CITY COUNCIL AGENDA REPORT

MEETING DATE: **February 17, 2004** **ITEM NUMBER:**

SUBJECT: **CONSIDERATION OF POTENTIAL NEW REVENUE SOURCES**

DATE: **FEBRUARY 10, 2004**

FROM: **FINANCE DEPARTMENT/ADMINISTRATION**

PRESENTATION BY: **MARC R. PUCKETT, DIRECTOR OF FINANCE**

FOR FURTHER INFORMATION CONTACT: **MARC R. PUCKETT (714)754-5243**

RECOMMENDED ACTION:

Provide direction to staff regarding potential new revenue sources.

BACKGROUND:

At the June 16, 2003, City Council meeting, Council directed staff to prepare a report regarding potential new revenue sources to be presented to Council at a study session. Specific, potential, new revenue sources mentioned at that time included the business license tax, transient occupancy tax and sanitation franchise fee.

Council members had also expressed interest in initiating conversations with the business community regarding consideration of a new business license tax structure and/or an increase in the existing business license tax structure. In addition, Council had expressed interest in moving forward with a ballot measure that would place an increase in the transient occupancy tax on the ballot.

Further, Council had requested that representatives of the Sanitary District Board, the Costa Mesa Convention and Visitors Bureau, and the Chamber of Commerce be invited to the Study Session to be available to respond to Council questions regarding the potential new revenue sources.

Staff presented the report at the December 5, 2003, study session. Included in the study session presentation were other potential new revenue sources for Council's consideration and review. These two additional potential new revenue sources were the FireMed subscription fee and the local sales tax provided for under SB 566.

ANALYSIS:

Each potential new revenue source is summarized herein. For each of the potential new revenue sources discussed herein, a description of the revenue source, taxing authority, overview of the fee, and estimated revenue collections are included.
Any increase in the business license tax, transient occupancy tax or the sales tax would require a vote of the people. Whether the ballot measure requires a simple majority (50% + 1 vote) or a

super majority (two-thirds of those voting in the affirmative) depends upon the ballot language and whether the question is placed upon the ballot as a general tax increase or a special tax increase. In making these determinations, there are a number of decisions that Council must make to place the matter before the voters. These issues were discussed in length with Council and thoroughly detailed by the City Manager in his July 7, 2000, memo to Council preceding the placement of the Transient Occupancy Tax question on the November, 2000, ballot. A copy of the City Manager's memo is attached (Attachment 1) and referenced herein with respect to the requirements of placing a ballot measure before the voters.

On page two of the memo, the City Manager discusses the five decisions that Council must make and the four ways that the ballot measure may appear before the voters on the ballot. These same decisions apply to each of the potential new revenue sources discussed herein requiring voter approval prior to implementation. The attachments to the City Manager's memo from the City Attorney's Office and the Finance department further delineate matters that need to be considered with respect to placing a ballot measure before the voters. It is suggested that these requirements be reviewed in detail with respect to issues concerning placement of a ballot measure before the voters as a general tax increase or a specific tax increase.

According to the Deputy City Clerk, cost estimates for placing a "stand-alone" local ballot measure before the voters is approximately $95,000 to $100,000. Costs for placing a local ballot measure on a "consolidated" ballot are currently estimated at approximately $25,000 to $32,000.

Business License Tax:

Description: The Business License Tax is a general tax on businesses for the privilege of conducting business within the City. As a general tax, use of revenues derived from the issuance of business licenses is unrestricted.

Authority: The authority to levy this tax is granted pursuant to the Government Code, sections 37101, et seq.

Overview: The Business License Tax is a type of excise tax imposed on businesses for the privilege of conducting business within the City. The tax is most commonly based on gross receipts or levied at a flat rate, but is sometimes based on the quantity of goods produced, number of employees, number of vehicles, square footage of the businesses or some combination of factors. Rates are set at each City's discretion but may not be discriminatory or confiscatory.

Cities may levy this tax for both regulatory and revenue-raising purposes. However, regulatory fees may only be levied to cover the costs of regulation.

Any increase in the Business License Tax will require voter approval.

Based upon the last available survey approximately five years ago, over 440 cities (93 percent of all cities) collect a business license tax as a general tax. Some of those that do not collect a business license tax, collect a business license fee based on cost recovery for licensing and processing or for other services provided.

During the last fiscal year ended June 30, 2003, the Business License Tax revenue collections equaled approximately $854,000. The current fee schedule has remained unchanged for over 18 years. The business license tax is not now a major revenue stream for the City. However, for many cities, it is a major revenue stream. A copy of the business license tax survey prepared and included in the Budget Study Session Workbook is attached (Attachment 2).

As noted in the survey, 27 out of 34 cities (80%) in Orange County levy a business license tax. Of those that levy a business license tax, 16 cities have variable rate structures and nine cities collect more revenue than Costa Mesa. Further, 24 of the 27 cities that levy a business license tax impose a tax structure that is higher, and in most cases significantly higher, than Costa Mesa.

If desirable, in order for Costa Mesa to generate a significant increase in business license taxes, the City would need to move to a fee based on a fixed percentage of gross receipts, say for example, between .4% and .8%. A fee based on a fixed percentage of sales such as this would maintain uniformity and equity for all businesses, small and large alike. Pursuant to the Government Code, rates are set at each City's discretion but may not be discriminatory or confiscatory.

With a tiered fee structure, businesses falling within the lower portion of the "range" would effectively pay more in tax on a proportional basis to gross sales than those businesses at the upper end of the range.

Potential rate structures were discussed with the president of the Chamber of Commerce, Ed Fawcett. Mr. Fawcett expressed his understanding of the City's need to consider new revenue sources in light of the economic climate, the condition of the cities budget and the state budget deficit condition. As such, he prepared and proposed a continuation of the tiered rate structure with upward adjustments made to each of the rates and the banding of each range. He has indicated that he supports and would advocate for increases in the business license tax as outlined in his proposed fee schedule. Per his estimates, he believes that the increases in the ranges as he has proposed (Attachment 3) will result in an increase in business license tax revenue of approximately $1 million. These estimates were based upon a review of the sales for the Top 20 business categories in the quarterly sales tax reports over the last four quarters. Gross receipts information for all businesses is not readily available in such a format that would allow staff to accurately estimate the revenue collections based upon Mr. Fawcett's proposed business license tax schedule. However, it should be noted that staff did review his methodology and it does appear reasonable.

Transient Occupancy Tax:

Description: The Transient Occupancy Tax is a general tax imposed on occupants for the privilege of occupying room(s) in a hotel, motel, or inn. Use of the revenues are unrestricted. However, some cities budget a portion of the revenues for tourism and business development purposes. Costa Mesa levys a 2% Business Improvement Assessment for the benefit of the Costa Mesa Convention and Visitors Bureau to assist that organization in promoting tourism travel to the area. The current TOT rate of 6% has remained unchanged for over 22 years.

Authority: The authority to levy this tax is promulgated from the State Government Revenue and Taxation Code being sections 7280 and 7281.

Overview: Cities may impose the transient occupancy tax on persons staying 30 days or less in a room(s) in a hotel, motel, inn, tourist home, non-membership campground or other lodging facility. Cities may also levy a tax on the privilege of renting a mobile home located outside a mobile home park, unless such occupancy is for more than 30 days or unless the tenant is an employee of the owner.

According to a 1989 survey by the League of Cities, rates ranged from 4 to 12 percent. The average rate was 7.6% with 8% being most typical . Nearly two-thirds (65.7 percent) of cities reported using their revenue for general fund purposes.

Currently, more than 80 percent of cities collect a transient occupancy tax.

Although Costa Mesa has one of the higher concentrations of available hotel rooms in the county, the transient occupancy tax levied is the lowest in the County. A copy of the transient occupancy tax survey prepared and included in the Budget Study Session Workbook is attached (Attachment 4). During the current fiscal year, it is estimated that the City will collect $3.8 million in transient occupancy taxes. This revenue estimate is $800,000 less than the actual revenue collections for fiscal year 2000-2001. Transient Occupancy Taxes, while finally on the upswing again, have not returned to the level of revenue collections prior to the 9-11 event.

Based upon a revenue estimate of $4 million, each 1% increase in the transient occupancy tax would generate approximately $665,000. A 2% increase in the Transient Occupancy Tax would generate approximately $1,330,000.

Benefits of considering an increase in the Transient Occupancy Tax include placement of a portion of the tax burden to provide city services on transient visitors to the community. Residents benefit from this spreading of the costs of services over a larger tax base including those visiting the community, therefore lowering the cost of services to residents.

Sanitation Franchise Fee:

Description: The Sanitation Franchise Fee is a fee that may be imposed upon exclusive or non-exclusive franchisees for the purposed of residential and commercial solid waste handling services within the City. Generally, a franchise fee is a fee paid to a municipality from a franchisee for “rental” or “toll” for the use of city streets and rights-of-way. Use of revenues generated from a Sanitation Franchise Fee are unrestricted and could be used for any purpose.

Authority: The authority to enter into such franchise agreements is found within the Public Resources Code sections 49520 through 49523. Further, adoption of a Sanitation Franchise Fee Ordinance would be necessary to set forth specific requirements for prospective franchisees.

Overview: Of the 34 cities in Orange County, 31 have Sanitation Franchise Fees. The most predominant form is a non-exclusive franchise agreement. Such franchise agreements allow the trash haulers to set their own rates without any controls by the City, thus preserving their free market system. Further, a non-exclusive franchise fee would provide for a means of monitoring the waste hauler rates to determine if in fact, waste hauler rates in Costa Mesa were indeed higher or lower than other communities with Sanitation Franchise Fees. A Sanitation Franchise Fee may be imposed upon residential, commercial and industrial waste haulers.

Based upon the attached survey (attachment 5), it is estimated that the Sanitation Franchise Fee may generate approximately $1 million in new revenues to the City.

FireMed Subscription Fee:

Description: The Fire Medical Subscription Fee is a voluntary membership program that is intended to improve the quality of emergency medical services. An annual membership fee is charged on a per household basis that covers all the people who live at the residence.

Overview: Generally speaking, the FireMed voluntary subscription service would fund all of the paramedic positions in the City, life saving equipment and advanced medical emergency training. FireMed covers everyone in the household for paramedic and fire department emergency ambulance services while they are within the City's borders. Membership includes an umbrella coverage for visitors when they suffer an emergency medical incident at a FireMed household.

Typically, the subscription fee is billed with water services and paid monthly. However, the subscription service can be billed in any number of ways. If paid separately from the utility bill, the subscription fee has usually been billed annually.

Use of Funds – The funds received from the FireMed subscription fee have generally been restricted in use to be used solely for EMS-related expenses. This is critical in order to justify the program, and to increase membership (i.e., must continually let the members know how their contributions are improving the City's EMS system and "saving lives").

In other cities utilizing FireMed subscription programs, the quality of the service improved after implementation of the program. Key features of these subscription programs in other Orange County cities are noted below:

HUNTINGTON BEACH FIRE DEPARTMENT (HBFD) – FireMed Program

- COST – $60.00/year per household, or $30.00/year for qualified low-income households.
- PEOPLE COVERED – Everyone residing in the household, and any visitors.
- SERVICES COVERED – All fire department EMS responses (ALS and BLS) within the city borders, and all emergency ambulance transports to an appropriate hospital within or outside of the city.
- PAYMENT – $5.00/month if placed on Municipal Services Bill. Otherwise, an annual charge will be billed via a separate invoice. Renewal statements are mailed 1 month prior to expiration date.
- CURRENTLY ENROLLED – 26,753 households (37%).
- REVENUE EXAMPLE – Last fiscal year: $906,071
- PAYS FOR – 1 EMS Coordinator position, 32 Paramedic positions, 4 ambulances, 24 full-time EMT Ambulance Operators, EMS equipment and supplies, EMS training, CPR training for FireMed members.
- MISCELLANEOUS:
  - FireMed bills member's insurance company and accepts whatever his/her current insurance provider pays for the response and transport as payment in full, even if there is a deductible, co-pay, partial payment, or denial.
  - FireMed members without health insurance to cover the response and transport will receive a discount of 20% of the total bill. Discounts for EMS responses and transports are *not* given to non-FireMed members.

- All members of a FireMed household receive free American Heart Association CPR training.
- The program was begun by the passage of a City Ordinance that authorized specific user fees for ALS, BLS, and voluntary FireMed membership services.

ANAHEIM FIRE DEPARTMENT – Paramedic Membership Program

- COST – $36.00/year per household.
- PEOPLE COVERED – The member and "those residing with the member," and visitors. Bedridden patients of a Senior Care Facility which maintains a business membership are covered, but not ambulatory patients.
- SERVICES COVERED – Excludes ambulance (Care Ambulance bills separately).
- PAYMENT – On utility bill, at $3.00/month.
- CURRENTLY ENROLLED – 60%

FULLERTON FIRE DEPARTMENT – Paramedic Subscription Program

- COST – $30.00/year per household.
- PEOPLE COVERED – Only permanent residents of a member's household.
- SERVICES COVERED – Excludes ambulance services (billed separately by ambulance company).
- PAYMENT – Fee shows up on water bill in May and June. To enroll or renew, include fee with bill. If decide not to enroll or renew, deduct the fee from the bill and pay the difference.

NEWPORT BEACH FIRE DEPARTMENT – Fire Medics Program

- COST – $48.00/year.

SANTA ANA FIRE DEPARTMENT

- COST – $36.00/year.
- PEOPLE COVERED – Only permanent residents of a member's household.

CITY OF ORANGE FIRE DEPARTMENT

- COST – $36.00/year.
- PEOPLE COVERED – "Everyone at the address."
- REVENUE EXAMPLE – Last fiscal year: $517,146.79
- MISCELLANEOUS: Insurance is billed.

The FireMed Subscription Program has a myriad of benefits that warrant a more in depth discussion but it should suffice to say that it is believed to be a superior system from a service delivery and revenue generation standpoint.

As additional background information, attached (Attachment 6) are frequently asked questions (FAQs) related to the FireMed Paramedic Subscription Program posted on Huntington Beach's website. Huntington Beach has been held out as a model FireMed program emulated by other Fire agencies.

Local Sales Tax:

Senate Bill 566 was passed on October 8, 2003 and authorized cities to seek voter approval to levy a transactions and use tax in multiples of 0.25%. There are two sections under the Senate bill authorizing cities to seek either a general purpose (simple majority to pass) tax increase or a special purpose (2/3 of those voting in the affirmative) tax increase at its discretion. This bill becomes effective on January 1, 2004.

Description: The sales tax is a tax imposed on the total retail price of any tangible personal property, unless specifically exempted.

Authority: The authority to levy a local sales tax is derived from SB 566 effective January 1, 2004 and the California constitution, Article XIII, subsection 29.

Overview: The sales tax is imposed on retailers for the privilege of selling tangible personal property. The use tax is imposed on the user of a product purchased out-of-state and delivered for use in California. Before 1955, cities and counties administered local sales tax ordinances. Those ordinances included varying tax rates and ordinances. In 1955, the legislature passed the Bradley-Burns Uniform Local Sales and Use Tax law. That law authorized the Board of Equalization to collect a 1 percent sales and use tax for all California cities and counties. By 1967, all cities and counties in California had contracted with the Board to collect sales and use taxes on their behalf. Consequently, for the first time, the local sales and use tax was the same for all cities and counties throughout California.

SB566 becomes effective January 1, 2004 and essentially makes it possible for cities to seek voter authorization to impose a local sales and use tax without first obtaining special legislation from the state.

The sales tax is the City's single largest source of revenue. It is estimated that the City will receive $37.5 million in sales tax during fiscal year 2003-2004. Imposition of a local sales tax in an increment of .25% would generate $9.375 million.

The key benefit of imposition of a local sales tax in Costa Mesa is the strength of the City's commercial and retail tax base. As a result of the sales tax benefits derived from the South Coast Plaza area and the Harbor Boulevard of cars, the majority of the City's sales tax revenues are derived from transient shoppers. Imposition of a local sales tax would shift a significant portion of the burden to fund local programs and services to the transient shoppers thereby reducing the tax burden on city residents.

Further, increasing the total sales tax rate from 7.75% to 8% would match the sales tax rate charged currently in Los Angeles County. An increase of .25% in the sales tax rate would amount to $.0025 per dollar of taxable sales. On $40,000 of taxable sales, an increase of .25% would amount to $100 of additional sales tax.

CONCLUSION:

There are several options available to the City to generate new revenues to meet the variety of community needs for which the revenues could be justifiably approved. The City is extremely accommodative to business. The business license tax and transient occupancy tax have remained unchanged for approximately twenty years. Further, 31 of 34 cities in Orange County currently assess a sanitation franchise fee.

During each Budget Study Session for the past three years, staff has noted that the guiding principles used to develop the operating and capital improvement budget were to maintain current programs and services at existing levels. This direction and philosophy is consistent with decreased budgetary flexibility with respect to how service delivery is funded. Staff has also discussed with Council a proposed policy related to new or expanded programs and services. Staff noted that there is a finite limit to programs and services that can be offered within existing resources and recommended that no new programs or services be added without first identifying a new revenue source.

The budget conditions that predicated this discussion still exist. Without the addition of a new revenue source, staff will need to consider reprioritizing existing service delivery to address any budgetary shortfalls.

It is recommended that Council provide direction regarding identification of potential new sources of revenue. Staff is available at your convenience to provide additional information if you have any questions.

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Marc R. Puckett
Director of Finance

Attachment 1: TOT Agenda Report regarding Ballot Measure
Attachment 2: Business License Survey
Attachment 3: Business License Fees
Attachment 4: Transient Occupancy Tax & Utility Use Tax Survey
Attachment 5: Sanitation Franchise Fee Survey
Attachment 6: FireMed Paramedic Subscriber Program FAQ
Attachment 7: HDL Companies – City Trans

Copy to: City Manager
Department Directors