LEAGUE OF CALIFORNIA CITIES

Revenue and Taxation Policy Committee
Thursday, February 10, 2022
1:00 – 4:00 p.m.

Register for this meeting:
https://zoom.us/meeting/register/tJYude-qrzIjE9Xkjy4d1NvCyPok6TQ9yHjR
Immediately after registering, you will receive a link and confirmation email to join the meeting.

AGENDA

I. Welcome
Speakers: *Chair Norma Martinez-Rubin, Council Member, Pinole*
Vice Chair Charles Bourbeau, Council Member, Atascadero
Cal Cities President Cindy Silva, Mayor Pro Tem, Walnut Creek
Cal Cities Executive Director and CEO Carolyn Coleman

II. Public Comment

III. General Briefing *Informational*

IV. Cal Cities 2022 Action Agenda (*Attachment A*) *Informational*

V. Update Existing Policy and Guiding Principles (*Attachment B*) *Action*

VI. State Legislative and Budget Review *(Attachment C)* *Informational*

VII. Business Roundtable Ballot Measure Review *Informational*

VIII. City Managers Sales Tax Work Group Plan Briefing *Informational*

IX. Adoption of 2022 Work Program *Action*

X. Adjourn

Next Virtual Meeting: Thursday, April 28, 1:00 pm – 4:00 pm

Brown Act Reminder: The League of California Cities' Board of Directors has a policy of complying with the spirit of open meeting laws. Generally, off-agenda items may be taken up only if:
1) Two-thirds of the policy committee members find a need for immediate action exists and the need to take action came to the attention of the policy committee after the agenda was prepared (Note: If fewer than two-thirds of policy committee members are present, taking up an off-agenda item requires a unanimous vote); or
2) A majority of the policy committee finds an emergency (for example: work stoppage or disaster) exists.

A majority of a city council may not, consistent with the Brown Act, discuss specific substantive issues among themselves at League meetings. Any such discussion is subject to the Brown Act and must occur in a meeting that complies with its requirements.

ATTACHMENT A

League of California Cities 2022 Action Agenda

1. **Secure funding to increase the supply and affordability of housing and reform state housing laws to retain local authority.** Secure adequate and sustainable funding for cities to increase construction of housing at all income levels, particularly affordable housing and workforce housing. Reform state housing laws to ensure cities retain local decision-making to meet the needs of their communities.

2. **Attain investments to strengthen and sustain critical infrastructure.** Advocate for policies that strengthen the conditions of local streets, highways, bridges, public transit, and broadband to improve workforce and economic development. Secure support for the modernization and expansion of the statewide water grid, including infrastructure, storage, and conveyance. Work with stakeholders to provide cities with access to the tools needed to ensure projects are delivered efficiently and cost-effectively to meet current and future needs.

3. **Secure increased funding and resources to prevent homelessness and assist individuals experiencing homelessness.** Secure additional ongoing, flexible resources to provide navigation assistance, emergency shelters, and permanent supportive housing. Enhance city and county coordination and strengthen partnerships with stakeholders to ensure adequate wraparound services are available for adults and youth at risk of, or already experiencing, homelessness in our communities, and effectively address mental health and substance use disorders.

4. **Strengthen disaster preparedness, resiliency, and recovery from climate change impacts through improved collaboration and resources.** Secure additional resources and support to mitigate the effects of climate change, including catastrophic wildfires, drought, and sea level rise. Promote collaboration with other city, state, and federal governments, to strengthen disaster preparedness, resiliency, and recovery.

ATTACHMENT B

Summary of Existing Policies and Guiding Principles
February 2022

Revenue and Taxation

Scope of Responsibility

The Committee on Revenue and Taxation reviews issues related to finance administration, taxation reform, revenue needs, and revenue sources at the federal, state and local levels.

Summary of Existing Policy and Guiding Principles

Cities and Cal Cities

<u>Preamble</u>
Inherent in these recommendations is the underlying principle that meaningful fiscal reform should allow each level of government to adequately finance its service responsibilities, with each being accountable to taxpayers for its own programs.

<u>Efficiency</u>
Cities and Cal Cities should continue to emphasize efficiency and effectiveness, encouraging
and assisting cities to achieve the best possible use of city resources.

<u>Authority and Accountability</u>
Cities must locally achieve political authority and accountability for revenues raised and services provided. For accountability, revenues should be logically linked to traditional and emerging responsibilities. Cities must effectively communicate the good news about city programs and operations, as well as information concerning financial conditions and city responsibilities.

<u>Alliances</u>
Cities should seek alliances with counties, schools, other cities, employee organizations, other local agencies, ~~**and**~~ business and professional organizations**<u>, and nonprofit organizations</u>** to support cooperation, sound financial policies and joint action.

<u>Initiative</u>
Cities and Cal Cities are prepared to use the statewide initiative process, if necessary, to secure fiscal independence and a sound intergovernmental financial structure. Initiative efforts should, to the extent feasible, incorporate and, in no case violate, the principles developed by the Fiscal Reform Task Force as follows:

- Cities require a greater share of the property tax and other reliable, discretionary revenues in order to finance local services to property.

- Cities require constitutional protection of their revenue sources in order to provide insurance against diversion by the state of these revenues in the future for non-municipal purposes.
- Major reforms in the unfunded mandate reimbursement process should be enacted to make it more workable and meaningful.

Legislature or the Voters

<u>Local Authority and Accountability</u>
To preserve local authority and accountability for cities, state policies must:

- Ensure the integrity of existing city revenue sources for all cities, including the city share and situs allocation, where applicable, of property tax, sales tax, vehicle license fees, etc.
- **<u>Ensure the integrity of city revenue sources by providing fraud deterrence and enforcement tools that improve the collection of public funds.</u>**
- Protect the authority of local governments to collect revenues from telecommunications providers and ensure that any future changes are revenue neutral for local governments.
- Oppose any state or federal legislation that would pre-empt or threaten local taxation authority including but not limited to Utility User's Taxes.
- Allow every level of government to enjoy budgetary independence from programs and costs imposed by other levels of government.
- Authorize a simple majority of the voters in a city or county to establish local priorities, including the right to increase taxes or issue general obligation bonds.
- Offer incentives to reward cities achieving program goals rather than withhold or reduce revenues to accomplish targets.

<u>State Legislative and Budget Reforms</u>.
To stabilize state funding and programs and reverse the trend of the state's reliance on local revenues to solve the state's fiscal crises, the state should implement fiscal and legislative reforms which may include for consideration the following:

- A two-year spending plan with the first session focused on expenditures over the period.
- Oversight hearings that review programs for savings, duplication or gaps in services.
- Limits on the number of bills that legislators may introduce.
- A prudent reserve fund.
- Official records kept of all Assembly and Senate official meetings.
- A balanced deficit reduction approach, which could include temporary revenue increases dedicated solely to retiring short-term debt, spending cuts, short-term borrowing and multi-year spending limitations.
- Long term restructuring measures, including increased local government property tax shares to create balanced growth and separate budget detail of all state expenditures at local level.

State Mandates

The state must provide full and prompt reimbursement to all local agencies for all state-mandated programs and/or infractions and losses associated with local revenue shifts.

Local agencies must be authorized to petition the Commission on State Mandates immediately after legislation is chaptered for determination of eligibility for reimbursement and reserve the right to directly pursue court intervention without an administrative appeals process.

Reforms are needed in the mandate approval and reimbursement process.

The State should be prohibited from deferring mandate payments.

Unless specifically requested by a city, no new duties, responsibilities or obligations should be assigned to a city or cities under state realignment.

Additional Revenue

Additional revenue is required in the state/local revenue structure. There is not enough money generated by the current system or allocated to the local level by the current system to meet the requirements of a growing population and deteriorating services and facilities.

When disasters **or emergencies** occur **statewide or** in various areas of the state, state government has traditionally stepped in to assist with recovery efforts through various means, including the passage of legislation to provide income and property tax relief to affected individuals and businesses, and reimbursing local governments for their losses. Cal Cities supports disaster recovery legislation that includes mitigation for losses experienced by local governments. **Cal Cities supports this aid being allocated to cities through a process that objectively accounts for the impacts that a disaster or emergency has had on a city's residents, infrastructure, economy, and revenues. In the event that aid is provided solely on a per-capita basis, Cal Cities support that it be done equally per resident.**

Cal Cities also supports establishing a federal debt guarantee program that supports state catastrophe insurance programs for post-event debt that they incur as a result of paying for insured losses caused by major natural catastrophes.

Cal Cities supports legislation that would make adjustments to the vehicle license fee-property tax swap of 2004 to ensure that the formula appropriately accounts for city incorporations and annexations of inhabited territory.

Cal Cities supports legislation that would bolster existing local efforts to enforce local ordinances and revenue collection associated with short-term rentals. **Legislation must protect local transient occupancy tax collection authority, tax rates, and enforcement authority associated with short-term rentals.**

Reduce Competition

Revenue from new regional or state taxes or from increased sales tax rates should be distributed in a way that reduces competition for situs-based revenue. (Revenue from the existing sales tax rate and base, including future growth from increased sales or the opening of new retail centers, should continue to be returned to the point of sale.)

The existing situs-based sales tax under the Bradley Burns 1% baseline should be preserved and protected.

Tax proceeds collected from internet sales should be allocated to the location where the product is received by the purchaser.

Restrictions should be implemented and enforced to prohibit the enactment of agreements designed to circumvent the principle of situs-based sales and redirect or divert sales tax revenues from other communities, when the physical location of the affected businesses does not change.

Sales tax rebate agreements involving online retailers are inappropriate because they have the effect of encouraging revenue to be shifted away from numerous communities and concentrated to the benefit of one. Any type of agreement that seeks to lure a retailer from one community to another within a market area should also be prohibited going forward.

Funding for Counties

Counties require additional funding if they are to fulfill their state-mandated and traditional roles.

As legal agents of the state, county expenditures in that capacity should be funded by the state. Their local programs should be financed locally.
The concept of "self-help" for counties should be expanded. An example might be that counties could receive certain state funding if they raise a specified level of revenue locally.

To alleviate competition among cities and counties, funding for counties should be accompanied by agreements on new development in undeveloped areas within the cities' sphere of influence.

Regional Revenues

Local government issues, programs, and services do not always recognize local government jurisdictional boundaries. In cases where regional issues, programs, and services are identified, multi-jurisdictional revenues should then be identified and implemented. As an example, the sales tax has been considered and used by many countywide areas to address multi-jurisdictional transportation issues.

Support regional cooperation on common interests and goals by providing access to share incremental growth in ERAF property tax.

Revenue Modernization

Property Tax
Cal Cities supports legislation which would clarify and improve the definition of "change of ownership" for property tax reassessment purposes to include when more than 90 percent of direct or indirect ownership interests in a legal entity are cumulatively transferred in one or more transactions. Such changes would reduce the use of complicated strategies employed to evade reassessment of property upon changes of ownership.

Sales Tax

- Sales and Use Tax Base: Cal Cities supports modernization to the sales tax through measures that would either broaden the tax base on goods, which includes reviewing existing exemptions on certain goods and expanding to digital forms of goods that are otherwise taxed, and expanding the sales tax base to services, such as those commonly taxed in other states. Specific proposals in these areas should be carefully reviewed so that the impacts of any changes are fully understood.

- Sales Tax Sourcing Rules: Support as Cal Cities policy that point of sale (situs) is where the customer receives the product. Specific proposals in this area should be carefully reviewed so that the impacts of any changes are fully understood.

  Cal Cities supports as policy allowing more direct reporting of use taxes related to construction projects to the jurisdiction where the construction activity is located by reducing existing regulatory threshold from $5 million to $100,000.

- County Pool Use Tax Allocations: Support Cal Cities working with the state California Department of Tax and Fee Administration to update the county pool allocation process to ensure that more revenues are allocated to the jurisdiction where the purchase or first use of a product occurs (usually where the product is delivered). Use Tax collections from online sales, including from the *South Dakota v Wayfair* Decision, should be shifted out of county pools and allocated to the destination jurisdiction whose Bradley Burns tax applies and not throughout the entire county.

- State Sales Tax Exemptions: Cal Cities opposes state legislation that proposes to grant exemptions for specific products that fails to protect those portions of the sales tax that are dedicated to local government.

- **Data Collection: Cal Cities supports efforts to modernize statewide sales tax data collection to improve understanding of out-of-state and in-state remote sales.**

Federal Streamlined Sales and Use Tax Agreement (SSUTA)

There are more questions than answers for California cities about potential state participation in the SSUTA. The SSUTA offers many more risks for California cities than benefits. Thus, Cal Cities should:

- Continue to monitor developments of the SSUTA and related federal legislations, but not support any additional efforts that would lead to California joining the agreement. This position can always be revisited at a future point if events change.
- Strongly oppose any federal effort that attempts to force California to conform to the Agreement, or amendments to federal legislation that would directly undermine California's utility user tax structure.
- Work with the California Department of Tax and Fee Administration and other parties on alternative efforts to increase the collection of use taxes within California. Share Cal Cities analysis of the SSUTA with interested parties, exchange information on use tax collection issues with municipal Leagues in other states, including those states with tax structures similar to California.

Federal Legislation Requiring Use Tax Collection

Cal Cities supports federal legislation that would require the collection of use tax from internet or "remote sales" that meets the following conditions:

- Is limited to the collection of sales and use taxes.
- Does not require states to participate in the SSUTA.
- Requires remote sellers to collect the full destination rate (combination of state and local rate at location the product will be delivered).
- Exempts intrastate (non-remote sales within California) from the destination rule.
- Provides sufficient flexibility to accommodate California's tax structure. (There are instances where the state, for policy reasons, has opted not to collect the state's share of sales taxes on an item, but the local rates on those items are still collected).

State regulatory actions and possible legislation may be needed to address issues raised by the collection of new revenue from remote sales. Implementation by the California Department of Tax and Fee Administration would likely require appropriate software for remote sellers to implement the new system.

Note: Cal Cities will review new legislation to determine how it relates to existing Cal Cities policies and guiding principles. In addition, because this document is updated every two years to include policies and guiding principles adopted by Cal Cities during the previous two years, there may be new, evolving policies under consideration or adopted by Cal Cities that are not reflected in the current version of this document. However, all policies adopted by Cal Cities Board of Directors or Cal Cities General Assembly become Cal Cities policy and are binding on Cal Cities, regardless of when they are adopted and whether they appear in the current version of "Summary of Existing Policies and Guiding Principles."

ATTACHMENT C

Revenue and Taxation Policy Committee
Legislative Agenda

Staff: Jessica Sankus, Senior Policy & Legislative Affairs Analyst, (916) 658-8283
Nick Romo, Legislative Representative, (916) 658-8232

Staff Policy Proposal: ***Supplemental Payments for Cities with Populations Impacted by Natural Disasters and Significant Economic Disruptions.***

Summary and Update to 2021 Staff Report:
At the June 2021 Revenue and Taxation Policy Committee meeting, the committee unanimously directed staff to explore and provide solutions for future consideration regarding options for mitigating drastic revenue losses from state programs allocated in part by population (i.e., local streets and roads funding). Cities that experienced major population loss since the last federal decennial census, such as those who have experienced natural disasters in the previous decade, are most impacted and were therefore the focus of these efforts.

Background:
Revenue and Taxation Code Section 11005.3 provides a methodology for determining the populations of cities and counties for the purpose of allocating many state revenues among local agencies. As interpreted by the State Controller's Office (SCO), a city's population, for the purpose of allocation of revenues, is the population determined by the most recent U.S. Census or a subsequent estimate prepared by the California Department of Finance, (DOF) whichever is greater.

As a result, a city with a sudden decline in population, for example due to a significant natural disaster, retains a level of revenue allocation based on their highest population estimate in a given decade, until the next decennial census. Therefore, for a period, a city is protected from drastic population-based revenue losses, which assists with the city's transition and recovery. This revenue drop-off "protection" effectively ends with the implementation of new federal census figures, which capture the city's population loss for the next decade (until the subsequent census count).

The 2020 federal census was released in mid-2021. The 2020 Census Count Question Resolution program, the means by which local governments and others may request a review of their official 2020 Census results, will be operational from fall 2021 until approximately September 2023.[1]

Following the federal decennial census, using this data as a basis, the DOF Demographic Research Unit annually prepares updates including revised, city, county and state population estimates. DOF may also provide a revised estimate upon the request of a city or county, for example in the case of an annexation or new incorporation.

[1] 2020 Census Count Question Resolution Operation

These population estimates are used by the state for apportionments to local governments for a variety of population-based funding allocations. A chief example is Local Streets and Roads revenue, which is the result of a per-gallon excise taxes on gasoline and diesel fuel, sales taxes on gasoline and diesel fuel and registration taxes on motor vehicles with allocations dedicated to transportation purposes.

The local (city and county) portions of these allocations flow through the Highway Users Tax Account (HUTA), the familiar gasoline tax revenues that have been in place for decades, and the Road Maintenance and Rehabilitation Account (RMRA) which allocates much of the revenue from the Road Repair and Accountability Act of 2017 (SB 1, Beall).[2]

Fiscal Impact:
Generally, Local Streets and Roads revenue allocations are pooled among cities (and among counties), the effect of any population adjustment is only on other cities, or on other counties in the case of a county adjustment. Without accommodations, cities that experience major disasters such wildfires may lose vast portions of their population and therefore proportionate loss of state population-based revenues, which impedes recovery.

For example, following the 2018 Camp Fire, the town of Paradise's population decreased from 26,218 to 4,608, or 84.2 percent of its population. Cal Cities staff estimates that Paradise will consequently lose as much as
$11 million of local streets and roads revenue over the next decade.

Existing Cal Cities Policy:
Additional Revenue

When disasters occur in various areas of the state, state government has traditionally stepped in to assist with recovery efforts through various means, including the passage of legislation to provide income and property tax relief to affected individuals and businesses, and reimbursing local governments for their losses. Cal Cities supports disaster recovery legislation that includes mitigation for losses experienced by local governments.

Staff Comments: Staff studied and considered the following options for policy and statutory changes:

- Amend the Revenue and Taxation Code to provide that the highest state or federal population estimate, either the most recent state estimate, or the preceding federal census, be used for the purpose of revenue allocation for local governments with economically significant population loss that meet specified qualifications.

[2] California Local Government Finance Almanac; Coleman

- Amend the Streets and Highways Code to provide supplemental payments for cities that meet specified qualifications to backfill the lost revenue resulting from significant population lost to aid economic recovery.

- Amend the California Disaster Assistance Act to add local streets and roads to the list of allowable projects for local governments with economically significant population loss that have experienced a natural disaster and would also add wildfires between 2018-2021 to the list of events that are eligible for 100 percent of total state eligible costs, instead of 75 percent.

- Provide supplemental payments for cities that meet specified qualifications to backfill the lost revenue resulting from significant population lost to aid economic recovery via provisional language in the annual state Budget Act, with no other statutory amendments.

Staff Recommendation:
Staff recommends reaffirmation of existing Cal Cities policies which supports supplemental payments for affected cities in the annual state Budget Act to mitigate significant impacts to local streets and roads programs due to recent natural disasters, significant economic disruptions, and pandemic-related census count issues. Staff concluded that the alternative policies and statutory changes considered and described above have many unknown variables or could result in unintended consequences of detriment to cities including sudden loss of streets and roads funding.

A case-by-case appropriation of supplemental payments allows Cal Cities to take into consideration the unique needs of each city and tailor budgetary requests to meet those needs, and to avoid statutory changes that are overly prescriptive or have unintentional impacts.

Committee Recommendation:

Board Recommendation: