REVENUE OPTIONS STUDY

September 2004

CITY OF PISMO BEACH

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CITY OF PISMO BEACH

1. EXECUTIVE SUMMARY

OVERVIEW

Stated simply, the purpose of this study is two-fold:

- Identify and analyze potential new revenues for the City of Pismo Beach.

  The Short Story: There is a broad range of reasonable revenue options available to the City, which together total about $3.1 million annually. However, almost all these new revenue measures would require either majority or two-thirds voter approval. The results of this analysis are further summarized below and presented in detail in Chapter 2.

- Discuss what would be required to successfully implement the new revenue sources under Proposition 218.

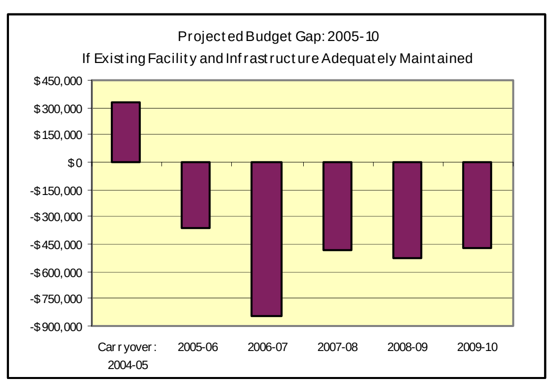
  The Short Story: Based on the experience of many cities in California, it is possible to successfully pass a revenue measure. However, doing so requires effective preparation by the City before placing the measure on the ballot; and an effective community-based group that will campaign for its passage afterwards. These results are also further summarized below and discussed in detail in Chapter 3.

BACKGROUND

This study was prepared in response to the Council's direction as part of the 2002-03 Budget to prepare a comprehensive, long-term Public Facilities Plan. In pro-actively addressing the probable results of this Plan, which is likely to identify needed infrastructure and facility improvements that are beyond the City's ability to fund within current revenues, the Council approved the preparation of this Study to identify and analyze the revenue options reasonably available to the City in helping to finance these improvements. In conjunction with this analysis of revenue options, the Council also approved the preparation of a General Fund forecast to better assess and define the City's fiscal capacity to undertake new initiatives, such as those that will be subsequently identified in the Public Facilities Plan.

On October 1, 2002, the Council contracted with William C. Statler to prepare the Revenue Options Study and the General Fund Fiscal Forecast. This report covers the revenue options portion; the results of the Fiscal Forecast are provided in a separate report.

Results of Five-Year Fiscal Forecast. As noted above, a separate General Fund fiscal forecast has been prepared in conjunction with this analysis of revenue options. It shows that revenues will exceed current operating and debt service costs by about $675,000 annually over the next five years. However, when funding to adequately maintain existing infrastructure and facilities (about $1.25 million on average over the next five years), a *negative* "budget gap" emerges of about $575,000. This underscores the need for new revenues if the City wants to continue current service levels and adequately maintain existing facilities and infrastructure—let alone achieve its



longer-term capital improvement goals or fund other new initiatives.

Revenue Diversity and Stability. Given the City's tourist economic base, the "usual suspect" for new revenues would be an increase in the transient occupancy tax (TOT) rate. However, in order to diversify and stabilize its revenue base, the City may want to consider other options to avoid "putting all of your revenue eggs in one basket." As such, this study takes a broad look at a wide range of reasonable revenue options available to the City that would also generate significant new revenues while diversifying and stabilizing the City's revenue base. Provided in Chapter 4 is a "White Paper" recently prepared for the Institute of Local Self Government (affiliated with the League of California Cities) that more fully explores this topic.

RESULTS OF REVENUE OPTIONS ANALYSIS

The following summarizes the results of this analysis, which are detailed in Chapter 2:

	Revenue Source		Required Approval			Annual Revenues
				Voter		
	Increase in Existing	New	Council	Majority	Two-Thirds	
Local Option Sales Tax: Set City rate at ¼%	x			If general purpose	If special purpose	$475,000
Transient Occupancy Tax: Increase rate from 10% to 12%	x			If general purpose	If special purpose	$940,000
Property Transfer Tax	x			If general purpose	If special purpose	Not allowed for General Law cities
Business License Tax: Increase rate by 20%	x			If general purpose	If special purpose	$24,000
General Obligation Bond		x			x	Varies
Parcel Tax: $100 per year per "Equivalent Dwelling Unit"		x			x	$722,000
Utility Users Tax: 5% on all utilities		x		If general purpose	If special purpose	$423,000
Admissions Tax		x		If general purpose	If special purpose	Not viable
Parking Tax		x		If general purpose	If special purpose	Not viable
Maintenance Assessments		x		x		$168,000
Mello-Roos: Existing Development		x			x	Varies
Mello-Roos: New Development			*			Varies
Higher Cost Recovery	x		x			$200,000
Franchise Fees: 2% on water and sewer utilities Increase refuse rate from 6% to 10%		x	x			 $70,000 $50,000

** With developer concurrence*

As reflected in this summary chart, only three of these revenue options can be implemented by the Council; and for one of these (Mello-Roos special taxes for new development), developer concurrence would also be required. Further, the revenue potential from the two revenues that can be set independently by the Council is relatively small compared with the other options.

This underscores the findings of this Study that any new significant revenues will require voter approval.

Focused Look. As set forth in the workscope approved by the Council, this Study does not take a detailed look at service charges, and does not address development impact fees at all. The City recently evaluated service charges on a comprehensive basis, and is in the process of reviewing development impact fees. As such, this Study focuses on possible non-fee based revenues.

User Fees Are Important. However, the importance of setting user fees at appropriate levels should not be understated. As discussed below, this is one of the few remaining areas where elected officials can still exercise local judgment. And the fact is that if there are areas where user fees should appropriately fund service costs – but they aren't – then this means that general-purpose revenues are being used instead. This reduces the resources available for critical services where significant fee options simply don't exist, and must rely upon general-purpose revenues. This includes services such as police, fire and streets – which are among the most important (and most costly) services that cities deliver.

Simply stated, if a city chooses to subsidize services with general-purpose revenues that could reasonably be funded with fees, the result will be reduced capacity to achieve other high-priority goals that can only be funded through general-purpose revenues. This is a straightforward trade-off with straightforward policy impacts. For example, if planning permit fees do not fully cover development review costs, then street maintenance is likely to suffer as a result. For any number of reasons, this may be an appropriate policy outcome – but it is one that should be made consciously, and not by default.

SUCCESSFUL REVENUE MEASURES

Background: Voter Approval Required for Most New or Increased Revenues

Under Proposition 218, a State Constitutional amendment approved by the voters in November 1996, most new revenue measures will require voter approval at some level:

Taxes. New and increased taxes require voter approval as follows:

- **General purpose.** If the revenues will be used for general purposes, majority voter approval is required. This must occur at the same time as regular Council elections, unless the Council declares an emergency by unanimous vote (in this case, the election may be held at any time).

- **Special purpose.** If the revenues will be "earmarked" for a specific purpose, two-thirds voter approval is required. This election can be held at any time.

Special Assessments. Whether for capital improvements or ongoing maintenance services, special assessments require majority voter approval by those being assessed (who are property owners), with each property owner's vote "weighted" by the amount of their assessment. For example, an owner with a property with an assessment of $1,000 would have ten votes for that parcel compared with one vote for an owner with a parcel assessment of $100. Additionally, Proposition 218 sets specific rules for how the benefit of special assessments must be apportioned. For this reason, many of the "grand-fathered" types of assessments, such as those for landscape maintenance and open space established under the 1972 Lighting and Landscape Maintenance Act, are no longer possible under Proposition 218 (or require much more complicated apportionment formulas, which may have the same affect).

Property-Related Fees. For fees that are levied as "an incidence of property ownership" (just because you own property), majority voter approval by those who will have to pay the fee is required. There are several specific exemptions under Proposition 218, including development review and impact fees under "AB 1600" (Section 65000 of the Government). Additionally, it is the general consensus that most fees charged by cities—such as recreation fees and water service charges—are not subject to Proposition 218, since they are usually based on use, not property ownership.

This means that service charges unrelated to property ownership are the one funding source that is subject to Council decision-making: virtually all others require some form of voter approval.

Preparing for Successful Revenue Measures

As discussed in further detail in Chapter 3, one of the major "mega-trends" affecting governance today at all levels is a fundamental change in the way decisions are made. Over the past thirty years, there has been a significant shift in voter preference from "representative democracy" to "direct democracy," especially in local government finance.

Proposition 13 did not start this trend, but it certainly resulted from it. Since its passage almost twenty-five years ago, there have been an increasing number of citizen-approved limits on the ability of elected officials at the local level to make resource decisions on behalf of the community. While Proposition 218 was the most recent (and sweeping) of these, it was simply the last in a long line of expenditure and revenue limitation ballot measures.

While there a number of possible explanations for this change, the fact remains that there is a decided shift to direct citizen decision-making in a broad range of issues previously thought to be too "technical" for this. While this has occurred in a number of areas such as insurance and campaign financing, it is especially prevalent in "ballot box budgeting." Citizens are no longer willing to give their proxy on financial issues to elected officials, or to their interest group representatives on "blue ribbon" committees. City finance is an issue they want to decide directly for themselves.

How does this shift affect the City's long-term fiscal health? Cities now need broad-based community support—in evidence on Election Day—to implement new revenue sources. In this new model of direct democracy, creating support among elected officials and community leaders—even if it broadly crosses a number of interest groups—is no longer enough. With these profound changes in voter approval requirements, cities must communicate a compelling vision for new revenues at a grass roots level among likely voters.

Even though this may seem a high-hurdle, many cities throughout the State have been successful in gaining voter approval for revenue measures, even at the two-thirds level. There are excellent examples here in San Luis Obispo County: the City of Arroyo Grande, Lucia Mar Unified School District and the City of Paso Robles have all recently approved revenue measures requiring two-thirds voter approval. In fact, the City of Pismo Beach has received two-thirds voter approval in the past for general obligation bonds (and a related increase in property tax rates) its share of seismic improvements to Lopez Reservoir; and for special parcel taxes to help pay for State Water contracts.

In summary, if the need is compelling—either to maintain current services or to improve them—and it is effectively communicated, the experience throughout the State shows that voter-approved revenue measures can be successful.

However, this experience also shows that doing so requires a significant commitment of time and resources by the City in preparing for the measure. More importantly, as discussed in greater detail in Chapter 3, it requires a strong community-based advocacy group that will aggressively raise funds and campaign for the measure once it is on the ballot.

This last issue cannot be stressed enough. Under State law, cities have broad discretion in using their funds for professional assistance in analyzing issues, researching public opinion, conducting public education programs and developing voter support strategies. However, once an issue becomes a formal ballot measure, cities cannot participate as an advocate in any way. For this reason, unless there is a strong community-based group that is willing to aggressively raise funds and campaign for the measure, it is not likely to pass, no matter how much preparation was undertaken by the City before placing the measure on the ballot.

The first pre-condition—effective preparation—is within the control of the City; the second one—an effective community-based group—is not.

In summary, new revenues require community support—in evidence on Election Day. Gaining this support requires more than a compelling need: it also requires communicating this need in a compelling way. And this requires effective preparation by the City before placing the measure on the ballot; and an effective community-based group that will campaign for its passage afterwards.

2. REVENUE OPTIONS

OVERVIEW

This Chapter takes a detailed look at all of the possible new revenues for the City of Pismo Beach. In the "Fact Sheets" beginning on page 11, the following information is provided for each of the thirteen possible new revenues identified in this Study:

- General description of the revenue source: what is it?
- Why is this an appropriate City funding source?
- Is it in place in Pismo Beach at this time? (Would this be a new source? Or an increase in an existing one?) If it is currently in place, how is the revenue used?
- Who pays it?
- Can cities increase this revenue? Under what conditions, if any?
- How much new revenue would it generate?
- What other cities have it? How does this compare with similar cities to Pismo Beach?
- What authority is required to implement it? (Can the Council adopt this revenue measure? Or is voter approval required? And if so, is majority or two-thirds voter approval required?)
- What is required to implement it?
- How can these revenues be used?
- How would these revenues be collected?
- How would this added revenue affect the diversity and stability of the City's revenue base?
- When could the new revenue be effective?
- Are there any special implementation issues?

SUMMARY OF STUDY FINDINGS

The following is a brief overview of the findings of this study, organized by whether voter or Council approval is required to implement it.

Requires Voter Approval

Two-Thirds Voter Approval

- **Property Tax Increase as Part of General Obligation Debt.** Adopted almost 25 years ago, Proposition 13 does not allow an increase in general purpose property taxes above the "1% of market value" limit under any circumstances. However, subsequent amendments to this constitutional limit allow for increases in property taxes for voter-approved bonded indebtedness. General Law cities may incur general obligation debt up to 3.75% of assessed value, which for the City would be about $55 million. Under current market circumstances, this translates into an annual revenue-raising capacity to meet annual debt service requirements of about $4.4 million. The proceeds are restricted to specified capital improvements. As noted above, the City has received voter approval for a property tax rate in excess of the "1%" maximum to pay for its share of seismic improvements to Lopez Reservoir.

- **Parcel Taxes.** With two-thirds voter approval, parcel taxes are allowed in any amount as long as they are not based on property value. They may set based on either a flat rate per parcel or a variable rate depending on the size, use or number of units on the parcel. As a "special" tax, they must be levied for a specific service—such as police, fire, emergency medical service, libraries or storm drainage. The City has one special tax in place today to pay for its State Water contract. In 2002-03, the parcel tax for this purpose was $104.31 per "Equivalent Dwelling Unit" (EDU), which generates $753,000 annually based on 7,226 EDU's in the City. For projection purposes, this means that a rate of $100 per EDU will generate about $722,000 annually.

- **Mello-Roos Special Taxes: Operating or Capital.** Mello-Roos "Community Facilities Districts" (CFD's) are typically formed to provide services or capital improvements to new developments (when there is usually just one "voter"—the developer/land owner), but they can be formed on a citywide basis in already developed areas as well. Depending how they are structured when approved, Mello-Roos special taxes can pay for operations and maintenance as well as capital improvements. If there are more twelve or more registered voters in the district, approval by two-thirds of the registered voters is required. However, if there are fewer than twelve registered voters, the district vote is by the property owners in the district. In this case, property owners have one vote for each acre of land they own in the District. For this reason, Mello-Roos CFD's are typically used in financing improvements and services for new development.

Majority (General Purpose) or Two-Thirds (Special Purpose) Voter Approval

The following revenue sources can be adopted by either majority or two-thirds voter approval, depending on their purpose. Revenue measures where the proceeds may be used for "general purposes" only require majority voter approval. However, revenue measures where the proceeds are "earmarked" and designated for specific purposes require two-thirds voter approval. In both cases, depending on how the revenue measure is structured, the proceeds could be used for operations or capital improvements (including debt service payments on capital projects financed by bonds).

- **Local Option Sales Tax.** Based on recent State legislation, cities are allowed to set their own "local option" sales taxes. Several cities, including Clovis, Fort Bragg and Truckee, have set increased sales taxes in the cities through local elections. Based on current sales tax revenues, a ¼ cent "local option" rate would raise about $475,000 annually, and a ½ cent rate would raise about $950,000 million.

- **Transient Occupancy Tax.** Last changed in 1993, the current rate is 10%, which raises about $4.7 million annually. This is the City's largest General Fund revenue source: it accounts for 40% of total General Fund revenues; and it is two-times bigger than the "Number 2" revenue, property taxes. Each "one percent" increase in the TOT rate would raise about $470,000 annually.

2. REVENUE OPTIONS

- **Property Transfer Tax.** Statewide, there is a property transfer tax of $1.10 per $1,000 of value when property is sold (or $275 on a property worth $250,000). For sales in a city, the proceeds are evenly divided between the city and the county, for an effective city rate of $0.55 per $1,000 of value. (For sales in unincorporated areas, the county retains all of the tax.)

  Prior to the adoption of Proposition 62 by State voters in 1986, all cities were allowed to set their own rate, but they had to give up their share of the $1.10 rate to do so. With the passage of Proposition 62, *General Law* cities lost the ability to do this, since among its many revenue-raising limitations (many of which were subsequently superceded by Proposition 218), is a prohibition on real estate transfer taxes.

  However, because Proposition 62 was a "statutory initiative" (as compared with a Constitutional amendment), its provisions only apply to General Law cities. As such, Charter cities are allowed to adopt this revenue source. Moreover, from 1986 until 1995, a number of appellate court rulings declared the provisions of Proposition 62 to be unconstitutional. For this reason, during this interim period, many General Law cities—along with Charter cities—implemented their own property transfer tax at rates ranging from $1.10 to $10.00 per $1,000 of value. The most common rate is $4.40 per $1,000. At this level, the City's own property transfer tax (which has averaged about $72,000 annually over the last five years) would raise about $580,000 annually, for a "net" increase of $500,000. However, in order to adopt this tax, the City would first have to become a Charter city. For this reason, while an option, it is not as viable as many of the other new revenue sources analyzed in this study.

- **Business License Tax.** Anyone doing business in the City is required to pay a business license tax. The amount is generally based on gross receipts depending on the type of business, with the tax rate *declining* as gross receipts increase. For example, at $100,000 in gross receipts, the tax due is $50; at $200,000, it is $75. This means that the second $100,000 in gross receipts is taxed at half the rate of the first $100,000. This currently generates about $115,000 per year. Each 10% increase in the rate (such as $55 per $100,000 of gross receipts) would raise about $12,000 annually.

- **Utility Users Tax.** Most residents and businesses in California pay utility users taxes (UUT) at rates ranging from 1% to 12.5%. It is a tax on the consumption of utility services (such as natural gas, electricity, water, sewer, telephone and cable), similar in concept to the retail sales tax on commodities. For this reason, most cities set their rates based on the sales tax rate in effect at the time they adopted their UUT ordinance, which accounts for some of the variability in rates. According to a 2000 survey by the League of California Cities, the average rate Statewide in 5.3%. UUT is a very stable revenue source, and would help diversify the City's revenue base. At 5% on all utilities, UUT would generate about $400,000 based on per capita revenues in similar cities in California.

- **Admissions Tax.** This tax is levied on the consumer for the privilege of attending theaters, concerts, movies, sporting events, museums and other performances. The tax can be a flat rate, a percentage of the ticket value or a sliding rate depending on the cost of the ticket. Although generally determined to be lawful, courts have struck down admissions taxes that are borne solely or primarily by activities protected by the First Amendment. These cases suggest that to implement this tax, a city must have substantial businesses or events that would be subject to it, which do not involve First Amendment rights and would bear a significant portion of the tax burden. For this reason, most cities that have this tax have professional sports teams, amusement parks or similar major event venues in their cities. As such, no revenues have been projected from this source for two reasons: the base upon which such as tax could potentially be levied in Pismo Beach is very small; and given the lack of any major venues in the City similar to those where this tax has been successfully implemented, it is unlikely that it would be legal to do so.

- **Parking Tax.** This tax is imposed on occupants of off-street parking spaces for the privilege of renting the space within the City. It is typically levied when there are a large number of privately-owned and operated parking lots and garages, and there is a high demand for these spaces. Since this is not the case in Pismo Beach, no revenues have been projected from this source.

- **Special Assessments: Operating or Capital.** Under Proposition 218, special assessments for either one-time improvements or ongoing maintenance are allowed; however, majority approval by those responsible for paying the special assessments, weighted by each property owner's benefit obligation, is required. The *Cost of Services Study* prepared by Revenue and Cost Specialists (RCS) in May 2001 identified $168,000 in ongoing costs for street sweeping and street lighting that could potentially be recovered through a special maintenance assessment district. Under similar ground rules, special assessment districts can be formed for one-time capital improvements. The City has extensive experience with this type of project financing.

Could Be Approved by the Council

The following revenue sources could be set or increased by the Council.

- **Mello-Roos Districts for New Development.** Many cities require that new development pay not only for the facilities needed to service them, but for day-to-day services as well. This could include park and landscape maintenance, street lighting, street sweeping, libraries and fire protection. While this sets up two classes of city residents—those who receive what may be perceived as general city services based on the general purpose tax revenues they pay, and those who must pay an additional premium for those same services—many cities have moved to this out of fiscal necessity. The revenue impact of this is difficult to assess, since it would depend on what services were subject to the special Mello-Roos tax. However, as discussed above, this would require the concurrence of the property owner in establishing this special tax district (assuming there are less than twelve registered voters in the District) before the start of construction.

- **Development Impact Fees.** The City can set impact fees at any level that will fully offset (but not exceed) the cost of constructing capital improvements needed to service new development. This can cover a broad range of public facilities, including water, sewer, transportation, parks, cultural facilities, community centers, civic center improvements and public safety facilities. As noted above, the City is currently analyzing development impact fees as part of a separate study, and as such, they are not covered in this report.

- **Higher Cost Recovery for "Personal Choice Public Services."** Based on a comprehensive *Cost of Services Study* prepared by RCS, the City recently implemented a higher level of cost recovery for "personal choice public services." While the Council approved most of the proposed fee increases proposed by RCS, it did not adopt all of them, or took a phased approach. Areas where higher cost recovery could be achieved under Proposition 218 with Council approval include some planning fees and fire engine company inspection fees**.** Fully implementing the fee recommendations in the RCS would raise about $100,000 annually.

- **Franchise Fees.** Similar to franchise fees charged to other utilities such as gas and electric, many cities assess a franchise fee on their water and sewer enterprise to reimburse the General fund for use of its right-of-way as well as "wear and tear" on its street pavement. Many studies have shown that one of the leading causes for shortened street life—and resulting higher maintenance costs—are the cuts made by utilities for underground lines. A modest 2% fee on gross receipts—the same rate set statewide by the State for gas and electric utilities—would raise about $70,000. For similar reasons, the City should also consider increasing its franchise fee on refuse from 6% to 10% (the average rate in the South County), which will generate about $50,000 annually.

COMPARISON CITIES

For each new revenue source, the "Fact Sheets" generally describe the revenue situation for cities throughout the State. In addition to this, they also summarize revenue information for the following ten comparison cities:

City	Population	County
Arroyo Grande	16,600	San Luis Obispo
Capitola	10,050	Santa Cruz
Carmel	4,100	Monterey
Del Mar	4,560	San Diego
Half Moon Bay	12,250	San Mateo
Indian Wells	4,430	Riverside
Morro Bay	10,500	San Luis Obispo
Pacific Grove	15,600	Monterey
Solvang	5,425	Santa Barbara
St. Helena	6,000	Napa
Pismo Beach	8,725	San Luis Obispo

All of these cities share three key characteristics with the City: they are under 20,000 in population, tourism is an important part of their local economy; and they all are known for (highly value) their "quality of life." They are located throughout the State, although they are largely coastal cities; and two of them—Arroyo Grande and Morro Bay—are located in San Luis Obispo County.

LOCAL OPTION SALES TAX

What is a local option sales tax?

This is an additional sales tax rate on retail sales within the City, which all cities in California are now allowed to adopt as a "local option" based on recent State legislation. Several cities, including Clovis, Fort Bragg, Santa Cruz, Sebastopol and Truckee, have set increased sales taxes in the cities through local elections. Based on current sales tax revenues, a ¼ cent "local option" rate would raise about $475,000 annually, and a ½ cent rate would raise about $950,000 million.

Why is this an appropriate City funding source?

Consumers benefit from a variety of City services while shopping in Pismo Beach: public safety, pleasant surroundings, streets and sidewalks. It is appropriate that consumers share in the cost of maintaining these service levels. Additionally, sales tax is broad-based, and generally reflects the ability of consumer to pay the tax. Lastly, since it is already in place, there are no significant added costs or administrative effort required. Given its revenue potential, this is one of the most cost-effective revenue options available to the City.

Is this tax in place today?

Yes. The City has a 1% sales tax rate that generates $1.9 million annually.

Who pays this tax?

It is paid by consumers and collected by retail outlets.

Who currently receives the revenue?

The revenue goes directly into the City's General Fund and is used for general municipal purposes.

Can cities increase their tax rate?

Yes. However as noted above, it would require special State legislation to do so. However, in all cases where local voters have approved a supplemental city sales tax, the State has authorized doing so without controversy.

How much revenue would this tax generate?

Based on current sales tax revenues, a ¼ cent "local option" rate would raise about $475,000 annually, and a ½ cent rate would raise about $950,000.

How does this compare with other cities?

As noted above, several cities have done this, including Clovis, Fort Bragg and Truckee. None of the ten comparison cities have adopted an additional city sales tax rate.

What authority is required to implement this tax?

- **General Purpose.** If the revenues will be used for general purposes, majority voter approval is required. This must occur at the same time as regular Council elections, unless the Council declares an emergency by unanimous vote (in this case, the election may be held at any time).

- **Special Purpose.** If the revenues will be "earmarked" for a specific purpose, two-thirds voter approval is required. This election can be held at any time.

As noted above, implementing this tax would also require special legislation. However, in all cases where there has been voter approval to do so, special legislation has been approved without controversy.

How can these revenues be used?

With majority voter approval, they can be used for any legitimate government purpose, such as parks, street maintenance, recreation, police or fire; or with two-thirds voter approval, they must be used for specifically dedicated purposes.

How would these revenues be collected?

The State Board of Equalization is responsible for collecting and distributing this tax.

How would this added revenue affect the diversity and stability of the City's revenue base?

Sales tax is the City's "Number Three" General Fund revenue source, accounting for 17% of total General Fund sources. Sales tax is a relatively broad-based revenue that is paid by both residents and visitors. By introducing a major added source of revenue that would decrease the City's reliance on Transient Occupancy Taxes, which currently accounts for 40% of total General Fund sources, a supplemental City sales tax would improve the diversity of the City's revenue base.

When could the increase be effective?

About six months would be required after its passage to coordinate its collection from local businesses by the State Board of Equalization.

TRANSIENT OCCUPANCY TAX

What is the Transient Occupancy Tax?

This is a tax on the occupant who resides temporarily in a dwelling (typically a hotel or motel) for 30 days or less based on the price of the rental.

Why is this an appropriate City funding source?

Placing this tax on visitors to the City appropriately recognizes that they receive municipal services and benefit from capital investments during their stay, and as such, they should share in the cost of providing them.

Is this tax in place at this time?

Yes. The transient occupancy tax (TOT) rate is currently 10% and provides the City with approximately $4.7 million annually.

Who pays this tax?

It is paid by visitors to Pismo Beach; it is not paid by local residents or businesses.

Who currently receives the revenue?

The revenue goes directly into the City's General Fund and is used for general municipal purposes.

Can cities increase their tax rate?

Yes. Cities can set the TOT rate at any level. There is no regulation of this revenue source by the State or Federal government.

How much revenue would an increase generate?

For each one percent increase, General Fund revenue will increase by about $470,000. The following summarizes additional revenues that would be generated from rates ranging from 11% to 15%, which would be within the range of rates charged by other "tourist-destination" communities in California.

TOT Rates: New Revenues	
11%	$470,000
12%	940,000
13%	1,410,000
14%	1,880,000
15%	2,350,000

How does the City's transient occupancy tax rate compare with other cities?

Based on the State Controller's most recent report on city financial transactions (2000), 383 cities in California have TOT revenues, with rates ranging from 4% to 15%. The most common rate is 10%. There are 33 cities with rates greater than 10% as follows:

TRANSIENT OCCUPANCY TAX

Cities with TOT Rates Greater Than 10%

County	City	Rate	County	City	Rate
Alameda	Berkeley	12.0%	Monterey	Seaside	12.0%
	Oakland	11.0%	Napa	Calistoga	12.0%
Fresno	Fresno	12.0%		Napa	12.0%
Kern	Bakersfield	12.0%		St. Helena	12.0%
Los Angeles	Agoura Hills	12.0%	Orange	Anaheim	15.0%
	Alhambra	12.0%		Buena Park	12.0%
	Beverly Hills	14.0%		Stanton	11.0%
	Calabasas	12.0%	Riverside	La Quinta	11.0%
	Culver City	12.0%		Riverside	11.0%
	Inglewood	14.0%	Sacramento	Citrus Heights	12.0%
	Long Beach	12.0%		Sacramento	12.0%
	Los Angeles	14.0%	San Bernardino	Ontario	11.75%
	Malibu	12.0%	San Diego	Del Mar	10.5%
	Monterey Park	12.0%		San Diego	10.5%
	Pasadena	12.11%	San Francisco	San Francisco	14.0%
	Santa Monica	12.0%			
	Torrance	11.0%			
	West Hollywood	11.5%			

The following summarizes TOT rates currently in place for the ten cities chosen for comparison with Pismo Beach:

TOT Rates: Comparison Cities	
Arroyo Grande	10%
Capitola	10%
Carmel	10%
Del Mar	10.5%
Half Moon Bay	10%
Indian Wells	9.25%
Morro Bay	10%
Pacific Grove	10%
Solvang	10%
St. Helena	12%
Pismo Beach	10%

TRANSIENT OCCUPANCY TAX

What authority is required to increase this tax?

- **General Purpose.** If the revenues will be used for general purposes, majority voter approval is required. This must occur at the same time as regular Council elections, unless the Council declares an emergency by unanimous vote (in this case, the election may be held at any time).
- **Special Purpose.** If the revenues will be "earmarked" for a specific purpose, two-thirds voter approval is required. This election can be held at any time.

How can these revenues be used?

With majority voter approval, they can be used for any legitimate government purpose, such as parks, street maintenance, recreation, police or fire; or with two-thirds voter approval, they must be used for specifically dedicated purposes.

How are these revenues collected?

Operators of "transient lodgings" (typically hotels and motels) are responsible for collecting TOT from the occupants and remitting it monthly to the City. As such, since this revenue source is already in place and no changes in collection method are required if the rate is increased, collection of added revenue from a rate increase can be easily implemented.

How would this added revenue affect the diversity and stability of the City's revenue base?

TOT is already the City's "number one" General Fund revenue source, accounting for about 40% of total General Fund sources. As such, in increase in the City's TOT rate would increase its reliance on this source.

When could an increase be effective?

Theoretically, an increase could be implemented immediately upon voter approval. However, an effective date that is 90 to 120 days from the date of adoption is recommended in order to ensure a smooth transition for the hotels and motels as they quote prices to tour companies for future bookings.

PROPERTY TRANSFER TAX

What is a property transfer tax?

This is a tax resulting from the transfer of real property ownership based on the value of the property.

Background. Prior to the adoption of Proposition 62 by State voters in 1986, all cities were allowed to set their own rate, but they had to give up their share of the $1.10 rate to do so. With the passage of Proposition 62, *General Law* cities lost the ability to do this, since among its many revenue-raising limitations (many of which were subsequently superceded by Proposition 218), is a prohibition on real estate transfer taxes.

However, because Proposition 62 was a “statutory initiative” (as compared with a Constitutional amendment), its provisions only apply to General Law cities. As such, Charter cities are allowed to adopt this revenue source. Moreover, from 1986 until 1995, a number of appellate court rulings declared the provisions of Proposition 62 to be unconstitutional. For this reason, during this interim period, many General Law cities—along with Charter cities—implemented their own property transfer tax at rates ranging from $1.10 to $10.00 per $1,000 of value. The most common rate is $4.40 per $1,000. At this level, the City’s own property transfer tax (which has averaged about $85,000 annually over the last five years) would raise about $685,000 annually, for a “net” increase of $600,000. However, in order to adopt this tax, the City would first have to become a Charter city. For this reason, while an option, it is not as viable as many of the other new revenue sources analyzed in this study.

Why is this an appropriate City funding source?

The City’s real property transfer tax would be paid by the buyers of Pismo Beach properties. As such, it is an appropriate way for new residents to pay their fair share of the amenities that have already been provided by existing residents. For properties changing hands through local buyers, the transfer tax reflects the enhancement of property values by the facilities and programs that the City provides.

Is this tax in place at this time?

Yes. Section 11901 of the Revenue and Taxation Code establishes a statewide property transfer tax at the rate of $1.10 per $1,000 of value (or $440 on a property with a transfer value of $400,000).

Who pays this tax?

Both the buyer and the seller are jointly liable for payment of the tax. However, it is customary for this tax to be paid by the buyer.

Who currently receives the revenue?

For sales in a city, the proceeds are evenly divided between the city and the county, for an effective city rate of $0.55 per $1,000 of value. For sales in unincorporated areas, the County retains all of the transfer tax revenues at the $1.10 per $1,000 rate.

PROPERTY TRANSFER TAX

Can cities increase their tax rate?

Yes, but as discussed above, only Charter cities are allowed to set their own rate separately from the provisions of Section 11901 of the Revenue and Taxation Code at this time. In this case, however, the County would retain the entire proceeds from the $1.10 rate specified in this section.

Have any other cities adopted their own property transfer taxes?

Yes. At least 22 cities in 10 counties throughout the State have adopted their own property transfer tax rates. Rates range from $1.10 per $1,000 in Torrance to $10.00 per $1,000 in Berkeley; and City size ranges from one of California's smallest cities (Cotati, with a population of 6,850) to its largest one (Los Angeles).

City	Population	Rate Per $1,000 Value	City	Population	Rate Per $1,000 Value
Berkeley	104,600	$10.00	Mountain View	71,600	$3.30
Oakland	408,800	9.50	Sacramento	426,000	2.50
Richmond	101,100	7.00	Sebastopol	7,850	2.20
San Mateo	94,400	5.00	Redondo Beach	65,700	2.20
San Francisco	793,600	5.00	Culver City	39,850	2.20
Piedmont	11,150	4.40	San Rosa	152,900	2.00
Los Angeles	3,807,400	4.40	San Rafael	56,700	2.00
Albany	16,750	4.40	San Leandro	81,300	2.00
Alameda	74,600	4.40	Cotati	6,850	1.90
Vallejo	118,600	3.60	Petaluma	56,100	1.15
San Jose	918,000	3.30	Torrance	142,100	1.10

How does this compare with similar cities?

None of the ten "comparison cities" have their own property transfer tax.

How much revenue would an increase generate?

This depends on two key factors:

- The value of property transferred annually.
- The tax rate established by the City.

For comparison purposes, the following is a summary of property transfer tax revenues received by the City over the past five years at the current rate of $0.55 per $1,000, and the amount that would have been received at rates ranging from $1.10 per $1,000 to $10.00 per $1,000:

	Actual	Projected Revenue					
Fiscal Year	**Revenues**	**@ $1.10**	**@ $2.20**	**@ $3.30**	**@ $4.40**	**@ $5.00**	**@ $10.00**
2003-04	91,093	182,186	364,372	546,558	728,744	828,035	1,656,070
2002-03	99,717	199,434	398,868	598,302	797,736	906,428	1,812,856
2001-02	86,527	173,054	346,108	519,162	692,216	786,530	1,573,060
2000-01	70,884	141,768	283,536	425,304	567,072	644,336	1,288,672
1999-00	80,625	161,250	322,500	483,750	645,000	732,881	1,465,762
5 Yr Avg	**85,769**	**171,538**	**343,077**	**514,615**	**686,154**	**779,642**	**1,559,284**
Net Added Revenue		**$85,769**	**$257,308**	**$428,846**	**$600,384**	**$693,873**	**$1,473,515**

PROPERTY TRANSFER TAX

Based on average annual revenues from this source over the last five years, net new revenues range from $85,000 at a rate of $1.10 per $1,000 of value, to $1.5 million at $10.00 per $1,000 of value. At the "mid-range" of the rate set by other cities with this revenue source ($4.40), net annual revenues would be about $600,000.

What authority is required to increase this tax?

- **General Purpose.** If the revenues will be used for general purposes, majority voter approval is required. This must occur at the same time as regular Council elections, unless the Council declares an emergency by unanimous vote (in this case, the election may be held at any time).

- **Special Purpose.** If the revenues will be "earmarked" for a specific purpose, two-thirds voter approval is required. This election can be held at any time.

How can these revenues be used?

With majority voter approval, they can be used for any legitimate government purpose, such as parks, street maintenance, recreation, police or fire; or with two-thirds voter approval, they must be used for specifically dedicated purposes.

How would these revenues be collected?

The County could continue to collect these revenues for the City. While this would require a formal agreement with the County, previous discussions with them by the City San Luis Obispo several years ago were favorable. But again, as noted above, implementing this tax would first require Pismo Beach becoming a Charter city.

How would this added revenue affect the diversity and stability of the City's revenue base?

Property transfer taxes currently account for less than 1% of General Fund revenues. As such, increasing revenues from this source would help diversify the City's revenue base. On the other hand, this revenue source is subject to fluctuations based on real estate market conditions. However, during the last five years, revenues from this source have been relatively stable.

When could an increase be effective?

Theoretically, an increase could be implemented immediately upon voter approval. However, an effective date that is 120 to 180 days from the date of adoption is recommended in order to ensure a smooth transition for the County, businesses directly involved in processing property transfers such as escrow, title and lending companies, and any individuals or companies with properties currently in escrow.

Are there any other implementation issues?

Yes. As noted above, under Proposition 62 this revenue source is only available to Charter cities. For this reason, while an option, it is not as viable as may of the other new revenue sources analyzed in this study.

BUSINESS LICENSE TAX

What is a business license tax?

Anyone doing business in the City is required to pay a business license tax. The amount is generally based on gross receipts depending on the type of business, with the tax rate *declining* as gross receipts increase. For example, at $100,000 in gross receipts, the tax due is $50; at $200,000, it is $75. This means that the second $100,000 in gross receipts is taxed at half the rate of the first $100,000.

Why is this an appropriate City funding source?

Placing this tax on the City's businesses appropriately recognizes that they receive municipal services, and as such, they should share in the cost of providing them.

Is this tax in place at this time?

Yes. As noted above, the amount paid is generally based on gross receipts, although there are a few flat rate categories. Business license taxes currently generate about $115,000 per year.

Who pays this tax?

Any person or company conducting business in the City is required to pay a business license tax. Business activities include property rentals, services, manufacturing, contracting and retail sales. This includes individuals and companies that may not have a fixed place of business in the City.

Are there any exemptions?

Very few:

- Persons with physical disabilities in some circumstances.
- Bonified non-profit organizations.
- Garage sales
- And while not specifically stated, any business types where the payment of local business taxes conflicts with applicable statues or constitution of the United States or the State of California. Banks and other lending institutions fall under this exemption.

Who currently receives the revenue?

The revenue goes directly into the City's General Fund and is used for general municipal purposes

Can the City increase the tax rate?

Yes. Cities can set the business license tax rate at any level, as long as they are not discriminatory or confiscatory, and they are not based on net income.

How much revenue would a rate increase generate?

Each 10% increase in the rate (such as $55 per $100,000 of gross receipts instead of the current $50) would raise about $12,000 annually.

BUSINESS LICENSE TAX

How does the City's business tax rate compare with other cities?

Comparing business license rates is very difficult due to the variety of different tax "measures" used by cities (such as gross receipts, flat fees, square footage and number of employees), tax rates and tax rate structures. For the ten comparison cities, the following summarizes the type of tax system they have in general (gross receipts or flat rates), the amount of revenue that business license taxes generate annually, and revenue per capita.

		Primary	Annual Revenues	
City	**Population**	**Tax Basis**	**Amount**	**Per Capita**
Arroyo Grande	16,600	Flat Rate	$50,000	$3.01
Capitola	10,050	Gross Receipts	$250,000	$24.88
Carmel	4,100	Gross Receipts	$350,000	$85.37
Del Mar	4,560	Gross Receipts	$160,000	$35.09
Half Moon Bay	12,250	Flat Rate	$225,000	$18.37
Indian Wells	4,430	Flat Rate	$10,000	$2.26
Morro Bay	10,500	Flat Rate	$160,000	$15.24
Pacific Grove	15,600	Gross Receipts	$300,000	$19.23
Solvang	5,425	Flat Rate	$15,000	$2.76
St. Helena	6,000	Flat Rate	$115,000	$19.17
Pismo Beach	8,725	Gross Receipts	115,900	$13.28
Average				$21.70

As reflected above, the City's business license tax revenues are about half of the average on a per capita basis.

What authority is required to increase this tax?

- **General Purpose.** If the revenues will be used for general purposes, majority voter approval is required. This must occur at the same time as regular Council elections, unless the Council declares an emergency by unanimous vote (in this case, the election may be held at any time).

- **Special Purpose.** If the revenues will be "earmarked" for a specific purpose, two-thirds voter approval is required. This election can be held at any time.

How can these revenues be used?

With majority voter approval, they can be used for any legitimate government purpose, such as parks, street maintenance, recreation, police or fire; or with two-thirds voter approval, they must be used for specifically dedicated purposes.

How are these revenues collected?

The City is currently responsible for collecting this tax via first time "over-the-counter" new applications and annual renewals in October. Unless there were significant changes in the structure, implementing an across-the-board increase in rates would be fairly simple to accommodate with minimal costs, since the collection system is already in place.

How would this added revenue affect the diversity and stability of the City's revenue base?

BUSINESS LICENSE TAX

Business license taxes currently account for about 1% of General Fund revenues. As such, increasing revenues from this source would help diversify the City's revenue base.

When could an increase be effective?

Theoretically, an increase could be implemented immediately upon voter approval. However, an effective date that is 120 to 180 days from the date of adoption is recommended in order to ensure a smooth transition for the City for required internal administrative and computer changes, and to communicate the changes to the business community. Additionally, any change should be carefully coordinated with to avoid any conflicts with the City's annual October renewal cycle.

GENERAL OBLIGATION BOND PROPERTY TAX

What is a general obligation bond property tax?

This is an increase in the property tax rate, levied against the assessed value of properties, in excess of the "1% of market value" limit under Proposition 13, in order fund the repayment of general obligation bonds for capital improvements.

Background. Adopted over 25 years ago, Proposition 13 does not allow an increase in general purpose property taxes above the "1% of market value" limit under any circumstances. However, subsequent amendments to this constitutional limit allow for increases in property taxes for voter-approved bonded indebtedness. The proceeds are restricted to specified capital improvements.

Why is this an appropriate City funding source?

Along with a number of other intangible factors, property values reflect the kinds and level of service provided by the City: good public safety services and well-maintained streets and parks enhance property values. Additionally, many of the improvements typically funded by general obligation bonds are directly tied to property-related services, and as such, sharing the cost based on value is a reasonable approach. Lastly, this is a very broad-based tax that spreads the tax burden over local businesses and residents as well as out-of-town property owners.

Is this tax in place at this time?

The City has previously received voter approval for a property tax rate in excess of the "1%" maximum to pay for its share of seismic improvements to Lopez Reservoir. However, an additional general obligation bond property tax rate above the "1% of market value" limit would be considered a new tax, not an increase to an existing one.

Who pays this tax?

Property owners within the City limits would pay this tax.

Who receives the revenue?

Proceeds from the added property rates would be accounted for separately by the City in a debt service fund, and used solely for the payment of annual principal and interest on the bonds.

Can cities increase their tax rate?

Yes, with two-thirds voter approval. General Law cities may incur general obligation debt up to 3.75% of assessed value, which for the City would be about $55 million. Under current market circumstances, this translates into an annual revenue-raising capacity to meet annual debt service requirements of about $4.4 million.

How much revenue would an increase generate?

This depends entirely on the amount of general obligation bonded debt that the City incurs. As noted above, the maximum amount of bonded indebtedness, that the City could have outstanding at any one time is about $55 million. However, it is highly unlikely that the City would (or should) consider approaching this maximum.

GENERAL OBLIGATION BOND PROPERTY TAX

Do other cities have general obligation bond property tax rates?

Many cities throughout the State of have passed general obligation bonds approved with two-thirds voter approval. Locally, this includes the Lucia Mar School District, and the Cities of Arroyo and Paso Robles – and as noted above, the City of Pismo Beach itself.

Of the ten comparison cities, Arroyo Grande and Del Mar have passed general obligation bond measures.

What authority is required to implement this tax?

General obligation bond property taxes require two-thirds voter approval. This election can be held at any time.

How can these revenues be used?

The proceeds from a general obligation bond are restricted to capital improvements.

How are these revenues collected?

They would be collected by the County along with other taxes and assessments on the property tax roll, and distributed to the City on the same remittance schedule.

How would this added revenue affect the diversity and stability of the City's revenue base?

Property taxes revenues are a very stable revenue source; and while a general obligation bond property taxes do not directly affect the revenue base or its diversity, shifting the burden for capital improvements from the General Fund to another stable revenue source has the affect of improving diversity.

When could an increase be effective?

An increase in property tax rates could be effective for the next tax year following voter approval and issuance of the bonds.

PARCEL TAXES

What is a parcel tax?

With two-thirds voter approval, parcel taxes are allowed in any amount as long as they are not based on property value. They may set based on either a flat rate per parcel or a variable rate depending on the size, use or number of units on the parcel. As a "special" tax, they must be levied for a specific service—such as police, fire, emergency medical service, libraries or storm drainage.

Why is this an appropriate City funding source?

Many of the City's services are directly related to property. Additionally, at modest levels parcel taxes are usually very straightforward and easy to communicate to the public. On the other hand, at high levels, a flat rate may appear unfair, since it is not based on the value of the parcel (like a property tax) or ability to pay (like sales or income taxes).

Is this tax in place at this time?

The City has one special tax in place today to pay for its State Water contract. For 2004-05, the parcel tax for this purpose is $79.66 per "Equivalent Dwelling Unit" (EDU), which generates $575,000 annually based on 7,226 EDU's in the City. However, any added parcel taxes would be considered a new tax, not an increase to an existing one, since it must be for a special service.

Who pays this tax?

Property owners within the City limits pay this tax.

Who currently receives the revenue?

The revenue from the existing special tax is accounted for in the Water Fund and used to pay State Water contract costs. The best approach of accounting for any new parcel taxes depends on its purpose, and whether it is fully or partially covering the cost. For example, if the parcel tax were to pay for only part of a specific service provided through the General Fund, then accounting for it in the General Fund would be appropriate. However, if it was intended to fully cover the cost of a specific service, then a separate fund may be warranted depending on the circumstances.

Can cities increase their parcel tax rate?

Yes. As long as the tax is not based on property value, there are no State or Federal limits on this revenue source.

How much revenue would an increase generate?

This depends on the rate and basis of the parcel tax. However, assuming the use of the same "EDU" approach use for the State Water contract, a rate of $100 per EDU will generate about $722,000 annually.

Do other cities have parcel taxes?

Over fifty cities in California—including the City of Pismo Beach—have adopted special parcel taxes for a broad range of services, including libraries, police service, fire service, paramedic services, storm water projects, cultural services and street maintenance. None of the ten comparison cities have special parcel taxes.

What authority is required to implement this tax?

Parcel taxes require two-thirds voter approval. This election can be held at any time.

How can these revenues be used?

While they must be designated for a specific purpose, parcel taxes can be used for any legitimate government purpose, such as parks, street maintenance, recreation, police or fire.

How are these revenues collected?

They would be collected by the County along with other taxes and assessments on the property tax roll, and distributed to the City on the same remittance schedule.

How would this added revenue affect the diversity and stability of the City's revenue base?

Parcel taxes are a very stable revenue source. By expanding the City's revenue base and decreasing its reliance on the "Top 3" revenues—Transient Occupancy Tax, Property Tax and Sales Tax, which together account for over 80% of General Fund revenues—parcel taxes would improve the diversity of the City's revenue base.

When could this new tax be effective?

An added parcel tax could be effective for the next tax year following voter approval.

UTILITY USERS TAX

What is a utility users tax?

This is a tax on the consumption of utility services (such as natural gas, electricity, water, sewer, telephone and cable), similar to the retail sales tax on commodities.

Why is this an appropriate City funding source?

Utility users tax is an established means of generating General Fund revenue. Most residents and businesses in the State pay utility users tax (about 60%). Additionally, it is very stable revenue source, and would help diversify the City's revenue base.

Is this tax in place at this time?

No. A utility users tax (UUT) would be a new a new revenue source for the City.

Who pays this tax?

Residents or businesses using the utility pay the tax at the time the utility bill is paid.

Can cities set and increase their tax rate?

Yes. Cities can set the UUT rate at any level. There is no regulation of this revenue source by the State or Federal government.

How much revenue would a rate increase generate?

This depends on three key factors:

1. What utility services are subject to the tax? The broader the base, the greater the revenue. Most cities include the following utilities: gas, electric, telephone, cable television and water.

2. What is the tax rate? Of the 152 cities in California reporting revenues from this source to the State Controller in 2000, rates range from 1.0% to 12.5%, with an average rate of 5.3%.

3. Which users are subject to the tax? In some cities, only non-residential users are subject to the UUT; and in others, the rates are different. Additionally, some cities exclude other governmental agencies, or provide reduced (or waived) levels for senior citizens/and or low-income customers.

Based on the most recent information available from the State Controller, the following summarizes UUT tax rates and revenues for all 36 cities in the State with this revenue source with a population under 20,000.

UTILITY USERS TAX

Utility Users Taxes: Cities Under 20,000 Population

			Utility User Taxes		
County	City	Population	1999-00 Revenues	Tax Rate	Per Capita Per 1% Rate
Alameda	Albany	16,750	$1,194,088	7.0%	$10.18
	Piedmont	11,150	666,180	7.5%	7.97
Butte	Oroville	13,050	892,694	5.0%	13.68
Contra Costa	Pinole	19,450	1,303,800	8.0%	8.38
Fresno	Firebaugh	5,450	258,927	9.9%	4.80
	Fowler	4,760	34,315	5.0%	1.44
	Huron	6,625	113,375	5.0%	3.42
	Orange Cove	8,500	197,866	7.0%	3.33
	Sanger	19,550	589,251	5.0%	6.03
Humbolt	Arcata	16,900	509,847	3.0%	10.06
Imperial	Holtville	5,800	310,586	5.0%	10.71
Los Angeles	Hidden Hills	1,960	227,942	5.0%	23.26
	Malibu	13,050	1,533,016	5.0%	23.49
	Palos Verdes Estates	13,750	2,137,200	10.0%	15.54
	San Marino	13,300	1,132,921	5.0%	17.04
	Sierra Madre	10,850	644,315	6.0%	9.90
Marin	Farifax	7,350	323,374	5.0%	8.80
Merced	Gustine	4,990	208,769	2.5%	16.73
Mono	Mammoth Lakes	7,425	465,650	3.5%	17.92
Monterey	Gonzales	8,050	157,000	4.0%	4.88
	Greenfield	12,700	280,489	6.0%	3.68
	King City	11,250	174,862	2.0%	7.77
	Pacific Grove	15,500	965,590	5.0%	12.46
Riverside	Beaumont	12,200	287,433	3.0%	7.85
	Desert Hot Springs	16,900	872,446	5.0%	10.32
San Luis Obispo	Grover Beach	13,150	116,815	1.0%	8.88
Santa Barbara	Guadalupe	6,700	167,382	5.0%	5.00
Santa Cruz	Scotts Valley	11,600	521,948	4.0%	11.25
Sonoma	Cloverdale	7,375	120,244	2.0%	8.15
Stanislaus	Waterford	7,175	228,711	6.0%	5.31
Tulare	Dinuba	17,500	797,669	7.0%	6.51
	Exeter	9,450	312,305	4.0%	8.26
	Lindsay	10,400	578,926	6.0%	9.28
	Woodlake	6,850	187,826	6.0%	4.57
Yolo	Winters	6,300	463,840	5.0%	14.73
Average Revenue Per Capita Per 1% Rate				5.2%	$9.76

Assuming that the UUT was set at a uniform rate for all users on all utilities, the following are estimated revenues at various rates based on the experience of similar cities:

UTILITY USERS TAX

Projected UUT Revenues for Pismo Beach

Tax Rate	Revenues
1.0%	$84,600
2.0%	169,300
3.0%	253,900
4.0%	338,500
5.0%	423,200
6.0%	507,800
7.0%	592,400
8.0%	677,100
10.0%	846,300

As reflected above, at the average rate of 5%, UUT would generate about $423,000 annually.

What is the UUT rate in similar cities?

Statewide, 152 cities have established a utility user tax ranging from 1% to 12.5%. Although a majority of cities do not have a utility users tax, an overwhelming majority of State residents (approximately 60%) are covered by the tax. Of the ten cities chosen for comparison, only Pacific Grove currently has a utility user tax, which is set at 5% on all utilities.

What authority is required to implement this tax?

- **General Purpose.** If the revenues will be used for general purposes, majority voter approval is required. This must occur at the same time as regular Council elections, unless the Council declares an emergency by unanimous vote (in this case, the election may be held at any time).

- **Special Purpose.** If the revenues will be "earmarked" for a specific purpose, two-thirds voter approval is required. This election can be held at any time.

How can these revenues be used?

With majority voter approval, they can be used for any legitimate government purpose, such as parks, street maintenance, recreation, police or fire; or with two-thirds voter approval, they must be used for specifically dedicated purposes.

How would these revenues be collected?

Utility companies are responsible for collecting this tax—at no cost to the City—and remitting it monthly to the City.

How would this added revenue affect the diversity and stability of the City's revenue base?

UUT would bring a new, very stable revenue base to the City. By broadening the City's revenue base and decreasing its reliance on the "Top 3" revenues—Transient Occupancy Tax, Property Tax and Sales Tax, which together account for over 80% of General Fund revenues—UUT would significantly improve the diversity of the City's revenue base.

UTILITY USERS TAX

When could this new tax be effective?

Theoretically, this new revenue could be implemented immediately upon voter approval. However, an effective date that is a least 180 days after adoption is recommended in order to allow enough lead time for notification to all utility companies and to allow them time to make the computer programming and billing changes required.

ADMISSIONS TAX

What is an admissions tax?

This tax is levied on the consumer for the privilege of attending theaters, concerts, movies, sporting events, museums and other performances. The tax can be a flat rate, a percentage of the ticket value or a sliding rate depending on the cost of the ticket. Although generally determined to be lawful, courts have struck down admissions taxes that are borne solely or primarily by activities protected by the First Amendment, such as movie theaters. These cases suggest that to implement this tax, a city must have substantial businesses or events that would be subject to it, which do not involve First Amendment rights and would bear a significant portion of the tax burden. For this reason, most cities that have this tax have professional sports teams, amusement parks or similar major event venues in their cities.

Given these constraints, no revenues have been projected from this source the base upon which such as tax could potentially be levied in Pismo Beach is very small; and given the lack of any major venues in the City similar to those where this tax has been successfully implemented, it is unlikely that it would be legal to do so.

Why is this an appropriate City funding source?

Placing this tax on those who attend major attractions appropriately recognizes that they receive City services during their attendance at major concerts, museums, sporting events, amusement parks or similar venues, and as such, they should share in the cost of providing them.

However, given the lack of major venues in Pismo Beach similar to those in communities where this tax is in place, this is not a good “fit” for the City,

Is this tax currently in place in the City?

No.

Who pays this tax?

The patrons of events held at theaters, auditoriums, sporting arenas, amusement parks or similar attractions and venues.

Can cities set and increase their tax rate?

Yes, but as noted above, there are First Amendment limitations on this tax, and for this reason, it is in place in very few cities.

Have other cities adopted this tax?

Yes, at least 16 other cities in the State have adopted an Admissions Tax, most typically in cities with large stadiums, sports arenas, auditoriums, amusements parks or museums.

Of the ten comparison cities, only Indian Wells has this tax. The rate is set at 5% of the ticket price, and it generates about $300,000 annually. (Note: The City of Del Mar has this tax “on the books” at a 10% rate, but it has suspended collection pending a court challenge.)

ADMISSIONS TAX

How much revenue would this tax generate?

No revenues have been projected from this source for two reasons: the base upon which such as tax could potentially be levied in Pismo Beach is very small; and given the lack of any major venues in the City similar to those where this tax has been successfully implemented, it is unlikely that it would be legal to do so.

What authority is required to implement this tax?

- **General Purpose.** If the revenues will be used for general purposes, majority voter approval is required. This must occur at the same time as regular Council elections, unless the Council declares an emergency by unanimous vote (in this case, the election may be held at any time).
- **Special Purpose.** If the revenues will be "earmarked" for a specific purpose, two-thirds voter approval is required. This election can be held at any time.

How can these revenues be used?

With majority voter These General Fund revenues can be used for any legitimate government purpose, such as parks, street maintenance, recreation, police or fire; or with two-thirds voter approval, they can be used for specific dedicated purposes.

How are these revenues collected?

Operators of the attractions are responsible for collecting the Admissions Tax from its patrons and (most commonly) remitting it the City on a monthly or quarterly basis.

How would this added revenue affect the diversity and stability of the City's revenue base?

Since this is not a viable revenue source for the City at this time, there is no impact.

When could this new tax be effective?

Until Pismo Beach has a variety of major entertainment facilities on which to impose an Admissions Tax, it is not a viable revenue source.

PARKING TAX

What is a parking tax?

This tax is imposed on occupants of off-street parking spaces for the privilege of renting the space within the City. It is typically levied when there are a large number of privately-owned and operated parking lots and garages, and there is a high demand for these spaces. Since this is not the case in Pismo Beach, no revenues have been projected from this source.

Why is this an appropriate City funding source?

Placing this tax on short-term visitors to the City appropriately recognizes that they receive municipal services and benefit from capital investments during their stay, and as such, they should share in the cost of providing them. Paying for this through parking taxes is one for short-term visitors to pay their fair share (compared with longer, overnight visitors via the transient occupancy tax).

However, due to the lack of a number of large, high-demand privately-owned and operated parking lots and garages in Pismo Beach, this revenue is not a “good fit” for the City.

Is this tax in place at this time?

No.

Who pays this tax?

Those visiting areas with for-fee parking lots and garages.

Can cities increase their tax rate?

Yes. There are no regulations on this source by the State or Federal government.

How much revenue would an increase generate?

Due to the lack of a number of large, high-demand privately-owned and operated parking lots and garages in the City, no revenues have been projected from this source.

Do other cities have this revenue source?

Based on a recent survey by the conducted via the California Society of Municipal Finance Officers, at least 20 cities in California have parking taxes, at rates ranging from 8% to 25%.

None of the ten comparison cities currently have this tax.

What authority is required to increase this tax?

- **General Purpose.** If the revenues will be used for general purposes, majority voter approval is required. This must occur at the same time as regular Council elections, unless the Council declares an emergency by unanimous vote (in this case, the election may be held at any time).
- **Special Purpose.** If the revenues will be “earmarked” for a specific purpose, two-thirds voter approval is required. This election can be held at any time.

PARKING TAX

How can these revenues be used?

With majority voter approval, they can be used for any legitimate government purpose, such as parks, street maintenance, recreation, police or fire; or with two-thirds voter approval, they must be used for specifically dedicated purposes.

How are these revenues collected?

They are collected by the parking facility operator, and typically remitted to the City on a monthly basis.

How would this added revenue affect the diversity and stability of the City's revenue base?

Since this is not a viable revenue source for the City at this time, there is no impact.

When could this new tax be effective?

Until there are a number of large, high-demand, privately-owned and operated parking lots and garages in Pismo Beach, this is not a viable revenue source.

MAINTENANCE ASSESSMENT DISTRICTS

What are maintenance assessments?

They are charges levied on property owners on a "benefit" basis for maintenance services, potentially for a broad range of activities such as fire suppression, public safety, tree trimming, street landscaping, streetlights, traffic signals, and parks and recreation facilities in the community.

Prior to Proposition 218, maintenance assessment districts were widely used throughout California for a broad range of services. However, forming maintenance assessment districts today that meet the rigorous "proportionate special benefit derived by each identified parcel" criteria is much more difficult. For example, before Proposition 218, parcels in a landscape maintenance assessment district would commonly each pay the same annual amount for thoe share of parkway maintenance costs. This straightforward, simple approach may no longer meet the proportionality test of Proposition 218. (Is the "proportionate special benefit" exactly the same for each residence?)

Why is this an appropriate City funding source?

The services funded by these assessments are a large part of what makes the City an attractive place to live and conduct business. Many also fall into the category of "community enrichment" improvements, such as a higher level of street lighting or special parkway or median landscaping), which should perhaps be appropriately financed from sources outside of the City's basic general fund tax revenues. Such financing would serve two purposes:

1. Protecting enhanced service levels from competing with other more basic services.
2. Providing additional revenue to more quickly enhance certain service

In many cases, maintenance assessments can help cities be more business-like and market-driven, by offering augmented services on an optional basis to only those who want them (and are willing to pay for them).

Does the City levy these types of assessments now?

No. While the City has extensive experience with assessment districts as a way of financing special-benefit capital improvements, it has not formed assessment district for maintenance purposes.

Who would pay these assessments?

The owners of property within established assessment districts.

Who would receive the revenue?

The City would establish separate funds to account for the revenues and expenditures in each District.

MAINTENANCE ASSESSMENT DISTRICTS

Who would administer these assessments?

The City would establish assessment districts and the formulas for apportioning assessments. Given the cost of conducting annual ballots, standard annual adjustment factors (such as changes in the Consumer Price Index) are typically approved when the district is formed. Assessments would be included on the County secured property tax roll, and collected by the County on the City's behalf.

Can cities determine the assessment methods and amounts?

Yes. Within the procedural requirements of Proposition 218, cities have a wide range of discretion in determining the apportionment methods and the amount to be raised. The only requirement is that the total amount generated cannot exceed the costs reasonably incurred in providing covered services; and the apportionment method must relate to the specific benefit received by each parcel.

How much could the City realize from these assessments?

The *Cost of Services Study* prepared by Revenue and Cost Specialists (RCS) in May 2001 identified $168,000 in ongoing costs for street sweeping and street lighting that could potentially be recovered through a special maintenance assessment district

What other cities have this kind of assessment?

Many cities throughout the State use maintenance assessment districts, although most were established before Proposition 218.

Three of the ten comparison cities have established maintenance assessments districts:

City	Purpose	Annual Revenues
Arroyo Grande	Parking lot/landscape maintenance	$5,800
Capitola		--
Carmel		--
Del Mar		--
Half Moon Bay		--
Indian Wells	Landscape maintenance	$600,000
Morro Bay	Landscape maintenance	$156,000
Pacific Grove		--
Solvang		--
St. Helena		--
Pismo Beach		--

How much could the City realize from these assessments?

The *Cost of Services Study* prepared by Revenue and Cost Specialists (RCS) in May 2001 identified $168,000 in ongoing costs for street sweeping and street lighting that could potentially be recovered through a special maintenance assessment district

MAINTENANCE ASSESSMENT DISTRICTS

What is the legal authority for these assessments?

There are at least 18 separate "Acts" governing assessment districts dating back to 1909 (such as the Landscaping and Lighting Maintenance District Act of 1972, Fire Suppression Act and Pedestrian Mall Law of 1960) and Park and Playground Act of 1909), the provisions of Proposition 218 override all these.

To start the assessment proceedings, the City must prepare an engineering report by a registered professional engineer, which includes a description of the work to be accomplished in the following fiscal year, an estimate of the costs for this work, a diagram of the assessment district, and the method apportioning costs among specific parcels within the district based on benefit. The Council then must adopt a resolution of intention to establish the assessment district and levy assessments and to announce a public hearing.

An assessment ballot is then conducted, and majority approval by those responsible for paying the special assessments, weighted by each property owner's benefit obligation, is required (based on those voting). In this case, the vote is not by "secret ballot," since the weight (and right to vote to begin with) must be determined.

These elections can be held at any time.

What services can maintenance assessments fund?

If carefully structured to comply with the requirements of Proposition 218, maintenance assessment districts can cover a broad range of costs, including maintaining trees, landscaping, fire suppressions services, streetlights, traffic signals, parks, recreation improvements and open space.

How are these revenues collected?

As noted above, they are collected by the County on the secured property roll based on information provide to them by the City.

How would this added revenue affect the diversity and stability of the City's revenue base?

Assessments are a very stable revenue source. By expanding the City's revenue base and decreasing its reliance on the "Top 3" revenues—Transient Occupancy Tax, Property Tax and Sales Tax, which together account for over 80% of General Fund revenues—maintenance assessments would improve the diversity of the City's revenue base.

When could these assessments take effect?

Initially establishing a district is time-consuming; and if approved, collection of assessments must be scheduled to start with a new fiscal year.

MELLO-ROOS SPECIAL TAX DISTRICTS

What are Mello-Roos special taxes?

They are special taxes set through "Community Facilities Districts" (CFD's). While they are typically formed to provide services or capital improvements to new developments (when there is usually just one "voter"—the developer/land owner), they can be formed on a citywide basis in already developed areas as well. Depending how they are structured when approved, Mello-Roos special taxes can pay for operations and maintenance as well as capital improvements.

Background. If there are more twelve or more registered voters in the district, approval by two-thirds of the registered voters is required. However, if there are fewer than twelve registered voters, the district vote is by the property owners in the district. In this case, property owners have one vote for each acre of land they own in the District. For this reason, Mello-Roos CFD's are typically used in financing improvements and services for new development.

Why is this an appropriate funding source for the City?

Forming Mello-Roos districts to cover the cost of facilities and services for new development is a strategy used by many cities to ensure that new development "pays its own way." In newly developed areas, the cost of all additional police, fire, recreation and flood control operating services could be covered through Mello-Roos taxes. Likewise, all additional facilities needed, like parks, fire stations and flood control projects, could be financed by these levies.

However, this potentially sets up two classes of City residents—those who receive what may be perceived as general city services based on the general-purpose tax revenues they pay, and those who must pay an additional premium for those same services. Nonetheless, many cities have moved to this out of fiscal necessity. The revenue impact of this is difficult to assess, since it would depend on what services were subject to the special Mello-Roos tax. However, as discussed above, this would require the concurrence of the property owner in establishing this special tax district (assuming there are less than twelve registered voters in the District) before the start of construction.

For existing development, parcel taxes (or other special) taxes may be simpler approach in achieving the same goal (with the same two-thirds voter approval requirement) than forming a Mello-Roos District.

Is this tax in place at this time?

No.

Who would pay this tax?

The owners of property within established CFDs.

Who would administer this tax?

The City would have to initially establish the CFDs and the structure of the tax. The tax could be collected on County tax bills in the same way ordinary ad valorem property taxes are collected.

MELLO-ROOS SPECIAL TAX DISTRICTS

How much additional revenue could the City realize from these taxes?

The revenue impact of this is difficult to assess, since it would depend on what services were subject to the special Mello-Roos tax. However, the "conventional wisdom" is that special taxes (and any other special assessments or tax rates) should not result in a total tax liability that is greater than 2% of assessed value (or 1% more than the 1% general-purpose tax limit under Proposition 13).

What other cities impose Mello-Roos special taxes?

Many cities throughout the State have formed Mello-Roos Districts, almost exclusively to finance infrastructure, facilities and services related to new development. None of the ten comparison cities have formed Mello-Roos Districts.

What authority is required to implement this tax?

Although Proposition 13 severely limited ad valorem property taxes in 1978, it included provisions allowing local governments to impose other special property taxes with a two-thirds vote of qualified electors affected. The Mello-Roos Community Facilities Act set up the mechanisms for local governments to levy these special taxes.

Establishing a CFD can start by legislative action or by petition of registered voters or property owners. Once a CFD is proposed, the Council must adopt a resolution of intention, hold a public hearing, adopt a resolution of formation and then put the issue to an election of qualified voters within the CFD. The proposition may be included on a general or special election ballot, or the election may be conducted by mailed ballot.

1. If there are twelve or more registered voters, the tax must be approved by two-thirds of the votes cast.

2. If there are fewer than twelve registered voters, the district vote is by the property owners in the district. In this case, property owners have one vote for each acre of land they own in the District.

If approved under either scenario, the Council must then adopt an ordinance in order to levy the tax.

Although legislation allows wide flexibility in apportioning Mello-Roos taxes, they may not be assessed in proportion to the value of real property within the CFD, because Proposition 13 restricted additional ad valorem taxation. Most Mello-Roos taxes have been assessed on the basis of development density, "equivalent dwelling units," per parcel, square footage or acreage.

How can these revenues be used?

They can pay for either services or capital facilities. Allowable services are narrowly defined: only additional services beyond those already provided are eligible and these services can only be in the following areas: police protection, fire protection, recreation, and flood control. Capital facilities may be special benefit facilities such as streets, water, sewer and drainage facilities or general benefit facilities like parks, police stations or administration buildings.

MELLO-ROOS SPECIAL TAX DISTRICTS

How are these revenues collected?

This tax could be collected by the County on the secured property tax roll.

How would this added revenue affect the diversity and stability of the City's revenue base?

Special taxes like Mello-Roos collected on the property tax role are a very stable revenue source. By expanding the City's revenue base and decreasing its reliance on the "Top 3" revenues—Transient Occupancy Tax, Property Tax and Sales Tax, which together account for over 80% of General Fund revenues—Mello-Roos special taxes would improve the diversity of the City's revenue base.

When could Mello-Roos taxes take effect?

At the earliest, the District could become effective 150 days after adoption of a resolution of intention.

HIGHER COST RECOVERY

What is the higher cost user fee cost recovery?

Based on a comprehensive *Cost of Services Study* prepared by RCS, the City recently implemented a higher level of cost recovery for "personal choice public services." While the Council approved most of the proposed fee increases proposed by RCS, it did not adopt all of them, or took a phased approach. Areas where higher cost recovery could be achieved under Proposition 218 with Council approval include some planning fees and fire engine company inspection fees**.** Fully implementing the fee recommendations in the RCS would raise about $200,000 annually.

Why is this an appropriate City funding source?

Setting user fees is one of the few remaining areas where elected officials can still exercise local judgment. If there are areas where user fees should appropriately fund service costs – but they aren't – then this means that general-purpose revenues are being used instead. This reduces the resources available for critical services where significant fee options simply don't exist, and must rely upon general-purpose revenues. This includes services such as police, fire and streets – which are among the most important (and most costly) services that cities deliver.

Simply stated, if a city chooses to subsidize services with general-purpose revenues that could reasonably be funded with fees, the result will be reduced capacity to achieve other high-priority goals that can only be funded through general-purpose revenues. This is a straightforward trade-off with straightforward policy impacts. For example, if planning permit fees do not fully cover development review costs, then street maintenance is likely to suffer as a result. For any number of reasons, this may be an appropriate policy outcome – but it is one that should be made consciously, and not by default.

Is this revenue in place at this time?

Yes. The City already collects user fees for a broad range of services.

Who pays these fees?

The users of the service are responsible for paying these fees.

Who currently receives the revenue?

The revenue is accounted for in the General Fund and is used to offset the cost of providing these services.

Can cities increase user fees?

Yes. Cities are allowed to set service fees at any level as long as they do not exceed the costs reasonably incurred in providing the service.

How much revenue would an increase generate?

Fully implementing the fee recommendations in the RCS would raise about $200,000 annually.

HIGHER COST RECOVERY

What authority is required to increase these fees?

The Council is authorized to set user fees. As noted above, this is one the few areas where the Council has revenue-raising discretion.

How can these revenues be used?

They can only be used to offset the costs of providing the service, including both direct and indirect costs.

How are these revenues collected?

User fees are typically collected by the operating department before providing services.

How would this added revenue affect the diversity and stability of the City's revenue base?

By expanding the City's revenue base and decreasing its reliance on the "Top 3" revenues—Transient Occupancy Tax, Property Tax and Sales Tax, which together account for over 80% of General Fund revenues—higher cost recovery would improve the diversity and stability of the City's revenue base.

When could an increase be effective?

An effective date that is 60 to 90 days from the date of adoption is recommended in order to ensure a smooth transition

FRANCHISE FEES

What are franchise fees?

These fees are charged to public utilities (such as natural gas, electricity, refuse collection, water, sewer and cable television) for the use of City right-of-way and impact on City streets in conducting their operations.

Background. Similar to franchise fees charged to other private utility companies, many cities assess a franchise fee on their water and sewer enterprise to reimburse the General fund for use of its right-of-way as well as “wear and tear” on its street pavement. Many studies have shown that one of the leading causes for shortened street life—and resulting higher maintenance costs—are the cuts made by utilities for underground lines. Another major impact on the condition of street pavement and related maintenance costs is the added “wear and tear” of heavy vehicles, like refuse collection trucks. For this reason, most cities assess franchise fees on private sector refuse companies.

Why is this an appropriate City funding source?

In assessing a reasonable franchise fees on water and sewer, the City would be treating its enterprise operations like businesses, and fairly recovering the cost of the use of its right-of-way and impact on City streets. In increasing franchise fees on refuse, the City would better recover the value of its right-of-way and the impact of refuse collection on street pavement.

Does the City collect franchise fees now?

Yes. The City collects various franchise taxes on all privately-owned utilities operating within the City, such gas, electricity, refuse and cable television. Under State law, telecommunication companies are exempt from local franchise fees.

- **Natural Gas and Electricity.** For these two utilities, the State regulates the amount of the fee cities can assess on a statewide basis: 2% of gross receipts arising from their use of the franchise (with an alternative minimum calculation if it results in a higher franchise fee). The City receives about $120,000 annually from these two franchises.

- **Cable Television.** The Federal government regulates cable television, and has established a maximum franchise fee of 5%. The City receives about $135,000 annually from this franchise.

Remaining areas where the City has discretion in setting franchise fee rates is refuse, water and sewer services:

- **Refuse Collection.** The City has set the franchise fee for refuse collection at 6%, which generates about $76,000 annually.

- **Water and Sewer**. The City does not assess any franchise fees on water or sewer.

Who pays these fees?

These fees are paid by the franchise holder. While they be passed on by the company (like any other operating expense), payment is the responsibility of the operator, not customers.

FRANCHISE FEES

How much additional revenue could the City realize by setting franchise fees on water and sewer?

Each 1% rate would generate about $35,000. As such, a modest 2% fee on gross receipts—the same rate set statewide by the State for gas and electric utilities—would raise about $70,000 annually.

How much additional revenue could the City realize by increasing refuse franchise fees?

Each 1% rate increase would raise about $12,500. As such, increasing the rate from 6% to 10% would raise about $50,000 annually.

What other cities have these fees and what rates do they charge?

All cities in California collect fixed franchise fees for electric and gas utilities under the statewide program; virtually all collect cable television franchise fees at the 5% level; and many assess franchise fees on refuse collection at a broad range of rates.

In the South County area, virtually all communities have now set refuse franchise fees at 10% except for Pismo Beach. (The County has set the rate at 10% in all unincorporated areas throughout the county.)

Several cities throughout the State assess franchise fees on their enterprise fund operations; however, none of ten comparison cities do this.

What authority is required to increase these fees?

As noted above, the City is pre-empted by the State in setting franchise fees for natural gas, electricity and telecommunications; and by the Federal government for cable television.

However, the Council has the authority to establish franchise fees and determine rates for water, sewer and refuse, although as fees, the amount charged should bare a relationship to the intensity of use of City right-of-way and impact on street wear and tear. For this reason, the franchise fee on refuse would typically be greater than on water or sewer.

How can these fees be used?

Franchise fees can be used for any legitimate government purpose.

How are these fees collected?

They are remitted to the City be the franchise holder. Gas and electric franchise fees are paid annually in April; other franchise fees are typically paid on a monthly or quarterly basis, depending on the terms of the franchise agreement.

How would this added revenue affect the diversity and stability of the City's revenue base?

By expanding the City's revenue base and decreasing its reliance on the "Top 3" revenues—Transient Occupancy Tax, Property Tax and Sales Tax, which together account for over 80% of General Fund revenues—higher cost recovery would improve the diversity and stability of the City's revenue base.

FRANCHISE FEES

What action is necessary to increase these taxes?

Raising franchise fees on refuse service would require amending the City's agreement with the franchise holder. Theoretically, the Council could amend this agreement any time, but it makes sense to do it in conjunction with the regular rate adjustment process.

Establishing franchise fees for water and sewer service can be approved by the Council as part of its budget and fiscal policies. While the City typically does this as part of its budget adoption process, this could occur at any time.

3. PREPARING FOR A SUCCESSFUL REVENUE MEASURE

OVERVIEW

For the past twenty-five years, the California has been on the path to a new era of governance, with fundamental changes in the way that decisions are made. While this is occurring at all levels, it is perhaps most pronounced for local agencies, since they are the level of government closest to the people, and the one most susceptible to these changes. The following is a brief overview of this change and it how directly affects the City of Pismo's Beach's ability to preserve its fiscal health while at the same time deliver current service levels, adequately maintain existing facilities and infrastructure, and achieve important community goals and capital improvements.

REPRESENTATIVE VERSUS DIRECT DEMOCRACY

One of major "mega-trends" affecting governance is a fundamental change in the way that decisions are made. Over the last twenty-five years, there has been a decided shift from "representative democracy" to "direct democracy," especially in local government finance.

Proposition 13 did not start this trend, but it certainly resulted from it. Since its passage over twenty-five years ago, there have been an increasing number of citizen-approved limits on the ability of elected officials at the local level to make resource decisions on behalf of the community. While Proposition 218 was the most recent (and sweeping) of these, it was simply the last in a long line of expenditure and revenue limitation ballot measures.

There are a number of possible explanations for this change:

- Lack of leadership (or at least the perception) by elected and appointed officials on important issues to the nation, state and community.
- Increasing distrust of government in general.
- Loss of community identity (and support) as places of work and home have become increasingly separated.
- Increasing frustration with the inability to affect government at the state and federal level, and an over-compensation at the one level – local government – where voters feel they can make a difference.
- Improved information about public issues, resulting in less reliance on others to make decisions on our behalf.
- Increased influence of highly-organized and well-financed special interest groups through the initiative process.

Whatever the reason, the reality is that there has been a major shift to direct citizen decision-making in a broad range of issues previously thought to be too "technical" for this. While this has occurred in a number of areas such as insurance and campaign financing, it is especially prevalent in "ballot box budgeting." Citizens are no longer willing to give their proxy on financial issues to elected officials, or to their interest group representatives on "blue ribbon" committees. City finance is an issue they want to decide directly for themselves.

3. PREPARING FOR A SUCCESSFUL REVENUE MEASURE

How does this shift affect the City's long-term fiscal health? Stated simply, the City will need broad-based community support – in evidence on Election Day – to implement new revenue sources. In this new model of direct democracy, creating support among elected officials and community leaders – even if it broadly crosses a number of interest groups – is no longer enough.

And based on the experience of other cities, achieving this support at the *ballot box* (the only place it matters) requires two key ingredients: a compelling vision of how the new revenues would be used; and an effective way of communicating this vision to likely voters.

PROSPECTS IN THE POST PROPOSITION 218 ENVIRONMENT

Under Proposition 218 adopted in November of 1996, the ground rules for municipal finance were fundamentally changed. In short, any major, broad-based revenue program will require voter approval. In the case of tax revenues, majority voter approval is required for general-purpose taxes; and two-thirds voter approval for special taxes. Assessments are still possible for selected services; however, they are limited in the kinds of services that can be funded through them (these typically fall into more traditional services such as streets, sidewalks and sewers where costs and benefits can be closely linked); and there are rigorous "assessment ballot" procedures. Any form of citywide assessment district with simple apportionment factors is virtually prohibited.

Limited Opportunities for the Council to Increase Revenues

As discussed in Chapters 1 and 2, there are a limited number of areas where revenues can be raised by the Council without voter approval, such as user fees. Along with these, grant revenues and enhanced economic development efforts can also play a role in augmenting the City's fiscal capacity. However, grant programs are few and far between; and those that remain are more competitive than ever. Moreover, they are focused (appropriately) on the goals and priorities of the granting agency, which may not be the same as the City's. For this reason, while they can be important in enhancing City projects and in providing funding for "pilot" programs, grant revenues cannot be relied upon as a long-term financing source for high-priority programs and projects. The same is true for even the most successful economic development programs: these are long-term programs, which can typically take five to twenty years before a community sees the benefits; and the results can never be guaranteed: while the City can be a partner in local economic development efforts, ultimately a healthy economy depends on successful private sector market decisions, which the City does not control.

Paramount Need for Broad-Based Community Support

Other than these limited resource options, the City will need strong community support – in evidence on election day – for anything else it does in implementing new or increased revenue sources.

Intensive, Community-Based Program Required for Success. Communities in California have been successful in generating broad-based voter support for new revenues when:

- There has been a major community-wide focus on desired programs. In these cases, revenue increases have followed these "visioning" efforts, not driven them. Cities in this category come in a lot of sizes, and include El Cerrito, Duarte, Brea, Torrance and Claremont.

- There are serious fiscal or service problems of crisis proportions. Locally, the passage of a bond issue several years ago in the Lucia Mar School District also falls into this category.

Although they were driven by very different factors – hopes versus fears – all of these successful efforts share one thing in common: they were the result of extensive community-based efforts, which included a combination of outreach tools, and professional assistance to use them effectively such as:

- Focus groups.
- Professionally conducted, scientific surveys.
- Town hall meetings.
- Direct mailings and/or newspaper inserts – "community budget-building" exercises.
- Strong follow-on advocacy group for ballot measure support.

Based on the experience of many cities and other local government agencies throughout the State, if the need is compelling and is effectively communicated, this effort is likely to be successful. However, it requires commitment, resources (more on this later), time, and most importantly, a strong community-based advocacy group that will aggressively raise funds and campaign for the issue once it is on the ballot.

This last issue cannot be stressed enough. Under State law, cities have broad discretion in using their funds for professional assistance in researching issues, conducting surveys, and developing voter support strategies. However, once an issue becomes a formal ballot measure, cities cannot participate as an advocate in any way. In short, unless there is a strong community-based group who is willing to aggressively raise funds and campaign for the measure, it is not likely to pass.

ELEMENTS OF A SUCCESSFUL REVENUE MEASURE

Three are three major steps in preparing for a successful revenue measure:

- ***Feasibility Assessment.*** Conduct public opinion research and assess the likelihood of a successful revenue measure.

- ***Education Program.*** If the public opinion research is favorable, develop and implement an educational campaign on why new revenues are needed.

- ***Ballot Measure.*** Place the measure on the ballot *if* there is a community-based group that will aggressively campaign for its passage.

The following further summarizes the components of each of these steps. It is important to stress that while the City can take the lead on these three tasks in preparing for the measure, once it is placed on the ballot it can no longer be an active participant in the process or commit resources to its passage in any way. For this reason even, though the results of the first two steps may have been very positive, placing the measure on the ballot should only occur if there is a community-based group has emerged that will campaign for its passage.

Feasibility Assessment

The first step in preparing the feasibility assessment is to hire a qualified team of a public opinion research firm and a revenue measure advisor. The results of the public opinion research are invaluable in assessing at the very beginning if there is adequate voter support for a new revenue measure. While support can subsequently be built (or maintained) through an education program, if there is very low support initially, an education campaign is unlikely to be successful in gaining voter support on Election Day.

The public opinion survey will typically surface three key issues:

- ***How does the community feel about the City and the services it delivers today?*** The experience from revenue measures in other communities show that it is very difficult to gain voter support for new revenues where there isn't already a high level of satisfaction with City services and trust in its government. In short, if voters do not feel that current revenues are being used wisely, they are not likely to approve more.

- ***What programs are most likely to attract voter support?*** What do voters see as the biggest problems in the community, and would be likely to approve additional funding for: Public safety? Street maintenance? Parks and recreation? What messages would be most effective in community the need for additional resources? On the other hand, which service areas are least likely to attract voter support? And what are the reasons why voters would not support a revenue measure?

- ***What revenues would voters most likely support?*** As discussed in detail in Chapter 2, there is a wide range of new revenue options available to the City. Which of these is most likely to attract to attract the most voter support? And how does support change based on the rate and level of revenue generated? In the final analysis, each of these revenue options has underlying philosophical reasons that might make them desirable, such as added revenue diversity (like utility users tax), stability (parcel tax) or shifting the tax burden to non-residents (transient occupancy tax or sales tax); however, the best candidate for a successful measure is probably the one that voters are the most supportive of at the outset.

From the results of this research, the City can evaluate the feasibility of a revenue measure; and if it is, determine the elements of an effective education program (which is the next step).

Public opinion research (and the evaluation of its results by a qualified advisor) will cost $25,000 to $50,000, and take 90 to 180 days to complete.

3. PREPARING FOR A SUCCESSFUL REVENUE MEASURE

Public Information Program

Before placing a measure on the ballot, this next step is essential in communicating the need for additional revenues to likely voters. It will probably include:

- Refining the new revenue purposes and uses.
- Selecting the financing mechanism.
- Developing and implementing a public education program.
- Conducting additional survey research (tracking poll) to assess shifts in support.

Refining the Measure

Based on the result of the public opinion survey, the City will need to decide which items to fund in the measure. This includes making a key strategic decision: should this be a majority or two-thirds voter approval measure? As discussed more fully in Chapters 1 and 2, general-purpose tax measures only require majority voter approval, while special taxes (general obligation bond measures), where the proceeds are restricted as to their use, require two-thirds voter approval.

On its surface, passage of a majority voter approval measure would appear "numerically" easier; however, since its proceeds cannot be earmarked for a specific purpose, it can be difficult to communicate the need for the measure, when in essence it calls for raising taxes for no particular reason. On the other hand, while it is obviously a greater challenge to gain two-thirds than majority voter approval, it has the advantage of communicating a more focused (and compelling) reason for added revenues.

In general, majority-voter approval measures are more successful when the purpose is to address a "fiscal crisis" in just meeting revenue needs to continue delivering essential day-today services. Two-thirds voter approval measure are more likely when the purpose is to improve services or make community improvements, like a library, fire station, street improvements, senior center or athletic fields.

One variation on this approach is the "A/B" measure, which has been successfully used in a few cases. This is a dual-component measure: the "A" measure function is simply an "advisory" vote on specific projects, asking of voters would support certain uses if new revenues were to become available. The "B" measure asks voters to approve a general-purpose revenue measure, but in the context of the specific project or programs identified in Measure "A," with the expectation that elected officials would be committed to using the new general revenues for these specific purposes. As such, "A/B" measures provide some specificity—although via a non-binding advisory measure, which can be appealing to the electorate. However, they need to be carefully structured from a legal standpoint; and because they are two separate measures with slightly different messages, it may be more difficult to conduct an effective campaign.

In short, regardless of whether it is a majority or two-thirds measure, the City needs to communicate a compelling reason for why it needs added revenues.

3. PREPARING FOR A SUCCESSFUL REVENUE MEASURE

Developing Key Messages

Once the City has determined the basic strategy (majority or two-thirds voter approval) and refined the funding items, assigned costs and select a funding mechanism, key messages are developed that:

- Address the need for such a measure, and why now—make the case that this is a necessary, responsible fiscal plan.
- If a two-thirds measure, include specifics of the items to be funded.
- Establish protections for ensuring money will be spent responsibly, such as outside audits and a Citizens Oversight Committee.

Building Community Support

Opinion Leaders. Depending on the funding mechanism and uses identified for the measure, building community consensus is essential. Early in this process, key constituents, stakeholders, business leaders and other public officials should be contacted and their support, questions or opposition evaluated. This also begins to identify possible members of the community-based group that will be essential later in advocating for passage of the measure.

Public Information Program. An effective public information program includes the following communications components:

- Personal meetings with external "Opinion Leaders" to educate them on the funding needs contained in the Measure and obtain input.
- A series of non-partisan, information-only mailings to Opinion Leaders, again about the City's funding needs.
- A series of non-partisan, information-only mailings to constituents determined by the public opinion survey as needing more information about the City's funding needs.
- A Free Media plan that includes (but is not limited to): non-partisan guest columns, "op-eds" and stories in neighborhood newsletters or other local outlets about the City's funding needs.
- Where appropriate, "fixed site visibility" activities where constituents and/or City representatives table or otherwise distribute non-partisan information about a potential revenue measure.
- A Speakers Bureau primarily led by constituents to make presentations to key community organizations as needed.

As part of the City's Media/Communications Plan, information-only fact sheets, brochures, letters, newsletters and guest columns are developed for mailing and distribution. Where time permits, these communications seek citizen input in an "interactive" manner.

Ideally, before placing a revenue measure on the ballot, the City's public information program has:

- Shifted public opinion further towards support of a possible revenue measure.
- Yielded letters and cards providing the City with guidance on how to further refine the measure.
- Answered questions about the City's funding needs.
- Generated greater community awareness before taking action to place a revenue measure on the ballot.

Additional Public Opinion Research

Following the public information program, the City should conduct another scientific public opinion survey—an abbreviated version also known as a "tracking poll"—just before placing the measure on the ballot. The purpose of this tracking poll is a final "litmus test" in ensuring that there is substantial voter approval at this point, and confirm financial thresholds: that the City is not asking for too little or too much money for the measure.

Conducting a tracking poll close to the time that the City makes a final decision in going forward with a ballot measure is the final opportunity to evaluate where the electorate is, and to make adjustments in the measure as necessary—including not going forward at all.

Timing and Implications of Other Ballot Measures and Issues

If the measure is for general-purpose revenues (majority voter approval), then it must be held in conjunction with Council elections (unless the Council unanimously declares an emergency). The next opportunity for this is November 2006. A two-thirds voter approval election can be held at any time.

Cost and Timing

An effective public information program will take 90 to 180 days, and cost $30,000 to $60,000 for direct mailings, tracking poll and professional assistance in preparing the public information program

Placing the Measure on the Ballot

The City's final action is to place the item on the ballot. As noted above, after this the City cannot commit any resources in advocating for its passage. For this, even if all the other factors to-date have been favorable, the City should seriously consider not placing the measure on the ballot if by this time an effective community-based group has not emerged that will be campaign aggressively for its passage.

3. PREPARING FOR A SUCCESSFUL REVENUE MEASURE

RESOURCES AND TIMING

The following summarize the general timing and resource requirements to prepare for a successful revenue measure:

Task	Time	Cost
Select research/advisor team	60 to 120 Days	
Conduct public opinion research and evaluate results; make "go/no-go" decision in proceeding further. If "go:"	90 to 180 days	$25,000 to $50,000
If "go:" Develop and implement public information campaign.	90 to 180 Days	$30,000 to $60,000
Evaluate results and make decision on placing measure on the ballot.	30 Days	
If "yes:" Vote on measure.	90 Days	
TOTAL	12 to 20 Months	$55,000 to $110,000

As reflected above, from the time a decision is made to seriously *consider* a revenue measure, 12 to 20 months are required to effectively prepare for one.

NEXT STEPS

Before seriously considering a revenue measure, the City may want to hear directly from other cities that have been successful in doing this. Locally, this includes the Lucia Mar School District, Cambria School District, City of Paso Robles and City of Arroyo Grande. Statewide, there are a number of cities have done this, including Claremont, El Cerrito, Fontana and Los Gatos.

In this way, the City can hear first hand the challenges that these communities faced, and how they successfully met them.

SUMMARY

Preparing for a successful revenue measure in this era of "direct democracy" requires an approach that will engage the City's voters in the decision-making process. Gaining this support—in evidence on Election Day—requires more than a compelling need: it also requires communicating this need in a compelling way. And this requires effective preparation by the City—doing its homework, and allocating adequate time and resources to this endeavor—before placing revenue measure on the ballot (which is within the control of the City); and an effective community-based group that will campaign for its passage afterwards (which is not).

4. REVENUE DIVERSITY AND STABILITY

The following "White Paper" was prepared for the Institute of Local Self Government and first presented at the League of California Cities Annual Conference as part of the "Symposium on the Future of Local Government Finance" on October 4, 2002.

LOCAL GOVERNMENT REVENUE DIVERSIFICATION, FISCAL BALANCE/FISCAL SHARE AND SUSTAINABILITY

by

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INTRODUCTION

This white paper examines the concepts of revenue diversity and sustainability, and argues that these concepts should be expanded to include achieving and maintaining an appropriate "fiscal share" of financial resources generated by a jurisdiction's local economy. It further argues that rather than only rail against the state for damaging local government finances, our energies should also be directed to using revenue diversity as a strategic tool for creating increased fiscal independence. Increased fiscal independence is essential to ensure the continued and uninterrupted financing of local government services in California.

THE CONCEPTS OF REVENUE DIVERSITY AND SUSTAINABILITY

Background

A review of the literature concerning revenue diversification and fiscal balance indicates that "revenue diversification" is generally understood to mean the process of creating multiple sources of revenue flows to finance local government operations. It is also generally understood to be a tool for achieving "fiscal balance": an appropriate mix of revenue sources and an appropriate mix of revenue bases by revenue source. For example, concerning revenue bases, a Business License Tax that applied various tax rates to all types of businesses in a community would be more diverse that a Business License Tax that only applied to selected types of businesses (i.e. who pays), and/or that overly relied upon a small set of relatively higher tax rates applied to some businesses for most of the Business License tax revenue (i.e. how much individual payers paid).

4. REVENUE DIVERSITY AND STABILITY

When an appropriate "fiscal balance" has been achieved through revenue diversification, it is generally argued that certain benefits accrue to the jurisdiction:

- A greater probability that the level of overall spending would be lower because less service disruptions and other operating inefficiencies associated with over reliance on more limited or uncertain revenue sources would have to be financed;
- A greater probability that sufficient revenues would be generated to sustain current services and service levels;
- Economic equity and efficiency would be improved by spreading the "burden" of financing local government among a broader base of revenue generators (i.e. taxpayers and fee payers) and the use of the lowest possible tax or fee rates;
- There would be a greater ability to avoid fiscal crisis due to fluctuations in the normal economic cycle, legal challenges, and political action because different revenue sources respond in different ways and over different time periods to such fiscal crises; and
- There would be an increased ability to generate more revenue to finance increased spending that may be necessary due to imposed judicial or legislative demands, natural disasters, or changes in public demands/service priorities.

While empirical studies to date have failed to either confirm or refute that such benefits result from revenue diversification, public finance professionals believe that revenue diversification is, nevertheless, desirable. For example, the Government Finance Officers Association has adopted the following best practice policy guidance 4.6 for governments:

"***Practice:*** *A government should adopt a policy that encourages a diversity of revenue sources.*

*"**Rationale**: All revenue sources have particular characteristics in terms of stability, growth, sensitivity to inflation, or business cycle effects, and impact on tax and rate payers. A diversity of revenue sources can improve a government's ability to handle fluctuations in revenues and potentially help to better distribute the cost of providing services."*

Over the last 30 years, empirical studies of local government revenue diversification generally conclude that revenues have become more diverse primarily as a reactive result of the need to replace lost revenue flows due to legislative and/or voter actions (e.g. the shift to a greater use of fee and other tax revenue sources following the lost of property tax revenue due to Proposition 13), rather than as the result of a revenue diversification strategy designed to achieve directly some of the benefits described above.

Relatively little has been written concerning the relationship between the concept of "sustainability" and local finance. Probably the best work to date appeared as an article, "Portland, Oregon: A Case Study in Sustainability" in the February 2002 issue of

Government Finance Review (pages 8 –12). In that article, sustainability was defined as:

> *"Simply put, sustainability is the notion that the current economic and consumption patterns should not reduce opportunities for future generations by depleting or impairing resources. Put another way, sustainability is the process of creating balance among the environment, the economy and social equity. The concept is derived from recognition that the earth's natural capital is limited and that pollution and wastefulness are a drain on the economy."*

The remainder of the article develops the argument that finance officers need to be more involved in local government policies that affect the balance among the environment, the economy and social equity because environmentally unsustainable policies simply cost more, and often a lot more, than sustainable policies.

Expanding on the Concepts of Revenue Diversity and Sustainability

The development, to date, of the concepts of revenue diversification and sustainability have focused primarily on increased fiscal performance assumed to result from revenue diversity/fiscal balance, and reduced local government costs from the adoption of environmentally sustainable policies. The authors of this white paper suggest, however, that these concepts may be more useful if they are expanded to include the goal of increasing local government fiscal independence.

For the many reasons explored in the next section of this white paper, local governments in California need to increase their fiscal independence. An expansion of the concepts of revenue diversity and sustainability can help local governments achieve this goal.

The authors suggest that "revenue diversity" needs to be viewed as a conscious strategy to implement and structure multiple revenue sources in such a manner as to ensure that a local jurisdiction's annual revenue flow represents a constant percentage or proportion of the gross local jurisdiction's economic product (i.e. the annual value of all goods and services produced/provided within the boundaries of the jurisdiction). In short, revenue diversification needs to be seen as a tool to achieve an appropriate "fiscal share" of financial resources generated by the local economy, rather than as a tool to achieve "fiscal balance."

This new way of understanding "revenue diversity" assumes that: a) the ability of a local economy to produce goods and services is, to a substantial degree, dependent on the range and quality of governmental services provided to the community by the local government; b) the kinds of governmental services and the quality of services provided by the jurisdiction are determined by the governing body of the jurisdiction; c) the minimum percentage or proportion of the jurisdiction's annual gross economic product to be "diverted" to the local government in order to finance governmental services is determined by the governing body of the jurisdiction through the design and implementation of the local revenue structure; and d) the provision of governmental services should not have to be varied simply as a result of fluctuations in the local economy and its ability to generate local revenue, or due to adverse legal or State political action.

Assumption "d)" is central to re-focusing "revenue diversity" to be a tool for achieving "fiscal share." It means that if the local economy should decline, the local governmental revenue structure would be designed to automatically adjust so as to ensure a sufficient amount of local government revenue continues to flow to maintain local services and service level. Alternatively, it could also mean that the revenue flow would only be reduced to a pre-defined level that would be sufficient to finance a minimally acceptable set of services/service levels as set by the local governing body. Further, it means that it is in the public interest that local government services be maintained at no less than some pre-defined level as determined by the jurisdiction's governing body.

For example, existing tax and/or other revenue sources could be redesigned so that if certain pre-defined changes happened in the local economy, tax rates or fee levels would automatically be adjusted (within appropriate limits) to provide some degree of offsetting revenue generation. Another possibility would be that if certain pre-defined changes happened, reserve fund balances (i.e. "rainy day" funds) would also automatically come into play on their own or in conjunction with other automatic adjustments in tax and/or fee rates. The point is that some flexibility would already be built into the local jurisdiction's revenue structure that is not only reliant on just the mix of revenue sources.

Establishing such revenue structures may require new voter approvals, or possibly additional legal authority for local jurisdictions so that they could craft revenue diversification strategies and technical implementing mechanisms specific to the particulars of a jurisdiction's local economy and service/service level mix.

Similarly, the concept of sustainability, as used in the context of local government finances, needs to be expanded to also include the maintenance over time of an appropriate fiscal share of the financial resources generated by the local economy in order to continue to finance local services/service levels. For example, the redesign of revenue structures discussed above might include the provision that implementation of the automatic features would extend over the following fiscal year, unless specifically halted by the local jurisdiction governing body.

THE NEED FOR GREATER FISCAL INDEPENDENCE

We're all well aware of the lousy hand that cities have been dealt over the last twenty-five years in our ability to manage our fiscal affairs. These include the:

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- Loss of control over what had traditionally been the mainstay of city finances—local property taxes—with the passage of Proposition 13 in 1978.

- Requirements to reach agreement on tax sharing in annexations with counties.

- State budget grabs like ERAF in the mid-1990's, further devaluing the importance of property taxes, our most stable revenue source.

- Increased State mandates. (Forget about reimbursing us for them: how about just not taking funds away at the same time?)

- Changing nature of our economy from goods to services, and the inability of most of our local revenue bases to effectively capture this change; and in terms of the smaller market for goods that remains, increasing competition from catalog and Internet sales.

- And the most recent pair of deuces in a game where it takes at least two-pair just to break even: Propositions 62 and 218, which further limited the discretionary ability of local elected officials to balance services and revenues.

For the most part, our institutional response to these has been to rail against the lousy hand we've been dealt, and try to get the "house" (the State) to play more fairly, and stop stacking the deck against us. Given the poor treatment we've received and the continued "dealing from the bottom of the deck," our view of ourselves as innocent victims is not unreasonable – because we are. This makes our desire for redress and restitution—and our collective efforts through the League to get them – also reasonable and understandable. And in this case, collective effort is essential for any chance of success: no one city can make these changes happen alone. Moreover, as we've seen, even cities together cannot be successful: this requires forging coalitions with other local agencies and "stakeholders."

But let's be realistic: the outcome from these efforts is uncertain at best. Should the State restore ERAF? Of course it should. Did the Governor run four years ago and promise to restore ERAF? Yeah. To paraphrase John Lennon, is life what happens while you're busy making other plans? Well, yeah again. And really, did anyone who ever stole something fair and square ever give it back?

(Just think: Native Americans. On the other hand, not to overstress this card game metaphor, but they did ultimately get legal gaming, so may be there is something to just persevering long enough . . . . . And okay: let's give the devil his due: the State promised not steal any more away from us, and it has honored this commitment . . . . so far.)

The point is this: as individual cities, there is little we can do on our own to get dealt a better hand. (And as the saying goes: we can't we win; we can't fold; we can't even quit the game!)

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However, we believe there are opportunities to better play the hand we already have, and this is where we should focus on efforts: on the things we can control.

In short, we need to re-up on our efforts for fiscal independence, using the tools we already have. To try a different metaphor, we can't control the weather—but we can put on an overcoat and galoshes when it rains. (And this means we thought about the rainy season before it came, and went out and got ourselves an overcoat and galoshes before the winter storms arrived.)

So, what are the "galoshes" available to us?

There are several, most of which involve clear fiscal policies that set the financial foundation for decision-making. These should be our "global positioning systems" and radar in stormy weather, and include clear policies on the appropriate use of debt financing, avoidance of long-term commitments and use of one-time revenues for one-time costs. They should also include:

- User fee cost recovery policies and plans to minimize the use of limited general-purpose revenues for services where fees are possible, in order to free them up for other purposes.

- Minimum fund balance policies to provide greater flexibility and stability in dealing with revenue swings, unexpected expenditures and other contingencies.

- And revenue diversity: doing all you reasonably can to keep from putting all your eggs in one revenue basket.

Other "white papers" in this series deal with the first two topics; revenue diversity is the focus of this one.

STRATEGIC IMPORTANCE OF DIVERSITY

The authors are strong champions of the strategic importance of diversity as a key success factor in achieving fiscal independence.

First, because it just makes intuitive sense: the more you can spread the risk of any one revenue among many diverse sources, the more you can limit the impact of losses in any one area and better mitigate against downturns. In short, avoiding over-reliance on any one sector of the economy minimizes the adverse impacts when some (but not all) things inevitably go south. This is a fundamental principle of investment portfolio management, and it applies regardless of the size of your investments. And it is equally applicable to your revenues, whether you are a large city or a small one.

But secondly, transcending the theoretical stuff: because we've seen the powerful (and positive) impacts that it has had in our own cities. Not that either of our cities are Camelot and bulletproofed against recession – because we aren't. Our cities have seen tough times, too; and we'll see them again. However, because of our underlying policies and diversification of our revenues, we have perhaps been able to navigate rough seas better than many other cities.

Some examples from San Luis Obispo:

Yes, we are heavily reliant on sales tax revenues just like the rest of you. (It accounts for about 30% of our General Fund sources). But we are relatively diverse within this source: in many cities, the top 5 sales tax generators account for 50% of total sales tax revenues. In San Luis Obispo, we have to go to our 50th generator to reach 50%. Transient occupancy tax (TOT) is a big part of our revenue picture, too. (It's our "Number 3" General Fund revenue source.) But again, we are relatively diverse in where our TOT revenues come from by property. The same is also true for our property taxes.

And we are also fortunate to have a pretty diverse revenue base within our "Top Five" revenues: sales tax, property tax, TOT, utility users tax and vehicle license in-lieu (VLF). Each of these draws on something different that's happening in our local economy. For example, within sales tax, our revenues from general consumer goods have been down for the last two quarters, but strong new car sales have offset this. (It takes a lot of sweaters to equal a car!) At the same time – while utility user taxes have been lukewarm and TOT has been down – property taxes and VLF are doing well. Overall, while not spectacular, we have been able to achieve modest growth in the past year in our General Fund revenues, but only because of their diversity.

We saw this in the mid-1990's recession, too, where modest growth in utility user taxes and TOT (which are now headed in the opposite direction) helped get us through severe downturns in sales tax and stalled property tax revenues.

Lastly, there is San Luis Obispo's "poster child" for diversity: our business tax ordinance. Before 1991, when we broadened the base and taxed all businesses on gross receipts at the same rate previously applied to retail ($50 per $100,000 of gross receipts), business tax revenues were about $400,000 annually. Today, they are $1.4 million making this by far our best performing revenue source over the past ten years (250% growth). ***Why?*** Because it has a broad and diverse base, and we're able to capture growth in all areas of our local economy: services, professions, construction, manufacturing, retail and tourism. (Just about everything except for telecommunications and financial services – and only because the State has pre-empted us there.)

Where to from Here?

First, take some time to assess the diversity of your revenue base, both by type (sales tax versus property tax versus VLF) as well as by key generators within each the type: who are your principal property tax payers? Who are your principal sales tax producers? What happens if they hit a slow-down? Or, worse leave altogether?

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Secondly, if you find you are highly dependent on just a few key sources, adopt as a core fiscal health strategy the goal of diversifying them. This can take several forms, and some approaches will be more difficult than others. (For example, with the strong involvement and support from our business community, we were able to make the "structural" changes to our business tax ordinance back in 1991 with Council approval; today, under Proposition 218, this would require voter approval.) So, voter approval may be required to do some of these things. But that's still local control, and many communities throughout the State have been successful in attracting voter approval when they have had a compelling vision to offer.

In order to build community support, one strategy for gaining acceptance for the importance of diversification on its own merits is to propose changes that would initially be revenue neutral, such as reducing rates in one area while broadening the base in others. While this may not have immediate benefits, it will better position you for the future. And that's a critical factor for success in playing your hand as well as you can: making hay while the sun shines; closing the barn door before all the horses get out; repairing the roof before it rains. In short, through the use of solid fiscal policies: planning ahead.

SUMMARY

While we should certainly hope (and work together) for a better hand to play, the fact is that we do not control the dealer, nor – even if the dealer is an honest one – the inherent randomness of the draw. But we do control how we play the hand we have.

This doesn't mean forever accepting a rigged game, and giving-up on working hard to make it fairer. (Here comes another game analogy.) But it does mean making the best use of the arrows that we do have in our quiver—that if shot well (with an overall game plan) can make a powerful difference when they hit their mark. We believe that our quiver strategy should be fiscal independence, and that a conscious strategy of revenue diversity is one the most powerful arrows in that quiver.