TO: CITY COUNCIL
FROM: CITY ADMINISTRATOR
DATE: JULY 24, 2018
SUBJECT: RESOLUTION PROPOSING AND SUBMITTING TO THE VOTERS AT THE GENERAL MUNICIPAL ELECTIONS TO BE HELD ON NOVEMBER 6, 2018, A PROPOSAL TO ADOPT AN INITIATIVE ORDINANCE ESTABLISHING A LOCAL ONE CENT TRANSACTIONS (SALES) AND USE TAX, DIRECTING THE CITY ATTORNEY TO PREPARE AN IMPARTIAL ANALYSIS, AND AUTHORIZING AND SETTING DEADLINES FOR THE FILING OF ARGUMENTS FOR OR AGAINST THE BALLOT MEASURE

FISCAL IMPACT: IF ENACTED BY VOTERS, GENERATES APPROXIMATELY $5,000,000 IN LOCALLY CONTROLLED REVENUE NOT SUBJECT TO SEIZURE BY THE STATE

SUMMARY:

The State of California has taken over $32.8 million in local tax dollars from Placentia since Fiscal Year 1992-93 and the City continues to lose an estimated $2.1 million dollars every year. Since 2012 the City has been forced to adopt General Fund budgets with structural deficits. For Fiscal Year (FY) 2017-18, the structural operating deficit grew to $6.1 million. Based upon the Citizens Fiscal Sustainability Task Force, the newly developed 10-year long term financial plan indicates that the City will continue to incur growing structural deficits each year ranging from $7.9 million to $11.3 million by FY 2028-29. In addition, in order to adopt a balanced budget for FY 2018-19, the City cut $2.7M or about 15% of its operating budget, with the largest reduction coming from the City’s Police Department. In total, this resulted in the elimination of 11 full-time equivalent positions, including one permanent police officer position, closing or reducing operating hours of community centers, and eliminating certain community-wide special events.

The City must identify and secure a reliable, long-term funding stream that is locally controlled where revenue is not subject to seizure or elimination by the State. Many other cities in California have used local funding mechanisms to achieve this goal, which ensures that taxpayer dollars stay local to address community priorities. The intent of tonight’s action is to allow the City of Placentia’s residents to decide if they wish to do so, approve a locally enacted revenue measure to ensure that the City is able to maintain vital services our community has identified, such as:

- Repairing and maintaining potholes, streets and sidewalks
- Providing quick 911 medical emergency response
- Providing fire protection and emergency medical services
- Maintaining our local Placentia Police Department

3.a.
July 24, 2018
• Reduce gang activity and drug related crimes
• Keeping public areas clean and free of graffiti

A local, one percent (1 cent) Transactions and Use ("Sales" Tax) would allow the City to fund services at levels consistent with the community’s priorities and the public’s desired quality of life, and would prevent the need for further significant cuts to vital City services and programs. This action approves a resolution proposing and submitting to the voters at the General Municipal Election to be held on November 6, 2018, a proposal to adopt an initiative ordinance establishing a one cent (TUT/sales tax), directing the City Attorney to prepare an impartial analysis, and authorizing and setting deadlines for the filing of arguments for or against the ballot measure.

RECOMMENDATION:

It is recommended that the City Council take the following actions:

1. Approve Resolution No. R-2018-XX, a Resolution of the City Council of the City of Placentia, California Proposing and Submitting to the Voters at the General Municipal Election to be Held on November 6, 2018, a Proposal to Adopt an Ordinance Establishing a Local, One Cent Transactions and Use ("Sales") Tax; Directing the City Attorney to Prepare an Impartial Analysis; and Authorizing and Setting Deadlines for the Filing of Arguments For or Against the Ballot Measure; and

2. Waive full reading, by title only, and introduce for first reading Ordinance No. O-2018-XX, An Ordinance of The City of Placentia, California Enacting a Local Transactions and Use Tax ("Sales Tax") to be Administered by The California Department of Tax and Fee Administration, Subject to Adoption By the Electorate; and

3. Authorize the City Administrator and/or his designee to execute all necessary documents, in a form approved by the City Attorney.

DISCUSSION:

The State of California has taken over $32.8 million in local tax dollars from Placentia since 1992. The City will continue to lose in excess of $2.1 million dollars every year in General Fund property tax revenues due to the State’s required shift of Education Revenue Augmentation Fund (ERAF).

In addition, despite the economy continuing to grow during the last two years, the City’s sales tax revenue has declined during the same period. The reduction in sales tax revenue can attributed to the trend of online retail shopping. Traditional retail ("Brick and Mortar") stores generate 1 cent of local sales tax revenue to the City for every dollar of sales volume. Internet sales, however, generate approximately 1/10th of 1 cent of local sales tax revenue to the City for every dollar of sales volume. With the trend toward online purchases increasing significantly in the last few years, the City has been experiencing a decline in sales tax revenue, despite the economy growing.
Like many other California cities, all of the above-mentioned revenue losses are due to factors outside the City’s control.

In response to decreasing revenues, the City has done much over the past several budget cycles to address its financial situation. Through various economic development strategies, revenue opportunities were created, including installing two digital billboards on City-owned property along the 57-freeway corridor. The two billboards generate a minimum of $500,000 annually in general fund revenue to the City ("Base Compensation"). Additional revenue may be provided to the City if the Base Compensation is less than twenty-five percent (25%) of the advertising company’s total annual net revenue. The City also entered into an Exclusive License Agreement with Galaxy Oil Company (Galaxy) for a period of ten (10) years for the purpose of constructing, installing, operating, and maintaining a retail self-service 76 Gasoline Station (Station) at a City-owned property located at 480 S. Placentia Avenue. The recently opened Station is estimated to generate $25,000 in base rent and between $200,000 and $350,000 annually in general fund revenue to the City.

In addition, primarily through sponsorships and limited grants from various nonprofits such as the Placentia Community Foundation, many of the City’s recreation and community services special programs and events have continued. Sponsorships and grants are key to raising funds to allow the City to have quality community events including the annual Concerts & Movies in the Park; Christmas Tree Lighting Ceremony; and the Heritage Parade and Festival. Furthermore, as a result of Volunteers in Policing (VIPS) and Radio Amateur Civil Emergency Service (RACES), thousands of volunteer service hours are given to the City to support vital public safety department operations and services.

The City Council has also sought to find ways to raise revenue in those areas under its control, such as the imposition of cost recovery fees for services and other items, ensuring that the City is capturing revenue when appropriate.

Fiscal Year 2018-19 Budget

It is important to note; the FY 2018-19 Budget does not maintain all of the prior service levels the City has provided in the past. Although no new services have been added, there are existing services or programs that have not been funded due to limited revenues. The City made a total of $2.7 million dollars in general fund revenue and expenditure reductions which includes the following:

- A reduction of 8 full-time vacant positions
- A reduction of 6,444 part-time hours
- All non-mandated training and conferences eliminated in all departments
- All department budgets reduced 15% except contracts or mandated costs
- All future vacant positions will be reviewed on a case-by-case basis before hiring a replacement
- Cuts to programs and expenditures including National Night Out and Concerts in the Park
Deferred critical maintenance to public infrastructure, including critically needed street paving
Non-replacement of City vehicles and equipment

These cuts, which add up to $2.7 million in ongoing costs are not nearly enough for the City to achieve and sustain long term fiscal health. As noted, the City has been addressing these forecasts with cuts throughout the organization; however, without a change in revenues, future budgets may not be balanced without drastic reductions to services. The City's financial situation is not in response to an action, but in spite of significant actions already taken. Unfortunately, these measures have not been enough to close the City's structural budget deficit. While the City has made great strides in economic development, obtaining grant funding and using restricted funding, the current General Fund budget does not address the following deferred infrastructure maintenance:

- Streets & Roads: Additional $3.7 million per year (Harris & Associates)
- Facilities & Parks: $700,000 to $900,000 per year (Jorgenson Report on Facilities)
- Vehicles & Equipment: $300,000 per year (City of Anaheim Evaluation Report)
- Unfunded Capital Improvement Projects: $1.3 million to $1.6 million per year (Approved CIP Cost Estimates)

Lastly, despite efforts to cut costs to balance the annual budget, there has been additional review and determination by the following entities that the City needs additional revenue to maintain the quality of services and build adequate reserves. These independent entities include:

- Citizens Fiscal Sustainability Task Force
- City's Auditors
- State Auditor’s Office
- Bond Rating Agencies

Citizen Fiscal Sustainability Task Force

In response to these ongoing challenges, on March 3, 2015 the City Council created a Citizens Fiscal Sustainability Task Force ("Task Force") and appointed seven members. The main goal of the Task Force was to develop a methodology to assess the City's fiscal sustainability status, identify areas of concern, solicit and evaluate expenditure reduction and revenue enhancement options from the community, Council and Staff and report their findings to the City Council. The Task Force conducted over 30 public meetings over a 2½ year period. Each public meeting lasted between two and three hours. They received reports on the City's financial situation, including the revenues the City receives and the various cuts and adjustments the City Council has made over the recent past; departmental presentations on department budgets, staffing, responsibilities, and previous steps taken to reduce costs; information on citywide costs and infrastructure projects; and a presentation on what local revenue options are available to the City.
On September 19, 2017, the Task Force presented a final comprehensive report to the City Council. The final Task Force report identified several areas of sustainability concern. One major work product contained within the final report is a 10-year financial forecast. This document was prepared with Task Force members using twenty (20) years of historical trend data, coupled with known factors as well as recent trends in revenue. This 10-year forecast verified the extent of the City's fiscal sustainability and determined that in FY 2019-20, the City is forecast to have a deferred infrastructure maintenance deficit of $6.1 million, increasing to $6.5 million by FY 2024-25, and total structural deficits ranging from $7.9 million to $11.2 million over that same timeframe. In summary, the final Task Force report included the following recommendations:

- Implementing cost-cutting and emergency reserve measures (the majority of which have now been implemented)
- Identifying options for revenue generation (several have been implemented)
- Continue to engage citizens on our fiscal sustainability efforts

Specifically, the City Council requested that the Task Force along with Staff host three (3) community meetings in October and November to engage the City’s residents on the City’s fiscal challenges, discuss community priorities and revenue solutions. In those meetings an informal survey was conducted to determine interest in examining a variety of potential locally controlled revenue solutions designed to make the City more fiscally sustainable. In addition to the community meetings, the City posted an online version of the community meeting presentation and solicited additional input.

Community Conversations and Feedback

In April 2018, the City retained the services of The Lew Edwards Group (LEG) to assist the City in its communications and outreach efforts regarding resident service priorities. That agreement included conducting a survey to ascertain public perceptions of the City, priorities for City services, and constituent views towards a potential locally enacted and controlled revenue measure.

Over the past few months, City Staff provided numerous presentations to resident and service organizations about the City’s fiscal condition and to obtain input on service priorities. Copies of the survey have been placed on the City’s website and various social media platforms. The City has received hundreds of responses to the community surveys which are designed to obtain feedback on what City services are important to our residents. In addition, community updates have been circulated to the residents, service groups and businesses through various informational mailers.

Based on feedback received from hundreds of community members, the top priorities for Placentia include in priority order:

- Paving potholes and streets
- Ensuring quick responses to 911 emergencies
- Keeping public areas clean and graffiti-free
• Providing fire protection and emergency medical services
• Repairing broken sidewalks, curbs and gutters
• Addressing gangs, drugs and crime prevention

In addition, the City in conjunction with LEG, commissioned Dr. Timothy McLarney from True North Research to conduct a scientifically valid quality of life survey of likely registered voters. The survey was conducted in May and a wide range of information was assessed to ensure a comprehensive, balanced and unbiased study.

While there are a number of local revenue measure options available to the City, and all of those options were presented to the Task Force and to the City Council at the September 19, 2017 City Council Meeting, based upon feedback received from the aforementioned community meetings and online survey, the True North survey tested ballot language for a one-cent local sales tax. The results indicate that Placentia voters are willing to support a sales tax (at 61%-65% for a simple majority requirement measure) in order to provide adequate funding for, among other things, core City services.

As illustrated in the diagram below, residents were highly supportive of efforts to preserve Placentia’s quality of life through maintaining public infrastructure including roads, sidewalks, and repairing potholes. Placentia residents were also very interested in maintaining the City’s low 911 response times and the local Placentia Police Department, especially the Police Department’s ability to provide crime prevention and investigation services. Finally, residents highly rated Placentia’s quality of life, and strongly supported efforts to protect and maintain existing services.
Local Infrastructure Needs

Over the last few decades the City has used restricted funding and grant revenues to help support the critical maintenance and repair of local streets and roads. Nonetheless, despite efforts to obtain additional grant and restricted funding, Placentia’s streets and roads are significantly deteriorating due to the lack of funds for consistent basic maintenance—and the City’s residents want them addressed. In fact, Placentia streets and roads have been rated the 2nd worst in Orange County by the Orange County Transportation Authority. Major repairs and street paving have been deferred over the past seven years. The City of Placentia is responsible for maintaining over 100 linear miles of streets and roads, and we wish to make these repairs now, before it becomes significantly more expensive in the near future. Placentia’s unfunded street and road repair liability has grown to $28.9 million and is projected to grow to $62.5 million if additional funding is not secured each year to address streets and roads.

Public Safety Needs

Public safety continues to be a priority in Placentia and represents over 52% of the City’s General Fund. However, due primarily to statewide early jail release laws, crime related to residential and commercial burglary and vehicle break-ins has increased in Placentia over the last year. Without a continued local funding source, the City will be forced to cut public safety services, including gang and drug prevention and proactive neighborhood police patrols. The City needs additional funds to continue to provide citywide crime prevention, gang and youth violence prevention and intervention programs.

Legislation on Sales and Use and Transactions and Use Tax

State Tax Laws and the “Sales and Use” and “Transactions and Use” Distinction State law prescribes the limits and authority for the State and its political subdivisions, including cities, to collect and impose sales taxes. While commonly known as the “sales tax,” State law distinguishes between a “sales and use tax” and “transactions and use tax” due to differences in tax base, with a transactions and use tax allowing for taxation on retail sales without being based on the location (or situs) of a sale.

Under State law, a Charter city may impose or increase a local transactions and use tax for general purposes if an ordinance is approved by a majority vote of a city council and a simple majority vote of the city’s qualified electors. As a local, voter-approved measure, these funds are locally controlled and cannot be taken by the state.

Despite the different provisions of State law that apply to “sales and use taxes” and “transactions and use taxes,” they both are commonly referred to as the “sales tax” and, as a practical matter, are administered similarly by State and local governments. As such, local ordinances and ballot measures that technically seek authority to collect a “transactions and use tax” are simply referred to as a “sales tax.”
Revenue from a sales tax may be used for general or specific purposes, but that designation is significant under State law. A “general tax” requires a simple majority vote of the electorate for approval, while a “special tax” requires a two-thirds majority of the electorate. Courts have determined a tax is general when its revenues are available for expenditure for any and all governmental purposes.

In 2004 and 2010, two statewide ballot initiatives (Propositions 1A and 22) were approved by California voters, both of which increased protection against State reallocation of local sales tax revenues to fund the State’s agencies or programs. Article XIII, Section 24(b) of the State Constitution, enacted by Proposition 22, provides, “The Legislature may not reallocate, transfer, borrow, appropriate, restrict the use of, or otherwise use the proceeds of any tax imposed or levied by a local government solely for the local government’s purposes.” A recent appellate court case confirmed the broad language and protection afforded cities by this provision. Therefore, revenues from a city-approved sales tax, used for the city’s purposes, are constitutionally protected from State-mandated revenue shifts away from the city pursuant to a State statute, including a shift that is part of a “budget trailer bill” enacted as part of the annual State Budget Act.

The Tax Fairness, Transparency and Accountability Act of 2018

A very recent attempt at proposed legislation could have severely limited the ability of cities and counties to generate new revenue. The Tax Fairness, Transparency, and Accountability Act of 2018 would have drastically limited local revenue authority. In part, it was designed to eliminate local authority to impose a tax for general purposes by majority vote and instead required all local proposed tax increases subject to a two-thirds vote. This proposal would have also required two-thirds approval of all members of the local legislative body before a tax can be placed on the ballot. For cities and other local agencies, it would have applied retroactively and, if approved, may have voided some local measures approved by local voters on or after January 1, 2018. While this Initiative has been withdrawn from this November’s ballot, pundits believe similar measures could arise in the future, making it critical that the City act decisively to secure local funding now, before a similar situation arises in the future that could affect our ability to do so.

Summary of Placentia’s Proposed Transactions and Use Tax

The City’s financial situation requires significant action. Placement of this measure on the November 6, 2018 ballot will allow Placentia voters to decide the future of the City. It is important to note that the Mayor, nor the City Council can legally decide on this matter. Only the voters of Placentia have the power to make this decision. The City Council only has the authority to place the measure before the voters, thereby determining whether voters can vote on the measure or not. Again, the City Council cannot and does not have the ability to vote to approve a tax measure.

The measure that is being proposed for the November 6, 2018 ballot has a number of benefits for the City’s long term fiscal sustainability:
• Costs would be shared by visitors, businesses, and residents of Placentia who purchase certain goods and products. Sales tax is not levied on food purchased such as groceries or prescription medication.
• The measure would ensure that the funds would stay locally in Placentia and cannot be taken away by the State.
• The measure would require independent annual audits and citizen oversight.
• The measure would include tough fiscal accountability and transparency controls to ensure that all funds were being used properly.
• Not be a specific parcel tax on individual homes or property.

As we continue to monitor Placentia’s short and long-term fiscal challenges, it is important to note the following:

• If we do not address the identified fiscal problems, the structural deficit will continue to grow
• Waiting for “things to get better” is not an option since we are at the economic peak now, yet continue to have a reduction in sales tax revenue due to online sales growth
• The City has a significantly low amount of undesignated reserves, which continue to get smaller and put the City at risk in a disaster or other large financial challenge
• The City has already made significant cuts in service levels and further cuts will impact public safety and other vital City services

FISCAL IMPACT:

The proposed one-cent local sales tax would generate $5,000,000 annually, which would address the City’s immediate and long-term fiscal challenges and the public’s priorities. The incremental cost of placing this measure on the November ballot is $8,500.

If the local ballot measure is approved, the operative date will be April 1, 2019, the first day of the first calendar quarter commencing more than 110 days after the adoption of the Ordinance, which is the day the City Council declares the vote. Therefore, the City would receive one quarter of the income in FY 2018-19 in the amount of $1,250,000. Given that the City eliminated $2.7 million from its operating budget this fiscal year alone, these additional funds would help ensure the City’s short-term budget is stabilized while providing the necessary funds to continue operating as a full-service City. If additional funds are not realized, it is highly likely that the City will have to reexamine its financial ability to provide public safety and other essential services.
Reviewed and approved by:

Luis Estevez
Director of Public Works

Reviewed and approved by:

Kim Krause
Director of Finance

Reviewed and approved by:

Darin Lenyi
Chief of Police

Reviewed and approved:

Rosanna Ramirez
Director of Administrative Services

Attachment:
Resolution No. R-2018-XX