



City of Arkansas City, Kansas

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Memorandum

FROM: Nick Hernandez, City Manager
TO: Mayor and City Commissioners
DATE: August 11, 2016
SUBJECT: SCKMC Sales Tax

On the morning of August 10, the State of Kansas notified the City of Arkansas City that the upcoming 1% hospital sales tax was in conflict with existing state statute and could not be implemented, as cities are capped at a maximum of 1% sales tax for special purposes. We were informed the 1/2% sales tax approved in 2009 for 10 years would be included in the calculation.

After receiving word of this technicality, I immediately pulled up the ordinance adopted by the City Commission to determine how this oversight occurred, and contacted both professional and legal staff of the City and South Central Kansas Medical Center.

The statute reads the City may approve up to 2% of general sales tax and up to 1% of special-purpose tax, for a total of 3%. There are a significant number of legislative exceptions to the cap; however, the wording of the question submitted to voters states the tax to be approved was a 1% special-purpose retailers tax to be utilized for debt service obligations. The formation and adoption of the language by the commission and hospital board, and subsequent approval of the measure by the voters, was consistently clear throughout the process that the tax was not a general sales tax in nature.

So how did this happen without the technicality being recognized sooner? The language utilized had been prepared by support staff, and reviewed by legal and administrative staff from both the City and the hospital.

Discussions initially began by the hospital requesting a 1/2% special-purpose tax (to pay debt service only) for five years, and it was later changed through joint study sessions of the hospital board and City Commission. A compromise was reached to make the proposed tax a 1% special-purpose tax for 10 years — combined with the previous 1/2% sales tax, that would total 1 1/2%. How this was not caught during that process as being in conflict with the state statute on special sales taxes, I cannot definitively say.

As the chief administrative officer for the City of Arkansas City, I am ultimately responsible for all work product and actions that occur by and within the City, and I cannot blame the oversight or find fault on any one individual or entity. A significant number of individuals overlooked it, and I apologize for not catching it.

The only option I see for the City Commission is to retire the existing half-cent sales tax immediately, with an effective date of September 30 of this year, thus ending the previous tax 2 1/2 years early. This will leave a greater than anticipated shortfall in bond and interest payments that will need to be covered by the hospital, which will hinder the hospital's ability to repay the City immediately for its special assessments and funds loaned to date.

This also will force the hospital to speed up its implementation timelines for changes currently being developed by Quorum Health Resources so they may meet its debt obligation to the City and the taxpayers.

City staff conservatively budgeted in the City's 2017 proposed budget anticipating that no payment would be received from the hospital for either special assessments or loan repayment, given the recent repayment history of the hospital.

I want you and the public to know that we will do our best to cover the remaining shortfall — it will **NOT** affect current City service levels and it will **NOT** affect 2017's budget as presented currently. If the hospital is unable to cover the expected shortfall in 2017, the City will make every effort to assist, as we have done the previous two years. ***This is only possible through the careful and efficient planning by financial and administrative staff, and by the commitment of all of our City employees to our community.***

The public will benefit as they will only see a half-cent increase in sales tax, making our effective tax rate 8.75%, a sales tax rate below that of Wellington and McPherson, only slightly higher than Ponca City (8.667%), and the same as in communities such as Augusta and Douglass.

Since my arrival more than five years ago, we have made tremendous strides to get the City of Arkansas City back to the commission priorities set forth year after year. These were to enhance public safety, invest in utilities and improve our basic infrastructure.

Working as a great team, we have been able to replace more water lines, reduce more wasteful spending, further enhance revenues and cash reserves, and better improve the overall quality of equipment and performance of our public safety professionals in the last five years than had been accomplished in the previous couple of administrations — all while helping other entities that have struggled greatly and maintaining a flat property tax mill levy.

I am confident in the ability of my staff to continue moving the City forward, regardless of this setback.

Again, I am sorry, but I can assure you that staff will continue to make the best decisions for this City.

Respectfully Submitted-

A handwritten signature in blue ink that reads "Nickolaus J. Hernandez". The signature is written in a cursive style with a large, stylized initial "N".

Nickolaus J. Hernandez