Municipal Finance Institute  ❖  12-13 December 2018

Legislative and Budget Update

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CaliforniaCityFinance.com
The California Local Government Finance Almanac

Legislative Analyst’s Office:
“It is difficult to overstate how good the budget’s condition is today.”
Consensus Economic Outlook

Growth Slowing
✓ Slow growth in U.S. GDP
✓ Flattening of stock prices
✓ Strong wage growth in 2018 & 2019, slower after
✓ Slow job growth
✓ Very low unemployment
✓ Trade disputes creating uncertainty

Housing Market Cooling
✓ Steady construction activity
✓ Rising supply of homes
✓ Tighter mortgage lending standards
✓ Higher interest rates
✓ Slower growth in home prices

Moderate State Revenue Growth Continues

<table>
<thead>
<tr>
<th></th>
<th>2017-18</th>
<th>2018-19</th>
<th>2019-20</th>
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</thead>
<tbody>
<tr>
<td>Personal income tax</td>
<td>$93,966</td>
<td>$97,865</td>
<td>$100,985</td>
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<tr>
<td>Sales and use tax</td>
<td>25,007</td>
<td>25,870</td>
<td>26,819</td>
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<tr>
<td>Corporation tax</td>
<td>12,260</td>
<td>12,728</td>
<td>13,566</td>
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<tr>
<td>Insurance tax</td>
<td>2,575</td>
<td>2,696</td>
<td>2,883</td>
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<tr>
<td>Other revenues</td>
<td>1,711</td>
<td>1,762</td>
<td>1,799</td>
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<tr>
<td>BSA transfer</td>
<td>-4,289</td>
<td>-2,766</td>
<td>-745</td>
</tr>
<tr>
<td>Other transfers</td>
<td>-305</td>
<td>-641</td>
<td>-241</td>
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<tr>
<td><strong>Totals</strong></td>
<td><strong>$130,925</strong></td>
<td><strong>$137,514</strong></td>
<td><strong>$145,065</strong></td>
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</table>
California State Spending Plan
Approved 2018-19 Budget

General Fund
$138 Billion

K-12 Education
Health and Social Services
Corrections
Other

Higher Education

Transportation

Health, Social Servcs

Other

Special Funds
$58 Billion

Required to BSA
$3.4 Billion

Debt reduction
$1.7

Supplemental 3.5
Prior balance 8.5
Total BSA $13.8

BSA Reserve $1.7
SFEU Reserve $2.0
new SafetyNet Reserve $0.2

Total Reserves $16.0 Billion
at end of 2018-19

Proposition 2
Rainy Day Fund & Debt Reduction

Proposition 2 Budget Act.

June Budget Act. Estimate the following:
1.5% of General Fund revenues.
Capital gains revenues over 8% of General Fund taxes.
Less amounts that must be spent on Proposition 98.

Debt/Reserve Estimates

50%

50%

Debt Payments

Budget Stabilization Account

Choose among the following:
Pay down certain "well of debt" items.
Make extra pension/retiree health payments.

Fill rainy-day reserve to 10% of General Fund taxes.

Infrastructure... excess after filling BSA to 10%

* Upon budget emergency declaration by Governor and majority votes of both houses of the Legislature, deposits may be suspended or reduced. Source: LAO

FY2018-19
Required to BSA $3.4 Billion

BSA Reserve $1.7
Supplemental 3.5
Prior balance 8.5
Total BSA $13.8

Total Reserves $16.0 Billion
at end of 2018-19
State Debts, Liabilities
Eligible for Accelerated Payments Under Prop2

<table>
<thead>
<tr>
<th>Budgetary Borrowing</th>
<th>Outstanding at start of 2018-19</th>
<th>Proposed Paydown 2018-19</th>
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<tbody>
<tr>
<td>Loans from Special Funds</td>
<td>$1,248</td>
<td>$205</td>
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<tr>
<td>Underfunding of Prop98 Settle-up</td>
<td>440</td>
<td>100</td>
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<tr>
<td>Weight Fees</td>
<td>1,150</td>
<td>382</td>
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<tr>
<td>Non-Prop98 (pre2004) Mandates</td>
<td>18</td>
<td>18</td>
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<tr>
<td>Repay Pre-Prop42 Transportation Loans</td>
<td>471</td>
<td>235</td>
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State Retirement Liabilities
- State Retiree Health: $91,008 (195)
- State Employee Pensions: $58,765 (611)
- Teacher Pensions: $103,468 (0)
- Judges Pensions: $3,277 (0)
- Deferred Payments to CalPERS: $682 (0)

University of California Retirement Liabilities
- UC Employee Pensions: $10,851 (0)
- UC Retiree Health: $19,331 (0)

Total: $290,709 (1,746)

Source: Governor's Budget Summary Fig INT-02

“Wall of Debt” nearly erased

State General Fund Condition: Improved From Adopted Budget

<table>
<thead>
<tr>
<th>($ in millions)</th>
<th>Approved Budget 2018-19</th>
<th>LAO Projection 2018-19</th>
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<tbody>
<tr>
<td>Prior Year Balance</td>
<td>$8,483</td>
<td>$10,076</td>
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<tr>
<td>Revenues and Transfers</td>
<td>133,332</td>
<td>137,514</td>
</tr>
<tr>
<td>Expenditures</td>
<td>(138,688)</td>
<td>(137,310)</td>
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<tr>
<td>Ending Fund Balance</td>
<td>$3,127</td>
<td>$10,280</td>
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<tr>
<td>Encumberances</td>
<td>(1,165)</td>
<td>(1,165)</td>
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<tr>
<td>Reserves</td>
<td></td>
<td></td>
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<tr>
<td>SFEU* balance</td>
<td>$1,962</td>
<td>$9,116</td>
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<tr>
<td>Safety Net Reserve</td>
<td>200</td>
<td>200</td>
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<tr>
<td>Budget Stabilization Account</td>
<td>13,768</td>
<td>13,768</td>
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<tr>
<td>Total Reserves</td>
<td>$15,930</td>
<td>$23,084</td>
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Required to BSA $3.4 Billion
FY2019-20
LAO Projected

BSA Reserve $0.745
Prior balance 13.768
Total BSA $14.513 B

Debt reduction $1.7
Infrastructure $915m

Source: LAO

*Upon budget emergency declaration by Governor and majority vote of both houses of the Legislature, deposits may be suspended or reduced. Source: LAO
Capital Update:
- New Administration
- Super-duper Dem Majority
- Focus on ...
  - Housing
  - Homelessness, increasing poverty
  - Healthcare
  - Early Childhood Education

Legislative Year: Turbulence
- Harassment investigations, resignations
- California v Trump: immigration, offshore drilling, etc.
- Wildfires, floods
- Legislation by ballot box threat threats to state/local revenues and programs
June 2018 Election Results

Prop. 68 Parks / Water Bond: climate adaptation, water quality/supply, flood protection. $4 billion. State bond repayment costs ~$200 million/yr for 40+ years.

Prop. 69 Transportation Funding Protection: Constitutionally requires SB1 Transportation funds to be used for transportation purposes.

Prop. 70 Cap and Trade Amendment: Requires, beginning in 2024, two-thirds majority of Legislature to authorize use of revenues.

Prop. 71 Ballot Measure Effective Date

Prop. 72 Rainwater Recapture Systems – property tax break

Prop 68 Park/Water Bond

✓ $200,000 per-city for parks – a few get more
  local park rehabilitation, creation, and improvement
✓ $725 million for “park-poor” communities

More ...
✓ $218 million to state parks
✓ $30 million for trails and greenways
✓ $25 million for recreational programs, parks in rural communities
✓ $20 million for coastal forests
✓ $35 million for marine protected areas, sustainable fisheries
✓ $5 million for coastal dune, wetlands, estuary protection
✓ $30 million for “lower cost coastal accommodation grants”
✓ $75 million for California Ocean Protection Trust Fund
✓ $48 million for wildlife corridors & open space (Wildlife Conservation Board)
✓ $115 million for fishery and riparian restoration projects (Dept. of Fish and Wildlife)
✓ $60 million for agricultural land conservation and stewardship (Dept. of Conservation)
✓ $50 million for “for ecological restoration of forests” including urban forests (CalFire)
November 2018 State Propositions

**Prop.1** Housing & Veterans' Loans Bond  $4.0 billion  Repay ~$200m/yr 40+ yrs

**Prop.2** Use Millionaire's Tax Revenue for Homelessness Prevention - Bond

**Prop.3** Water & Watershed Bond Initiative  Water, groundwater, surface water supply & storage, dam repairs, watershed & fisheries, habitat protection & restoration.  $8.877 billion  Repay ~$433m/yr 40 yrs

**Prop.4** Children's Hospital Bond Initiative  construction, expansion, renovation, equipping.  $1.5 billion  Repay ~$84m/yr 35yrs

**Prop.5** Property Tax Transfer Initiative.  Allow homebuyers 55+ or disabled to transfer AV from to new home, no matter (a) new home’s market value; (b) new home’s location; or (c) number of moves.  $2 billion/yr loss to cities, counties, special districts, schools

**Prop.6** Repeal SB1 Gas & Vehicle Taxes, Halt Transportation Projects.  $5 billion/yr loss

**Prop.10** Allow local governments to adopt rent control

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Proposition 6 Fails Nov 2018

Ensures, over the next 10 years,

- $52 billion in state & local transportation funding
- $26 billion to cities & counties, incl $15 billion formula-based
- Local streets & roads funding doubled
- 2/3+ of local streets & roads will move to “good repair”
- Pavement conditions will stabilize.
Proposition 6 Defeat: Thank You

- Every city accepting new SB 1 revenue,
  - Submitting Annual Project Lists
  - Submitting Annual Expenditure Reports
- City officials helped defend local transportation funding
- Educating residents about the local transportation projects and public benefits to be provided under SB 1
- Cities that supported the passage of SB 1, sending in letters of support, providing public testimony, etc.

Housing and Land Use: Year in Review

- **Housing Package 2017**: 15 bills, Prop1&2
- Housing and land use legislation 2018: hundreds of bills
  - **SB 827 (Wiener)**. Rezone within 1/2-mile “major transit stop” or 1/4-mile of transit stop on “high quality transit corridor.” *Halted in Senate.*
  - **SB 831 (Wieckowski)** to prohibit fees on second-units.
  - **SB 828 (Wiener)** and **AB 1771 (Bloom)** comprehensive changes to Regional Housing Needs Assessment (RHNA) process;
  - **AB 2162 (Chiu)** requires that supportive housing be “use by right” where multiple dwelling uses are permitted, including mixed-use zones;
  - **AB 2923 (Chiu and Grayson)** provides the Bay Area Rapid Transit (BART) land use authority over its property.
  - Add’tl $500 million (one-time) for homeless programs
Housing and Land Use: Coming at Us

- Roll-out of $500 million, Prop1, Prop2
- Newsom: 3.5 million housing units by 2025
- $ penalties on cities for not building housing?
- Cap/reduce/eliminate local impact fees?
- Mandatory state densities around transit
- Eliminating fees for accessory dwelling units
- Regional solutions
- CEQA “stadium” streamlining for affordable housing
- Increasing tenant protections
- Housing land use fire-prone areas
- Newsom: expand housing tax credits from $85 to $500 million
- Tax increment tools

Public Works & Transportation

**AB 636 (Irwin)** Streets & Roads Reporting. Reports are now due to State Controller (SCO) December 1 (previously Oct 1)

*Note: this change does not apply to SB 1 expenditure reporting requirements, which are still due October 1*

**SB 848 (Budget)** Cities and counties may reimburse themselves from Road Maintenance and Rehabilitation Account funds across multiple fiscal years for transportation projects consistent with the uses allowed under SB 1
Contracting  General Law Cities

**AB 2249 (Cooley)** Bidding Thresholds.
- Increases no-bid cap from $45,000 to $60,000
- Increases informal bid range of $45,000 to $175,000 to new range of $60,000 to $200,000
- Formal bidding procedures for any project over $200,000

Wildfire and Disaster Response

**SB 901 (Dodd)**
- $1 billion+ over five years for forest management and fire prevention;
- Streamlines procedures for forest thinning and fuel reduction;
- Increases energy production from biomass fuels;
- Advance placement of firefighters, equipment and fuel reduction;
- Requires utilities adopt wildfire mitigation plans;
- Utilities may securitize wildfire debts, recover costs from ratepayers;
- Establishes the Commission on Wildfire Cost Recovery.

**SB 833 (McGuire)** improves emergency notifications, provides $50 million for pre-positioning emergency equipment.
Revenue and Taxation

**AB 1838 (Budget)** Prohibition of Taxation on Groceries-Soda
- Prohibits local taxes on groceries for 12 years
- Charter cities: sales taxes withheld if they enact a tax
- Upon the Governor’s signature, “Tax Fairness and Accountability Act” removed from November 2018 ballot

Tax Increment Financing

**AB 2035 (Mullin)** Affordable Housing Authorities
- Makes helpful revisions to improve usefulness of the law
- Allows use of base year five-years prior
- Allows financing of infrastructure to support affordable housing
- Does not allow property tax revenue from former RDA area until debts are repaid.
Tax Increment Financing

**SB 961 (Allen)** EIFD-NIFTI-2

- EIFD must be coterminous with establishing city/county
- 40% dedicated to below 60% AMI (half must be spent on below 30% AMI)
- 10% must be spent on parks, urban forestry, pedestrian or bicycle facilities.
- Residency priorities to those displaced or employed w/in 2 miles of district.
- Remaining revenues must be spent on:
  - Multi-family affordable housing with commercial space on ground floor.
  - Transit capital projects.
  - Transit-oriented development projects.
  - Capital projects that implement a complete streets programs.
  - Parking structures in lieu of onsite parking for proposed developments.
- No public vote of EIFD bond issuance if comprehensive public protest/vote options are complied with that are identical to provisions required of Community Revitalization Investment Authorities (CRIAs)

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Housing, Redevelopment, etc: Looking Ahead

**SB 5 (Beall/McGuire)** A city, county, or JPA would be eligible for additional property tax if project contains: (1) affordable housing, (2) transit-oriented development, (3) infill development, (4) revitalizing and restoring neighborhoods, and (5) planning for sea level rise. $2 billion /yr.

**AB 11 (Chiu)** the Community Redevelopment Law of 2019. No less than 30% of taxes allocated to increase, improve, preserve low- and moderate-income housing. Strategic Growth Council approves development plans re greenhouse gas emission redux.
Housing, Redevelopment, etc: Looking Ahead

SB 50 (Wiener) “Equitable Communities Incentive.”
Revision of SB827 transit oriented development. Targets transit and job-rich areas, includes a “sensitive communities” designation to allow gentrifying communities the ability to opt out of SB 50 with their own community plans.

Tax Reform: League Activity
✓ League policy re sales tax
   • Expand the base
     ▪ Digital goods
     ▪ Services
   • Improve Allocation & Collection
     ▪ County pools – use tax
     ▪ Tax shifting agreements
     ▪ Destination sourcing – sales tax
✓ Years of task forces, study, policy committee discussion
✓ City Managers Sales Tax Working Group
✓ SCA20 (Glazer)
Tax Reform: Looking Ahead

Sales Tax
- *South Dakota v Wayfair* implementation
- “Sales tax” on services - Hertzberg
- Local allocation “point of sale” – Glazer
- County pools

Tax Reform: Looking Ahead

Property Tax
- Property-Tax in Lieu of VLF for annexations & incorporations
- Split roll property tax on November 2020 ballot
- Realtors want new version of Prop5 (Prop13 AV transfer)
  - LAO: benefit going to dependents who rent out the property
Tax Reform: Looking Ahead

- 2/3rds vote for taxes cap?
- 55% vote for bonds ACA1 (Aguiar-Curry)
- Newsom: State Tax Reform Discussion

Pensions

- Pension/OPEB sustainability and reform
- Outcome of Cal Fire “California Rule” decision
- CalPERS litigation against defaulting agencies
Labor

✓ Renewed focus on prohibiting contracting for services: AB 1250 (2017)
✓ Workers comp: off duty claims, cumulative trauma and apportionment re: race/gender

Federal: Looking Ahead re Local Finance

✓ Infrastructure funding
✓ FCC & limiting cable franchise fees
✓ Cannabis banking
✓ 5G wireless cell siting
✓ Post South Dakota v Wayfair proposals