

TO: Honorable Mayor and City Council

FROM: Laura C. Kuhn, City Manager
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SUBJECT: AUTHORIZATION TO INITIATE AN ORDINANCE TO RENEW AND MODIFY THE TRANSACTIONS AND USE TAX PREVIOUSLY APPROVED AS MEASURE M FOR CONSIDERATION ON THE NOVEMBER 8, 2016 BALLOT

DISCUSSION:

At the June 14, 2016 City Council meeting, the City Council requested staff to bring back additional information for consideration of a tax measure to renew and modify Measure M that was approved by the voters in 2012. This measure would be for consideration of placement on the November 8, 2016 ballot. This report provides a review of the impact of Measure M on the City's finances, discussion of various continuing financial challenges and potential alternatives for a tax measure (or measures) for City Council consideration.

The Great Recession was a turbulent period for the City. To address a variety of issues, the City placed two tax measures on the ballot in November 2012, known as Measures I and M. These measures passed and have greatly assisted the City in its financial recovery. In addition to the additional revenues generated by these measures, the City Council took several actions to address various financial issues and new government accounting standards. The City Council established two policies, the first for the level of General Fund reserve, and the second to address how the City would provide funding to achieve the annual required contribution for the unfunded liability posed by our other post-employment benefits (OPEB). Through the help of Measure M, the City's General Fund reserve has been restored, albeit temporarily. Also, the City has made its first investment toward meeting its annual required contribution for retiree health care, but additional commitments are necessary. As shown in Attachment 1, Measure M has generated over \$4 million on an annual basis, or roughly \$4.8 million for Fiscal Year 2016.

Other areas of major progress resulting from Measure M include: (1) The City has reinstated some of its key staff positions lost during the recession; (2) The City has made great progress in rebuilding our fleet of equipment and vehicles; and, (3) The City has made major financial commitments to invest in its aging facilities and infrastructure.

The City's 5-year financial forecast shows the impact of Measure M's expiration in April 2018 (see Attachment 2). By the year 2019, it is expected that the General Fund Reserve will be depleted. Therefore, Measure M was successful in that it shored up the City's finances, but there continues to be additional issues that impact the long-term solvency of the City, such as:

- Aging infrastructure and buildings, as well as a competitive bidding environment, make it more and more difficult for the City to maintain its facilities, infrastructure and equipment.
- New state and federal mandates require additional local investment in general operations and services.
- Staffing levels have never recovered to pre-recession levels, while the demand for services continues to grow, and the City's inventory of facilities (such as parks and streets, and related infrastructure) continues to grow.
- PERS rates for employee pensions and health care costs continue to rise, such that they continue to eat up more of the overall budget.

- The City needs to continue making additional contributions towards the OPEB unfunded liability to ensure the long term health of the City.

Review of Alternative Tax Measures

Changes in the legal framework for local government funding, stemming as far back as Proposition 13 in the late 1980's, have resulted in significant losses of local tax revenues or created a system that triggers voter approval of additional funding sources. These changes have resulted in most local governments having to request their citizens to approve a variety of measures ranging from property or parcel taxes, special taxes, utility user taxes and, the most common, sales and transaction taxes. A summary of the current sales tax rates for similar Northern California cities, as well as the other cities in Solano County, are provided in Attachment 3. Most of the cities in Solano County have either approved moving forward with or are considering general tax measures to adopt new or extend previously approved measures. Therefore, Vacaville is not alone in considering renewal of Measure M. Regardless, Vacaville retains one of the lowest sales tax rates in the County.

The recent customer service poll (see Attachment 4) queried likely voters to see what level of potential support could exist for a sales tax measure in Vacaville. The highest ranking proposal would be a simple extension of the current ¼ percent sales tax. Other options include additional rates in quarter percent increments, up to a total of one percent. Another key consideration is the term of any renewal or modification. Measure M was originally passed for a 5-year period. A renewal could take the form of a 5-year or longer period, up to an indefinite period. Given the financial issues facing Vacaville, a simple 5-year renewal of a ¼ percent sales tax will not provide for financial solvency of the City. Attachment 5 provides an analysis of varying tax rates over the 5-year forecast period. Forecasts for longer periods of time are not provided due to lack of reliable data to guarantee major cost items that affect our forecast.

After considerable consideration, staff recommends that the tax rate be proposed to increase by ½ percent, for a total of ¾ percent. It is also recommended that the tax be proposed for a minimum period of 20 years. Should the City Council concur with this approach, the proposed language for the ballot question could be:

Vacaville Essential Services Protection Measure. *To protect essential city services such as police programs to fight domestic violence, child/elder abuse, gang activity and neighborhood crime; fire/paramedic services for quick emergency response times; street lighting for safety; and other city services, shall Ordinance 2016- be adopted renewing City of Vacaville's sales/use tax for 20 years at the rate of 0.75%, providing approximately \$14,700,000 per year in locally controlled funding that stays in Vacaville?*

The above language would be included in any ordinance brought forward at a future meeting of the City Council.

Transient Occupancy Tax and Marijuana Taxes:

The City Council also requested information on the Transient Occupancy Tax (TOT). Currently the TOT rate is 12%. This includes a base rate of 8%, Measure I rate of 2% and a 2% rate for Visit Vacaville. See the chart below, which demonstrates our current TOT rate in comparison to regional cities.

City TOT Rates

City	City TOT Rate	PLUS Extra TOT Rate	TOTAL TOT RATE
Concord	10.000%	3.000%	13.000%
Fairfield	10.000%	3.000%	13.000%
Vallejo	11.000%	(a)	11.000%
Walnut Creek	8.500%	1.000%	9.500%
Davis	12.000%	0.000%	12.000%
Sacramento	12.000%	(b)	12.000%
West Sacramento	12.000%	0.000%	12.000%
Napa	12.000%	2.000%	14.000%
Vacaville	8.000%	4.000%	12.000%
Roseville	6.000%	(c)	6.000%

Note - The City of Vacaville has 2% extra for Measure I and 2% for Visit Vacaville

(a) - Vallejo has a flat rate of \$2 per night for visitor's bureau

(b) - Sacramento has an additional 1-3% for visitor's bureau depending upon location

(c) - Roseville has an additional flat rate of \$1.50 per room night for visitor's bureau

While TOT taxes can be an attractive way to generate revenue for cities as they have little impact on the residents (as the tax is charged on local hotel rooms). An increase of 1% in the TOT rate would raise approximately \$174,500 annually for the City and would place Vacaville among the highest rates in the region. The funding from a TOT increase is based on the number of hotel rooms and the room rates, and therefore it would not generate enough tax revenues to resolve the longer term issues that face the City's General Fund. To ensure that the City's efforts are focused on the most beneficial form of tax measure overall, it is not recommended that a TOT measure be considered at this time.

The November 8, 2016 election will likely include at least one proposition to allow the recreational use of marijuana. As of this writing, one marijuana proposition is with the Secretary of State's Office to verify signatures to qualify for the election. This proposed proposition would impose a 15% sales tax on non-medical marijuana sales. (Note, medical marijuana sales would NOT be taxed under this proposition). Those funds would be distributed to numerous state agencies. The proposition does contain a provision for a County to impose its own tax on nonmedical marijuana, however, the proposition does not contain any language either allowing or barring a municipality from imposing its own tax. Currently, there is no way to determine what volume of recreational marijuana sales would be for the City of Vacaville and therefore, no way to estimate any potential revenue enhancements from a marijuana tax.

The down side of considering a tax on marijuana at this time is the unknown result of the proposition. Other cities who have passed marijuana taxes, but not allowed sales, have been faced with conflicting issues that passage of a tax on a non-allowed activity. Given these conflicts, it is recommended that the City await the outcome of the proposition and discuss options before moving forward with any taxation issues surrounding marijuana.

FISCAL IMPACT:

Measure M has provided \$14.8 million in additional funding for the past 3 years and is projected to provide an additional \$8.7 million over the rest of its term. These funds have covered operating deficits to maintain service levels, provided for the replacement of essential capital

equipment and facilities repairs, and restored General Fund reserves. However, the current rate of Measure M revenue, and its pending expiration do not provide for longer term stability of the City's reserves without significant cuts in services and without impacting the City's long term solvency.

RECOMMENDATION:

By simple motion, direct staff to prepare an ordinance to place a measure on the November 8, 2016 ballot to renew Measure M for a ¼ cent transactions and use tax and to increase the transactions and use tax by an additional ½ cent for an additional ¾ cent transaction and use tax for a period of 20 years.

ATTACHMENTS:

- Attachment 1 – Actual and Estimated Funding from Measure M
- Attachment 2 – Five Year Financial Forecast
- Attachment 3 – Customer Service Poll Results
- Attachment 4 – Comparison of Sales Tax Rates
- Attachment 5 – Forecasted Impacts of Tax Rate Alternatives