What Today’s Fire Chiefs Need to Know About Municipal Finance

Michael Coleman
coleman@muniwest.com
530.219.3691

Cities Vary ... Counties Vary ... Special Districts Vary ... and so do their finances.

- Geography: proximity, climate, terrain, access
- Community Character / Vision: Land use
- Size – urban / rural
- Governance / service responsibilities
  full service city - vs. - not full service city

❖ Statewide generalizations often mask trends among sub-groups
Taxes

✓ Charges which pay for public services, facilities that provide general benefits.
   No need for direct relationship between a taxpayer’s benefit and tax paid.
✓ Cities may impose any tax not otherwise prohibited by state law.
   (Gov Code § 37100.5)
✓ The state has reserved a number of taxes for its own purposes including:
   cigarette taxes, alcohol taxes, personal income taxes.
✓ General & Special
   □ General Tax - revenues may be used for any purpose.
      Majority voter approval required for new or increased local tax
   □ Special Tax - revenues must be used for a specific purpose.
      2/3 voter approval required for new or increased local tax
      Parcel tax - requires 2/3 vote

Everything is a Tax Except ...

California Constitution per Prop26

Any levy, charge or exaction of any kind imposed by a California government, is a tax except:

1 & 2. A charge imposed for a specific benefit, privilege, service or product, granted directly to the payor that is not provided to those not charged...

3. A charge imposed for the reasonable regulatory costs for issuing licenses and permits, performing investigations, inspections, and audits … and the enforcement and adjudication thereof.

4. A charge imposed for entrance to, use of, purchase, rental, or lease of local government property.

5. A fine, penalty, or other monetary charge imposed as a result of a violation of law.

6. A charge imposed as a condition of property development.

7. Assessments and property-related fees imposed in accordance with …Article XIII D.
   A charge not “imposed”
### Taxes and Fees/etc. Approval Requirements

*(California Constitution)*

<table>
<thead>
<tr>
<th></th>
<th>TAX- General</th>
<th>TAX- Parcel or Special (earmarked)</th>
<th>G.O.BOND (w/tax)</th>
<th>Fee / fine / rent</th>
</tr>
</thead>
<tbody>
<tr>
<td>City / County</td>
<td>Majority voter approval</td>
<td>Two-thirds voter approval</td>
<td>Two-thirds voter approval</td>
<td>Majority of the governing board.*</td>
</tr>
<tr>
<td>Special District</td>
<td>n/a</td>
<td>Two-thirds voter approval</td>
<td>Two-thirds voter approval</td>
<td>Majority of the governing board.*</td>
</tr>
<tr>
<td>K-14 School</td>
<td>n/a</td>
<td>Two-thirds voter approval (parcel tax)</td>
<td>55% voter approval*</td>
<td>Majority of the governing board.*</td>
</tr>
<tr>
<td>State</td>
<td>For any law that will increase taxes of any taxpayer, two-thirds of each house of the Legislature ...or majority of statewide voters.</td>
<td>Statewide majority voter approval</td>
<td>Majority of each house.</td>
<td></td>
</tr>
</tbody>
</table>

---

### California City Revenues

- **Taxes**
- **Fees**
- **State/Fed Aid**
- **Rents, penalties**
- **Other**

**Not Restricted 36%**

- **Utility Fees** (Water, Sewer, Refuse, Electric, Gas, etc.) 29%
- **Other Fees** 12%
- **Benefit Assessments** 2%
- **Federal Grants** 5%
- **State Grants** 4%
- **Special Taxes** 3%
- **Sales Tax** 7%
- **Property Tax 14%**
- **Bus Lic Tax 2%**
- **Utility User Tax 3%**
- **Trans Occ Tax 2%**
- **Other Tax 3%**
- **Franchises 2%**
- **State & Fed <1%**
- **Other 3%**

**Source:** Author’s computations from California State Controller data. Does not include the City/County of San Francisco.
Counties are hybrid local/state

- state/federal programs: Aid to families (CalWORKS), food stamps, foster care, In-Home Support Services (IHSS), alcohol & drug treatment
- countywide services: jails, courts, elections, property tax collection & allocation
- “city” services to unincorporated areas

Counties have

- more mandates,
- less discretionary $, and
- are more vulnerable to state budgetary action

Source: Author’s computations from California State Controller 2014-15 data. Includes the City/County of San Francisco.
California Special District Revenues

- **Typical Non-Enterprise District** (e.g., fire, parks, library)
  - Licenses, Permits <1%
  - Federal Grants <1%
  - State Grants <1%
  - Service Fees 22%
  - Other Revenues 11%
  - Property Taxes / Assessments 65%
  - Interest, Rents <1%

- **Typical Enterprise District** (e.g., water, sanitation)
  - Property Taxes / Assessments 2%
  - Interest, Rents 9%
  - Other Revenues <1%
  - Service Fees 89%

Source: Author's computations from California State Controller data.

Where Your Property Tax Goes

- **Typical city resident**

  - **Shares Vary!**
    - Non-Full service cities: portion of city shares go to special districts (e.g. fire)
    - Pre-prop13 tax rates
    - Every city, county gets Prop-Tax In Lieu of VLF.

  Includes Property Tax in-lieu of VLF.

Typical homeowner in a full service city not in a redevelopment area.
For taxable sales in unincorporated areas, the local 1% rate goes to the county.

Initiative #21-0042A1

Huge Threat to Public Services

Draconian, Impractical Ballot Initiative Headed to the November 2024 Ballot
Draconian, Impractical Ballot Initiative – November 2024

Initiative #21-0042A1: Limits Ability of Voters and State and Local Governments to Raise Revenues for Government Services. Initiative Constitutional Amendment

Chokes local tax authority. Requires:
- Requires voter approval for taxes applied to territory that is annexed
- Requires sunset date on all new taxes
- General tax ballot label must say “for general government use”
- Repeals Upland exception for initiative special taxes
- Local tax advisory measures are prohibited (the Measure A/B approach).

Restricts local fee authority
- Fees by limiting limited “actual cost” of providing the product or service for which the fee is charged. “Actual cost” is defined as the “minimum amount necessary.”
- Fees - including for use of government property - must be “reasonable to the payor”
- Repeals fee for “special benefit” exception to Prop 26 “tax” definition
- Fees must be adopted by legislative body by ordinance, not staff or a commission
- Changes legal standard from “preponderance of the evidence” to “clear and convincing evidence” to prove a fee or charge is not a tax and does not exceed “actual cost.”
Draconian, Impractical Ballot Initiative – November 2024

Initiative #21-0042A1: Limits Ability of Voters and State and Local Governments to Raise Revenues for Government Services. Initiative Constitutional Amendment

Also ...

▪ Fines require “adjudicatory process”
▪ No VMT tax or fee as condition of development or occupancy
▪ Retroactive window: taxes, fees approved after Jan 1, 2022 will sunset in Dec 2025 if not readopted in compliance with the initiative
  • At least $2 billion of taxes approved in 2022-2024 must be re-adopted in 2025
  New ballot language, new sunsets, new voter thresholds
  • $ Billions of fees must be readopted to comply in 2025

A Brief Look at the California Municipal Financial Health Diagnostic Tool
Bad Brew in Troubled Cities

- Over-reliance on land development revenue
- Risky financing schemes
- Fear and Denial
- Toxic Relationships
- Ceding of management and policy choices to others
- Unsustainable / intractable employee compensation esp. public safety pension, retiree health care
- Unsustainable decline in core revenues

Defining Municipal Financial Health

Solvency

1. **cash solvency** - ability to meet immediate financial obligations; i.e. over next 30 or 60 days (accts payable, payroll).

2. **budgetary solvency** - ability to meet all financial obligations during a budget year.

3. **long-run solvency** – ability to meet all financial obligations into the future.

4. **service-level solvency** – ability to provide the desired level of services for the general health and welfare of the community.
Difficulties in Assessing Municipal Financial Health

- Published data are not complete or timely.
- Do we know what the numbers mean? Are they enough to draw conclusions?
- Comparisons are often false.
- Requires analysis, forecasting, context, legal
  - *it’s not just an accounting or statistical exercise*
  - *history doesn’t tell you enough about the future*

You Need a Financial Health Diagnostic

- **Validate** areas in which your city is *fiscally healthy*
- **Identify problems**, areas to *improve*
- **Act to remedy** problems *before* they get worse or unmanageable
- **Avoid being blind-sided** by problems
- **Add credibility** to your fiscal evaluation
- **Help others** (labor associations, taxpayers and other interested parties) *understand* your financial position
### Our Approach

**California Municipal Financial Health Diagnostic:**

- Get to the primary indicators - useful & essential
- Leave out extraneous / secondary
- Add in overlooked & underappreciated factors
- Drill down to the real numbers
- Allow for nuance / clarification / differences
- Reduce invalid conclusions and comparisons
- Constructive, thoughtful approach

### The California Municipal Financial Health Diagnostic

<table>
<thead>
<tr>
<th>Financial Health Indicators - Summary Checklist</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Net Operating deficit/surplus. There are no recurring general fund operating deficits. General revenues are sufficient to meet the net general revenue demand of programs.</td>
</tr>
<tr>
<td>2. Fund balance. Reserves are sufficient over multiple conservative years and in compliance with adopted policy.</td>
</tr>
<tr>
<td>3. Capital Asset Condition. The city is keeping pace with the upkeep of its capital assets.</td>
</tr>
<tr>
<td>4. Utilization. Cash and short-term investments are sufficient to cover current liabilities (including short-term debt and accounts payable within 60 days).</td>
</tr>
<tr>
<td>5. Fixed costs (including debt service and other contractual obligations). Salaries and benefits are stable or decreasing over multiple years relative to reasonably expected revenue growth.</td>
</tr>
<tr>
<td>6. General fund subsidies of other funds. Any general fund subsidies other enterprises or special funds are sustainable and in compliance with adopted policy.</td>
</tr>
<tr>
<td>7. Constraints on budgetary discretion. The city council’s authority to make budget changes is not excessively constrained by charter, statute, or law.</td>
</tr>
<tr>
<td>8. Balancing the budget with temporary funds. The use of reserves, selling assets, deferring asset maintenance to balance the general fund has been limited, prudent, and in compliance with adopted policy.</td>
</tr>
<tr>
<td>9. Balancing the budget with borrowing. The use of short-term borrowing, internal borrowing, or transfer from special funds to balance the general fund has been limited, prudent, and in compliance with adopted policy.</td>
</tr>
<tr>
<td>10. Balancing the budget by deferring employees compensation costs. Pension liabilities and other non-salary benefits have been determined, disclosed, and actuarially funded in compliance with adopted policy.</td>
</tr>
<tr>
<td>11. Balancing the budget with back-loaded deferred service payments. Debt service payments have not been ‘back-loaded’ into future years.</td>
</tr>
<tr>
<td>12. Funding operating costs with non-recurring revenues. Ongoing operating costs are being funded with ongoing rather than temporary revenues (e.g., bond development, etc.).</td>
</tr>
<tr>
<td>13. Timeliness and accuracy of financial reports. Financial reports are being filed on time (CAR, Annual Audit, State Controller’s Financial Transactions Report).</td>
</tr>
<tr>
<td>14. Service level/solvency. Public service levels meet the standards and needs in this community.</td>
</tr>
</tbody>
</table>
The Importance of Good Financial Policies

- Use of temporary funds
- Reserves, fund balance
- Short-term borrowing
- Interfund transfers
- Payment of Employee comp costs (pension, OPEB)
- Payment of Unfunded Liabilities
- Pay-as-you-go financing
- Debt management and affordability
- Long Range Financial Planning

Essential Element of Financial Strength: Multi-Year Budget Forecasting

**Financial**
- Improves understanding of major revenue and expense budget drivers
- Identifies structural budget issues

**Strategic**
- Promotes long-term view
- Informs policy decisions e.g. impact on reserves, budget sustainability