

Issue: Revenue Opportunities

The City's revenue base has not kept up with the demand for service. What options does the City have for maintaining a revenue base that will keep pace with a growing community's needs?

Background:

The General Fund has been significantly impacted by State takeaways, changing legal interpretations and increasing expenditures both internally and outside of the City's control. As a result, Council and staff have worked together to develop and implement budget reduction scenarios for the last three years. Every effort has been made to achieve greater cost efficiencies and other fiscal strategies in order to preserve city services and ensure a certain quality of life for the citizens of Modesto. While citizens may not have noticed the decline, beginning in FY 2005-06 significant reductions to services will occur. Even on-going services will erode as growth continues. The programs and services impacted include Police, Fire, Parks, Streets, Economic Development, as well as other general government services.

Maintaining a revenue base that is diverse and is able to keep pace with the community's needs is critical to the prospects of any city. Reviewing revenue resources and options is a continuous process. As staff continues to propose and implement budget reductions, a review and discussion of potential increases to existing revenues and/or addition of new revenue sources becomes prudent. A change in the General Fund's major revenue sources or the addition of a comprehensive financing option has the ability to restore and sustain citizen's safety and quality of life programs and services.

The City of Modesto's major revenue sources include Sales Tax, Property Tax, Utility Users Tax (UUT), Vehicle License Fees, Business Licenses, Construction Fees, Franchise Tax, and the Transient Occupancy Tax (TOT). Many of these revenue sources vary in local control and risk. Over time, the ability of cities to levy taxes has been restricted by State actions and various voter-approved initiatives. The passage of Propositions 13, 62 and 218 has created and refined the distinction between **general** and **special** taxes.

Options:

Option 1: Sales Tax Increase

Modesto residents pay a sale and use tax of 7.375 cents per dollar (see **Financial Summaries** section of this document for city comparisons). Of this amount, the City actually receives one cent, from which Stanislaus County deducts 5% based on a 1950's flood control agreement. Recent changes in the law (SB566 2003) permit a city or county to place a local transaction and use tax proposal before the voters with a two-thirds vote of the governing board of the agency. A general tax proposal requires a majority voter approval. A special tax (earmarked for a particular purpose) requires a two-thirds voter approval.

Because of sales tax exceptions and other point of sale issues, a city will not see a 100% straight across-the-board increase. Base on a Modesto Sales District analysis, a factor of 82% will need to be applied to estimate the actual dollar increase. Examples shown below:

1/8% increased sales tax	=	\$3.8 million x 82%	=	\$3.1 million
1/4% increased sales tax	=	\$7.6 million x 82%	=	\$6.2 million
1/2% increased sales tax	=	\$15.3 million x 82%	=	\$12.5 million
3/4% increased sales tax	=	\$23.0 million x 82%	=	\$18.9 million
1% increased sales tax	=	\$30.5 million x 82%	=	\$25 million

What Other Agencies Have Tried

In the November 2004 election, five public agencies decided to propose a sales tax increase for **specific** purposes, such as public safety. Three of the five achieved the needed two-thirds vote. These results suggest overall that earmarking a tax for a special purpose is not worth the two-thirds vote requirement, and advisory votes do not appear to be worthwhile. It is interesting to note, however, that all citizen initiatives to repeal or limit taxes failed.

In November 2004, voters in twenty-two cities and five counties considered proposals to increase sale taxes for **general** purposes. Two of these were advisory votes. Of the twenty-two measures, ten passed.

Option 2: Property Tax Increase

Stanislaus residents pay a **general** property tax of 1%. Approximately 73% of the amount collected goes to the schools, 11% to the County, 5% to Redevelopment, 3% to Special Districts, and the City's share is about 7%. As a comparison, the assessed value of Stanislaus County is \$29 billion compared to San Joaquin's \$43 billion. That difference is 48% higher. Property taxes assessed value is 1% on the entire county; however, San Joaquin has a **higher base** than Stanislaus County.

This variance is due to Assembly Bill 8 (rate allocation), which occurred in the aftermath of Proposition 13. Proposition 13 set property values at one-percent of the assessed value and transferred control from local government to the State. AB-8 set up the allocation rate that each city would get and was tied into a formula that was based on block grant funds. Under AB-8, there were 6 counties (Stanislaus County is one of the 6) that were not awarded any additional property tax revenues.

The City of Modesto's AB-8 factor is 3.6%. Stockton's is 5.8%. This means Modesto receives 3.6% of the 1% assessed value of the county's property rolls while Stockton gets 5.8% of the 1% assessed value of their county's property rolls. The net result is twice as much property tax in their General Fund. **It would take legislation action to change the AB-8 factor.**

In November 2004, fifteen cities attempted a parcel tax for a **specific** purpose requiring a two-thirds voter approval with seven of the fifteen achieving voter approval.

A tax on each parcel could generate a stable base of new annual revenue for core city services such as public safety. The calculations based on 53,000 residential parcels are:

53,000 parcels x \$30 = \$1.6 million
53,000 parcels x \$50 = \$2.6 million
53,000 parcels x \$75 = \$4.0 million
53,000 parcels x \$100 = \$5.3 million
53,000 parcels x \$200 = \$10.6 million

Option 3: Formation of Special Assessment Districts

The California Constitution provides a method for local governments to assess property-related fees through the formation of assessment districts. Assessment districts could be formed for citywide landscaping and/or lighting urban forestry, or maintenance for medians and City facilities. An assessment is defined as “any levy or charge upon real property by an agency for a special benefit conferred upon the real property”. Funding generated by these assessments must be used for the specified purpose outlined in the initiative.

There are three funding strategies associated with an assessment.

1. Benefit Assessment District. This type of funding is used to link the cost of a public improvement or service to landowners who specifically benefit from the improvement. Balloting for a benefit assessment district is done through public hearing and ballots are mailed to landowners identified as benefiting from recommended improvements.
2. Special Assessment Tax. This type of funding is used to pay for public services and facilities that provide a general benefit. A general benefit does not require a direct relationship between the taxpayer’s benefits from the services provided. This requires a ballot measure during a general election and requires a 2/3 vote to pass.
3. Fee for Service. This is a charge imposed on an individual or property owner for a service or facility provided directly to that individual or landowner. This type of funding requires a public hearing and the approval of the City Council.

The City currently has Assessment District #29 (improvements located by the Mall) and Public Facilities #6 (pocket improvements throughout the City). These levies are placed on Stanislaus County’s tax roll and collected with the owner’s property taxes. The County then transmits payment to the City.

Option 4: Mello-Roos Community Facilities Tax

The Mello-Roos Community Facilities Act allows cities to enact a special tax within a defined district (which can encompass the entire city). Such a tax is used to finance a number of facilities and related services, *in conjunction with new development*. The authorized facilities allowable include parks, recreation and open-space, schools, libraries, childcare, street improvement and parking facilities. The authorized services include public safety, recreation programs, library programs, operations and maintenance cost for parks, open-space, museums and other cultural programs.

Option 5: Increases to General Fund Major Revenues:

- Utility Users Tax (UUT): The City of Modesto levies a 6% tax on the users of utilities such as electricity, water, telephone service, gas, and a 3% on cable television. The tax is capped at \$1,500 per taxpayer per utility, which limits the tax burden on businesses. This tax is unpopular and is susceptible to reduction attempts as it is viewed as regressive in nature. Most cities are in the 5-7% range.
- Business License Fees: The City of Modesto imposes an annual registration fee and gross receipts tax on firms doing business within the City. The tax rate is one dollar per thousand of sales for retail businesses and two dollars per thousand of sales on service businesses.
- Transient Occupancy Tax (TOT): The City of Modesto has a 9% tax on hotel and motel stays. In years past, portions of this revenue have been allocated to the Convention and Visitor's Bureau (CVB) and the Modesto Redevelopment Agency (RDA). A 1% increase generates about \$230,000.
- Construction Fees: The City of Modesto charges a variety of fees for building and planning activities, such as building permit fees and plan check fees. Different cities apply a construction tax based on valuation. Some cities require a supplemental payment to build within city limits based on the scarcity of infrastructure resources available.
- Franchise Tax: The City of Modesto has a franchise tax on solid waste businesses, cable television and gas and electric services. A Cable Franchise fee increase from 3% to 5% could potentially generate \$500,000. A Cable Franchise "pass through" of \$.25 to \$.55 per month per customer could generate \$150,000 to \$300,000.

Surveyed Revenue Options - Other Cities

Staff surveyed other cities on what type of new revenue options they were considering as shown below:

- Sharing the costs of repair and replacement of damaged sidewalks with homeowners.
- "Check Off " donations as voluntary donations to specific programs.
- Emergency 911 Fee to recover the costs of providing the local emergency service.

Key Elements of a Successful Revenue Measure Effort:

- Develop a ballot measure responsive to the public concerns: gather information about the public's concern through polling.
- Develop an ad hoc committee to work on recommendations.
- Develop a fiscal plan with accountability measures.
- Draft factual ballot language and persuasive ballot arguments.
- Gain unanimous support for the measure from Council.
- Educate the community

Recommendations:

Staff recommends the Council review the above revenue options and provide feedback and direction on which option(s) to pursue.