation in the county once a week for three consecutive weeks prior to the election.
November 8, 2016	**Election Day.**
Mid-November 2016	Electoral Board certifies election results to the State Board of Elections, the Clerk of the Board of Supervisors and the Clerk of the Circuit Court.
Late November/December2016	County Attorney moves for entry of a final order; Circuit Court enters final order.
January 2017	Board authorizes advertisement of a public hearing on a meals tax ordinance; advertisement is published twice.
February 2017	Board holds public hearing and adopts ordinance establishing the amount and terms of the meals tax. The ordinance must be adopted by a majority of all members elected to the governing body, not just a majority of those present and voting. The ordinance may establish a delayed effective date if the Board deems it appropriate so that the restaurant industry will have time to make changes necessary to enable it to collect the tax.

ATTACHMENT C

Response to Questions on the 2016 LOBs

Request By: Board of Supervisors **Relevant LOB(s):** N/A

Question: Provide information regarding the Business, Professional and Occupational License (BPOL) Tax including a brief history / explanation of current state maximum rates, Fairfax County rates and a comparison with surrounding jurisdictions.

Response:

The BPOL tax became a revenue source at the state level following the War of 1812. Except for a reduction in the tax rate for Research and Development firms, state maximum rates have not changed since 1978. A 1978 report to the Governor and General Assembly by the Revenue Resources and Economic Commission, noted that these maximum rates reflect the relative differences in operating ratios between broad categories of similar activities, i.e., the gross profit ratios for similar business activities as reported by the Internal Revenue Service in Statistics of Income: Business Income Tax Returns, 1970.

Fairfax County's authority to levy a BPOL tax dates back to 1952; however the County first exercised its taxing authority in 1967 when it imposed a Retail Merchants Tax. A business license tax was levied on all types of businesses beginning in FY 1970. Attachment 1 provides a summary of Code Amendments to the BPOL Tax in Fairfax County.

Staff located three studies relating to Fairfax County's BPOL Tax. In 1982, Fairfax County hired John L Knapp, to study the equity of the County's BPOL Tax rates. That study concluded that because the BPOL tax is passed on to the consumer any attempt to adjust tax rates for business' profitability are unnecessary. The Executive Summary of this study is provided in Attachment 2.

In 1993, KPMG Peat Marwick completed a study of the County's business taxes including BPOL, Business Personal Property and the Consumer Utility Tax. The study outlined options for reform or replacement of the BPOL Tax. The Executive Summary of the KPMG study is provided in Attachment 3.

In 1994, the Business Tax Study Group and comprised of private sector officials released a report on the BPOL Tax. The study resulted in several changes to the BPOL ordinance (summarized in Attachment 1.) The Executive Summary of the Business Tax Study report is provided in Attachment 4.

Rate Comparison
Attachment 5 provides the State maximum BPOL rate by category, BPOL rates of all Northern Virginia localities and selected other large jurisdictions in Virginia.

In addition, the publication *Virginia Local Tax Rates, 2014* published by the Weldon Cooper Center for Public Service provides the median tax rate for a few business categories by type of locality. That information is reproduced below with state maximums and Fairfax County's rate added for comparison.

Maximum and Median BPOL Tax Rates Per $100 in 2014
Compared to Fairfax County's Rates

		Median Rates*			
Business Category	**State Maximum Rate**	**Cities**	**Counties**	**Towns**	**Fairfax County Rate**
Contracting	$0.16	$0.16	$0.12	$0.13	$0.11
Retail	$0.20	$0.20	$0.15	$0.14	$0.17
Repair, Personal Services & Business Services	$0.36	$0.36	$0.20	$0.18	$0.19
Financial, Real Estate & Professional Occupations	$0.58	$0.58	$0.32	$0.25	$0.31
Wholesale**	$0.05	$0.12	$0.05	$0.05	$0.04

*Median rates were calculated by the Weldon Cooper Center for Public Service, Virginia Local Tax Rates, 2014
**The median city rate of $0.12 is above the state maximum of $0.05 because many cities operate under grandfather clauses that allow them to impose a higher rate.

Fairfax County
History of Business Professional Occupational License Code Amendments

1964 - Virginia General Assembly authorized all counties to impose a local business license tax.

1967 - Fairfax County imposes a Retail Merchants Tax.

October 1, 1969 - Fairfax County adopts a comprehensive BPOL tax on businesses effective for FY 1970. The ordinance includes the taxation of Research and Development (R&D) firms.

July 1970 - The Board eliminates taxation on two of the three categories of R&D including electronic and physical science research service and science research and development service.

July 1973 -The Board removes the third category (economic and social science research services) of R&D from taxation.

November 28, 1988 - The Board removes the exemption for R&D firms and taxes these firms at a rate of $0.31/$100 of gross receipts effective January 1, 1989.

January 29, 1990 - The Board approves amendments to the BPOL ordinance that 1) excludes from the definition of gross receipts amounts paid by advertising agents for any customer for advertising space, radio time, television time, electrical transcription, pressings, art work, engraving, plate, mats, print, printing stock and postage; and 2) licensing advertising agents and firms as a business service rather than a professional, specialized occupation.

FY 1991 - While no change in the local ordinance was required, the state created a uniform definition of a motor vehicle dealer's gross receipts for BPOL whereas, automobile dealers are allowed to exclude trade-ins from their gross receipts beginning in FY 1991.

April 27,1992 - The Board approves an amendment that temporarily reduces the tax rate on Real Estate brokers from $0.31/$100 of gross receipts to $0.01/$100 in FY 1993 and FY 1994; $0.10/$100 in FY 1995; and back to $0.31/$100 in FY 1996 and beyond.

July 27, 1992 - The Board approves an amendment that separates gross receipts from management fees and sales commissions of Real Estate Brokers. The tax on management fees is reduced from $0.31/$100 of gross receipts to $0.01/$100 in FY 1993 and FY 1994; $0.10/$100 in FY 1995; and to $0.19/$100 in FY 1996 and beyond.

September 21, 1992 - The Board adopts an amendment to exempt from BPOL taxation non-profit businesses with an Internal Revenue Code 501 (c) (6) designation from the IRS. Previously, only membership dues collected by trade, business, professional, services, or civic associations were exempt from BPOL taxation.

February 22, 1993 - The Board adopts an amendment that clarifies taxation of craft show merchants. Craft show promoters are not to be taxed on the proceeds of the craft show merchants, but are taxed on their commissions at $0.20 per $100. Individual craft show merchants are taxed on their sales (if sales at a rate of $0.17 per $100).

May 17, 1993 - The Board adopts an amendment to reduce the BPOL tax rate on gross receipts from federally funded Research and Development from $0.31 per $100 to $0.03 per $100, the maximum rate allowed following approval of state legislation during the 1992 Virginia General Assembly.

July 12, 1993 - The Board adopts an amendment that excludes from the definition of gross receipts the pass-through funds of any money lender organized, registered and doing business as a cooperative association.

April 18, 1994 - Based on a recommendation of the Business Tax Study Group, the Board adopted an amendment that levies a flat $30 fee for businesses with gross receipts between $10,000 and $50,000 rather than a tax rate based on gross receipts. Those businesses with gross receipts less than $10,000 continued to have no BPOL tax liability.

November 21, 1994 - Following the Business Tax Study Group recommendations, the Board adopts changes to the BPOL ordinance in order to equalize service rates, align the tax burden with cash flow for builders and developers and increase administrative efficiency and simplify filing. The approved amendments reduced the number of tax rate categories from 17 to ten. In addition, exemptions were adopted for income generated from subleasing property if the revenue was incidental to the company's primary business activity.

September 9, 1996 - Following legislation that required statewide uniformity of BPOL ordinances, the Board approved amendments that included the exemption of certain nonprofit organizations and a change in the tax threshold which exempted firms with gross receipts between $50,000 and $100,000 from the BPOL Tax, but charged a flat fee of $50.

November 24, 1997 - The Board adopts an amendment to provide for a three-year phase-out of the BPOL Tax on all gross receipts solely derived from the design, development, or other creation of software for lease, sale, or license in the following manner: 33 1/3 percent excluded in FY 1999; 66 2/3 percent excluded in 2000 and 100 percent excluded in FY 2001 and beyond.

THE EQUITY OF THE FAIRFAX COUNTY BUSINESS, PROFESSIONAL, AND OCCUPATIONAL LICENSE TAX

by

John L. Knapp, Ph.D. Economic
Consultant

March 1982

Executive Summary

The statutory incidence (legal liability for payment) of the business, professional, and occupational license tax (BPOL tax) is clearly upon business firms. Economic incidence—the final distribution of the tax burden after the process of shifting the burden has been completed—is more difficult to measure. Nonetheless, the determination of economic incidence is crucial for any examination of tax equity. This study describes and analyzes many theories about the economic incidence of the BPOL tax and concludes that the long-term economic incidence of the BPOL tax is similar to that of a general sales tax which is borne by consumers. If this is the case, then attempts to adjust the tax rate for business firms' ability to pay as measured by some indicator of profitability are unnecessary. Such a viewpoint is not the one implicit in the state guidelines for a BPOL tax. .

The state guidelines, which establish maximum rates for four major classifications of business, are based on the implicit assumption that rates should be adjusted for (1) business firms' use of the market, and/or (2) profitability, both of which are measured by operating ratios. "Operating ratio" is defined as follows:

$$\text{operating ratio} = \frac{\text{gross receipts - cost of goods}}{\text{gross receipts}}$$

Based on an analysis of U.S. Internal Revenue Service (IRS) data, this study concludes: (1) operating ratios are not a good indicator of profitability; (2) operating ratios vary over time; (3) operating ratios for different forms of business organization, (proprietorship, partnership, and corporation) within the same industry vary, and a major reason for this variation is the manner in which businesses report items on their income tax returns; (4) operating ratios vary among subcategories of business which are grouped under the same general industry; and (5) operating ratios vary by size of firm even after allowance *for* industry and form of business organization.

Fairfax County has several options in regard to the BPOL tax in addition to the status quo. A tabular summary of the options is shown below:

	Total Revenue Based on 1980 Gross Receipts[a]	Numberof Present 14 CategoriesPaying[b]		
		More Tax	Less Tax	Same Tax
Status quo	$ 8,879,260			14
Conformity with state guidelines				
Option 1. Maximum rates .	13,601,377	14	0	0
Option 2. Proportionate rates, no increase in total revenue	8,838,550	6	8	0
Option 3. Proportionate rates, no tax increase for any category	3,562,859	0	13	1
Nonconformity with state guidelines				
Option 4.--Uniform rate ($0.16) for all business classes	8,745,822	2	11	1
Option 5.--Limited subclassifications	<13,601,377	Depends on number of classes and operating ratios		
Option 6.—Numerous subclassifications	<13,601,377			

Source: Table 7.

a/ Excludes license taxes on rental owners, wholesalers, and utilities since they are not covered by state guidelines of the 14.

b/ In 1980, there were no firms in 2 of the 14 categories; those without taxable sales were premium stamp suppliers and vending machine operators.

When it commissioned the study, the Board asked several-specific questions:

1. <u>"Can BPOL rates be more equitable?"</u> The answer depends on the theory of economic incidence which is accepted. In my view, in the long-run, the tax is borne primarily by consumers. If this is the case, then there is no need to adjust the tax rate for business firms' ability to pay as measured by some indicator of profitability and a uniform rate (Option 4) would be preferable.

Creation of many tax rates for particular types of business (Options 5 and 6) would simply cause greater administrative complexity without making the tax more equitable. Although the state guidelines permit numerous subclassifications within each of the four broad classes, I feel that such subclassifications would violate the spirit and intent of the guidelines. The staff work which was the. basis for the guidelines contained no suggested maximum rates for subcategories, and when the staff examined the IRS data base which presumably would be the basis for establishing subcategories, the staff questioned the feasibility of using it for precise adjustment. Furthermore, a major reason for enacting the guidelines was the desire to eliminate relatively high tax rates that some localities had imposed on narrow business categories. By establishing four broad categories, the General Assembly simplified BPOL tax structures and, removed some of the perceived inequities. Establishment of numerous sub-categories would be a policy in an opposite direction from the guidelines ' approach.

An alternative to the status quo or a uniform rate would be to abandon Fairfax County's present fourteen business tax categories in favor of the four "categories in the state guidelines (Option 1, 2, or 3). The state guidelines represent a compromise between the common business attitude that the tax is borne completely by business and the economic theory assumption that most of the tax is shifted to consumers. Thus, the guidelines establish the four major categories on the basis of profitability, but there is no attempt to vary rates within major categories. Although I would prefer that the same rate be used for all types of businesses, I feel that the state guidelines can be tolerated, since products and services within very broad classes of consumption are treated equally. Moreover, the guidelines crudely approximate a tax on value added. Value added may be considered a broad measure of market use.

Implementation of the guidelines could be accomplished by using state maximum rates (Option 1), proportionate rates with no increase in revenue (Option 2), or proportionate rates with no tax increase for any category (Option 3).

Since Options 1 and 2 would involve tax increases for some businesses, and since in the short-run a portion of the economic incidence is borne by businesses, the Board might wish to make rate adjustments over several years rather than all at once.

2. "Are the [present Fairfax County] rates within the guidelines established by the General Assembly?" The answer is "yes." Therefore, the status quo could be continued.

3. "Can a relationship between the tax and the profitability of various business categories be established?[11]- The answer is "no", since economic incidence is not a direct function of profitability. Furthermore, operating ratios, the basis for establishing different rates for a classified gross receipts tax, are a poor measure of profitability since they include many costs that are subtracted in deriving net income, and they depend to some extent on the tax accounting procedures employed.

4. The Board also "..requested that the study include a review of the proper groupings, i.e., businesses which cannot pass along costs should not be placed in the same category with those which can." The inability to shift the tax would be a short-run phenomenon depending primarily on consumers' responsiveness to an increase in price. This will depend on many factors including the size of the item in consumers' budgets, the existence of substitutes, and the time and travel cost of shopping elsewhere. These factors will vary for individual firms, even those of thesame size and in the same industry. Thereis no source that contains the type of information desired by the Board.

COMPARATIVE STUDY OF FAIRFAX COUNTY BUSINESS TAXES

Submitted to:

**Fairfax County
and the
Fairfax County Chamber of Commerce**

Presented By:

**Policy Economics Group
KPMG Peat Marwick**

September, 1993

EXECUTIVE SUMMARY

The Policy Economics Group of KPMG Peat Marwick conducted this study of business tax policy for Fairfax County and the Fairfax County Chamber of Commerce to accomplish the following three objectives:

- to provide an objective and comprehensive comparison of Fairfax County's overall business taxes on selected industries with those of competitor jurisdictions;
- to evaluate current Fairfax County business taxes with a focus on the Business Professional and Occupational Licensing (BPOL) tax, the utility consumer tax, and the personal property tax on equipment; and
- to assess the implications of major business tax policy alternatives for Fairfax County on a revenue neutral basis.

Methodology

The Business Tax Competitiveness Model developed by the Policy Economics Group of KPMG Peat Marwick is a key analytical tool that has been used to perform the analysis of current and alternative Fairfax County business tax policies.

The Business Tax Competitiveness Model calculates before and after-tax rates of return on a prototype investment by a representative firm in each industry. Balance sheets and income statements for the representative firms are based upon actual financial data for each industry. The Model projects income and taxes over a thirty year period. Effective tax rates are calculated as the measure of overall tax burdens on investment The effective tax rate is the difference between pretax and after-tax rates of return divided by the pretax rate of return on investment. The effective tax Tate is the widely-accepted measure of business tax burden since it accounts for the time value of money over the life of an investment The impact of tax law provisions that are sensitive to timing, such as tax depreciation rules and property tax assessment policies, are properly measured.

The study includes eight industries that were selected because of their significance to the economic development of Fairfax County. It is important to note that these results are limited to the jurisdictions and industries that are included in the study. Given the small sample of industries and jurisdictions, the results cannot be generalized to all industries and jurisdictions in the U.S. The eight industries are:

- Management Consulting and Public Relations
- Engineering and Architecture
- Printing and Publishing
- Computer Manufacturing
- Wholesale Trade
- Retail Trade
- Leasing
- Computer Services

Eight comparison jurisdictions have been included in the study. These jurisdictions are generally perceived to be attractive locations for the service and high-technology businesses that form the core of the Fairfax County economy. The eight competitor jurisdictions are:

- Montgomery County, Maryland
- DeKalb County (Atlanta), Georgia
  Raleigh, North Carolina
- San Jose, California
- Charlotte, North Carolina
- Indianapolis, Indiana
- Austin, Texas
- Princeton, New Jersey

The Business Tax Competitiveness Model has also been used to examine the implications of business tax policy alternatives to the BPOL tax.

Key Findings

<u>Comparative Business Tax Analysis</u>

- Based upon the quantitative analysis of the sample industries and jurisdictions included in the study, structural issues have been identified relating to three specific Fairfax County business taxes:

  - the Business Professional and Occupational Licensing tax;
  - the personal property tax on equipment; and
  - the utility consumer tax.

- These three taxes are sources of concern regarding the competitiveness, efficiency and equity of the Fairfax County business tax structure.

- Business tax burdens vary across industries depending upon a variety of factors. For example, industries that have disproportionate shares of computers and other equipment will tend to have relatively high effective tax rates in jurisdictions such as Fairfax County, which include personal property in the property tax base. Industries with low profit margins will have above-average tax burdens under a gross receipts tax.

Of the eight industries included in the study, retail trade, engineering and architectural services and leasing have relatively high effective tax rates in Fairfax County. Effective tax rates on the two manufacturing industries are relatively low in Fairfax County.

Retail trade and engineering and architectural services are disproportionately burdened by the BPOL (gross receipts) tax and the utility consumer tax.

Evaluation of Current Fairfax County Business Taxes

- Competitiveness, economic efficiency (uniformity across industries), and equity are three key criteria for evaluating state and local business tax policy.

- Structural issues relating to these three criteria have been analyzed with respect to the Fairfax County BPOL tax, utility consumer tax and personal property tax on business equipment.

- The imposition of a gross receipts tax by local governments as a general business tax is relatively uncommon. In addition to Fairfax County, only two of the eight competitor jurisdictions - DeKalb County, Georgia and Charlotte, North Carolina - impose a gross receipts business tax.

- The BPOL tax ranks low in terms of uniformity. The gross receipts tax base tends to result in cascading or multiple taxation as business-to-business transactions as well as final sales to consumers are included in the tax base. Effective tax rates vary considerably and tend to be highest on businesses with high ratios of cost of goods sold to gross receipts.

- The BPOL tax raises equity concerns because it burdens small businesses or startup businesses which operate on relatively low profit margins and are therefore especially sensitive to these concerns.

- The study industries with the highest effective tax rates under the BPOL tax are retail trade, engineering and architectural services, and computer services. These industries play a very important role in the service-based Fairfax economy.

- The personal property tax on business equipment is an issue of special importance to businesses in an era in which information technology is key to maintaining a competitive edge. For example, faster depreciation for computers to reflect more rapid technological advances could improve the competitiveness and economic efficiency of Fairfax County business taxes.

- The utility consumer tax has an uneven impact across industries since it depends upon how intensively an industry uses energy and telecommunications services. Retail trade, printing and publishing and wholesale trade have the highest effective tax rates under the utility consumer tax.

- With respect to the BPOL tax, a number of administrative and legal issues have been identified relating to nexus (jurisdiction to tax), allocation of receipts of multi-jurisdictional businesses, and classification of firms which operate more than one line of business. Although resolution of these issues is beyond the scope of this study, these issues merit further study.

Assessment of County Business Tax Policy Options

- Four revenue-neutral alternatives have been identified for consideration. These options are illustrative alternatives and should not be construed as KPMG Peat Marwick recommendations.

  - reform of the BPOL tax by restructuring tax rates to better reflect the relationship of net income to business receipts;

  - replacement of the BPOL tax with a county corporate income tax with a rate of 6 percent;

  - replacement of the BPOL tax with an additional 0.7 percent local sales tax rate;

  - replacement of the BPOL tax with a tax applied to the gross income of businesses after subtraction of cost of goods sold.

- Option 1, the BPOL tax would be restructured so that the rate structure more closely relate to observed differences in profits-to-gross receipts As a result, the BPOL tax would be more neutral in its impact across industries. However, the BPOL tax would continue to impose an additional burden on businesses in Fairfax County that would not be experienced by businesses in most competitor jurisdictions.

- Under Option 2, the BPOL tax would be replaced with a county corporate income tax with a rate of 6 percent. This option would be more efficient in relating the tax burden to a firm's ability to pay. However, local corporate income taxes are relatively uncommon and the combined state-local tax rate of 12 percent would be among the highest in the U.S. A local corporate income tax could have a significant adverse impact on Fairfax County's image as a place to locate businesses.

- Under Option 3, the BPOL tax would be replaced with an additional local sales tax at a rate of 0.7 percent. Although the BPOL tax is often viewed as a business tax and the sales and use tax is viewed as a consumer tax, both taxes are similar in that they use gross receipts as the tax base. The sales and use tax has two advantages. First, the structure of the sales and use tax is designed to reduce cascading or multiple taxation. Second, the state sales and use tax statutes and regulations provide a relatively clear framework for defining the tax base so as to minimize compliance issues related to interpretation of the tax law. However, they differ significantly in terms of the extent to which services are included in the tax base.

- Option 4 which would substitute gross income for gross receipts as the business tax base would be more equitable than the current gross receipts base since business purchases of goods would not be double-taxed. However, simply using gross income would create new inequities because of the differences in accounting across industries.

EXECUTIVE SUMMARY:

BUSINESS TAX STUDY GROUP

REPORT AND RECOMMENDATIONS

FAIRFAX COUNTY, VIRGINIA

SEPTEMBER 14, 1994.

SEP 2 6 1994

EXECUTIVE SUMMARY: BUSINESS TAX STUDY GROUP

SEPTEMBER 14, 1994

BACKGROUND:

Since the fall of 1993, a Study Group comprised of private and public officials has been analyzing business taxes in Fairfax County. This group, chaired by Supervisor Robert B. Dix, Jr., Hunter Mill District, was formed to build upon the initial findings of a Comparative Study of Fairfax County Business Taxes presented by the Policy Economics Group of KPMG Peat Marwick. This study was a public/private venture jointly commissioned by the Board of Supervisors and the Fairfax County Chamber of Commerce.

On December 6, 1993, the Initial Report and Recommendations of the Business Tax Study Group was presented to the Board of Supervisors. As noted in the December report, the Study Group made the following recommendations:

I. Replacement of BPOL with a corporate income tax was not a desirable alternative, and replacing BPOL with a BPOL-type levy on gross income could in fact create even more challenges than exist today.

II. Possibility of replacing the current BPOL levy with an increase in the local option portion of the sales tax by approximately one-half cent should be left on the table for further consideration.

In recommending this, the Business Tax Study Group wants to emphasize that it views BPOL as an undesirable tax which, in the long run, should be replaced or phased-out. The Business Tax Study Group recognizes however that this is a complex issue and the Study Group will continue to review and consider all available options in pursuit of this goal.

The local sales tax proposal was transmitted to the State for their consideration as they conduct, a state-wide study of BPOL taxes pursuant to a mandate from the 1994 General Assembly. A copy of this letter, dated December 20, 1993, is attached to the Executive Summary.

Additionally, two other proposals were transmitted to the State for their review, along with the local sales tax issue. This includes the possibility of establishing a local option administrative appeal procedure for BPOL similar to the present boards of equalization: and, a request that the State committee carefully review the present statutory exemptions to BPOL, such as those granted to insurance companies, insurance agents, publishers, broadcasters and manufacturers.

As a general rule, the Business Tax Study Group supports the State effort to establish greater statewide uniformity in the administration of the BPOL tax. It is also the consensus of the Study Group that businesses should not have to pay the tax during the review of a legitimate appeal. If the appeal is upheld however, the appropriate penalties and interest should accrue to the original due date.

III. Additionally, two specific proposals first raised' in the Study Group's December 6, 1993, report have now been ' formally adopted in Fairfax County. The first was an amendment to the taxable threshold for BPOL taxes adopted by the Board of Supervisors on April 11, 1994. This amendment authorized businesses with gross receipts between $10,000 and $50,000 to be taxed at a flat rate of $30.00, rather than on a percentage of gross receipts. While this action had some revenue loss, it should improve the economic climate for many small businesses. Of 9,749 business accounts affected, it was estimated that 76% experienced an average tax reduction of approximately $39.

The second Study Group recommendation was that the depreciation of business computer equipment be accelerated for personal property tax purposes. This proposal recognized the prevailing market conditions for computer equipment and helped support the competitive advantage of the County for economic development. This proposal was formally endorsed by the Board of Supervisors, and the depreciation schedule was 'changed in the summer of 1994 after an-extensive study by the Office of Assessments. The changes will officially take effect in 1995 (FY 1996).

CURRENT REPORT:

IV. Finally, the group also committed to further study possible reforms to the current BPOL structure, evaluating business categories, classifications, definitions and exemptions. The present report is a product of the group's continuing study in this area. The focus of the current report is on BPOL taxes only. The Study Group has reviewed the Business Utility Tax and decided not to propose any changes to the current law.

To the highest extent possible, the charter of the study group was to keep its proposals revenue neutral. This goal was not completely achievable as a number of progressive recommendations could result in the potential loss of approximately $1.0 million in General Fund revenue. This is approximately 1.8% of the BPOL revenue estimate in the FY 1995 Adopted Budget Plan. However, it is important to note that BPOL revenue collections at the end of FY 1994 were stronger than anticipated. If this trend continues in FY 1995, BPOL revenue collections in excess of the budgeted estimate could offset the loss from the Study Group proposals.

A final caveat should be noted in this regard. Responsible estimates of the revenue impact have been attempted throughout this study. However, in a couple of cases there was simply insufficient data from which to make a complete analysis. Thus, half of the $1.0 million reduction is a "soft" estimate. In this case it was necessary to make revenue extrapolations from very small data sets. Therefore, the reliability of these estimates cannot be established prior to implementation. The other half of the estimated revenue loss stems from the proposed tax rate - changes. These estimates are substantiated by available data.

NEW PROPOSALS:

1. Amend Section 4-7-22, Renting .By Owners-- adopt new exemption which eliminates a BPOL requirement on gross receipts earned, from subleasing property where the sublease revenue is incidental to the company's primary business activity. This, would be deemed non-taxable miscellaneous income. Applicable only where a tenant (non-owner) sublets rented space to another occupant. Rental receipts of the property owner would still be fully subject to BPOL.
Potential impact = $(452,000).

2. Amend Section 4-7-1 B (1)-- adopt new exemption which excludes from taxable revenue general and administrative (G&A) intra-company reimbursements or transfer payments. This exclusion would generally involve companies that simply have their "headquarters" here, and have no other specific sales made or services rendered from the Fairfax location.
An example of this is an internal division "paying" corporate headquarters for G&A services. Applies only to internal company transfer payments. Does not apply to payments between separate corporate entities, subsidiaries or partnerships. Existing state code exemption already deals with inter-company payments between affiliated corporations. Potential impact = $(130,955).

3. Rate Chancres Collapses the existing 17 separate categories into only 10. Of the current 17 categories, 11 will have no rate change, 3 will have a lower rate, and 3 will have a tax increase. Potential impact = $(438,557).

Three categories receive lower tax rate (Business Services, Personal Services, Telephone Co.) which reduces the tax rate for approximately 3,451 business accounts.

Two categories receive a rate increase (Money Lenders, Repair Services). Also, Builders and Developers keep their existing tax rate but will now be taxed on gross receipts instead of gross expenditures. These changes will result in a tax increase for approximately 1,396 business accounts.

Combined .with the collapsed categories is improved clarification/modernization of businesses specifically listed.in each category.

Key benefits

- SIMPLICITY, CLARITY, AND PREDICTABILITY FOR BUSINESSES
- FACILITATES CUSTOMER SERVICE
- HELPS EQUALIZE "SERVICE" RATES
- HELPS EFFICIENCY OF ADMINISTRATION
- BRINGS TAX BURDEN IN SYNC WITH CASH FLOW (builders & developers)
- 71% OF' THE 4,847 ACCOUNTS AFFECTED WILL GET TAX REDUCTION

TIMING

- 17 individual categories would be retained for 1995, but all tax rate changes can be made and implemented as of January 1, 1995.
- Total collapse into 10 categories (i.e., form taxpayers use, data on computer screens) would be completed by 1996 due to computer programming requirements.

-- CATEGORY AND RATE CHANGE SUMMARY --

Business Categorv	Existing Rate	Proposed Rate	Greatest Est. Tax Chancre	' Average Est. Tax Change	% Change
Research & Development	. 03	. 03			
Wholesale Merchants	.04	. 04			
Builders & Developers	.05	.05	$ 10,972	$ ' 429	33.11%[1]
Real Estate Brokers	.10	. 10[2]			
Contractors	.11	.11			
Retail Merchants	.17	.17			
Retail/Wholesale Merchants	.17	.17			
Business Services	.20	.19	$(13,243)	$(211)	(5.00)%
Personal Services	.22	.19	$ (144,233)	$(258)	(13.64)%
Repair Services	.18	.19	$ 6,814	$ 58	5.56 %
Money Lenders	.16	.19	$ 11,494	$ 535	18.75 %
Utilities	.24	.24			
Telephone Co. ' s	.26	.24	$(19,903)	$ 7,434	(7.69)%
Amusements	.26	.26			
Hotels/Motels	.26	.26			
Renting By Owners	.26	.26			
Professional & Specialized	.31	.31			

Builders and Developers are currently taxed per $100 of gross, expenditures. Study Group proposal is to tax them on gross receipts instead. Current data suggests that aggregate receipts for this category exceed aggregate expenditures by roughly 33%. THIS SHOULD DEFER THE TAX LIABILITY SO THAT IT BECOMES IN SYNC WITH BUSINESS CASH FLOW.

For 1994, Real Estate Brokers are still taxed at $0.01 per $100 of gross receipts. Under current law this will increase to $0.10 in 1995 and back to $0.31 in 1996. This future rate structure for brokers is retained by the Study Group proposal.

NEW PROPOSALS, continued:

(THESE PROPOSALS CODIFY AND CLARIFY EXISTING LAW OR ADMINISTRATIVE PRACTICE; OR HAVE NEGLIGIBLE REVENUE IMPACT)

4. Further amend Section 4-7-1-- Consolidates and clearly identifies the exclusions, exemptions and special definitions in one 'main section:

   A. Codifies the need for apportionment among other jurisdictions and spells out the type of taxes that factor into apportionment formula.

   B. Codifies existing administrative policy to exclude from taxation receipts from gifts, miscellaneous dividends and interest income.

   C. Proposes new exemption for the .miscellaneous sale of capital assets when such receipts are incidental to the business activity of the person. (Estimated revenue loss is negligible).

   D. Proposes special definition for businesses leasing or renting aircraft to classify them as a Wholesale Merchant. This is a business recruitment initiative.

5. Amend Section 4-7-11, Penalties--

   A. Incorporate State law whereby "upon nonpayment reasonable attorney's or collection agency fees may be recovered by the County." Such fees shall not exceed 20% of the delinquent tax bills.

   B. Reflect 1994 State law change by adding section which halts collection activity while taxes are being appealed to the Office of Assessments.

6. Amend Section 4-7-22, Renting bv Owners-- changes the rental threshold for BPOL (i.e., from 2 to 4 before liable).

7. Amend Section 4-7-30, Telephone Companies-- instead of taxing a telephone company only on their 'Local Exchange' gross receipts, wording has been changed. Tax basis would- now be on "all sales of goods or services to the ultimate consumer with an exclusion of all receipts from long distance telephone calls." Supports the County's ability to tax- the local' receipts generated by cellular telephones.

8. Produce an Informational Booklet on BPOL-- Law and Administration. This should be a joint project between the County and the Fairfax County Chamber of Commerce.

FY 2016 BPOL Rate Comparisons (per $100 of Gross Receipts)

	Amusement	Builders and Developers	Business Service Occupations	Consultant/ Specialist	Contractors
State Max	**$0.36**	**$0.16**	**$0.36**	**$0.36**	**$0.16**
Fairfax County	$0.26	$0.05	$0.19	$0.31	$0.11
Vienna	flat rate	$0.12	$0.22	$0.22	$0.12
Falls Church	flat rate	$0.16	$0.36	$0.36	$0.16
Fairfax City	$0.00	$0.16	$0.27	$0.27	$0.16
Arlington	$0.25	$0.16	$0.35	$0.36	$0.16
Loudoun	$0.21	$0.13	$0.17	$0.17	$0.13
Prince William	flat rate	$0.13	$0.21	$0.13	$0.13
Herndon	$0.21	$0.13	$0.21	$0.40	$0.13
Alexandria	$0.36	$0.16	$0.35	$0.35	$0.16
VA Beach	$0.36	$0.16	$0.36	$0.36	$0.16
Henrico	$0.20	$0.15	$0.20	$0.20	$0.15
Chesterfield	$0.19	$0.14	$0.20	$0.20	$0.14
Richmond	$0.36	$0.19	$0.36	$0.36	$0.19
Average Rate if Levied, w/o Fairfax County	**$0.27**	**$0.15**	**$0.27**	**$0.28**	**$0.15**

FY 2016 BPOL Rate Comparisons (per $100 of Gross Receipts)

	Rent of House/ Condo	Repair Service	Research & Development	Retail Merchants	Telephone Companies	Wholesale Merchants
State Max	$0.00	$0.36	$0.03	$0.20	$0.50	$0.05
Fairfax County	$0.26	$0.19	$0.03	$0.17	$0.24	$0.04
Vienna	$0.17	$0.22	$0.00	$0.17	$0.50	$0.10
Falls Church	$0.38	$0.36	$0.00	$0.19	$0.50	$0.08
Fairfax City	$0.27	$0.27	$0.03	$0.20	$0.50	$0.05
Arlington	$0.28	$0.35	*see note	$0.20	$0.50	$0.08
Loudoun	$0.16	$0.16	$0.03	$0.17	$0.50	$0.05
Prince William	$0.00	$0.21	$0.03	$0.17	$0.50	$0.05
Herndon	$0.05	$0.21	$0.00	$0.13	$0.50	$0.05
Alexandria	$0.50	$0.35	$0.00	$0.20	$0.50	$0.05
VA Beach	$0.00	$0.36	$0.00	$0.20	$0.50	$0.12
Henrico	$0.00	$0.20	$0.00	$0.20	$0.50	varies
Chesterfield	$0.00	$0.20	$0.10	$0.19	$0.50	$0.10
Richmond	$0.58	$0.36	$0.00	$0.20	$0.58	$0.22
Average Rate w/o Fairfax County	$0.30	$0.27	$0.05	$0.18	$0.49	$0.08

*Arlington does not have a Research and Development classification. Those activities are classified as Professional or Specialized with a tax rate of $0.36/$100.

ATTACHMENT C

Attachment 5

FY 2016 BPOL Rate Comparisons (per $100 of Gross Receipts)

	Hotels and Motels	Money Lenders	Personal Service Occupations	Professional and Specialized	Real Estate Brokers
State Max	$0.36	$0.58	$0.36	$0.58	$0.58
Fairfax County	$0.26	$0.19	$0.19	$0.31	$0.31
Vienna	$0.22	$0.52	$0.22	$0.52	$0.52
Falls Church	$0.07	$0.52	$0.36	$0.52	$0.52
Fairfax City	$0.40	$0.40	$0.27	$0.40	$0.40
Arlington	$0.36	$0.36	$0.35	$0.36	$0.36
Loudoun	$0.23	$0.16	$0.23	$0.33	$0.33
Prince William	$0.26	$0.33	$0.21	$0.33	$0.33
Herndon	$0.26	$0.20	$0.21	$0.40	$0.40
Alexandria	$0.35	$0.35	$0.35	$0.58	$0.58
VA Beach	$0.36	$0.58	$0.36	$0.58	$0.58
Henrico	$0.20	$0.20	$0.20	$0.20	$0.20
Chesterfield	$0.20	$0.20	$0.20	$0.20	$0.20
Richmond	$0.36	$0.58	$0.36	$0.58	$0.58
Average Rate if Levied, w/o Fairfax County	$0.27	$0.37	$0.28	$0.42	$0.42

ATTACHMENT D
Prepared by the Restaurant Association of Metropolitan Washington, Virginia Restaurant, Lodging, and Travel Association, National Restaurant Association and the NOVA Chamber of Commerce

April 22, 2016

Fairfax County Proposed Food Tax: Foodservice Industry White Paper

The proposed meals tax is a tax on all prepared foods including restaurants, grocery stores, delis, food trucks, convenience stores, caterers, movie theater concessions, hotel food services and coffee shops. The proposed food tax in Fairfax County singles out the foodservice industry to raise revenue for the general fund, as the Fairfax Board of Supervisors cannot guarantee that money raised through this tax will go directly to the school budget. The unfairly targeted food tax would only be a one-time boon for the County, and not address constant budgetary shortfalls, and would only diversify the County budget by 2.4 percent. (Source: 2014 Meals Tax Task Force) Voters in Northern Virginia counties have never approved a meals tax referendum as the meals tax is recognized as an especially unpopular measure.

A meals tax of 4 percent would result in a $90 million tax increase for County diners. Fairfax County estimates 72 percent of the $90 million tax increase would be paid by Fairfax County residents and 28 percent of the $90 million tax increase would be paid by visitors and employees working in Fairfax County. (Source: Fairfax County Meals Tax White Paper, 2014) The addition of 4 percent meals tax to the current 6 percent sales tax the state charges would constitute a 66 percent tax increase on Fairfax County residents and visitors totaling a 10 percent sales tax on prepared food.

Currently, Fairfax County has a strong competitive edge over neighboring jurisdictions. The advantage is especially noted when deciding to open businesses such as restaurants, convenience stores, grocery stores, hotels and movie theaters or when planning conventions, meetings, galas or conferences. Restaurants are the amenities that larger employers look for when choosing areas to locate. As restaurants are driven to counties that do not have a meals tax such as Loudoun, Prince William, and Montgomery County, large employers and jobs will follow. The restaurant industry has a dramatic effect on the local economy and produces enormous local direct and indirect tax dollars. For every one dollar spent in a restaurant, two dollars are spent in other industries further increasing local tax revenues. (Source: National Restaurant Association)

Who Will a Food Tax in Fairfax County Effect?

Restaurants are an essential part of daily life for many Americans. Nearly half of all adults are restaurant patrons on a typical day, and the average American spends nearly one-half of their food money in restaurants. According to the Bureau of Labor Statistics' Consumer Expenditure

Survey, the average U.S. household spent $2,787 on restaurant food in 2014, which represented 4.2 percent of its pre-tax income.

Low to Middle Income Families - A greater majority of low and middle income families buy meals from restaurants or prepared food at the market to feed their families on a daily basis. Among households with annual incomes of less than $30,000, spending on restaurant food represented 7.9 percent of their pre-tax income, which is four full percentage points above the national average. Low and middle income families live on a fixed income and cannot afford increased food costs resulting from a meals tax, yet will bear a greater burden than other demographics. (Source: Bureau of Labor Statistics, National Restaurant Association; 2014 data)

Senior Citizens - Senior Citizens dine out to a much higher degree than the average Fairfax resident. For the most part these citizens live on fixed incomes. While many of these residents have tight budgets, they will be forced to support a larger portion of this tax increase. (Source: AARP Public Policy institute and US Census, http://www.census.gov/newsroom/releases/archives/aging_population)

Restaurant Employees - Wait staff in full-service restaurants will be greatly affected by the proposed meals tax increase, as their main source of income is gratuity left by diners. The gratuities on meals are immediately reduced by customers when a locale imposes or increases a meals tax. As noted in a restaurant case study, these employees will often lose 20 percent of their wages directly resulting from a food tax. Job creation for restaurants located in areas with a food tax have stalled compared to restaurants in localities without a meals tax. One in three Americans got their start in the restaurant industry and 90% of managers started as hourly paid employees. (Source: National Restaurant Association) Historically, restaurants have been the industry of opportunity, providing jobs for people with little to no experience and allowing these people to work their way up the ranks while earning a competitive wage and learning along the way, however the imposition of a meals tax raises the barriers of entry to a once inclusive industry. It is predicted that a meals tax would result in a loss of hundreds of jobs in the County. (Source: Data collected from local restaurant owners)

Restaurants - In addition to the three groups most affected by the meals tax, restaurant revenue will also suffer. Restaurants often absorb the increased cost of a meals tax in price reductions. This is designed to prevent losing business as a result of the tax increase. Restaurants operate with razor thin profit margins of approximately 4 percent nationally, and an additional tax equaling profit margins will decimate business. (Source: National Restaurant Association Operation Report 2013-2014) A decrease in restaurant revenue most often yields a reduced rate of growth in restaurant sales, and a reduction of staff size and available hours. Local restaurants have reported a reduction of staffing by approximately 17 percent for restaurants located in areas that later imposed a meals tax. (Source: Data collected from local restaurant owners)

Operational Facts and Data on the Restaurant Industry

Food and labor are the two largest general cost categories for a typical restaurant. The cost of food and beverage is about one-third of the sales dollar, while salaries and wages account for another third.

The average profit margin for a restaurant is approximately 4 percent. In other words, for one dollar of sales the average restaurant takes home four pennies. (Source: National Restaurant Association Operation Report 2013-2014 www.Restaurant.org) If Fairfax County is successful in instituting a 4 percent food tax, the total tax on meals in Fairfax County will be 10 percent, or, for every one dollar in sales, 10 cents would go back to Fairfax County while only 4 cents go to the restaurant. Under the proposed food tax the County and the state will take over two times the amount the restaurant owner earns.

Food prices, are at an all-time high, rent is constantly increasing, the price of fuel continues to climb and restaurants are forced to absorb these record high commodity prices. Increasing operational costs combined with a 4 percent meals tax hike will place unprecedented burdens on the foodservice industry in Fairfax County. (Source: USDA Economic Research Data April 2014, www.ers.usda.gov/data-products/food-price-outlook)

Case Study of Meals Tax increases in Northern Virginia

Through surveying restaurants in Fairfax County that own units in jurisdictions with and without a meals tax, a restaurant group with very similar restaurant units in Fairfax County and Arlington County was able to provide data on the negative impact of a meals tax increase.

This restaurant group owns and operates two restaurants of similar size, theme and price point and has for over twenty years. These two restaurants had very similar revenue and net profits before Arlington County imposed a meals tax. These two restaurants are provided with the same quality control mechanisms, employee and server training, same food quality and food pricing, and same management group. Key findings from a basic study of the two restaurants show:

- The Arlington County restaurant has experienced a sales growth rate 49.74 percent lower than the similar restaurant in Fairfax without a meals tax.
- The wait staff in the Arlington County restaurant earns 20 percent less than the wait staff in the Fairfax County restaurant.
- Staff turnover at the Arlington County restaurant is 30 percent higher than the staff turnover rate at the Fairfax County restaurant.

- The two restaurants had similar staffing levels before the County of Arlington imposed a meals tax. Now, the restaurant in Arlington employs 17 percent fewer employees than the restaurant in Fairfax.
- In the 20 years since Arlington County imposed a meals tax, the difference in sales between the two restaurants has been over $3 million less for the Arlington County restaurant.

While there are certainly other economic factors involved, it is undeniable that the meals tax has had a large adverse effect on the Arlington County restaurant.

A History of Meals and Sales Tax Referendums in Northern Virginia

Historically, food tax ballot referendums do not pass, as they are not supported by the voter base. In 1992, a meals tax referendum failed in Fairfax County. The revenue produced, if the referendum had been successful, was to be spent on educational purposes.

The last meals tax referendum in Loudoun County, introduced in November 2008, failed by a margin of 70 to 30 percent. The revenue produced, if the referendum had been successful, was to be reserved for school construction. Loudoun County was at the time the fastest growing County in the nation and building schools faster than any County in the nation.

In 2002, the Northern Virginia region, including Fairfax County, rejected a referendum that would have raised sales tax for transit and road construction projects. The campaign for the sales tax increase was very well funded: almost all Northern Virginia officials endorsed the tax and the Governor strongly campaigned for the tax. This sales tax referendum failed in a landslide.

The voters in Northern Virginia and Fairfax have continuously rejected referendums to raise the sales and meals taxes. There is no reason to expect different results. It would seem that placing a meals tax on referendum would be a waste of tax payer dollars and a waste of Fairfax County resources.

Restaurants currently strongly support the Fairfax County school system, the Fairfax County PTOs, the Fairfax County Fire and Rescue community and many Fairfax County charitable organizations. Restaurants have donated over $1.25 million to Fairfax County non-profit organizations and schools through charitable donations, contributions to fundraisers and scholarship funds. (Source: Data collected from local restaurant owners)

ATTACHMENT D
Prepared by the Restaurant Association of Metropolitan Washington, Virginia Restaurant, Lodging, and Travel Association, National Restaurant Association and the NOVA Chamber of Commerce

The foodservice industry considers the Fairfax County Government a partner in their community and is proud to support these causes whenever possible. We hope the county does not decide to mount a campaign to impose a meals tax, as it will be considered an attack on the livelihood of the foodservice industry and it could cause irreparable damage in the partnership and community relationship that currently exists.