REVENUE AND TAXATION POLICY COMMITTEE
Thursday, April 12, 2018
10:00 a.m. – 3:00 p.m
Sheraton Fairplex Hotel & Conference Center, 601 West McKinley Avenue, Pomona

AGENDA

SPECIAL ORDER: State Budget and Issues Briefing for all policy committee members
10:00 – 10:45 a.m., Room California 2, Sheraton Fairplex Hotel & Conference Center

I. Welcome and Introductions

II. Public Comment

III. Legislative Action Items Review
SCA 20 and SB 1466 (Glazer), Local Sales Tax Allocation (Attachment A) – Action

IV. Discussion on Next Steps on Sales Tax Modernization
- City Manager Sales Tax Working Group Update (Attachment B)
- Pending Quill decision (Attachment C)
- SB 993 (Hertzberg), State Services Tax (Handout)

V. Legislative and Policy Update
- League Supported June Ballot Measures: (Attachment D)
  o Prop 68: $4 billion park/water bond
  o Prop 69: Protecting transportation funds
  o Prop 72: Rainwater capture, prop tax exemption
- League Supported November Ballot Measures:
  o SB 3 Beall) $4 billion affordable housing bond
- League Opposed Measures Gathering Signatures for November Ballot:
  o Business Roundtable 2/3rds Vote Measure (17-0050 A #1) (Attachment E)
  o Repeal & Restrictions on Transportation Funding (17-0033 A#1) (Attachment F)
- Legislative Responses to Impacts of Federal Tax Reform
- League Sponsored Incorporation and Annexation Bills: AB 2941 (Cooley) and AB 2268 (Reyes) (Attachment G)

VI. Presentation on Next Steps on Tax Increment: (Attachment H)
Dan Carrigg: PowerPoint

VII. Pension Reform Update
Dane Hutchings, League Legislative Representative, Governance, Transparency and Labor Relations (Attachment I)

Next Meeting: Thursday, June 7, Sacramento Convention Center, 1400 J Street, Sacramento

NOTE: Policy committee members should be aware that lunch is usually served at these meetings. The state’s Fair Political Practices Commission takes the position that the value of the lunch should be reported on city officials’ statement of economic interests form. Because of the service you provide at these meetings, the League takes the position that the value of the lunch should be reported as income (in return for your service to the committee) as opposed to a gift (note that this is not income for state or federal income tax purposes—just Political Reform Act reporting purposes). If you would prefer not to have to report the value of the lunches as income, we will let you know the amount so you may reimburse the League.

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.

Informational Items: Any agenda item listed for informational purposes may be acted upon by the Policy Committee if the Chair determines such action is warranted and conforms with current League policy. If the committee wishes to revise League policy or adopt new policy for an item listed as informational, committees are encouraged to delay action until the next meeting to allow for preparation of a full analysis of the item.
1. SCA 20 (Glazer) and SB 1466 (Glazer) Local sales taxes: online sales. (Full Bill Text Here) (Full Bill Text Here)

**Bill Summary:**
SCA 20, a proposed Constitutional Amendment, authorizes the Legislature, effective January 1, 2020, to change the method for allocating the local Bradley-Burns Uniform Local Sales and Use Tax derived from sales of tangible personal property by a qualified retailer that is “transacted online,” as that term is further defined by the measure.

SB 1466 would become operative on January 1, 2020, if ACA 20 is approved by the voters, and defines the location where an online retail sale of tangible personal property occurs is the point of the delivery of that property to the purchaser’s address or any other address designated by the purchaser. The definitions in the language mirror the language in SCA 20.

**Bill Description:**

SCA 20, a proposed Constitutional Amendment, requires a two-thirds legislative vote to be placed on the ballot, and does the following:

1) Authorizes the Legislature, effective January 1, 2020, to change by a majority-vote statute the method for allocating the local Bradley-Burns Uniform Local Sales and Use Tax Law derived from sales of tangible personal property by a qualified retailer that is transacted online.

2) Defines “transacted online” as transaction where:
   a. The purchaser’s order and payment for the sale is transacted and completed on an Internet Web site or web-based application.
   b. The purchaser’s order and payment is not initiated by the retailer using the retailer’s equipment at the retailer’s qualified place of business.
   c. The purchaser does not receive the tangible personal property at the qualified retailer’s place of business or at another location designated by the qualified retailer.

3) Defines a “qualified retailer” as a retailer whose total cumulative annual gross receipts from all of the retailer’s sales, of tangible personal property transacted online for the preceding 12 months exceeds ($100,000) one hundred thousand dollars.

SB 1466 would become operative on January 1, 2020, if ACA 20 is approved by the voters, and defines the location where an online retail sale of tangible personal property occurs is the point of the delivery of that property to the purchaser’s address or any other address designated by the purchaser. The definitions in the language mirror the language in SCA 20.

**Background:**
Senator Glazer’s impetus for this measure is derived from the recommendations from the [2017 California State Auditor’s Report](#), which raised numerous issues with the
allocation of the local Bradley-Burns Uniform Local Sales and Use Tax. This report recommends that the Legislature amend the Bradley-Burns law to allocate revenues from Internet sales based on the destination of sold goods rather than their place of sale. The report goes further and recommends the Legislature should regularly review and evaluate tax expenditures, including exemptions and exclusions to the Bradley-Burns tax and general sales and use taxes. The report also recommends that the California Department of Tax and Fee Administration should help address California’s e-commerce tax gap and further ensure out-of-state retailers’ compliance with state law regarding nexus by implementing a two-year pilot of its authorized reward program for information resulting in the identification of unreported sales and use taxes.

**Fiscal Impact:**
Changing the allocation of the local Bradley-Burns can have major consequences to affected local agencies, especially cities. Internet purchasing is a major and growing trend which is rapidly eroding traditional “brick and mortar” sales. Depending on how the reallocation is directed by the Legislature, this measure would result in major shifts of revenue for some cities, affecting their budgets by millions per year.

It is critical to note, that SCA 20, as drafted, creates two major uncertainties for local revenue:

1) It does *not limit how* the Legislature can reallocate local sales taxes derived from online purchases. While SB 1466 currently proposes that the revenue be allocated to the location where products are received by the purchaser, the Legislature could change the criterial to any other method by a majority vote.

2) It removes the current protections for local sales taxes from legislative shifts placed in the Constitution by Proposition 1A of 2004. Prop 1A, prohibits the ability of the Legislature to “change the method for distributing revenues derived under, the Bradley-Burns....as that law read on November 3, 2004.” Prop 1A currently allows only two exceptions:
   - A local agreement between individual local agencies to exchange shares of property tax revenue for sales tax revenue.
   - To allow the state to participate in an interstate compact or comply with federal law.

SCA 20 would remove those protections for revenues derived from online sales.

**Existing League Policy:**
Sales tax is a very important revenue source for cities. Fundamental changes, however, are taking place in e-commerce and the retail marketplace that are eroding the growth of sales tax as a revenue source and changing its allocation. This change is happening quickly and affects cities and their budgets even if they do nothing. Contributing factors include:

- a shifting economy driven more by services than sales of tangible goods;
- difficulties associated with collecting taxes from remote internet sales;
a changing retail marketplace which relies on distribution from large warehouses rather than brick and mortar purchases which can change where sales tax is allocated;

- games played by tax consultants and corporations seeking local rebate agreements to shift where sales tax is allocated, and

- overall tax rates (combined state and local rates) approaching 10 percent in some areas, resulting in higher rates for consumers on a narrowing base.

In 2015 and 2016 the League Revenue and Taxation held extensive discussions on potential modernization of tax policy affecting cities, with a special emphasis on the sales tax. The issues had been identified by League leadership as a strategic priority given concerns in the membership about the eroding sales tax base and the desire for the League to take a leadership role in addressing the associated issues. The policy committee ultimately adopted a series of policies that were approved by the League board. Among its changes were a recommended change to existing sales tax sourcing (determining where a sale occurs) rules, so that the point of sale (situs) is where the customer receives the product. The policy also clarifies that specific proposals in this area should be carefully reviewed so that the impacts of any changes are fully understood.

In the fall of 2017, the League City Managers Department convened a working group of city managers representing a diverse array of cities to review and consider options for addressing issues affecting the local sales tax. Given the importance of the sales tax and its allocation to cities, it remains important for cities to help shape any future policy direction in this area. The group has met twice, and will hold a third meeting in conjunction with League policy meetings in Pomona in mid-April. The primary focus of the working group is dealing with the sensitive issues associated with a potential shift to destination allocation, and options to minimize financial burdens associated with a transition.

**Below is the League’s Existing League Policy Affecting Sales Tax**:  
**Sales and Use Tax Base**: The League 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.

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1 These excerpts are from the League’s 2016 Summary of Existing Policy and Guiding Principles.  
Sales Tax Sourcing Rules: Support as League 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.

County Pool Use Tax Allocations: Support the League working with the state Board of Equalization 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).

State Sales Tax Exemptions: The League 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.

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.

Federal Legislation Requiring Use Tax Collection
The League 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 State
Board of Equalization would likely require appropriate software for remote sellers to implement the new system.

**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, the League 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 State Board of Equalization and other parties on alternative efforts to increase the collection of use taxes within California. Share the League’s 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.

**Comments:**

1) The release of the State Auditor’s report last fall, and the introduction of Senator Glazer’s legislation this spring, provide additional momentum to a discussion affecting the allocation of local sales tax dollars to California cities and counties. As reflected in the summary of past League policy discussions, there is nothing new here. City officials are well aware of how the Internet and changing retail market place is eroding revenue from traditional “brick and mortar” stores and changing where local dollars go. Shifting to a destination allocation process may be the right policy, but any transition needs to be managed in a careful and thoughtful manner to mitigate major harm to affected agencies. Senator Glazer’s measure proposes a shift on or after January 1, 2020; such a change will likely be too abrupt for negatively impacted communities that have made economic development and budgetary projections decisions based upon existing rules and revenues.

2) Before wading into policy issues, Senator Glazer’s intent with SCA 20 needs to be further clarified. Since that measure, as drafted, would allow the Legislature to shift local sales tax derived from internet purposes based upon other criteria going forward. Any such open-ended legislation would be a gateway for future state takeaways from local government, and undermine the hard won victory in Proposition 1A of 2004. If a fix is to be drafted, in needs to be narrowly–crafted and ensure local revenue remain protected from future state shifts. League staff has contacted the author’s staff on this issues and it appears the author is
willing to narrow the language so that it is limited to the destination allocation issue.

3) With the prospect of legislation pending, the formation of the existing League City Manager Working Group to focus on sales tax allocation issues was timely. Yet this group should be able to continue its work in an effort to develop a thoughtful approach for cities. An update will be provided to the League’s Revenue and Taxation Committee at its April meeting. It would be unfortunate if such efforts were derailed by what may be well-intentioned, but premature legislation.

4) Several terms used in this measure require further clarification and definition. The definition of “transacted online” has several potential problems. It may be difficult to determine that the purchaser’s order and payment is not initiated by the retailer using the retailer’s equipment at the retailer’s qualified place of business. It would be difficult to know if a retailer initiated the sale or not without a clearer definition of “initiate.” A definition of “qualified retailers place of business” is also needed, and there will likely be other necessary definitions and clarifications.

5) It is not clear why an exception needs to be made here for smaller retailers with less than $100K in online sales. If there are required to collect and remit sales taxes, why not apply the revised process to all online sales?

Support-Opposition: (as of 04/04/2018): None Received: Author’s staff states that many groups are still analyzing the measure.

Staff Recommendation: Support efforts by League City Manager Working Group to develop the details of a proposed solution; report back at June 7th Committee meeting. Request the author to narrow the existing version of SCA 20 to only apply to destination allocation of internet sales—with no opportunity for future legislative shifts for other purposes-- then keep the issue as a “work in progress” while the League works to develop an acceptable transition mechanism and timeline, that is appropriately sensitive to impacts on negatively affected cities.

For the last several years, the League has had extensive internal discussions on sales tax modernization. The reasons for these discussions is that Internet sales is rapidly changing the retail environment and eroding and shifting local revenue. Cities have the most at stake when it comes to allocation issues, and the League should be a leader in developing solutions. Not leading at this juncture, is not a desirable option, because it allows the vacuum to be filled by others who are less sensitive to city interests.

Committee Recommendation:
Local Sales and Use Tax “Sourcing”: Rules for Rate and Allocation

“Sourcing” is the term used by tax practitioners to describe the rules used to determine the place of sale, and therefore, which tax rates are applied to a given purchase and which jurisdictions are entitled to the local and district taxes generated from a particular transaction. In most cases, this doesn’t affect over-the-counter sales where the location of the business and the location of receipt by the purchaser are the same.

However, in cases where the location of the purchaser, the seller and the product are in different locations, the definitions of source become important. Location of the seller’s office? Location of the product inventory? Location where the product is delivered to the consumer? Location where the product is first used? This has become a critical issue for cities as the nature of retail transactions changes.

Origin Sourcing

“Origin sourcing” is a sales tax practice under which sales taxes for purchases of goods that are shipped to purchasers are generally sourced to the business location of the retailer where the sale originates.

In an origin sourcing framework, the sale of a product is sourced to the place of business of the seller - whether the product is received by the purchaser at the seller’s business location or not. However, if the tangible personal property sold is delivered to an out-of-state destination or to a common carrier for delivery to an out-of-state destination, the sale is exempt from tax.

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<th>States Using Origin as the Situs for Sales Tax Allocation</th>
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<td>Arizona</td>
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<td>California</td>
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Destination Sourcing

“Destination sourcing” rules stipulate that retail sales be sourced to the location where the purchaser receives the property. If this information is not available to the retailer at the time of sale, there are alternate methods to source the tax.

In a destination sourcing framework, the sale of a product is usually be sourced as follows:

1. When the product is received by the purchaser at the seller’s business location, the sale is sourced to that business location. (Same as Origin Sourcing in practice)
2. When the product is not received by the purchaser at the seller’s business location, the sale is sourced to the location where receipt by the purchaser occurs, including the location a) indicated by delivery instructions known to the seller or b) the address for the purchaser as indicated in the seller’s records.

Most states use destination-based sourcing rules for sales tax.

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<th>States Using Destination as the Situs for Sales Tax Allocation</th>
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California’s Blended Method

California is primarily an origin-based sourcing state. However, California uses a form of destination sourcing for the local use tax and for district taxes (also known as “transactions and use taxes” or “add-on sale and use taxes”).

In summary, California’s origin sourcing rules for the local sales tax (i.e., Bradley Burns 1%) are:

1. The sale is sourced to the place of business of the seller - whether the product is received by the purchaser at the seller’s business location or not.
2. If the tangible personal property sold is delivered to an out-of-state destination or to a common carrier for delivery to an out-of-state destination, the sale is exempt from tax.
3. If the retailer maintains inventory in California and has no other in state location, the source is the jurisdiction where the warehouse is situated.
4. If the order desk/sales office is located in California but the merchandise is shipped from out of state, the tax from transactions under $500,000 is allocated via the county pools. The tax from transactions over $500,000 is allocated to the jurisdiction where the merchandise is delivered.
5. When a sale cannot be identified with a permanent place of business in the state, the sale is sourced to the allocation pool of the county where the merchandise was delivered and then distributed among all jurisdictions in that county in proportion to ratio of sales. If the county of delivery cannot be identified, the revenue is distributed among all jurisdictions in the state in proportion to ratio of sales.

California’s Bradley Burns Sales and Use Tax

The allocation of the Bradley-Burns local sales tax revenue in California first depends on whether the transaction is subject to sales tax or to a use tax. Sales tax applies on a taxable sale if 1) the seller’s registered place of business is in California and 2) title of the goods passes to the customer within this state. If both of these conditions are not met, the transaction is subject to a use tax.

Sales tax is allocated to the jurisdiction where the principal negotiations are carried out or where the order is taken. For a site within a given jurisdiction to qualify as a “point of sale,” “the seller must have a proprietary interest in the site (owns or leases) and have its own employees operating at the site who customarily negotiate sales or take orders.”¹ If the seller does not have a sales office or order desk in California but does maintain an in-state stock of goods that the seller owns and controls through its own employees, the in-state location from where the goods are delivered becomes the “point of sale.”²

The Jet Fuel Exception.
The tax on jet fuel is allocated to the jurisdiction where the plane is fueled. By contrast, the tax on fuel (e.g. motor vehicle fuel, etc.) sold at unmanned cardlock stations is allocated to the jurisdiction where the contract is negotiated.

¹ Territorial sales people working out of their homes and independent manufacturer’s representatives do not qualify as a “point of sale.”
² If the sales price includes permanent affixation to the buyer’s property or if the transaction is financed by lease for a period of 30 days or longer, the transaction is subject to use tax.

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Use tax applies when title to the purchased goods passes to the customer from out-of-state which is the case for most catalog or online orders when shipped from out-of-state destinations. Title is deemed to pass to the customer at the time the goods leave the seller’s dock and are turned over to the common carrier who will be delivering the merchandise. Other transactions subject to use tax include catering trucks, auctions, vending machines, and itinerant vendors where it is impractical to identify the multiple jurisdictions where the seller operates. Purchases of vehicles registered at the Department of Motor Vehicles from private parties without a sellers permit are also considered as use tax.

The local (i.e. Bradley Burns) share of use tax is allocated to the county where the property is first placed into first functional use, the so-called “county pool.”

Jet Fuel Exception. The tax on jet fuel is allocated to the jurisdiction where the plane is fueled. By contrast, the tax on fuel (e.g. motor vehicle fuel, etc.) sold at unmanned cardlock stations is allocated to the jurisdiction where the contract is negotiated.

Countywide and Statewide Pools in California

Under current California State Board of Equalization (BOE) regulations, a substantial portion of local use tax collections are allocated through a countywide pool to the local jurisdictions in the county where the property is put to its first functional use. The state and county pools now constitute over 15% of local sales and use tax revenues. Under the pool system, the tax is reported by the taxpayer to the countywide pool of use and then distributed to each jurisdiction in that county on a pro-rata share of taxable sales. If the county of use cannot be identified, the allocation goes to the state pool for pro-rata distribution on a statewide basis.

BOE rules call for the use of these pools rather than sending the revenue to the jurisdiction of first use despite the fact that - in most cases now - transactions include a district tax component which is allocated not to any pool, but to the specific jurisdiction. For example, Amazon collected an 8% rate on my purchase of a book last week, the total rate in my hometown. This includes a 0.5 percent rate, the add-on transactions and use tax (district tax) allocated to my city. But the Bradley Burns one percent portion of the tax I paid goes into the county pool and is shared among all cities and the county. Under destination sourcing rules, that local one percent would be allocated to the city, a stronger move toward true situs allocation.

The largest components of these pools are from:

- Private party sales of vehicles, vessels and aircraft registered at the Department of Motor Vehicles, and mobile homes reported by the Department of Housing and Community Development.
- Private party sales of vessels (not required to register with the DMV) and aircraft purchases.
- Use tax paid by contractors who are considered consumers of materials purchased without tax, but used by the contractor in the improvement of real property, and whose job site is regarded as the place of business.
- Merchandise shipped directly to consumers by common carrier from inventory located outside the state with the title passing out of state.

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3 Free On Board - FOB is a trade term requiring the seller to deliver goods on board a vessel designated by the buyer.

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• Long term leases of tangible personal property except long term leases of motor vehicles (see below).
• Catering trucks, itinerant vendors, vending machine operators and other permit holders who operate in more than one local jurisdiction and are unable to readily allocate taxable transactions to specific points of sale.
• Use tax on purchases consumed at non-selling facilities (research and development, for example.)
• Use tax on motor vehicle leases negotiated by out-of-state leasing companies.

State law does provide special allocation procedures for use taxes collected on certain products. Generally, these special allocation rules allow use tax revenue that would otherwise be shared via the countywide and statewide pools to be directly allocated to the jurisdiction of use. These include:

• **Long Term Leases of Motor Vehicles (greater than four months)**: Sales tax from rentals of equipment and vehicles is allocated to the jurisdiction where the rental company is located. Rentals exceeding four months or longer are considered long term leases. When the leased vehicle is either purchased from a California dealer or leased by a California dealer-lessee, the tax is allocated to the place of business of the dealer or lessor. If the leased vehicle comes from an out-of-state source, the tax is allocated through the county-wide use tax allocation for the county in which the vehicle is registered.

• **Auctioneers** conducting auction events at locations other than their regular place of business when the taxable sales total $500,000 or more: The local tax is to be allocated to the jurisdiction in which the auction occurs.

• **Construction Contracts equal or greater than $5,000,000**. Construction contractors have the option to allocate use tax on materials consumed and fixtures furnished directly to the jurisdiction where the jobsite is located if the sales or purchase value exceeds $5 Million. The Board of Equalization will not allocate to the jobsite if a sub permit for the location is not taken out prior to commencement of the project.

• **Sales and Purchases of $500,000 or More Subject to Use Tax**. Use tax from transactions by out-of-state retailers who are engaged in business in California is allocated to the jurisdiction in which the first functional use of the property occurs. This generally is deemed to be the jurisdiction to which the goods are shipped.

**California’s District Taxes (Transactions and Use Tax add-on rates)**

There are currently 135 municipal (city) transactions districts and 44 countywide districts with voter approved transactions and use tax rates apply in addition to the 7.25% combined state and local sales and use tax. Unlike the rest of the California combined sales tax rate, these district transactions and use taxes generally use a form of destination sourcing.

If the seller in a taxable transaction is engaged in business in a district where the property is shipped for use, the retailer is required to collect the district use tax from their customers in that district. This applies to most taxable transactions.

4 However, the transactions and use tax does not apply if the property is delivered by the retailer or his or her agent to an out-of-state or out-of-district destination, or to a common carrier for delivery to an out-of-state or out-of-district destination.

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If a retailer is engaged in business\textsuperscript{5} in a district where the property is shipped for use, the retailer is required to collect the district use tax from their customers in that district.

In cases where the tax applies but is not collected (e.g., where the seller has insufficient legal nexus in California, etc.), the use tax component of the district transactions and use tax rate is to be paid by the purchaser.

In implementation, district transactions and use taxes are applied the same as the sales and use tax except:

- Sales of property made in a tax district and delivered to a customer outside the district may not be subject to the district tax.
- Retailers located outside a district delivering property into a district may be required to collect the district’s tax if they are “engaged in business” in the district.
- Retailers or lessors of vehicles or undocumented vessels are required to collect district use tax imposed in the district(s) of registration.
- Sales of tangible personal property, other than fuel or petroleum products, to operators of aircraft are exempt if (1) the aircraft is used as a common carrier of persons or property and (2) the property purchased will be used or consumed principally outside the district where the sale was made.
- Fixed price contracts, including leases entered into prior to the starting date of a new district tax may not be subject to that district tax.

In the particular case of motor vehicle sales, the district tax is sourced to the location where the property is registered.

\textsuperscript{5} “Engaged in business” means that the seller does any of the following: • Maintains, occupies, or uses any type of office, sales room, warehouse, or other place of business in the district, even if it is used temporarily, indirectly, or through an agent or subsidiary. • Has any kind of representative operating in the district for the purposes of making sales or deliveries, installing or assembling tangible personal property, or taking orders. • Receives rentals from a lease of tangible personal property located in the district. • Sells or leases vehicles or undocumented vessels which will be registered in a district. • Leases, stores, or consumes tangible personal property in the district.
Fig 4: Remote (Online) Sale—In-State Business Office

- Seller’s Place of Business
  - Sales Office: City A
  - Warehouse: City C or out of state
  - Factory: City B or out of state

- Buyer Receives at
  - Residence or Place of Business

Product Delivered

*If the seller is in the same Transactions and Use Tax “district” as the buyer, then the seller is responsible for collecting and remitting the tax. If the buyer is in a different district, the buyer is responsible.

Fig 5: Remote (Online) Sale—In-State Warehouse, Out-of-State Sales Office

- Seller’s Place of Business
  - Sales Office: Out of State
  - Warehouse: City C
  - Factory: City B or out of state

- Buyer Receives at
  - Residence or Place of Business

Product Delivered

*If the seller is in the same Transactions and Use Tax “district” as the buyer, then the seller is responsible for collecting and remitting the tax. If the buyer is in a different district, the buyer is responsible.
Fig 6: Remote (Online) Sale — Out of State Business

- **Seller’s Place of Business**
  - Sales Office: Out of State
  - Warehouse: Out of State
  - Factory: Out of State
  - Third-Party Warehouse: City C

- **Buyer Receives at**
  - Residence or Business

- **Product Delivered**
  - City D

- **Product Drop-shipped**
  - City C

**Guidelines for Allocation of Local Tax - Online and In-Store**

<table>
<thead>
<tr>
<th>Place of Sale</th>
<th>Location of Goods at the Time of Sale</th>
<th>How Customer Receives Goods</th>
<th>Allocation of Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Online — Order is placed or downloaded outside</td>
<td>California Fulfillment Center</td>
<td>Shipped to California Customer</td>
<td>Local tax is allocated to the jurisdiction in which the fulfillment center is located</td>
</tr>
<tr>
<td>California</td>
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<tr>
<td>Online — Order is placed or downloaded in California</td>
<td>California Fulfillment Center</td>
<td>Shipped to California Customer</td>
<td>Per CDTFA Regulation 1802, local tax is allocated to the jurisdiction where the order is placed</td>
</tr>
<tr>
<td>Online</td>
<td>Out of State Fulfillment Center</td>
<td>Shipped to California Customer</td>
<td>Local tax is allocated to the countywide pool based on point of delivery</td>
</tr>
<tr>
<td>Online</td>
<td>Out of State Fulfillment Center</td>
<td>Picked Up In-Store (Click &amp; Collect)</td>
<td>Local tax is allocated to the countywide pool based on point of delivery</td>
</tr>
<tr>
<td>Online</td>
<td>California Fulfillment Center Owned and Operated by Third Party Vendor</td>
<td>Drop-Shipped to California Customer</td>
<td>Local tax is allocated to the countywide pool based on point of delivery</td>
</tr>
<tr>
<td>Online</td>
<td>In-Store (Goods withdrawn from store inventory)</td>
<td>Shipped to California Customer</td>
<td>Local Tax is allocated to the jurisdiction where the store is located</td>
</tr>
<tr>
<td>Online</td>
<td>In-Store (goods withdrawn from store inventory)</td>
<td>Picked Up In-Store (Click &amp; Collect)</td>
<td>Local Tax is allocated to the jurisdiction where the store is located</td>
</tr>
<tr>
<td>In-Store</td>
<td>In-Store (Goods withdrawn from store inventory)</td>
<td>Over the Counter</td>
<td>Local Tax is allocated to the jurisdiction where the store is located</td>
</tr>
</tbody>
</table>

*Courtesy of HdL Companies*

*CaliforniaCityFinance.com*
Tax Incentive Programs, Sales Tax Sharing Agreements

In recent years, especially since Proposition 13 in 1978, local discretionary (general purpose revenues) have become more scarce. At the same time, options and procedures for increasing revenues have become more limited. One outcome of this in many areas has been a greater competition for sales and use tax revenues. This has brought a rise in arrangements to encourage certain land use development with rebates and incentives which exploit California’s odd origin sales tax sourcing rules.

The typical arrangement is a sales tax sharing agreement in which a city provides tax rebates to a company that agrees to expand their operations in the jurisdiction of the city. Under such an arrangement, the company generally agrees to make a specified amount of capital investment and create a specific number of jobs over a period of years in exchange for specified tax breaks, often property tax abatement or some sort of tax credit. In some cases, this has simply taken the form of a sales office, while customers and warehouses and the related economic activity are disbursed elsewhere in the state. In some cases the development takes the form of warehouses, in which the sales inventory, owned by the company, is housed.6

Current sales tax incentive agreements in California rebate amounts ranging from 50% to 85% of sales tax revenues back to the corporations.

Today, experts familiar with the industry believe that between 20% to 30% of local Bradley-Burns sales taxes paid by California consumers is diverted from local general funds back to corporations; over $1 billion per year.

Moving to Destination Sourcing: The Concept7

A change from origin sourcing rules to destination sourcing rules for the local tax component of California’s sales tax would improve overall revenue collections and distribute these revenues more equitably among all of the areas involved in these transactions.

A change from origin based sourcing to destination based sourcing would have no effect on state tax collections. However, it would alter the allocations of local sales and use tax revenues among local agencies. Most retail transactions including dining, motor fuel purchases, and in-store purchases would not be affected. But in cases where the property is received by the purchaser in a different jurisdiction than where the sales agreement was negotiated, there would be a different allocation than under the current rules.

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7 The same issues that are of concern regarding the local sales tax do not apply to California’s Transactions and Use Taxes (“Add-on sales taxes”) as these transactions, when not over the counter, are generally allocated to the location of use or, as in the case of vehicles, product registration. There is no need to alter the sourcing rules for transactions and use taxes.

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Under California’s current origin based sourcing rules, retail sales are generally sourced to the local jurisdiction of the retailer’s place of business and where the principal sales negotiations took place. Under destination based sourcing, sales are instead sourced to the jurisdiction where the purchaser receives the property, if the information is available to the retailer at the time of sale. If the location where the purchaser takes possession of the property is not known by the seller, alternative methods to source the tax include (in order):

- the location indicated by delivery instructions known to the seller,
- the location indicated by the address of the purchaser available in the seller’s records,
- the location of the purchaser’s payment instrument, or
- the location from which the property is shipped.

Moving to destination based sourcing rules will not reduce the amount of local tax collected (in fact it will INCREASE the overall amount of tax retained by cities and counties), but it would result in different allocations among local jurisdictions. These differences would occur in cases where a retailer ships or delivers the property sold to locations outside the local jurisdiction of the retailer’s place of business. Specifically, a different allocation would occur under destination sourcing if:

1. The sold property is delivered to the purchaser in another taxing jurisdiction, or
2. The purchaser receives the property at a retailer’s business location other than where the principal negotiations took place.

Cities and counties that are comprised of a large number of retailers that routinely sell property that is shipped or delivered to purchasers outside their local jurisdiction may see a reduction in tax revenues compared to the current origin based system. But cities and counties that are comprised of businesses with a significant amount of over-the-counter sales and residences that receive property from outside their local jurisdiction, may see an increase in local revenues.

Moving to Destination Sourcing: Issues

1. **Destination Sourcing Would Add Some Complexity for Some Sellers.**

For most transactions, including brick and mortar transactions and any transaction in which the seller delivers the product within the same jurisdiction, the seller’s tracking and reporting would be no different under destination rules. However, for deliveries outside the jurisdiction in which the seller resides, destination sourcing requires more information tracking. Under origin-based sourcing, sellers generally only have to know the sales tax rates in effect where their place of business is located. Destination-based sourcing requires sellers to properly apply sales tax rates for all the jurisdictions into which they deliver taxable items.

However, California’s transactions and use taxes (district taxes), now numbering over 121, require a seller to collect and remit the tax for a district if a delivery is made into that district AND the seller is “engaged in business” in that district. Large retailers with multiple locations are now, as a matter of practice, tracking collecting and remitting district tax rates. So the location of “receipt” is already being tracked and used for tax reporting. It seems no more difficult to apply this information to the sourcing of rest of the sales tax. In fact, it is arguably simpler and many large remote sellers are – for various reasons - already sourcing their transactions as “use tax” rather than sales tax.
A switch to destination sourcing would create a greater compliance burden for smaller sellers who do not currently use programs or databases to assist them in properly collect taxes. However, such programs are readily available.

2. **Destination Sourcing Would Increase City and County Revenues**

A switch to destination sourcing would increase city general fund revenues by over $800 million and as much as $1.5 billion per year. This amounts to an increase in sales tax revenues for every city of $25 to $50 per resident per year.

3. **A Switch to Destination Sourcing would Alter Revenue Allocations Among Cities and Counties**

The greatest concern regarding the switch from origin-based to destination-based sourcing is the redistribution of local sales taxes from jurisdictions where taxable items are purchased to jurisdictions where the items are delivered.

A switch to destination sourcing would cause some shift in sales and use tax revenue allocation among cities and counties. Cities with less than average per resident taxable sales of products that are delivered to locations outside the jurisdiction will see an increase in revenues. Cities with a greater-than-average per resident amount of taxable sales of products delivered other locations will see some loss. In some cases, this loss will exceed the gain in revenues from the added amount of revenues to all cities (above). It is not possible to derive reasonable estimates of the effect of this redistribution for each of California’s 533 cities and counties.

4. **Destination Sourcing Rules Reduce the Incentive for Tax Rebate Agreements**

Add-on transactions and use taxes would not need to change. California’s Transactions and use tax is already a form of destination sourcing. The exception is the special provisions for motor vehicles where the district tax is sourced to the location where the property is registered. A change in the sourcing method of the Bradley Burns rate would not require an alteration of these rules. In effect, taxes would be applied to auto sales just as they are now.

5. **Out of the Pool: Destination Sourcing Would Allocate Revenue to the True Locations of Economic Activity.**

As a part of the shift to destination based sourcing, most revenues currently allocated to pools would instead be allocated to the specific jurisdiction where the property is received. Statewide and countywide pools would only be used when it is too difficult for a retailer to identify and report tax to specific jurisdictions. In this way destination sourcing allocates these tax revenues more closely to the situs of the economic activity (the sales transaction).
Destination Sourcing Scenario 1: Full-On

"Over the Counter"

Seller’s Place of Business: Retail Store in City A
Buyer Receives at: Sales Tax in City A, Transactions Tax in City A

Automobile ... just like over the counter and Transactions Tax exception remains

Seller (dealer) is at Sales Office in City A
Buyer registers (uses) vehicle at Residence or Business in City B

Remote Sale

Seller’s Place of Business: Sales Office in City A or out of state, Warehouse in City C or out of state, Factory in City B or out of state
Buyer Receives at: Residence or Place of Business in City B

Product Delivered

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Destination Sourcing Scenario 2: Split Source

- Same as now for “over the counter” and automobile.
- Leave 0.25% on current seller if instate (origin)
- Could be phased in.
ATTACHMENT ONE: Existing League Policy

The League of California Cities’ existing policies and guiding principles include the following pertinent points:

1. 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.)

   Comment: The origin sourcing system - and the current excessive and unnecessary use of county and statewide pools for use tax allocation – encourages competitive arrangements that divert local sales tax revenue from the true “situs” location of economic activity and service impact. Destination sourcing rules reduce excessive and wasteful forms of competition.

2. The existing situs-based sales tax under the Bradley Burns 1% baseline should be preserved and protected. Restrictions should be implemented and enforced to prohibit the expansion of questionable businesses formed to circumvent the principle of situs-based sales and used to divert sales tax revenues from other regions in return for favorable treatment.

   Comment: The origin sourcing system has enabled and encouraged “the expansion of questionable businesses formed to circumvent the principle of situs-based sales and used to divert sales tax revenues from other regions in return for favorable treatment.”

3. Cities and the League should continue to emphasize efficiency and effectiveness, encouraging and assisting cities to achieve the best possible use of city resources.

   Comment: The origin sourcing system has enabled and encouraged the wasteful rebating of billions of local tax dollars, a counterproductive use of limited city resources.

4. Revenues should be logically linked to traditional and emerging responsibilities.

   Comment: The origin sourcing system has enabled the diversion of local tax revenue away from many locations of service responsibility and cost impact.

5. 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.

   Comment: The origin sourcing system - and the current excessive and unnecessary use of county and statewide pools for use tax allocation - divert local sales tax revenue from the true situs location of economic activity and service impact.

6. To preserve local authority and accountability for cities, state policies must ... offer incentives to reward cities achieving program goals rather than withhold or reduce revenues to accomplish targets.

   Comment: The current origin sourcing system creates incentives that are counter-productive to achieving program goals for most cities and encourages many to withhold and reduce revenues (i.e. through rebates). The origin sourcing approach has caused a substantial reduction in revenues for most cities.

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8 League of California Cities “Summary of Existing Policy and Guiding Principles” Revenue and Taxation section. CaliforniaCityFinance.com
ATTACHMENT TWO: California’s Special Allocations - Exceptions to the Rule

California state statutes and regulations provide for a number of exceptions to the basic sourcing rules for local taxes.

• **Retailer has more than one place of business.** If a retailer has more than one place of business in California, the sale occurs at the place of business where the principal negotiations are carried on.9

• **Retailers under Section 6015: salespersons, representatives, peddlers, canvassers, agents, etc.** The place of sale is the business location of the retailer where the principal negotiations are carried on, exclusive of any door-to-door solicitations of orders.10

• **Vending machine operators.** The place of sale is the place where the vending machine is located.11

• **Auctioneers.** The place of sale by an auctioneer when the taxable sales are less than $500,000 is the place where the auction is held and the local sales tax distributed through the countywide pool. If taxable sales are more than $500,000 in aggregate, the local sales tax is allocated to the participating jurisdiction in which the sale takes place instead of the countywide pool.12

• **Out-of-state retailers who maintain a stock of tangible personal property in California.** The place of sale is the location of the property from which delivery or shipment is made.13

• **Construction contractors.** The jobsite is regarded as the place of business of a construction contractor or subcontractor and is the place of sale for “fixtures” and the place of use for “materials,” purchased, furnished and installed by the contractor or subcontractor.

  - If the contractor reports local tax of $600 or less per year, the sale is sourced to the countywide pool.
  
  - If the contractor reports local tax of more than $600 per year, the sale sourced to the countywide pool. However, over-the-counter sales are sourced to the specific jurisdiction of the jobsite instead of the countywide pool.

  - For contracts or subcontracts for $5,000,000 or more, the contractor may elect to obtain a subpermit for the jobsite. Tax would then be sourced to the specific jurisdiction of the specific jobsite.14

• **Factory-built school buildings.** The place of sale or purchase of factory-built school buildings is the place of business of the retailer regardless of whether the sale includes installation or whether the building is placed upon a permanent foundation.15

• **Jet fuel.** In general, the sale of jet fuel is sourced to the point of delivery to the aircraft if the principal negotiations for the sale are conducted in this state and the retailer has more than one place of business in the state. If the retailer only has one place of business in the state, the sale is sourced to the retailer’s business location.16 However, for “multi-jurisdictional airports,” where an airport that is owned or operated by a city, county, or city and county that imposes a local sales tax, and is different from the city, county, or city and county in which the airport is located, the 1.00% local tax derived from the sale of jet fuel at multi-jurisdictional airports, except for San Francisco International Airport and Ontario International Airport, half of the tax is reported to the jurisdiction which owns or operates the airport and half to the jurisdiction in which the airport is located. The 1.00% local tax from the retail sale of jet fuel

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9 Rev & Tax Code Sections 7205(b)(1), 7263, Regulations 1802(a)(2), 1822(a)(2)
10 Regulation 1802(b)(3)
11 Regulations 1802(b)(1), 1822(b)(1)
12 Regulation 1802(b)(4)
13 Regulations 1802(b)(5), 1822(b)(5)
14 Regulation 1806(b), Audit Manual, Chapter 12, Construction Contractors, Section 1207.25
15 Regulations 1802(b)(6), 1806(b)
16 Rev & Tax Code Section 7205(b)(2), Regulation 1802(b)(7)
delivered to aircraft at Ontario International Airport is reported to the City of Ontario in the amount imposed by the city and to the County of San Bernardino in the amount imposed by the county.\(^{17}\)

- **Use tax on transactions of $500,000 or more.** A seller who is registered to collect use tax or a person who is required to report and pay use tax directly to the Board shall report the local use tax directly to the participating jurisdiction where the first functional use of the property is made instead of the countywide or statewide pools.\(^{18}\)

- **Retail florists.** A retail florist is a person selling any flowers, potted ornamental plants, floral arrangements, floral bouquets, wreaths, or any similar products at retail, but does not include any flower or ornamental plant grower who sells his or her own products. Tax applies to amounts charged by the florist who makes the sale whether the delivery occurs instate or out-of-state. Tax does not apply to amounts received by California florists who make deliveries in this state pursuant to instructions received from the instate or out-of-state florist who made the sale.\(^{19}\)

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\(^{17}\) Rev & Tax Code Section 7204.03, Regulation 1802(b)(7)(C)

\(^{18}\) Regulation 1802(c)

\(^{19}\) Rev & Tax Code Section 6077, Regulation 1571
U.S. Supreme Court Case Update: South Dakota v. Wayfair, Inc.

Nearly twenty-six years ago, the U.S. Supreme Court held in Quill Corp. v. North Dakota (1992) 504 U.S. 298 that states cannot require retailers with no physical presence in a state (e.g., online retailers) to collect that state’s sales tax. The U.S Supreme Court will reconsider that holding this term when it decides the case of South Dakota v. Wayfair, Inc (Docket No. 17-494).

The South Dakota v. Wayfair case involves a challenge to South Dakota’s “remote seller compliance law.” The law requires retailers to collect sales tax if the property, products, or services they deliver into the state amount to either $100,000 or more in gross revenues or 200 or more transactions. South Dakota adopted the law specifically to challenge the Court’s ruling in Quill, after Justice Kennedy signaled in 2015 that the Court may be inclined to reconsider its holding in light of the astronomical growth of internet sales since 1992.

The Supreme Court will hear oral argument on April 17 and is expected to issue a decision by the end of June.

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Corrie L. Manning, Esq.
Asst. General Counsel, League of California Cities
Proposition 68
California Drought, Water, Parks, Climate, Coastal Protection, and Outdoor Access For All Act of 2018
Chapter 852, Statutes of 2017 (Urgency)

SB 5 (De Leon), now Proposition 68, places a $4 billion bond on the June 2018 statewide ballot for parks, water, and climate and environmental programs. If the voters approve SB 5, local governments will receive funding for local park improvements and will be eligible for numerous grants to fund water, local parks, coastal and climate resiliency projects. The following is breakdown of funding in bond:

Parks Funding (Total $1.283 billion)

- $725 million for competitive grants for safe neighborhood parks
- $200 million for per capita grants to cities, counties, and parks districts for local park improvement and rehabilitation
- $15 million for competitive grants to urbanized counties
- $30 million for competitive grants for state park facilities in regional parks districts
- $40 million for per capita grants to local agencies that obtained voter approval for revenue measures between November 1, 2012 and November 30, 2016
- $218 million for restoration of existing state park facilities, including $5 million for urgent needs of local agencies that operate a unit of the state park system
- $30 million for competitive grants for non-motorized infrastructure development
- $25 million for competitive grants through the Roberti-Z'Ber-Harris (RZH) Urban Open Space and Recreation Program

Water Funding (Total $1.19 billion)

- $250 million for competitive grants for clean drinking water programs
- $550 million for flood protection and repair, including $100 million for stormwater, mudslide and flash-flood-related protections and $100 million for multibenefit flood management projects and storm water capture in urbanized areas
- $290 million for competitive grants and loans for drought and groundwater regional sustainability
- $100 million for grants or loans for water recycling programs

Climate and Environmental Programs Funding (Total $1.547 billion)

- $443 million for competitive grants for climate adaptation and resiliency programs
- $162 million for the California River Parkways Program for grants to enhance urban creeks
- $567 million for state conservancies and the Wildlife Conservation Board
- $200 million for Salton Sea restoration activities and habitat
- $175 million for coastal and ocean protection resources, including $30 million for grants for lower cost coastal accommodations
Proposition 69
June 2018 Statewide General Election

In April, 2017, the Legislature adopted SB 1 – The Road Repair and Accountability Act of 2017 and Assembly Constitutional Amendment 5. Among its many provisions, SB 1 increases the sales and use tax on diesel fuel and imposes a new transportation improvement fee. ACA 5, now Proposition 69, is a ballot measure that would amend the Constitution to protect revenues from the increased tax and new fee for transportation purposes only. Other revenue increases found in SB 1 are already protected for transportation purposes by Article XIX of the California Constitution.

The Public Transportation Account: This is a trust account in the State Transportation Fund currently protected by the State Constitution. Funds in the Public Transportation Account may only be used for transportation planning and mass transportation purposes. Funds cannot be loaned or transferred to the State General Fund or any other fund or account in the State Treasury. The state sales tax on motor vehicle fuel is deposited into the Public Transportation Account.

New Revenues from SB 1: SB 1 – the Road Repair and Accountability Act of 2017 increased the state sales tax on diesel fuel by 4%; and the state use tax on diesel fuel by 1.75%.

SB 1 also imposed a transportation improvement fee payable with an automobile registration. The fee ranges from $25 for an automobile with a market value of $4,999 to $175 for an automobile with a market value of $60,000. The fee is $100 for an automobile with a market value between $25,000 and $34,999.

Protecting New Revenues from SB 1: Proposition 69 is a measure on the June 2018 statewide ballot to amend the California Constitution. Majority voter approval is required to amend the Constitution. The amendment makes two changes to the Constitution:

- **New diesel fuel sales and use tax** must be deposited into the Public Transportation Account where their use is restricted for public transit services and capital improvements.

- **New transportation improvement fee** must be deposited into the Public Transportation Account where they can be used only for research, planning, construction, improvement, maintenance and operation of public streets and highways and public transportation systems.

The proposed constitutional amendment will ensure that the revenues from the increase in the diesel fuel sales and use tax and from the new transportation
improvement fee will be deposited into the Public Transportation Account. The Legislature cannot change how these funds are used once they are protected by the Constitution.

**Frequently Asked Questions**

Q1. When did the increase in sales tax on diesel fuel go into effect?
A1. November 1, 2017

Q2. When did the new transportation improvement fee go into effect?
A2. January 1, 2018

Q3. Does SB 1 require that the sales tax increase on diesel fuel be used for certain purposes?
A3. Yes. The Road Repair and Accountability Act of 2017 requires that:

- All but 0.5% of the total sales and use tax paid on diesel fuel be allocated to the State Transit Assistance Program for use by transportation planning agencies, county transportation commissions and the San Diego Metropolitan transit Development Board; and
- The remaining tax revenues (generated from 0.5%) be allocated for intercity rail and commuter rail for the state’s three intercity rail corridors and for commuter rail services.

Q4. Does SB 1 require that the new transportation improvement fee be used for certain purposes?
A4. Yes. SB 1 - The Road Repair and Accountability Act of 2017 allocated these revenues for the following programs:

- State Transit Assistance Program
- Congested Corridor Program
- Road Maintenance and Rehabilitation Account for local street and road maintenance

Q5. Why was Proposition 69 adopted by the Legislature when it passed SB 1?
A5: To ask the voters to amend the Constitution to ensure that the revenues from the diesel tax and the transportation improvement fee would be used for transportation planning, public transit, and transportation capital improvements.

Q6. What happens if Proposition 69 does not pass on the June 2018 ballot?
A6. The Legislature can decide to use revenues from the sales tax increase on diesel fuel and the new transportation improvement fee for purposes other than research, planning, construction, improvement, maintenance, and operation of public streets and highways and public transportation systems.
Proposition 72
June 2018 Statewide General Election

SCA 9 (Glazer) & SB 558 (Glazer), now Proposition 72, if approved by California voters, would exclude the construction or addition of a “a rain water capture system,” from being classified as “newly constructed” for the purposes of property tax assessment under Proposition 13A of the Constitution.

- Offering a property tax exclusion from the definition of “new construction” for purposes of assessing property, can be an incentive for a property owner to add a specific feature as part of new construction. The voters have authorized several exemptions from the “new construction” definition to advance various desirable policies including seismic safety, fire sprinklers, solar energy and disabled access.

- After careful consideration in our policy committees, the League opted to support this measure, because it will advance water conservation policies supported by the League. This included weighing the fiscal impacts, such as solar installations, with other exceptions to the “new construction” definition. Ultimately, we deemed the initial fiscal impacts acceptable given that a property tax exclusion from new construction only applies to the initial construction. Real property values tend to appreciate over time and the full value of the property will be assessed upon resale.

- California has been susceptible to severe drought; other countries facing such conditions have been much more aggressive in incorporating rainwater capture into their water use and conservation strategies. Incentivizing rain water capture systems in new construction will help to insulate California against future drought conditions.
SB 3 (Beall) Veterans and Affordable Housing Bond Act of 2018.
Chapter 365, Statutes of 2017
November, 2018 General Election

This measure places a $4 billion general obligation bond on the November 2018 ballot to fund affordable housing programs and the veterans homeownership program (CalVet). If approved by voters, SB 3 would fund the following existing programs:

- Multifamily Housing Program: $1.5 billion, administered by HCD, to assist the new construction, rehabilitation and preservation of permanent and transitional rental housing for lower-income households through loans to local public entities and nonprofit and for-profit developers;

- Transit-Oriented Development Implementation Program: $150 million, administered by HCD, to provide low-interest loans for higher-density rental housing developments close to transit stations that include affordable units and as mortgage assistance for homeownership. Grants are also available to cities, counties and transit agencies for infrastructure improvements necessary for the development;

- Infill Incentive Grant Program: $300 million, administered by HCD, to promote infill housing developments by providing financial assistance for infill infrastructure that serves new construction and rehabilitates existing infrastructure to support greater housing density;

- Joe Serna, Jr. Farmworker Housing Grant Fund: $300 million, administered by HCD, to help finance the new construction, rehabilitation and acquisition of owner-occupied and rental housing units for agricultural workers;

- Local Housing Trust Fund Matching Grant Program: $300 million, administered by HCD, to help finance affordable housing by providing matching grants, dollar for dollar, to local housing trusts;

- CalHome Program: $300 million, administered by HCD, to help low- and very low-income households become or remain homeowners by providing grants to local public agencies and nonprofit developers to assist individual first-time homebuyers. It also provides direct loan forgiveness for development projects that include multiple ownership units and provides loans for property acquisition for mutual housing and cooperative developments;

- Self-Help Housing Fund: $150 million – Administered by HCD, this program assist low and moderate income families with grants to build their homes with their own labor; and

- CalVet Home Loan Program: $1 billion, administered by the California Department of Veterans Affairs, provides loans to eligible veterans at below-market interest rates with few or no down payment requirements.
1. **Tax Fairness, Transparency and Accountability Act of 2018**

**Summary:**
This measure (AG 1700-50 Amd #1) proposed for the November ballot would drastically limit local revenue authority, while making comparatively minor modifications to state authority. For cities and other local agencies, it applies retroactively and voids any local measure approved by local voters on or after January 1, 2018, but prior to the effective date of this act, that does not comply with the provisions of the act, and:

**Restricting Local Tax Authority:**
- a) Eliminates local authority to impose a tax for general purposes by majority vote and instead requires all local proposed tax increases subject to a two-thirds vote. This proposal also requires two-thirds approval of all members of the local legislative body before a tax can be placed on the ballot.
- b) Requires a two-thirds vote to “extend” a tax to new territory, a new class of payor, or expanded base. For cities, this would limit all future annexations by requiring a separate two-thirds vote of the affected residents prior to applying any existing city tax. Other limitations may apply to a local interpretation that an existing local tax applies to a business or product.
- c) Expands the definition of a tax to include payments voluntarily made in exchange for a benefit received, which may cover local franchise fees.
- d) Prohibits any tax to be placed on the ballot unless it either specifically identifies by binding and enforceable limitation how it can be spent, with any change requiring reapproval by the electorate, or states in a separate stand-alone segment of the ballot that the tax revenue is intended for “unrestricted revenue purposes.”
- e) Requires tax measures to be consolidated with the regularly scheduled general election for members of the governing body, unless an emergency is declared by a unanimous vote of the governing body.
- f) Expands the application of this act to include actions and “legal authority” that may be “enforced” or "implemented" by a local government.
- g) Requires a tax imposed by initiative to also be subject to a two-thirds vote, to address concerns over the Upland decision.
- h) Clarifies a levy, charge, or exaction retained by and payable to a non-governmental entity is a tax, if the local agency limits in any way the use of the proceeds, to address concerns over the Schmeer decision.
- i) Exempts existing school bond (55% vote) construction authority from the application of the bill.

**Restricting Local Fee Authority:**
Restricts the ability of a local government to impose fees or charges, other than those subject to Prop. 218, by:
- a) Prohibiting a fee or charge from being imposed, increased or extended unless approved by two-thirds vote of the legislative body.
- b) Authorizing a referendum on decisions of a legislative body to impose, increase or extend a fee or charge triggered by petitions signed by 5% of affected voters.
- c) Requiring a fee or charge proposed by initiative to be subject to a two-thirds vote of the electorate.
- d) Narrows the legal threshold from “reasonable” to “actual” costs for fees applied to local services, permits, licenses, etc. Further, the measure authorizes new avenues to
challenge “actual” costs by enabling a payor to also second-guess in court whether they are “reasonable.” Opens up further litigation and debate by replacing the existing standard that fees and charges bear a “fair and reasonable relationship to the payors burdens and benefits” with a more rigorous “proportional to the costs created by the payor” standard.

e) Increases the legal burden of proof for local agencies from “preponderance of evidence” (more likely than not) to “clear and convincing evidence” (high probability) to establish that a levy, charge or other exaction is: (1) not a tax, (2) the amount is no more than necessary to cover the actual costs, and (3) the revenue is not being used for other than its stated purpose.

Provisions Applicable to State Actions:

a) Requires a tax contained in a regulation adopted by a state agency must be approved by two-third vote of the Legislature (unless the Legislature adopted a state tax that authorized the action of the state agency). This change is responsive to the recent Chamber of Commerce decision on cap and trade revenues.

b) Unlike the retroactive provisions that apply to local government, the application of this Act to the state is only prospective.

c) Requires a fee contained in a regulation adopted by a state agency to be approved by majority vote of the Legislature.

d) Imposes the same burden of proof changes applied to local governments.

Background:
This initiative is sponsored by the California Business Roundtable, an organization that claims membership from some of the state’s largest companies including, Wells Fargo, Albertsons, KB Home, Blackstone Group, Chevron, Farmers Insurance, Granite Construction and others. http://www.cbrt.org/members/.

The initiative contains over three pages of findings and statements maintaining that the state’s tax burden is high compared to other states, including state revenue growth of 68 percent since 2009. Concerns are also raised over employee pensions increasing costs and other issues affecting the economy and business climate.

One paragraph among the three pages declares one of the purposes of the measure is to overturn “loopholes” created by Cannabis Coalition v. City of Upland (concern that voters could enact special taxes via initiative by majority vote); Chamber of Commerce v. Air Resources Board (a recent case lost by the Chamber which alleged that the state Cap and Trade Program was an illegal tax) and Schmeer v. Los Angeles (which held that a locally imposed-grocer retained bag fee was not a tax). This measure, however, has much broader impacts than such fixes.
Protect Existing Transportation Funding for Local Priorities

League’ 2018 Strategic Goal: "Protect existing transportation funding for local priorities and oppose efforts that would reduce or eliminate funding for cities."

Transportation: Defending SB 1’s $26 Billion for Local Transportation Funding
From now through November, the League of California Cities (League) is encouraging all its member cities to promote all of their local transportation projects through social media, op-eds, press releases, signage, resolutions, press conferences, and more. The League has prepared a toolkit that has samples for each of these items for cities to use, as well as talking points, FAQ’s, the do’s and don’ts of ballot measure activity, and more.

With over $70 billion in funding needs over the next 10 years, the League is aggressively defending the more than 100% increase in transportation funding every city is set to receive for road repair, maintenance, and rehabilitation over the next 10 years ($7.5 billion statewide for cities alone). In addition, it is important to remember that $11 billion in grant funding is available to cities and counties over the next 10 years for local planning, active transportation, transit & intercity rail, self-help jurisdictions, and commuter rail in the following amounts (10-year totals):

Here’s the local money worth defending:
- $15 billion for local streets and roads, including:
  - $7.5 billion for cities
  - $7.5 billion for counties
- $3.3 billion for the Transit and Intercity Rail Capital Program (TIRCP)
- $3.55 billion for State Transit Assistance (STA)
- $2 billion for the State-Local Partnership Program (SLPP)
- $1 billion for the Active Transportation Program (ATP)
- $360 million for Commuter Rail and Intercity Rail
- $250 million for Local Planning Grants

Note: These local funds are in addition to the $26 billion worth of infrastructure investments to the State’s transportation network, including the state highway system, bridges & culverts, congested commuter corridors, trade corridors, freeway service patrol, transportation research at the UC & CSU, and workforce development.

Transportation Funding Repeal:
A repeal effort backed primarily by California State and Congressional Republicans in an attempt to increase voter turnout among their base is still in the process of gathering signatures to qualify for the November 2018 ballot. If qualified and passed by the voters in November, the measure would repeal the funding for every city and county and require statewide voter approval for any increase to the gas tax or any fee for the privilege of using the road, making it highly unlikely any future funding comes to fruition.
Ongoing developments suggest the repeal proponents are on pace to qualify. To date, over $1.3 million have been raised to fund the repeal, most of which has been funded by the California Republican Party. Over 500,000 of the 580,000 signatures have already been collected. If qualified, it will require tens of millions of dollars to defeat. The League has joined its founding members from the Fix Our Roads Coalition, including the California State Association of Counties and the California Alliance for Jobs to build a broader coalition for the newly formed campaign committee, the Coalition to Protect Local Transportation Improvements.

The coalition is growing every day and represents a broad range of organizations that represent business, labor, environmental groups, local governments, regional transportation planning agencies, public safety groups, and elected officials. Given the benefits guaranteed to every community, the League is encouraging all cities to formally join the coalition.

**Proposition 69:**
The League is actively supporting Proposition 69 on the June ballot, which prevents the legislature from diverting or borrowing the new transportation revenue sources not already protected by the California Constitution, including the Transportation Improvement Fee and the increases to the diesel sales and excise taxes. Early polling results suggest this measure is very popular with voters across all demographics (i.e. race, gender, age, political affiliation, etc). The passage of Proposition 69 is key to providing additional assurances to voters that SB 1 funding will be dedicated to transportation. For this reason, the League encourages cities to both support Proposition 69 and to oppose the SB 1 repeal.

For cities looking to join in the League’s advocacy efforts, both to oppose the repeal effort should it qualify for November 2018 and to support the constitutional protections on the June 2018 ballot, please visit [https://fixcaroads.com/](https://fixcaroads.com/) to learn more.
**OFFICE OF ASSEMBLYMEMBER**  
Eloise Gómez Reyes  
FORTY-SEVENTH ASSEMBLY DISTRICT

**AB- 2268**

<table>
<thead>
<tr>
<th><strong>SUMMARY</strong></th>
<th><strong>THIS BILL</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>AB 2268 restores revenues previously allocated to cities that annexed inhabited territory prior to the passage of SB 89 of 2011. The bill would also restore incentives to support future annexations of inhabited areas as encouraged by existing state policies.</td>
<td>AB 2268 proposes to provide the identical financial fix for annexing cities that was approved by the Legislature in SB 130 for four recently incorporated cities.</td>
</tr>
</tbody>
</table>

**EXISTING LAW/BACKGROUND**

In 2011, SB 89, a budget trailer bill passed during state budget difficulties, swept away $200 million annually in vehicle license fee (VLF) revenues from cities. Over 140 annexing cities lost revenue that they relied on to provide essential community services to new residents. The affected cities depended on these revenues when they made the policy decision to annex and serve new residents.

SB 89 has also reduced interest in annexations of inhabited territory because they have become less fiscally viable. Restoring previous annexation incentives will also support several state policy goals including promoting compact growth, reducing vehicle miles travelled and assisting disadvantaged communities.

In 2017, after numerous legislative efforts, SB 130 (Budget) provided a financial fix for four recently incorporated cities that were also severely harmed due to SB 89. AB 2268 proposes an identical fix for cities that suffered losses connected to city annexations.

As with SB 130, this bill restores lost funding to affected cities via an allocation of Property-Tax-In-Lieu of VLF revenues. As with SB 130, the fix proposed by this measure would only be prospective (not retroactive) for the affected cities.

Formulas in both SB 130 and AB 2268 mirror the way Property-Tax-In-Lieu-of-VLF functions for all other city growth, by increasing the city’s Property-Tax-In-Lieu-of-VLF amount by the growth in assessed valuation (AV) from the annexation.

The cost of an annexation fix would be approximately $5 million (about one-fourth of the cost attributed SB 130, $19 million).

Attached is a list of cities that lost revenue because of SB 89.

<table>
<thead>
<tr>
<th><strong>SUPPORT</strong></th>
<th><strong>CONTACT</strong></th>
</tr>
</thead>
</table>
| League of California Cities (Sponsor) | Matthew Hamlett  
Legislative Director  
(916) 319-2047  
Matthew.Hamlett@asm.ca.gov |
<table>
<thead>
<tr>
<th>City Name</th>
<th>FY 2011-12 Loss SB 89 New Annex</th>
<th>City Name</th>
<th>FY 2011-12 Loss SB 89 New Annex</th>
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<td>American Canyon</td>
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<tr>
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<td>Hemet</td>
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The League’s Fiscal Policy Advisor, Michael Coleman, developed these estimates in 2012. The numbers reflect the data we had at the time and may need an update using information from the affected cities. The League does not expect the total updated cost to exceed five million dollars even with the current financial data.

<table>
<thead>
<tr>
<th>City Name</th>
<th>FY 2011-12 Loss SB 89 New Annex</th>
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<td>Oakley</td>
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<tr>
<td>Yuba City</td>
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</table>

**Total: $4,316,109**

1 The League’s Fiscal Policy Advisor, Michael Coleman, developed these estimates in 2012. The numbers reflect the data we had at the time and may need an update using information from the affected cities. The League does not expect the total updated cost to exceed five million dollars even with the current financial data.
AB 2491 provides the same financing mechanism for future city incorporations that was approved by the Legislature in SB 130 (2017) for previously incorporated cities.

For the past seven years, despite the state's population increasing by 2 million residents, no new cities have formed in California. A primary factor for this is the passage of SB 89 in 2011, which removed a financing mechanism communities previously relied on to assist incorporation.

Residents who wish to incorporate are motivated by a desire to improve their quality of life and services in their community. A city government can oftentimes be more responsive to local issues. Currently, local community members throughout California are exploring the opportunity to incorporate their community into a new city, but the funding eliminated by SB 89 makes it fiscally unrealistic.

To restore options for future city incorporation and the enhanced civic engagement and benefits to local services and quality of life that it can offer to residents, AB 2491 applies the same financial fix for future incorporations that was provided last year to four recently incorporated cities harmed by SB 89.

To help close an enormous state budget gap in 2011, the Legislature passed SB 89 (Chapter 35, Statutes of 2011). The measure removed allocations of the Vehicle License Fee (VLF) from cities. These local VLF revenues included special funding allocations dedicated to assist newly incorporated cities.

With SB 89’s passage, four recently incorporated cities experienced severe financial hardship and lost up to 40 percent of their General Funds. All other incorporation efforts in the state were no longer fiscally viable and stalled.

Last year, a fix for the four recent-incorporated cities harmed by SB 89 was agreed to in SB 130, which allocated shares of property tax to offset the amount of VLF revenue the cities would otherwise have received.

The solution crafted for the four cities is based upon an agreement between local governments and the state in 2004 known as the VLF-Property Tax Swap. The swap allowed all cities and counties in existence on that date to permanently exchange, dollar-for-dollar, the amounts the state owed them after the Legislature decided to reduce the VLF and then promised to offset local losses.

AB 2491 proposes that the Legislature provide the same financing solution that was provided in SB 130 for future city incorporations.

- The League of California Cities

For More Information
Brendan Repicky; Legislative Assistant
Brendan.Repicky@asm.ca.gov; 916-319-2008
League Efforts to Develop New Tax-Increment Financing Tools: A Brief Overview

When redevelopment was eliminated, developing new tools that cities could use for infrastructure and economic development became a top League priority. The League formed a Task Force on the Next Generation of Economic Development Tools in spring 2012, chaired by then-League President Bill Bogaard. The city officials serving on the task force provided key direction for the League to work on giving cities more options going forward. For the past six years, the League has focused on creating these options.

The League’s initial effort concentrated on making Infrastructure Financing District (IFD) law a useful tool. IFD law had many problems. It had been in place for 22 years and was rarely used. A major impediment was the requirement for two separate two-thirds public votes: one to establish a district, the other to issue debt. These vote requirements were sufficient to deter most agencies from considering further action. The League’s attorneys determined that these statutory vote requirements were not constitutionally required and identified other proposed changes to the law. Working in partnership with the California Building Industry Association, the League supported a series of amendments to SB 214 (Wolk), which passed in the Legislature. Regrettably, Gov. Jerry Brown vetoed this measure along with several others, including SB 1156 (Steinberg), which would have reauthorized redevelopment in a more limited form. The governor’s veto messages stressed his desire to keep cities focused on dissolving redevelopment.

In 2014, the League’s work on SB 214 resurfaced as part of a tool called the Enhanced Infrastructure Finance District (EIFD) proposed by the Brown administration. Rather than amending IFD law, as SB 214 had proposed, the administration opted to craft an entirely new statute that mirrored many of IFD’s elements. In the ensuing negotiations, the League succeeded in eliminating a requirement to have a public vote prior to establishing a district. Though a 55 percent voter approval requirement to issue bonds remains in the law, other ways to secure financing have been identified. EIFD law was enacted by SB 628 (Beall, Chapter 785, Statutes of 2014). The League sponsored a cleanup bill to EIFD law in 2015 — AB 313 (Atkins, Chapter 320, Statutes of 2015).

In addition, the League sponsored legislation to bring back the tools and powers of redevelopment through a three-year partnership with Assembly Member Luis Alejo (D-Watsonville) to craft the Community Revitalization Investment Authority (CRIA) law. The first effort, AB 1080 (Alejo) in 2013, stalled in the Appropriations Committee after the administration made it clear that no new economic development legislation would be signed that year. The following year, Gov. Brown vetoed AB 2280 (Alejo), with a veto message that sought drafting changes. In 2015, Gov. Brown signed AB 2 (Alejo and E. Garcia, Chapter 319, Statutes of 2015) into law. And in 2016, the League sponsored a cleanup bill, AB 2492 (Alejo and E. Garcia, Chapter 524, Statutes of 2016).

Keeping in mind the “give us options” direction from its Task Force on the Next Generation of Economic Development Tools, the League also took advantage of growing legislative and administration interest in addressing the challenges faced by disadvantaged unincorporated communities. The League drafted and sponsored amendments to SB 614 (Wolk) to craft a simple tax-increment financing tool that cities and counties could use — as part of a city annexation of a
disadvantaged unincorporated community — to repair and upgrade infrastructure. Gov. Brown signed it into law (Chapter 784, Statutes of 2014).

In 2017, the League drafted and sponsored SB 711 (Hill), which would authorize the use of the school share of property taxes to be invested as part of local tax-increment financing projects using EIFD, CRIA or other tools — if approved through a process using the state’s Strategic Growth Council — for projects that advance important state goals such as reducing greenhouse gas emissions reductions and vehicle miles traveled and supporting affordable housing production and transit-oriented development. The bill included requirements for program oversight, reporting, criteria, and caps for the state’s financial exposure. Although that effort did not gain momentum, it is likely that such a concept will be revisited as discussions evolve over a redevelopment 2.0 mechanism.

The League and its attorneys also provided significant technical assistance in 2017 with drafting AB 1598 (Mullin, Chapter 764, Statutes of 2017), which used existing CRIA law as a model for adopting a new financing tool for affordable housing production.

As these new tools were developed, the League produced various white papers, hosted webinars, participated in workshops and collaborated with the California Association for Local Economic Development in the formation of a Tax-Increment Financing Technical Committee that has issued additional guides to the uses of these new tools (available at [https://caled.org/tif-technical-committee](https://caled.org/tif-technical-committee)).

In recent months, League representatives have also met with gubernatorial candidates, legislators and their staff on how to restore and further enhance local community economic development tools. Several bills have been introduced in 2018, intended to refine discussions in anticipation that the next Governor would be willing to approve a revised tool.

**Summary of New Tax-Increment Tools**

The **Enhanced Infrastructure Financing District (EIFD)** law (beginning with Section 53398.50 of the California Government Code) is the most popular tool so far. It provides broad authority for local agencies to use tax increment to finance a wide variety of public infrastructure. Private projects can also be financed, including affordable housing, mixed-use development and sustainable development, industrial structures, and facilities to house consumer goods and services. No public vote is required to establish an authority, and though a 55 percent vote is required to issue bonds, other financing alternatives exist.

Unlike former redevelopment, the EIFD imposes no geographic limitations on where it can be used and requires no blight findings. An EIFD can be used on a single street, in a neighborhood or throughout an entire city. It can also cross jurisdictional boundaries and involve multiple cities and a county. Though an individual city can form an EIFD without participation from other local governments, the flexibility of this tool and the enhanced financial capacity created by partnerships will likely generate creative discussions among local agencies on how the tool can be used to fund common priorities. Recent legislation, AB 1568 (Bloom, Chapter 562, Statutes of 2017), authorizes EIFDs to access sales tax in instances when the boundaries are
“coterminous” with the boundaries of the underlying city or county and 20 percent of the revenue is spent on affordable housing on infill sites.

**Community Revitalization and Investment Authorities (CRIAs)** law (beginning with Section 62000 of the California Government Code) have all the former powers of redevelopment agencies. A CRIA focuses on assisting with the revitalization of poorer neighborhoods and former military bases. While similar to redevelopment, a CRIA is more streamlined. Accountability measures are included to ensure that the use of the CRIA remains consistent with community priorities, and a 25 percent set-aside is included for affordable housing. Although an initial protest opportunity exists, no public vote is required to establish a CRIA, and bonds and other debt can be issued after a CRIA is established.

**Affordable Housing Authority (AHA)** financing law (beginning with Section 62250 of the California Government Code) is a new statute that authorizes a city or county to create by resolution an affordable housing authority, coterminous with its boundaries, with various powers and dedicate a portion of its property tax increment, sales tax and other revenues to develop affordable (up to 120 percent of area median income) housing.

An AHA may issue bonds, borrow, receive funds from and coordinate with other entities, remove hazardous substances, provide seismic retrofits, loan funds to owners and tenants to repair, improve or rehabilitate buildings in the plan area, and take other actions. The AHA has broad property acquisition and disposal authority. Creating an AHA or bond issuance does not require a public vote.

**Annexation Development Plan (ADP)** law (Section 99.3 of California Revenue and Tax Code) authorizes consenting local agencies (city and/or a county or special district) to adopt tax-increment financing to improve or upgrade structures, roads, sewer or water facilities or other infrastructure as part of annexing a disadvantaged unincorporated community. An ADP can be implemented by a special district either formed for this purpose or incorporated into the duties of an existing special district. After the Local Agency Formation Commission (LAFCO) approves the annexation, the special district can issue debt without an additional vote.

**Seaport Financing Districts (SPDs)** law (Section 1710, Harbors and Navigation Code) establishes a financing tool for seaport infrastructure based on a modified form of the EIFD law.

**Military Base Infrastructure and Revitalization Financing Districts (MIRFDs)** law (beginning with Section 53369 of the California Government Code) creates infrastructure and revitalization financing districts separate and apart from existing law that established infrastructure financing districts (IFDs), authorizes a military base reuse authority to form a district and allows these districts to finance a broader range of projects and facilities.
Strategic Goal #2 – Ensure Sustainability of Public Pension and Retirement Health Benefits.

Consistent with the League’s adopted pension sustainability principles, work with affected stakeholders, employees, CalPERS, legislators and the Governor to achieve meaningful options for cities to address growing unfunded pension liabilities that will ensure cities remain solvent and provide services to residents while continuing to offer employees meaningful and sustainable pension and health benefits.

GTLR Response Team and City Official Tool-Kit

As part of the Governance Transparency and Labor Relations (GTLR) Committee 2018 work plan goals, the committee established the GTLR CalPERS Response Team. This group is made up of city officials, both staff and elected. The response team represents nearly every League Division in the state. A call was held on Monday, March 26 to discuss CalPERS related legislation and strategies aimed at the overarching strategy of driving awareness on the issue.

League staff was instructed to create a city official toolkit to assist members of the response team on general education and outreach. Below is a list of the items in the Toolkit:

- League of California Cities Pension Sustainability Study
- Primary Factors Contributing to CalPERS Funded Status
- LCC Statewide Fact Sheet
- Cal Fire Local 2881v. CalPERS Fact Sheet
- Sample Op-Ed
- Sample Letter to the Editor

As of April 4, 2018 the toolkit has been distributed. Additionally, each response team member has been charged to author an op-ed and to use the toolkit to educate the appropriate audience in their city or town by the GTLR committee chair.

Additionally, meetings are being scheduled with the President of the CalPERS Board of Administration (Priya Mathur) as well as the Local Government Employer representative (Bill Slaton) for select members of the GTLR response team along with League Executive Officers.

League of California Cities Files Amicus Brief in Cal Fire Case

On February 21 the League filed a friend-of-the-court (amicus) brief in the case involving the constitutional challenge to pension reform.

In 2012, the State enacted the Public Employees’ Pension Reform Act (PEPRA), which, among other things, eliminated the option for employees enrolled in PERS to purchase up to 5 years of service credits to add to their pension benefit (commonly referred to as “airtime”).
After the State implemented PEPRA, Cal Fire Local 2881 sued arguing that the airtime benefit was a vested contractual right of those employees who were employed prior to the 2013 implementation date for PEPRA. Therefore, under the so-called “California Rule” of vested pension rights previously articulated by the California Supreme Court, eliminating the airtime benefit was an unconstitutional impairment of contract unless the State offered employees a comparable new pension benefit to replace it, which PEPRA does not do.

The lower courts disagreed and held that no comparable new benefit was required and that the elimination of the airtime benefit did not affect the employees’ right to a substantial and reasonable pension. The California Supreme Court granted review last year.

The League’s brief supports the state’s argument that PEPRA’s elimination of the option to purchase airtime prospectively did not result in an unconstitutional impairment of contract. Consistent with board-approved policy, among the arguments the League’s brief makes are:

- Even contractually-vested pension or other retirement benefits can be modified without providing a comparable new advantage, so long as the modifications are reasonable.
- Modifications that are made to prospective benefits (i.e. to benefits attached to time not yet worked as opposed to time already worked) are reasonable so long as they bear a “material relation to the theory of a pension system and its successful operation” and leave employees with a “substantial and reasonable” pension.
- An economic emergency is not required in order to modify prospective benefits.

The brief also extensively discusses the current fiscal hardships that cities are facing due to the unsustainable rise in pension costs, including citing extensively to the League’s recent Retirement System Sustainability report published in January.

It is our hope that this discussion will help the Court understand the need to move this case forward quickly in order to provide the state and local governments with the flexibility to sustainably manage their pension obligations.

The timeline for when the Supreme Court will issue a decision in this case will depend on when it sets oral argument. The Rules of Court do not impose any timeline under which the Court must set an oral argument, but once oral argument is held and the Court takes the case under submission, it has 90 days within which to issue an opinion.
Stakeholder Outreach and Political Climate

As detailed in the strategic goal and outlined in board adopted polices, League staff has been directed to reach out to all impacted stakeholders in an effort to find collaborative solutions to address rising pension costs. League staff continues to meet with state lawmakers, PERS committee consultants, CalPERS board members, employee organizations as well as high ranking officials within the Governor’s administration. Below is a list of notable meetings (excludes multiple meetings with the Governor’s office and CalPERS):

- **Assembly Members:** Cooley (D), Cooper (D), Dahle (R), Baker (R), Gray (D), Eggman (D), Cervantes (D), Rodriguez (D), Quirk (D), Daly (D), Calderon (D)
- **Senators:** Glazer (D), Moorlach (R), Pan (D), Leyva (D), Newman (D), Bates (R), Allen (D), Stern (D), McGuire (D).
- **Representatives From:** SEIU States Council, AFCME, California Professional Fire Fighters (CPF), Californians for Sustainable Retirement, Police Officers Research Association of California (PORAC), California Police Chiefs Association, California Fire Chiefs (Professional Department).

Overall there is a consensus by all parties that there is a funding problem that needs to be addressed. In retrospect this is a significant turnaround from the lack of awareness on this issue in 2017. The increased level of global stakeholder awareness can be directly attributed to the work of League members, the League’s Retirement System Sustainability Study, the increased advocacy presence at the CalPERS Board and the significant amount of earned media detailing the challenges our cities face.

However despite the awareness and acknowledgment of the challenges, organized labor and by extension the State Legislature demonstrate an unwillingness to address the issues proactively. Rather, they have subscribed to the “wait and see” approach, viewing any proactive legislative solution as concession or claw back of employee vested rights. Moreover, employee groups feel strongly the Court will uphold the “California Rule” currently being deliberated at the California Supreme Court.

While the Governor has still not ruled out the idea of getting a comprehensive package finished in his final year in office, it is unlikely he will spearhead major reforms without organized labor at the table. The League will continue to work with the Governor to explore opportunities for potential legislative reforms as well as seek out opportunities to further align with the Governor this year to try and bring employee groups to the table.

Conversely, the League is actively engaged in several PERS related measures trying ‘hold the line’ on measures that would add additional administrative burdens and/or increased retirement related liabilities to cities. The most notable measure is Assembly Bill (AB) 1912 (Rodriguez). As amended the measure places substantial burdens and new unworkable requirements on local and state agencies. It applies retroactive as well as prospective joint and several liability for all retirement related obligations to any current or former member of a JPA since inception. Such obligations include active employee normal pension costs, retiree unfunded accrued liabilities (UAL), as well as
both active and retiree healthcare and other post-employment retirement benefits (OPEBs). These costs cannot be overstated. According to the State Controller’s Office’s most recently available data, the unfunded liability of California’s 130 state and local government pension plans stand at $241.3 billion and $125 billion for retiree healthcare costs.

AB 1912 is sponsored by SEIU States Council and is being authored by the Chair of the Assembly PERS committee. The measure is set to be heard in the Assembly PERS committee on Wednesday April, 18. League staff is leading the opposition coalition.