Revenue Options

To pay for additional operational expenses for Automatic Aid

A municipality has essentially two local revenue streams it can assess to pay for annual operational expenses: a local municipal sales tax and/or a property tax. There are advantages and disadvantages of each revenue stream as illustrated in the below tables:

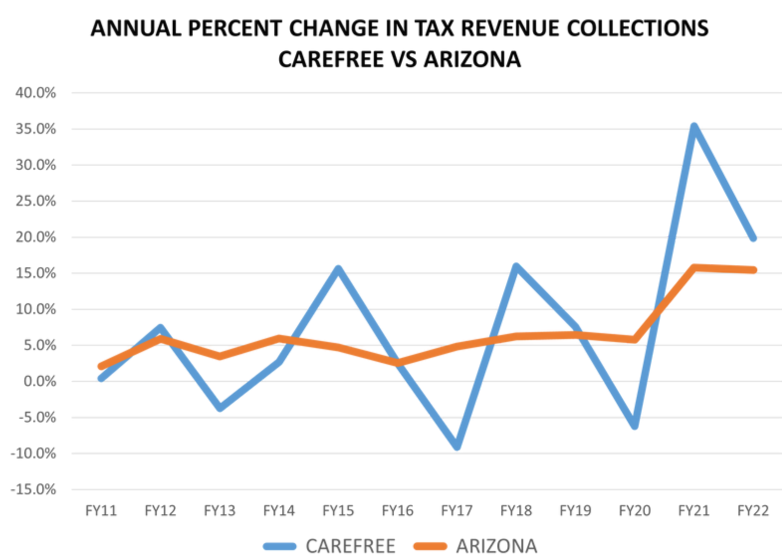
SALES TAXES

ADVANTAGES	DISADVANTAGES
• Simple & straight forward • Existing 1% sales tax dedicated to the Fire Fund (3% total rate) • Grows over time with economic activity	• Not aligned with benefits received • Not recession proof • Limited number of sales tax generators in Carefree • Increasing sales taxes drive shoppers to lower-rate jurisdictions

PROPERTY TAXES

ADVANTAGES	DISADVANTAGES
• Costs correlate with size/value of structures being protected • Stable revenue source • Part-time residents pay their share • Legislative limits safeguard 'Runaway' property tax (annual levy growth limit of 2%, the so-called 'Truth in Taxation' process, a valuation growth limit of 5%)	• Unpopular tax • Politically challenging to establish new tax • Requires approval from Town Council AND vote from the People • Tax levy limits may not 'keep up' with escalator clauses in new master contract

Sales Taxes:
Sales taxes are considered a volatile revenue stream as it tracks with economic cycles. The table below illustrates the fluctuations of sales tax revenue in Carefree (illustrated in blue) and for comparison purposes, at the broader state level (illustrated in orange). Due to Carefree's limited tax base, the sales tax revenue can make dramatic swings which makes it difficult to pay for the persistent costs to provide municipal services. When compared to other nearby communities, Carefree has one of the highest sales tax rates. As a result, this establishes a ceiling as further increases in this rate would result in business migrating out of Carefree to nearby lower taxed communities and a potential reduction in sales tax revenue.



The volatility of Carefree's tax revenues indicates sensitivity to changes in the economy and makes forecasting difficult.

SALES TAX RATES BY CITY/TOWN

CAREFREE - 3.0%

CAVE CREEK - 3.0%

FOUNTAIN HILLS - 2.9%

PHOENIX - 2.3%

SCOTTSDALE - 1.75%

Revenue Options (continued)

An example of trying to match sales tax revenue with the annual costs of providing fire and emergency services is the existing Fire Fund used to pay for the master contract with Rural Metro. The Table below illustrates the total costs of the master contract which began 6 months into the 2007 fiscal year. Originally, a 1% sales tax was implemented in fiscal year 2005.The adoption and collection of this revenue two years prior to the initial funding of the master contract permitted a surplus to build up in the Fire Fund. However, after the 2008/2009 economic contraction, an imbalance or what is termed a structural deficit began in FY 2010. Over the next 11 fiscal years, this structure deficit averaged over $400,000 annually. However, in the most recent two fiscal years, due to economic growth, enough revenue was generated by the 1% sales tax to pay for the fire coverage. It is important to note with the recent short-term contract renewal with Rural Metro at approximately $1.86MM, a structural deficit may once again occur as economic activity contracts and reduces sales tax revenue. With a shift to Automatic Aid, it is anticipated that the most cost-effective approach would be to contract with Daisy Mountain Fire Department. This could increase the annual costs of providing fire and emergency services by approximately $1 million annually. Combine this new annual financial commitment with the past average annual structural deficit as well as inflationary increases to any future contract and the structural deficit could exceed $1.4 million annually.

FISCAL YEAR	TOTAL CONTRACT	FIRE FUND	GENERAL FUND
FY07	574,150	574,150	0
FY08	1,216,071	1,216,071	-
FY09	1,264,714	1,264,714	-
FY10	1,285,793	837,947	447,846
FY11	1,315,303	767,260	548,043
FY12	1,367,914	911,943	455,971
FY13	1,246,295	946,434	299,861
FY14	1,277,459	834,884	442,575
FY15	1,306,835	892,322	414,513
FY16	1,339,509	893,006	446,503
FY17	1,372,997	967,919	405,078
FY18	1,412,122	1,063,539	348,583
FY19	1,442,505	1,053,850	388,655
FY20	1,478,568	1,198,900	279,668
FY21	1,515,532	1,515,532	-
FY22	1,553,420	1,553,420	
FY23	1,860,000	TBD	TBD

THE FIRE FUND HAS GENERALLY **NOT BEEN SUFFICIENT TO FUND** RURAL METRO FD MASTER CONTRACT.

Revenue Options (continued)

The Town hired fiscal analyst Rounds and Associates to study the Town's sales tax centric financial model to further determine if it had sufficient capacity to fund the additional annual financial commitment based upon its current sales tax centric funding. Rounds and Associates specializes in studying the fiscal impacts of public policy and provides consulting services to local, county and state governments. The model assumes there is no change to the Town's current tax revenue structure and a portion of the recent sales tax revenue gains are transitory. The following assumptions were also folded into the model.

Midpoint Forecast - Select Considerations

- Town specific tax revenue history and trends were reviewed. Inflation will be an issue for 2+ more years.
- The Federal Reserve Board will continue to increase interest rates and remove money from the economy at a sufficient pace to cause a recession. The forecasted national recession in 2023 was adjusted for the Town.
- The "Midpoint" forecast assumes the economic recession will be a "hard landing." However, the worst-cast scenario will not be fully realized.
- Greater Phoenix will exit the downturn with enough strength to allow for reasonable rates of growth for the rest of the decade and beyond.
- The federal government will continue to spend at relatively high rates for the next 2 years and then moderate the spending moving forward.

Based upon these economic assumptions, Rounds and Associates modeled the capacity for the Town to pay for the additional reoccurring expenses associated with the costs of joining Automatic Aid. The following three scenarios were run. The first two scenarios assume that the Town uses its saving funds allocated for maintaining its aging assets such as its streets and drainage structures and positions these funds to cover the future costs associated with Automatic Aid. Both scenarios illustrate that the Town will be in a negative financial position and unable to keep up with maintaining its aging infrastructure. This provides an unsustainable and financially insolvent position for the Town. On the other hand, if nothing changes and the Town maintains its relationship with Rural Metro and is not part of the Automatic Aid regional dispatch system, the Town can financially maintain a more solvent position by funding Fire and Emergency Services at the current level without qualifying for Automatic Aid but still fund future investments in its aging streets and drainage structures. As stated earlier in the report, staying with Rural Metro will create a higher level of risk for the community as regional assistance associated with simultaneous, long duration, widespread and/or unique emergency events may not be available.

Midpoint Forecast Summaries:

Scenario 1: Assumes Capital Improvements Will Be Required Beyond the Current Plan

Ending Fund Balance w/Reserves (Deficit)	$14.76	$10.61	$8.34	$9.04	$7.45	$2.67	$1.10	($0.65)	($2.81)	($5.19)	($7.73)

Scenario 2: Extended Capital Improvements Requirements + Losing One Major Retail Store

Ending Fund Balance w/Reserves (Deficit)	$14.76	$10.51	$8.04	$8.54	$6.75	$1.77	($0.00)	($1.95)	($4.31)	($6.89)	($9.63)

Scenario 3: Using Rural Metro Instead of Town Fire Dept.

Ending Fund Balance w/Reserves (Deficit)	$14.76	$11.70	$9.78	$11.52	$11.07	$7.53	$7.30	$7.01	$6.43	$5.76	$5.05

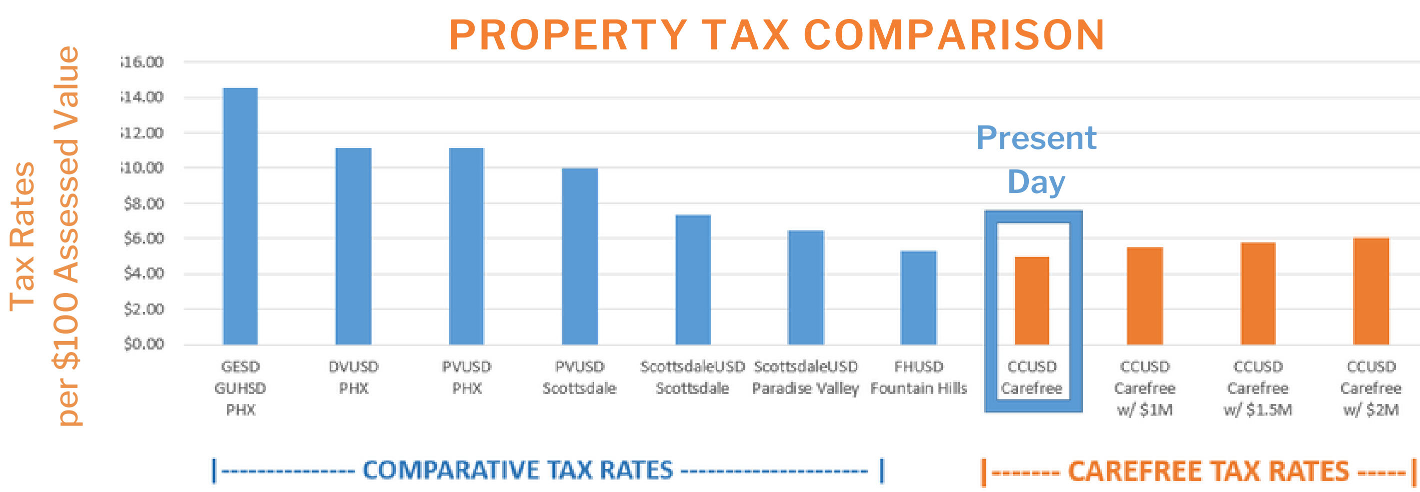
Scenarios 1-2:
Reduced capacity to annually save funds to replenish Capital Reserve Funds.
When next cycle of street projects are added in, there are insufficient funds to maintain assets.

Scenario 3:
Does not permit Automatic Aid but maintains ability to fund street projects.

PRIMARY PROPERTY TAX

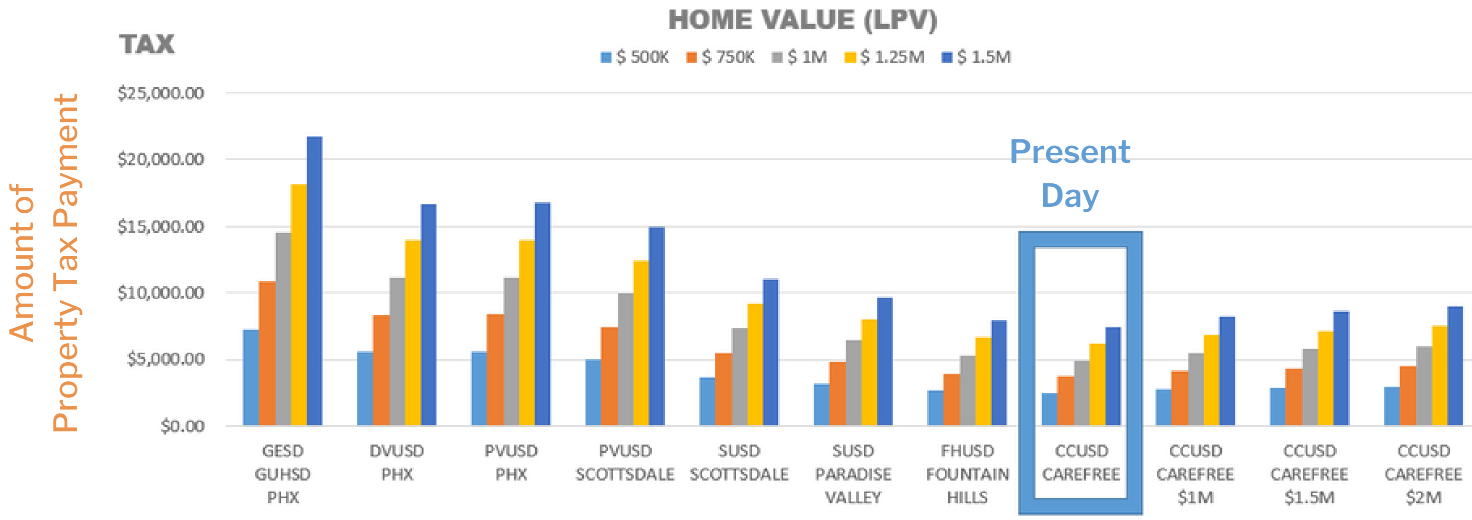
The analysis by Rounds and Associates identifies that Carefree will not have sufficient funds to pay for the option that includes Automatic Aid within the forecast period and beyond. Furthermore, there are only two realistic options to cover the costs for Automatic Aid: a sales tax increase or the implementation of a property tax. Within Carefree the sales tax has historically been very volatile from one year to the next which makes fiscal planning more difficult. A property tax will prove to be a more stable source of revenue. If Automatic Aid is demanded by the Town, in the specific case of Carefree, the implementation of a property tax would be recommended if fiscal sustainability is also a concern.

When comparing the current property taxes paid in Carefree (collected by entities not associated with the Town), it clearly illustrates that Carefree residents have the lowest tax rates in the region and perhaps the state. Even if a modest property tax is considered to offset the financial commitment the Town needs to meet to qualify for Automatic Aid, the citizens would continue to enjoy one of the smallest property taxes in the region. The following chart illustrates what different ranges in the tax assessment would yield and how it compares to neighboring communities.



In Arizona, property taxes are levied on limited property value (LPV) not the value someone pays for your property, market value. LPV is a reduction in the market value of your residence which limits growth of the value of your property for purposes of taxation. For reference, the average residential LPV in Carefree is approximately $630,000 but the average market value is significantly above this number. Annually, the Maricopa County Assessor's Office distributes a statement which defines the LPV on one's property. Based upon this LPV, in the next chart, one can compare the tax payment in nearby jurisdictions to the current Carefree tax payment and the impacts if a tax levy between between $1 million and $2 million is assessed.

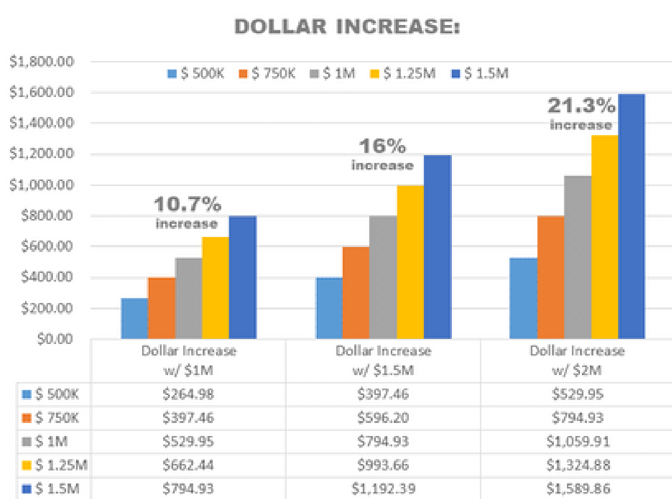
PROPERTY TAX COMPARISON

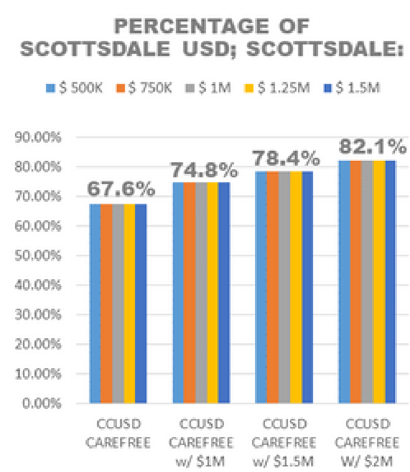


More specifically, from a dollar perspective, the following charts compare the respective increases. Using the average LPV in Carefree of $630,000:

- a $1.5 million tax levy would translate to $41.73 per month or $501 annually,
- a $1.75 million tax levy would translate to $48.69 or $584 annually,
- a $2 million tax levy would translate to $55.64 per month or $668 annually.

PROPERTY TAX COMPARISON





Primary Property Tax (continued)

What would the tax levy be?
It is anticipated that a primary tax levy should be $2.0 million. However, this levy does not cover the entire costs of funding the contract with an Automatic Aid partner. The Town will balance the annual costs of its new fire contract with the Town's annual sales tax collection. This levy will offset the past structural deficit of the fire fund which has averaged over $400,000 annually, pay for the cost differential in joining Automatic Aid, cover annual cost increases over the first 10 years of the contract and provide funds to retire aging fire equipment.

As stated above, a primary tax level of $2.0 million would translate for the average home in Carefree with a LPV at $630,000, to $55.67 per month or $668 per year. From a comparative perspective, prior to the Town assuming the master contract with Rural Metro, residents were paying an average of $750 annually to Rural Metro for an individual subscription. Today, that annual subscription would exceed $1,000 annually. In other words, under the scenario that a $2.0 million levy is approved by the residents of Carefree, they would be paying less than they were originally paying for individual subscriptions and be provided a higher level of Fire and Emergency Services. This levy of $2.0 million will permit the Town to make the 25-year commitment to Automatic Aid through Daisy Mountain Fire Department while closing the structural deficit on the current Fire Fund and permit the Town to continue to maintain its aging infrastructure and reinvest in capital assets as their useful life are exhausted.