ATTACHMENT

CITY COUNCIL AGENDA REPORT

MEETING DATE: July 10, 2000 ITEM NUMBER:

SUBJECT: POTENTIAL INCREASE IN THE TRANSIENT OCCUPANCY TAX (T.O.T.) FOR PARK AND OPEN SPACE ACQUISITION AND DEVELOPMENT

DATE: JULY 7, 2000

FROM: CITY MANAGER'S DEPARTMENT

PRESENTATION BY: ALLAN L. ROEDER, CITY MANAGER

FOR FURTHER INFORMATION CONTACT: ALLAN L. ROEDER, CITY MANAGER (714) 754-5327

RECOMMENDED ACTION:

Review and comment.

BACKGROUND:

The City Council adopted Community Objective 01-C3 in January 2000. The Community Objective, requested by Council Member Joe Erickson, requests that the City Council consider placement of a measure on the June 2000 Primary Ballot to increase the Transient Occupancy Tax (TOT) by 2% to be dedicated to the acquisition and development of Park and Open Space. The Objective goes on to request that the matter be discussed with the Costa Mesa Tourism & Promotion Council as well as with the Newport Mesa Unified School District (NMUSD). The later direction related to consideration as to when the NMUSD would place its bond measure for school repairs before the voters. That measure was voted on in June 2000 and received the required two-thirds voter approval.

As of this date, the majority of the City Council Members have attended at least one meeting with the Costa Mesa Tourism & Promotion Council where the subject of the proposed increase was discussed. The Tourism Council, comprised of the seven largest hotels in Costa Mesa, has expressed concern with the concept of a 2% increase in the TOT on the basis that it may impact their ability to remain competitive in the marketplace. A 1% increase appears to be much more acceptable to the hotels although no official position has been taken on an increase in the TOT by either the Tourism Council or the other hotels/motels in the community.

ANALYSIS:

While there are several detailed steps required in placing this issue before the voters, there are five (5) decisions that require City Council consideration and action. Those topics are as follows:

- Does the City Council choose to obtain voter approval for a "General Tax" requiring a simple majority or a "Special Tax" which requires two thirds voter approval?
- If a Special Tax is requested, to what use should the funds be restricted?
- When should the issue be placed before the electorate?
- How should the election be funded?
- Does the City Council desire to submit a ballot argument in favor of the measure and who shall sign the argument?

Attachment A, prepared by the City Attorney's Office, responds to the relevant issues involved in the first decision. Basically, should the City Council choose to restrict the use of the proceeds from an increase in the TOT, a two thirds approval will be required from those voters casting ballots in the subject election. Should use of the proceeds be unspecified, a simple majority approval is required. In either event, a two thirds approval of the City Council is required to place the matter on the ballot.

There are at least four different ways in which the matter may appear on the ballot:

1. The City Council may simply request voter approval to increase the TOT by a specified percentage without designating the use of the proceeds from the tax increase.

2. The City Council may request approval of an increase in the TOT to a specified level with the proceeds to be designated for a limited use.

3. The City Council may request voter authorization to increase the TOT to a specified level. In so doing, the City Council would retain the authority to increase the TOT from it's current level of 6% up to the specified level or any point in between.

4. The City Council may place a two-part measure on the ballot. The first part would request voter authorization to increase the TOT to a specified level. The second measure would request voter preference as to the use of the proceeds from the tax increase. Please refer to Attachment B as prepared by the Finance Director for further details on this option.

In terms of the second issue pertaining to a Special Tax, the request of Council Member Erickson is that the proceeds be limited to the acquisition and development of Park and Open Space. Clearly, the City Council retains the authority to specify

the use of the tax proceeds as it so chooses. Staff believes it is important to provide an operational definition for whatever request is placed before the voters so there is a clear understanding as to what the tax proceeds may and may not be used for should voter approval be obtained.

In terms of Council Member Erickson's request, staff would offer the following as a starting point for defining the use of the tax proceeds, if approved:

A. Acquisition of real property for the exclusive purpose of providing park, open space and recreation facilities. This includes the purchase of property from private parties, surplus property declared by the Newport Mesa Unified School District, County of Orange, State of California, Federal Government or other public entities.

B. Development of property under the ownership, leasehold or other control of the City of Costa Mesa for park and recreation purposes. This shall include any and all improvements as identified in Table 11 of the City's adopted Parks, Open Space and Recreational Facilities Master Plan (see Attachment C). Development related expenses eligible shall include real property appraisals, preparation of environmental documents, project design, construction and project management services.

C. Development of open space shall include parkways and medians under the control of the City of Costa Mesa. Said improvements may include construction of curb, gutter and sidewalk, only where such improvements are needed to provide for additional landscaping.

D. Proceeds from an increase in the TOT may not be used for park, open space or recreational facility maintenance, repair or operation. No proceeds from the TOT increase may be used for development, maintenance or operation of park, open space and recreational facilities exclusively for private use or to supplant landscape, open space or related requirements on a new development.

The next date available for this matter to be placed before the voters is the November General Election. While the City Council does not have the option to call for a Special Election on this matter pursuant to State law, the measure may be placed on any subsequent Statewide Primary, General or regularly scheduled local election. In order for the measure to be placed on the November General Election, the City Council simply needs to adopt a resolution calling for the placement of the matter on the ballot by August 11, 2000. **In order for this matter to appear on the November ballot, City Council action would be required at either the July 17, 2000 or August 7, 2000 regular City Council meetings.** Adoption of the resolution may be accomplished following a Public Hearing should the City Council so desire. Placement of the matter on the City Council Agenda as a Public Hearing would

require that this matter appear on your August 7, 2000 agenda to meet posting and noticing requirements.

The cost to place this matter on the November General election ballot is approximately $5,000. This is simply the cost to place the matter on the ballot and does not include the cost of providing public information materials on the measure or related expenses. Attachment A addresses the limitations as to what the City may or may not expend public funds on in terms of providing informational material on the ballot measure.

Should the City Council direct that the matter be put before voters in the November Election, staff would recommend that the above expense be funded by way of an appropriation from the Net Revenue "Special Projects" allocation which is reserved for requested studies, projects and requests of the City Council.

The City Council does have the option to submit a ballot argument in favor of the proposed measure. The ballot argument must be submitted to the County Registrar of Voters within 10 days following action to place the measure on the ballot and no later than August 21, 2000. The argument may be signed by up to four individuals. Rebuttals to the ballot argument must be filed within 10 days following the submission of the argument in favor.

FISCAL REVIEW:

As noted previously, the City's existing TOT is 6%. At this rate, the TOT generates almost $4 million dollars per year to the City of Costa Mesa. Each 1% TOT generates approximately $650,000 per year. The requested increase of 2% would therefore be expected to generate revenue in excess of $1 million per annum. As hotel room rates increase and/or as new hotel rooms are added, this amount will increase.

Attachment D depicts the current TOT percentages for all Orange County Cities in relationship to Costa Mesa's 6% levy. It is important to keep in mind that the City's 6% TOT does not include the 2% collected along with the TOT as a Business Improvement Assessment and subvented to the Tourism & Promotion Council which consists of the 7 major hotels in Costa Mesa. Therefore, the effective levy on customers at the 7 major hotels is 8% with 6% going to the City and 2% going to the Tourism Council. A 2% increase in the TOT as proposed in Community Objective 01-C3 would place Costa Mesa at a total levy of 10%.

LEGAL REVIEW:

Attachment A provides the legal review as it relates to the requirements for ballot measures. In the event the City Council desires that an actual ballot measure be drafted and adopted by resolution, the City Attorney and City Manager will see that such a measure is prepared along with the accompanying documents required.

CONCLUSION:

The TOT has not been increased in over 20 years and is well below the Orange County market and will remain below the County average even with the requested increase of 2%. While respectful of arguments from the hotel industry that an increase in the TOT will make Costa Mesa hotels "less competitive" in the Orange County marketplace, there simply is no factual evidence to support that contention. Indeed, the 7 major hotels in Costa Mesa have not substantiated any adverse impacts from the recently enacted 1% addition to the Business Improvement Assessment in January 2000. This is not to say that the TOT should be increased without respect to its economic impacts on the industry and tourism generally. However, staff simply has not been able to identify any factors that would suggest that an increase in the range suggested will adversely impact Costa Mesa hotel properties.

There are a number of very important community needs and interests to which this increase in revenue could be justifiably approved. Besides the suggested Acquisition and Development of Park, Open Space and Recreation Facilities, valid arguments can also be made for the increase to be allocated to Street Maintenance, Traffic Improvements, increased Public Safety, upgrading Public Infrastructure such as utility undergrounding, expansion of the Police Facility or construction of new/additional library facilities and even for local government operating needs. All are important to some degree to all members of the community. Staff believes there are some unique attributes that can be attributed to allocating the funds as requested in Community Objective 01-C3 that require notation:

- The opportunity to secure Open Space and Parkland is increasingly limited. As demand for real property continues to increase, the cost and opportunity to secure parcels of a size that can be of value to the community continues to shrink. As those opportunities do appear – be it through private sale or the disposition of public property – the City must have in place a financial means to take advantage of land availability. The City does not enjoy the ability to simply reduce the General Fund Budget, cut programs/services or borrow whenever such opportunities arise.

- With the exception of the recently enacted Proposition 12 – which the City will receive a one time $1.2 million dollar allocation early next year – the opportunities for outside funding for the acquisition and development of Park, Open Space and Recreation facilities are limited. While a good deal of creative work has been done in the area of private and corporate sponsorship in this area, it is not nearly enough to support the level of demand in the community for these amenities. At the same time, there has been extremely limited resident support or interest in the establishment of assessment districts to fund these amenities, even though the practice is commonplace in many communities throughout California. Finally, voter support for local bond measures – which has historically funded much of the acquisition and development of

Public Open Space such as the 1974 Costa Mesa Park & Open Space Measure – has been virtually non-existent for many years. Given the collective implications of the preceding, it is clear that an additional revenue source must be developed if the City is to expand in this area to any significant degree in the near future.

- Acquisition and development of Public Open Space can clearly improve the overall appearance and add value to the community. The availability of Park and Recreational Facilities can be important factors not only for families but adults and senior community members as well. Development of Parkway and Median Landscape areas in commercial, industrial and residential areas adds to property values and is one of the more defining features of newer communities. Development of recreation facilities offers positive outlets for young members of the community, and hopefully a deterrent to entrance into the Juvenile Justice System, compounding cost for greater investment in Public Safety.

City staff is prepared to take the necessary steps to enable the City Council to place this matter before the voters for the November General Election or at any subsequent election date as deemed appropriate.

ALLAN L. ROEDER, CITY MANAGER

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ATTACHMENTS: A – Legal Review
B – TOT Ballot Measure
C – Community Center and Park Improvement Costs
D – Transient Occupancy Tax Survey

DISTRIBUTION: City Attorney
Deputy City Clerk
Administrative Services Director
Finance Director
Public Services Director

CITY OF COSTA MESA
CITY ATTORNEY'S OFFICE
MEMORANDUM

CONFIDENTIAL / ATTORNEY-CLIENT PRIVELEGE
ATTORNEY WORK PRODUCT

TO: Allan L. Roeder, City Manager

FROM: Marianne Reger, Deputy City Attorney

DATE: June 26, 2000

SUBJECT: TOT Ballot Measure

QUESTIONS PRESENTED

1. What is the legal process and/or what action must the City Council take to place a measure on the ballot for the November General Election?

2. If the proceeds from the increase in the Transient Occupancy Tax ("TOT") are specified for a specific use or for a few specific uses, would the increase be deemed a general or special tax?

3. What is the requirement for voter approval of general versus special taxes?

4. Does the law require voter approval of a specific tax increase, or may the voters approve an "adjustable" and/or maximum tax increase, leaving the actual tax increase/decrease to the discretion of the City Council?

5. What, if any, are the legal restrictions regarding expenditure of public funds for the ballot measure?

SHORT ANSWERS

1. The ordinance or resolution proposing the tax must be approved by a two-thirds vote of the City Council and must also meet specific statutory requirements discussed below. A public hearing is not required, although the Council may elect to hold a public hearing on the matter.

2. The answer is dependent on the wording of the measure. If strictly advisory, the measure would likely be deemed a general tax.

3. A general tax requires a majority vote of the electorate while a special tax requires a two-thirds vote of the electorate.

4. Both a general or special tax may state a range of rates or amounts. There are restrictions if the tax is based on a percentage calculation as discussed below.

5. The City is prohibited from using public funds to assist in the passage or defeat of a ballot measure, but may use public funds to educate and inform voters.

BACKGROUND FACTS

The City is considering placing two ballot measures on the ballot for the next November General Election. One ballot measure will be to increase the TOT. The information on the other ballot is varying. Marc Puckett has indicated in a separate memo that the second measure would be "advisory" and merely ask voters to express their preference as to how the new tax revenue would be spent. You have indicated in your memo that the second ballot measure would be specific in directing the spending of the tax increase to the development of parks, open space and landscaping. Depending on how the second ballot measure is worded, (i.e., advisory or specific uses), will have a direct impact on if the tax increase, if approved, will be labeled a general or special tax as well as the voter requirements, as will be discussed below.

ANALYSIS

1. What is the legal process and/or what action must the City Council take to place a measure on the ballot for the November General Election?

The process for placing either a general or special tax on the ballot is set forth in Gov't Code §53720 et seq and more particularly in Gov't Code §53724. This statute requires that:

1. Any general or special tax shall be proposed by an ordinance or resolution of the Council. The ordinance or resolution proposing the tax must include the type of tax, the rate of tax, the method for collection of the tax, the date upon which an election shall be held on the tax, and if a special tax is proposed, the purpose or service for which the special tax is sought.

2. The ordinance or resolution proposing the tax, whether general or special, must be approved by a two-thirds vote of the Council.

3. The election on the proposed tax must be consolidated with a statewide primary, general or regularly scheduled local election at which all electors of the city are entitled to vote.

Once the above special provisions regarding a new general or special tax are met, any other regular provisions for placing a measure on a ballot would apply. Please note that no public hearings are <u>required</u> for either a general or special tax. However, public hearings may be held and many cities are following the notice and hearing requirements for levying assessments.

In general, the last day to submit a ballot measure, summary and arguments to the Registrar of Voters for the November general election is August 11, 2000. Therefore, if the Council wishes to have a tax measure on the November ballot, they would need to vote on the ordinance or resolution no later than August 7, 2000. However, if the Council chose to hold a public hearing

on the matter, then the notice and posting requirements would need to be calculated into the time frame. If the measure is submitted by the August 11th deadline, the last day to submit rebuttal arguments is August 21, 2000 or if the measure is adopted before August 11th, the deadline for rebuttal arguments is 10 days after the direct arguments are submitted.

2 If the proceeds from the increase in the Transient Occupancy Tax ("TOT") are specified for a specific use or for a few specific uses, would the increase be deemed a general or special tax?

There answer to this question is dependent first, on how specific the wording would be stated in Measure A, and second on whether the specific uses stated are truly advisory or if in fact, would be binding on the City Council in expending the revenue derived from the increase.

Pursuant to Prop 218 amendments, the California Constitution Art. XIII C (a) and (d) were amended to redefine general and specific taxes. A "general tax" is now defined as "any tax imposed for general governmental purposes. A "special tax" is now defined as "any tax imposed for specific purposes, including a tax imposed for specific purposes, which is placed into a general fund." However, the designation of general versus special tax is still open to some debate as discussed herein below.

In a pre Prop 218 case Coleman v. County of Santa Clara, 64 Cal.App.4th 662 (1998), the court addressed a very similar question to that posed here. In the Santa Clara case, the county had two measures on the ballot. The first measure was an advisory measure that stated in part "This measure is not a tax. It is an advisory measure that states Santa Clara County voters' intent that any new sales tax funds be spent on [a list of] transportation improvements . . ." The second measure stated in part that "This measure authorizes the enactment of a ½ cent retail transaction and use (sales) tax for general county purposes." The court held that even though Measure A listed several projects for which the tax increase could be used, because Measure A did not require that the tax increase only be used for those listed projects, and the revenue from the tax went into the general fund making the funds available for general governmental purposes, the tax was a general tax.

In a more recent case, Rider v. County of San Diego, 1 Cal.4th 1, 2 Cal.Rptr.2d 490 (1992), the court held that despite the county agency's designation of the proposed tax increase as a "general tax" which was deposited in the agency's general fund, the tax was designated for "the purpose of financing the construction and operation of criminal detention and/or courthouse facilities . . ." and was therefore a special tax.

Since Prop 218 redefined the definition of a "special tax" the Measure A/Measure B strategy of combining a general tax with an advisory measure is not without risk of challenge. In fact, Howard Jarvis Taxpayers Assoc.'s ("HJTA") Annotated version of Prop 218's definition of Special tax, sent to the League of California Cities, December 6, 1996 states:

"(d) "Special tax" means any tax imposed for specific purposes including taxes imposed for specific purposes which are placed into a general fund.

["Annotation: This reinforces language of Rider v. San Diego dealing with special taxes. The key is the purpose of the funding, not the name of the bank account. A number of analyses

of Proposition 218 prepared by local governments have stated that the revised transportation tax in Santa Clara County (proposing "dual" measures on the ballot) would be illegal under this definition.]"

Although one must consider the source of the annotation, it gives us a clear idea of how HJTA may view any "dual" ballot measure proposed by the City under Prop 218.

Therefore, the answer to this question is tied very closely to how the "advisory" ballot measure is worded. If the ballot measure specifies that any proceeds from the increased tax would be used only for a few specified projects, it would likely be deemed a special tax subject to the supermajority vote. However, if the measure is worded so that it is strictly advisory, (i.e., not binding on the City Council), even if it listed some areas for expenditures, such as development of parks, open space and landscaping, it would likely be deemed a general tax as the City Council would still have discretion to designate the final expenditures.

3. What is the requirement for voter approval for requirement for general versus special taxes?

Under Prop 218, the imposition, extension or increase of general taxes requires a majority vote of the electorate voting in an election on the tax. (See Cal. Const. art. XIIIC, §2(b)). The imposition, extension or increase of a special tax requires a two thirds vote of the electorate voting in an election on the tax. (See Cal. Const. Art. XIIIC, §2(d)).

4. Does the law require voter approval of a specific tax increase, or may the voters approve an "adjustable" and/or maximum tax increase, leaving the actual tax increase/decrease to the discretion of the City Council?

A proposed tax, either general or special, may state "a range of rates or amounts." If a range of rates is approved, the governing body may impose up to the maximum amount approved. See Gov't Code § 53739. A proposed tax, either general or special, may also provide for inflationary adjustments to the rate or amount, unless the tax is to be determined by using a percentage calculation. If a tax is to be determined on a percentage basis, inflationary adjustments cannot be used. Furthermore, the ordinance or resolution must clearly identify the formula for adjustments.

The HJTA annotation (referred to above) concurs that "the ballot language could incorporate future increases and if the ballot measure is approved, then the government would not have to go back to the voters for those increases. The City Council could initially levy a lower tax than the maximum approved by the voters and could then later raise the tax to the maximum tax as approved by the voters.

5. What, if any, are the legal restrictions regarding expenditure of public funds for the ballot measure?

The City is prohibited from using public funds to assist in the passage or defeat of a ballot measure. (See generally, Miller v. California Commission on the Status of Women, 198 Cal.Rptr. 877 (1984). Notwithstanding, the City may spend public monies to educate and inform voters about the consequences of a particular measure. Any information disseminated must be objective and impartial. It is very important that any information disseminated by the City not be construed as advocating voter approval or rejection. There is a fine line between

educating the public and advocating a position, it is recommended that this office review any information disseminated to the general public before distribution.

CONCLUSION

I hope that the information provided herein has addressed your questions. If I can be of any further assistance regarding these issues, please contact me at ext. 5289.

c: Jerry Scheer, City Attorney
Tom Wood, Asst. City Attorney

CITY OF COSTA MESA
DEPARTMENT OF FINANCE
INTEROFFICE MEMORANDUM

MARC R. PUCKETT
DIRECTOR OF FINANCE

TO: JERRY SCHEER, CITY ATTORNEY

FROM: MARC R. PUCKETT, DIRECTOR OF FINANCE

COPY TO: ALLAN L. ROEDER, CITY MANAGER (memo only)

DATE: MAY 1, 2000

SUBJECT: *TOT BALLOT MEASURE*

At the CSMFO annual conference, which I recently attended, there was much discussion about Proposition 62 and Proposition 218. In one of the breakout sessions conducted by representatives of Richards, Watson & Gershon some very useful handouts were distributed which we may find helpful as we consider our strategy towards developing a TOT ballot measure. A copy of these handouts are attached (attachment 1) for your information.

A substantial portion of the breakout session was spent discussing the "Measure A/ Measure B" strategy for placing a tax question on the ballot. This strategy involves putting an advisory measure on the ballot, which would ask voters to express their preference as to how the new tax revenue would be spent together with a ballot measure that would be a general tax increase. This strategy allows Cities to raise new tax revenue by simple majority and thus eliminates the supermajority requirements for a specific tax while still allowing residents to express a "preference" in terms of how the new revenue should be spent.

The case of Coleman v. County of Santa Clara was cited as the legal authority for this strategy. In this case, the 6th District Court of Appeal held that a sales tax imposed by Santa Clara's Measure B, was not a special tax subject to the 2/3 voter approval requirements of Proposition 13 and 62. The ballot also included a Measure A which asked voters if they preferred the proceeds of the tax be devoted to a specific list of local transportation projects. The Court stated a two-part test for the identification of special taxes. First, the law asks whether the entity which imposed the tax is a general-purpose entity or a special-purpose entity, which can impose only special taxes by its very nature. Second, if the tax is imposed by a multi-purpose or general-purpose entity, the law asks if the proceeds of the levy are legally obligated for a special purpose. The Court stated that the Measure A/ Measure B strategy did not reflect such inseparability that, as a matter of law, the two measures must be considered as one. On the contrary, the Court ruled that the two measures were not legally connected. This court case is outlined in the attached handouts.

It is my belief that we should pursue this Measure A/ Measure B strategy for the TOT ballot measure to eliminate the supermajority requirement for a specific tax and most importantly, to maintain flexibility in terms of how the new revenue may be spent. While there are a number of Parks projects that have been discussed as uses for this new revenue, there may be other projects, from time to time, which are deemed a higher priority when the budget document is developed for the ensuing fiscal year. Maintaining maximum flexibility within our revenue stream is critical to our ability to address changing priorities as they occur. Regardless of the direction we ultimately decide to pursue, a TOT ballot measure should receive supermajority approval whether it is considered a specific or general tax increase.

As an aside, the representative from Richards, Watson & Gershon offered to provide "free" legal assistance to any City that was considering preparing a ballot measure of this type to ensure that the chances of any challenges from a group such as the Howard Jarvis Taxpayers Association were minimized. It sounded a little like a sales pitch but I thought it was worth mentioning. Let me know if you would like to discuss this matter further.

MARC R. PUCKETT
Director of Finance

Attachment