

MEMORANDUM

To: Aaron Frank, Assistant Town Manager and CFO
From: Stephen Falbel
Re: Potential Impact on Colchester Residents of Local Option Tax
Date: November 24, 2014

In a separate memorandum, we estimated the potential net revenue of a 1% Local Option Tax (LOT) to the Town of Colchester of about \$1.3 million in 2016. A key question for the Town is how much of the burden of this tax will fall on Colchester residents, since one purpose of instituting the tax would be to reduce the amount of property tax burden on town residents.

There are two ways to approach this estimate: 1) consider how much Colchester residents spend and then estimate how much they spend within their own town, or 2) consider how much Colchester businesses sell and estimate how much of these sales go to Colchester residents. The best available source for the first approach is the annual Consumer Expenditure Survey conducted by the US Census. The best available source for the second approach is the revenue estimates from the Dun & Bradstreet listing of Colchester businesses.

The Census Consumer Expenditure Survey shows how much the average household spends on various items. In order to choose the most relevant results, statistics for the Northeast Region were used. Among the many line items in the survey, expenditures for goods that would be taxable under the LOT were extracted. The table below shows these goods and the average annual expenditure per household in the Northeast Region.

Expenditure Item	Annual Spending
Alcoholic beverages	\$527
Food away from home	\$2,811
Other Taxable Sales	
Housekeeping supplies	\$648
Household furnishings and equipment	\$1,665
Audio and visual equipment and services	\$1,011
Toys, hobbies, and playground equipment	\$145
Other entertainment supplies, equipment, and services	\$310
Personal care products and services	\$626
Reading	\$117
TOTAL SPENDING on Taxable Items	\$4,522

After extracting these figures, the expenditure figures were normalized to reflect the difference between the mean income in Colchester and the mean income among the households in the

Consumer Expenditure Survey. That is to say, because Colchester households have an average income (according to the Census) of \$80,810, while the households in the survey have an average income of \$71,606, it is likely that Colchester households spend somewhat more than the average Northeast Region households. Thus, the relevant expenditure figures in the table above were increased by 12.9% to reflect the difference in mean incomes. The final step was to multiple the average household expenditure by the number of households in Colchester, which was 6,314 in the 2010 Census. The resulting estimates of expenditures by type are as follows:

Expenditure Item	Annual Spending for all Colchester Households
Alcoholic beverages	\$3,755,181
Food away from home	\$20,030,008
Other Taxable Sales	\$32,221,876

Note that there is no estimate of expenditures on rooms (hotels) in the expenditure survey. It is also very unlikely that Colchester residents spend any significant amount of money on hotel rooms in Colchester.

Total sales in Colchester, as described in the companion memorandum are as follows:

Expenditure Item	Annual Sales
Alcohol	\$2,917,086
Meals	\$22,308,465
General Taxable Sales	\$128,047,327

Sales of alcoholic beverages cover “served” beverages—that is, in restaurants and bars—while expenditures on alcohol would also cover purchases made in liquor stores or markets. Thus, even though the amount spent by Colchester residents and the amount sold in Colchester are reasonably close, there is no compelling reason to think that the majority of sales of served alcoholic beverages in Colchester are to Colchester residents. More likely, these sales are correlated with meals served.

Certainly, there is some overlap in meals served at Colchester restaurants and food away from home purchased by Colchester residents. Unfortunately, there is no data source to indicate how much overlap there is. It is likely that Colchester residents go out to dinner in Colchester some of the time, but they also likely go out to dinner in Burlington, Winooski, Williston and other places as well. Because the revenue from meals served and the household expenditures on meals away from home are similar for Colchester businesses and households, respectively, the percentage of meals served to Colchester residents (from the perspective of the restaurant) and the percentage of Colchester meals served consumed by Colchester residents (from the perspective of the households) would also be similar. A reasonable estimate of these percentages is that between one in four and one in three diners in Colchester restaurants are Colchester residents. As a midpoint, it is assumed that 30% of Colchester expenditures happen in Colchester restaurants, and that represents about 30% of meal sales in those restaurants. This also implies that about 30% of the tax on served alcoholic beverages would be for Colchester residents.

The final, and largest, category is general sales. Colchester has a wide range of retailers, from small markets that serve mostly local customers to a major regional entity (Costco) that draws buyers from

all over Chittenden County and beyond. For the large retailers, Colchester customers may account for 10% of sales or less, while for the small retailers, residents may account for 60% or more of sales.

As shown above, according to the Consumer Expenditure Survey, Colchester households spend about \$32.2 million annually on taxable items, while Colchester businesses sell about \$128 million in taxable items. If all of the Colchester purchases occurred at Colchester businesses, that would represent 25% of the sales. Given the proximity of other retail options in Burlington, South Burlington and Williston, it is certain that less than 100% of purchases by Colchester residents occur at Colchester stores. Indeed, because a large portion of Colchester sales—very likely over 50%—occur at the large retailers which are a regional draw, and where Colchester residents likely make up no more than 10% of the customers, a portion of Colchester residents' purchases would have to take place in other towns.

Using the annual revenue figures in the Dun & Bradstreet data as a reference point, an estimate was made for each retailer in Colchester as to what percentage of sales would go to Colchester residents. These estimates range from 10% or below for the largest retailers up to 60% for local markets and pharmacies. The average of the assumed shares was 18%, but the weighted average, taking into account the annual revenue and thus weighting the large retailers more heavily, was 11.6%.

If 11.6% of sales by Colchester retailers are made to Colchester residents, that means that Colchester households spend about \$14.8 million at Colchester businesses (11.6% times \$128 million in taxable sales). This, in turn, means that of the \$32.2 million in taxable purchases by Colchester households, about 46% of them take place at Colchester businesses. This would seem to be a reasonable estimate of the share of household purchases that take place within the Town of Colchester.

To summarize the findings of this analysis, it appears that the impact on Colchester residents of the proposed LOT would be as follows:

- Meals tax: about \$60,000 (27% of the estimated revenue)
- Alcohol tax: about \$8,000 (27% of the estimated revenue)
- Rooms tax: about \$1,500 (1% of the estimated revenue)
- Sales tax: about \$150,000 (11.6% of the estimated revenue)

These figures incorporate many assumptions and thus should be considered as one point in a potential range. As mentioned above, the meals and alcohol tax could range from 25% to 33% of revenue, but it is unlikely to be higher than 40% of the revenue. The sales tax could range from 10% to 15% of the revenue, but it is very unlikely to be higher than 20% of the revenue.

Considering the Meals, Alcohol, Rooms and Sales components of the LOT together, the impact on Colchester residents would be:

- **\$219,500 (13%) of the estimated revenue.**