REVENUE AND TAXATION POLICY COMMITTEE  
Thursday, June 7, 2018  
10:00 a.m. – 3:00 p.m.  
Sacramento Convention Center, 1400 J Street, Sacramento  

Individuals who wish to review the full text of bills included in this packet are encouraged to do so by visiting the League’s website at www.cacities.org and clicking on “Bill Search” found at the left column. Be sure to review the most recent version of the bill.  

AGENDA  

SPECIAL ORDER: State Budget and Issues Briefing for all policy committee members  
10:00 – 10:45 a.m., Room 204, Sacramento Convention Center  

Upon adjournment, individual policy committee meetings will begin  

I. Welcome and Introductions  

II. Public Comment  

III. Additional Discussion of State Budget  
   Informational  
   • Governor’s May Revise: Click Here  
   • LAO Comments: Click Here  
   • League Analysis of May Revise: Click Here  
   • Disaster and Emergency Response Budget and Legislation Update (Attachment A)  

IV. Legislative Update  
   Informational  
   a. June Primary Election results  
   b. Business Roundtable 2/3rds Vote Measure Update & Other Items on Nov. Ballot  
      b. https://protectourcommunitiesca.com/  
      c. https://citipac.org/prop69/  
   c. Transportation Funding SB 1Expenditure Reports due Oct. 1  
   d. Prop 68 Park/Water bond funds (Presuming Voter Approval, June 7)  
      https://www.cacities.org/Resources-Documents/Policy-Advocacy-Section/SB-5-(de-Leon)/Appendix-SB-5-Park-and-Water-Bond.aspx  
   e. Status of AB 2268 (Reyes) and AB 2491 (Cooley) Annexations and Incorporation  
   f. Western City Magazine articles on Tax Increment  
   g. http://www.westerncity.com/Western-City/May-2018/Reassembling-Redevelopment/  

V. (11:30 a.m.) Invited Guest: Discussion of Tax Policy Issues  
   Informational  
   Assembly Member Autumn Burke (Chair), Assembly Committee on Revenue and Taxation  
   Click here for her bio.  
   Appointment as Chair of Assembly Revenue and Taxation Committee Press Release: Click here  

VI. Discussion on Next Steps on Sales Tax Modernization  
   Informational  
   • City Manager Sales Tax Working Group Update (Attachment B)  
   • Pending Quill decision update  
   • SB 993 (Hertzberg), State Services Tax
Governor’s Budget Press Conference comments indicate post-budget focus on tax reform.

VII. Legislative Action Items Review
SCA 20 (Glazer), Local Sales Tax Allocation (Attachment C)  
Action

VIII. Nov. Ballot Measure: (Attachment D)
Transfer of Property Tax Base to Replacement Property  
Action
Sponsored by California Association of Realtors®  
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Next Meeting (tent.): Annual Conference, Long Beach, September 12
Staff will notify committee members after July 20th if the policy committee will be meeting in September.

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 information 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.
Disaster and Emergency Response Budget and Legislation Update:

The wildfires in Northern and Southern California in October and December were the most costly and destructive in California history. California no longer has a traditional fire season that spikes in the highest heat of the summer and early fall. As last year’s October and December destructive and costly wildfires illustrate, extreme fire conditions has become a year-round concern.

The costs of responding to extreme disasters are staggering. It is estimated that the disaster response costs for the October-December 2017 fires is $1.8 billion. This does not include the nearly $12 billion in losses claimed on insurance policies.

Legislation:
More than 70 bills were introduced in the 2018 legislative session that can be categorized as relating to better emergency preparedness, property insurance, and utilities.

While the League has existing policy that addresses fire services, emergency services and emergency preparedness, the League’s Policy Committees and Board are working to fill in gaps that have been identified in certain areas.

In April, Policy Committees recommended, and the Board approved, policy related to better natural disaster preparation and residential property insurance. The Environmental Quality and Transportation, Communications, and Public Works policy committees discussed liability standards for utilities and directed staff to draft policy for consideration.

Budget
The risk of ongoing fire danger has led the newly-formed Disaster Readiness for Safer Communities (DRiSC), which the League of California Cities is a part of, to mobilize and urge a $100 million appropriation to the Office of Emergency Services (OES) to assist local agencies prepare for and respond to fire emergencies.

With the Legislature aiming to finalize the State Budget by June 15, the League is part of an effort to urge lawmakers to appropriate $100 million for fire prevention and mutual aid support. This budget request is a cost effective investment that can save lives, structures and reduce the cost of disaster response.

Talking Points
Cities are encouraged to call your legislators and legislative leadership, as well as send letters to the Governor and legislative leadership. Below are some sample talking points for discussing this issue:

- I urge Assembly Member/Senator [NAME] to support an additional $100 million to the Office of Emergency Services (OES) for local fire prepositioning and emergency communications upgrades and include it in the State Budget.
$100 million in funding is needed to allow local fire agencies to employ pre-positioning as a disaster readiness strategy and to equip them with the 21st century tools they need to get in front of fast-moving fires and other disasters.

Getting help to a disaster in a few hours is no longer enough to protect communities. We need help in the initial minutes of a disaster. Waiting for a disaster to strike is no longer an acceptable strategy. We can save lives and protect communities by pre-positioning firefighters and equipment in areas where high risks are predicted.

We ask that Assembly Member/Senator [NAME] ask Senator Atkins/Speaker Rendon to include the $100 million in the Budget.
Update on Discussions by League City Manager Sales Tax Working Group

In the fall of 2017, Jim Lewis, President of the League’s City Manager Department, and City Manager of Pismo Beach, began the process of appointing a working group of city managers to work with League staff on issues related to local sales taxes, more specifically on one of the thorniest internal issues for cities: exploring how to accomplish a potential shift to destination allocation of online sales.

The League’s support for the principle of destination allocation of the local Bradley Burns Sales and Use Tax derived from online sales is an extension of the League’s longstanding support for “situs” allocation of local sales taxes (meaning the dollars should be allocated to the jurisdiction where the customer physically purchased and received the product). With “brick and mortar” transactions, the customer purchases and receives the product at a physical location. With “online” purchases the customer receives the product at the time it is delivered. Consistent with the “situs” principle, League policy now supports the policy of allocating the local sales tax derived from an online transaction to the location where the customer receives the product.

The need for this group was supported by several factors:

- In both 2015 and 2016, League leadership had identified the erosion of local revenues from e-commerce and other factors as organizational strategic goals. The establishment of these goals triggered an extensive internal policy discussion within the League’s Revenue and Taxation Committee and led to the development of updated sales tax policies [Existing League Policy Affecting Sales Tax], one of which supported a transition to destination allocation.
- While the League had established support for the policy goal of shifting to destination allocation, the policy lacked the critical details on how such a transition should be accomplished. Engagement by city managers in that discussion was critical.
- In November, 2017, the State Auditor released a report on local Bradley-Burns sales tax allocation which was sent to all legislators, advocating for a shift to destination allocation. While this recommendation mirrored League policy, the League lacked internal consensus on how to effect such a transition.
- The state political environment was also ripening for a larger discussion of tax reform. The state budget is overly dependent on volatile personal income revenue for over 70 percent of its budget. Sales tax was eroding for the state as well. In the fall of 2017, former Assembly Speaker and now Senator Bob Hertzberg, was competing for the Senate’s leadership post. Since his return to the Legislature he has been advocating for a broader discussion of tax reform, including changes affecting sales taxes. While such measures had not yet gained momentum, a consideration was that could change if he secured the leadership position in the Senate. And while Governor Brown had avoided focusing on tax reform, a new Governor would take office in 2019. However, during the press conference for the Governor’s 2018 May Revise, Governor Brown mentioned that he was going to be asking his Director of Finance to prepare a framework for possible discussion after the Budget is adopted.
- The advisability of the city manager’s working group within the League was further confirmed when on March 22, Senator Glazer introduced SCA 20, proposing to shift sales tax allocation—consistent with the Auditor’s report-- to destination.
Summary of Discussions of the Working Group
Following an initial briefing call in early February, the group has met three times and held another conference call. Another meeting via conference call is scheduled for June 11th. The primary focus of the working group is to attempt to work through the sensitive issues associated with a potential shift to destination allocation, and develop options to minimize financial burdens associated with a transition. Briefings of the group have been provided by consultants from Hdl Companies and MuniServices and the League’s Fiscal Advisor Michael Coleman, that have focused on the issues involved with a potential transition to destination allocation, including:

- How to handle existing sales tax agreements between local governments and retailers;
- The growing role of logistics, fulfillment centers and warehouses will play in the economy as more goods are purchased online and shipped to customers;
- The challenges faced by communities dependent upon business-to-business transactions;
- Additional revenue potential from a change to the federal Quill decision; and
- Issues associated with differences between how use tax is allocated directly to point of first use from local voter approved add-ons (transactions and use taxes), while the Bradley Burns revenue from the same transaction is allocated to county pools. Some Bradley Burns use taxes can currently be allocated directly under a direct-pay permit or where value of transaction is above $500,000.

When presenting SCA 20 at legislative committee hearings, Senator Glazer has repeatedly expressed his interest in working with the League on the details associated with a transition to destination allocation and the efforts of the City Manager Working Group. The Senator attended one of the group’s meetings in Sacramento.

City Managers Serving on LCC Sales Tax Working Group:

- Wade McKinney, Indian Wells & CCMF - wmckinney@indianwells.com
- Scott Carney, Asst. Stockton - scott.carney@stocktonca.gov
- Scott Ochoa, Ontario City Manager (former Glendale Manager) sochoa@ontarioca.gov
- Christina Turner, Morgan Hill - Christina.Turner@morganhill.ca.gov
- Troy Brown, Tracy - troy.brown@ci.tracy.ca.us
- Joe Chinn, Ross - jchinn@townofross.org
- Brad Kilger, Martinez - bkilger@cityofmartinez.org
- Phil Wright, West Sacramento - philipw@cityofwestsacramento.org
- Al Boling, Ontario Deputy City Manager - aboling@ontarioca.gov
- Rob Jensen, Roseville - rjensen@roseville.ca.us
- Andrea Miller, San Bernardino - Miller_an@sbcity.org
- Jennifer Vasquez, South El Monte - jvasquez@soelmonte.org
- Linda Andal, Interim, Anaheim - landal@anaheim.net
- Paul Navazio, Woodland - paul.navazio@cityofwoodland.org
- John Gillison, Rancho Cucamonga) - john.gillison@cityofrc.us

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1 This is the original list of appointees. Not all appointed members have had the opportunity to fully participate in the various meetings of the group.
Draft Discussion Proposal for Working Group  
May 17, 2018

After several meetings of the working group where various concepts were explored, League staff prepared a discussion draft for the group that contained several concepts. Note: These concepts do not represent a final consensus of the group, but rather some rough parameters of the conversation to date:

1. **Bradley-Burns Sales Tax** (*sales tax is collected when there is a physical nexus with the online retailer within California*): Phase in to destination allocation over nine years (2021-2029) with allocation of revenue divided between “principal place of business of retailer” and “point of delivery.” Final allocation formula (beginning January 1, 2030): 20% to shipping jurisdiction; 80% to “point of delivery.”

Exemption for existing sales tax agreements until 2030: This revised method of allocating online sales tax es would not apply until January 1, 2030, to jurisdictions that entered into an agreement with a retailer prior to January 1, 2018, unless the agreement terminates at an earlier date according to its own terms.

Comment: This proposal attempts to accomplish three objectives:
   1) Providing a long phase-in period would give cities time to plan and adjust to any change.
   2) Leaving 20 percent of the revenue at full phase-out permanently in “shipping” jurisdictions. This reflects an effort to recognize the infrastructure impacts and important role that cities with logistics centers, warehouses, and fulfillment centers play in supporting the ultimate delivery to customers of products purchased online.
   3) Grandfathering existing agreements with retailers (proposed here until 2030) is an effort to recognize the importance of such agreements to some communities and allowing sufficient time before they are affected by destination allocation.

2. **Bradley-Burns Use Tax** (*Use tax is collected from retailers or their customers on out-of-state purchases of products which lack a physical nexus with California*): Phase in over 11 years (2021 – 2031). Final allocation (beginning January 1, 2032): Following the phase-in, 100% to the local jurisdiction in which “the first functional use of the property is made.” Existing option for retailers to self-report use tax directly to a jurisdiction is preserved throughout phase-in.

Comment: This proposal is in response to the following issues:
   1) “*Use tax*” is supposed to be allocated to where a product is *used*. Antiquated practices by the former Board of Equalization, however, have resulted in distributing local use tax revenues derived from the same sale in two different ways:
      a. If the local government has a local transactions *use tax*, and the location of the purchaser is known, the revenues are sent directly to the jurisdiction where the customer receives and “uses” the product. (These funds are already allocated based upon destination)
b. The 1% Bradley Burns use tax revenues, however, are distributed via county pools based on a jurisdiction’s relative share of sales tax within a county. To achieve a transition to destination allocation, these Bradley Burns funds should be directed to the jurisdiction of first use. An 11-year phase-in approach is proposed here as well to mitigate effects that would otherwise be caused by an abrupt transition.

2) If the US Supreme Court overturns or alters the Quill decision (South Dakota v. Wayfair outcome expected in June 2018) then more use tax revenue could flow to state and local agencies. Directing these new revenues to the communities where the customer receives the product (rather than being dispersed via a countywide pool) is consistent with destination allocation. The timing of this additional revenue would boost revenues to all cities and could help to cushion negative effects of a transition in situs rules.

3. Exemption for certain items: Proposal would not affect allocation of sales tax from sales of:
   - New or used vehicles from licensed dealers (this is a settled policy area for cities, where Bradley Burns goes to jurisdiction of dealership, and any applicable transaction and use tax goes to jurisdiction where the purchaser lives)
   - Jet fuel (This is already allocated by state statute on destination – dollars go to where planes are fueled).
1. **SCA 20 (Glazer) Local sales taxes: online sales**

**Bill Summary:**
SCA 20, a proposed Constitutional Amendment, provides that, effective January 1, 2020, 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, shall be consummated at the point of delivery of that property to the purchaser’s address or any other delivery address designated by the purchaser. The author has proposed amendments to phase-in this transition over nine years.

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

- Provides that, effective January 1, 2020, the method for allocating the local Badley-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, shall be consummated at the point of delivery of that property to the purchaser’s address or any other delivery address designated by the purchaser.
- Defines “transacted online” as transaction where:
  - The purchaser’s order and payment for the sale is transacted and completed on an Internet Web site or web-based application.
  - 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.
  - 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.
- Defines a “qualified retailer” as a retailer whose total cumulative annual gross receipts from all of the retailer’s sales, of tangible personal property to purchasers in this state transacted online for the preceding 12 months exceeds ($100,000) one hundred thousand dollars.
- Clarifies that the measure shall not be interpreted to prevent cities and counties from entering into sales tax sharing agreements to apportion revenues between them approved by two-thirds votes of their governing boards, as authorized by subdivision (b) of Section 29 of Article 13.

**Author’s Proposed Amendments in Senate Appropriations Committee:** On May 22, the author presented proposed amendments to SCA 20 to the Senate Appropriations Committee which would:

- Phase in to full destination over a 9-year transition, between January 1, 2020 and January 1, 2029, increasing each year in 10-percent increments.
- Require qualified retailers to report the following information to the Department of Tax and Fee Administration on a form for online transactions to be provided by the Department which would include:
The jurisdiction where the place of business is located and the jurisdiction where the delivery occurred.

The amount of the tax.

- Make other minor conforming changes.

**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. The author has made an effort to respond to the impacts of a shift to destination allocation by proposing a 9-year phase in in recent amendments.

The current April 23rd version of the bill, reflects revisions proposed by the League to remove an unintended loophole in the original draft that would have undermined the existing protections for local sales taxes from legislative shifts that were established by League-sponsored Proposition 1A of 2004. The existing measure now is focused on a proposed shift to destination allocation, while continuing to protect this local revenue from future Legislative shifts for other purposes.

**Existing League Policy:**
Sales tax is a very important revenue source for cities. Past legislative efforts to shift local sales taxes and other revenue away from cities has always been vigorously opposed by the League, and culminated in the League’s sponsorship of 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.

**Recent League Policy Development Affecting Sales Taxes:**

Each fall, city leaders are convened by the League, and participate in setting several “Strategic Goals” for the organization to focus on in the coming year. For two years in a row, 2015 and 2016, one of the League’s strategic goals was to:

> “*Update the Local Government Tax Structure to Respond to the “New Economy.”* Consistent with the constitutional protections for property, sales and local taxes contained in Propositions 1A and 22, develop policy options, where feasible, for responding to the erosion of the major local government revenue sources resulting from the expansion of e-commerce, increased consumption of retail services rather than goods, changing patterns of commerce, and innovations in technology.”

This strategic goal reflected the fundamental changes in e-commerce and the retail marketplace that are eroding the growth of sales tax as a revenue source and changing its allocation among cities. 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 committee held extensive discussions on potential modernization of tax policy affecting cities, with a special emphasis on 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 committee ultimately adopted a series of policies that were approved by the League board. (Existing League Policy Affecting Sales Tax) Among its changes were a recommended change to existing sales tax sourcing rules (determining where a sale occurs), so that the point of sale (situs) is where the customer receives the product. Below is the applicable League policy affecting allocation of sales taxes:
“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.”

Outreach to City Managers:

The reason for the second sentence above was that it was understood that any change in this area would have to be crafted carefully to avoid major negative impacts on some cities. It was also clear that the only way to attempt to work through the details associated with a transition to destination was to get our city managers involved.

In the fall of 2016, at the League’s Annual Conference, League staff met with the officers of the League’s City Manager’s Department at the League’s Annual Conference to update them on the revised sales tax policies and also express the need to develop internal consensus on how to transition to destination allocation.

A session on this issue was held at the February 2017 City Manager’s Conference. Later in the fall, the president of the League’s City Manager Department began to appoint a working group of city managers drawn from a representative group of cities. The group has met four times and will hold a fifth meeting via conference call on June 11th. The primary focus of the working group is to attempt to balance the sensitive issues associated with a potential shift to destination allocation, including options to minimize financial burdens associated with a transition.

**Draft Discussion Proposal for Working Group**  
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Comment: This proposal is in response to the following issues:

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   b. Jet fuel (This is already allocated by state statute on destination – dollars go to where planes are fueled).
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.

**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;

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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:
- 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 projection decisions based upon existing rules and revenues. His proposed nine-year phase-in is a step in the right direction, but fails to address important internal issues such as grandfathering existing sales tax agreements for some time period and recognizing the important role and impacts of logistics, warehouses and fulfillment centers as backbones of online commerce supporting delivery of products to customers.
At the committee’s last meeting to discuss this measure in April, the decision was made to keep the issue as a “work in progress” and support efforts by the League’s City Manager Working Group to continue to develop the details of a proposed solution and report back at June 7th Committee meeting. The author took an amendment drafted by League attorneys to ensure that the measure did not erode protections from Prop. 1A of 2004.

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 are 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. The formation last fall of the League’s City Manager Sales Tax Working Group was an effort to continue to advance the internal discussion on an issue. Now with a report by the State Auditor advocating a shift to destination allocation and a Senator introducing a proposed Constitutional Amendment on the same topic, justifies the League’s efforts to lead on this issue.

Since April, opposition from cities negatively affected by SCA 20 and retailers has contributed to slowing the progress of the measure in the Legislature. Given the politics of the issue and the dollars involved, this was not unexpected. An abrupt change would create too great a hardship for some communities, and all local agencies need time to digest how such a change would affect them. Senator Glazer's recent proposed phase-in has not removed any known opposition to date. Other concerns with the measure relate to timing and the Senator's efforts to seek passage by both houses of the Legislature by June 28, so that the measure would appear on the November, 2018 ballot—this timeline is too rushed for a proposal of such consequence.

Support-Opposition: (as of 06/04/2018):

Support: City of Buena Park, City of Chino Hills, City of Mission Viejo, City of Placentia, Orange County Transportation Authority


Staff Recommendation:
• Request the author to hold off on attempting to push his proposal for the November 2018 ballot, while the League works to finalize a proposal for the November 2020 ballot, to be introduced in the 2019 Legislative Session.

• Request the City Manager Working Group to continue its efforts to refine a proposed transition to destination allocation that would be presented to the League’s Revenue and Taxation Committee and the City Manager’s Department Meeting at League’s 2018 Annual Conference in Long Beach. An update would also be provided to the League Board. (By July 1, if not earlier, the President of the City Manager’s Department should update the membership of the working group to ensure it remains properly balanced, including ensuring representation from each of the League’s 16 regions with a total membership not to exceed 30 people.)

• The City Manager Working Group will take input received at the League’s Annual Conference and a final proposal will be presented to the League’s Revenue and Taxation Committee at its January 2019 meeting, with a recommendation forwarded to League Board.

**Committee Recommendation:**
People’s Initiative to Protect Proposition 13 Savings, Version 3 (17-0013)

Initiative Summary:
The California Constitution offers a one-time property tax saving opportunity for four categories of homeowners (those over 55 years old, the severely disabled, individuals displaced by a natural disaster, or moving from contaminated housing) who move to another home. All of these individuals have the ability to transfer their Proposition 13 property tax base-year value from their current dwelling to a replacement dwelling of equal or lesser value within the same county. Transfers to other counties are prohibited unless the county agrees to allow such transfers.

This measure (17-0013A1) sponsored by the California Association of Realtors® and eligible for the November ballot would, beginning January 1, 2019, expand this property tax break for these "qualified" individuals in the following ways:

- Reducing the taxes, per a specified formula, below the existing Prop. 13 base-year value for those who move to a dwelling of equal or lesser value.
- Providing a tax break, per specified formula, when the move is to a replacement dwelling of a greater value.
- Allow such transfers to all counties.
- Allow individuals to use such transfers multiple times.

- Formula applicable to moving to a home of equal or lesser value: (Prop 13 base year of original property / full cash value of original property x full cash value of replacement property. For the purposes of this example:
  o Full Cash Value of Replacement Property = $300,000
  o Full Cash Value of Original Property = $600,000
  o Base Year Value of Original Property = $100,000

  $100,000/$600,000 = .167 x $300,000 = $50,000. In this case, a qualified homeowner who transfers their base-year of $100,000 to a replacement property, would reduce their base-year to $50,000.

- Formula applicable to moving to a home of greater value: (full cash value of replacement property – full cash value of original property + Prop. 13 base-year of original property. For the purposes of this example:
  o Full Cash Value of Replacement Property = $1,000,000
  o Full Cash Value of Original Property = $600,000
  o Base Year Value of Original Property = $100,000

  $1,000,000 – $600,000 = $400,000 + $100,000 = $500,000. In this case, a homeowner moving to a more expensive home would pay half of the amount they would otherwise pay in property taxes.
Background
Property taxes are a major revenue source for local governments, raising nearly $60 billion annually. Although the state receives no property tax revenue, property tax collections also affect the state’s budget, because state law guarantees schools and community colleges (schools) a minimum amount of funding each year through a combination of property taxes and state funds. If property taxes received by schools decrease, state funding generally must increase.

Proposition 13 of 1978 capped local property taxes levied by cities, counties, schools, and special districts at 1 percent of full cash value which is based on the full cash value at the time a property is sold. The sale of the property establishes a base-year, and the property tax assessment cannot increase by more than 2 percent annually. Since home values often increase by more than 2 percent annually, homeowners and other property owners receive an additional benefit when they hold their properties for a longer period. Examples of these scenarios can be drastic in regions like the Bay Area where homes purchased years ago for $100,000 are now valued in the millions.

While Prop. 13’s one-percent cap on property taxes is already considered a good deal for homeowners compared to tax levels in other states, the Constitution provides additional benefits to seniors over 55 years old, the severely disabled, individuals displaced by a natural disaster or from contaminated dwellings by allowing them to transfer their Proposition 13 property tax base-year value of their current dwelling to a replacement dwelling of equal or lesser value. Such transfers are limited to the same county. Transfers to other counties are prohibited unless the county agrees to allow such transfers, and such decisions by counties are made in consultation with local government agencies that would be impacted such as cities and school districts.

The policy rationale behind this subsidy is to assist seniors looking to downsize because they are retiring and living on lower incomes, assist the disabled and others who have had homes destroyed by disaster or had to move from a contaminated property. The policy rationale in letting counties decide whether to accept out-of-county transfers is in recognition of the potential financial impacts on “destination” counties where retirees may move to because local services, including medical, library, parks, and other services that support retirees, must be paid for. Currently, 11 counties (Alameda, El Dorado, Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Mateo, Santa Clara, Tuolumne, and Ventura) allow these transfers. Whether within a county or across counties, a homeowner can transfer their assessed value only once in their lifetime.

According to the Legislative Analyst’s Office (LAO) some research suggests that the existing property tax benefit does affect the timing of when seniors may move. For example, California homeowners who were 55 years old were around 20 percent more likely to move in 2014 than 54-year-old homeowners. This suggests that some
homeowners who were interested in moving delayed doing so to avoid paying higher property taxes.

Some cities and counties also impose taxes on the transfer of homes and other real estate. These transfer taxes are based on the value of the property being transferred. Transfer taxes are equal to $1.10 per $1,000 of property value in most locations but exceed $20 per $1,000 of property in some cities. Statewide, transfer taxes raise around $1.1 billion for cities and counties.

Fiscal Impact:
The LAO reports that the initiative would likely change the number of homes bought and sold each year by encouraging more older homeowners to sell their existing homes and buy other homes. In recent years, between 350,000 and 450,000 homes have sold each year in California. Under the measure, home sales could increase by as much as tens of thousands per year.

The LAO projects—that while the reassessments from more homes sold could offset some impacts—overall property taxes would decrease for local governments. In the first few years, property tax losses would be a few hundred million dollars per year, with schools and other local governments (cities, counties, and special districts) each losing around $150 million annually. Over time these losses would grow, likely reaching between $1 billion to a few billion dollars per year (in today’s dollars) in the long term, with schools and other local governments each losing $1 billion or more annually.

This measure will also likely have disparate impacts on cities depending on where seniors move to. For instance, Bay Area local governments would benefit when seniors sell their homes, but cities that are retiree destinations would receive less revenue than otherwise. Since there are no income restrictions on this subsidy and seniors are free to also buy more expensive homes, wealthier enclaves could be affected as well.

https://www.cacities.org/Resources-Documents/Policy-Advocacy-Section/Legislative-Resources/Property-Tax-Assessment-LAO-Analysis.aspx

Existing League Policy:
Over recent years the League has joined with the California State Association of Counties in opposing similar proposals to this one when they have been proposed in the Legislature, primarily out of a concern for the impacts on local revenue.

Related League Revenue and Taxation policies and principles include:
- Additional revenue is required in the state/local revenue structure. There is not enough money generated by the current system or allocated to the local level by the current system to meet the requirements of a growing population and deteriorating services and facilities.
- Meaningful fiscal reform should allow each level of government to adequately finance its service responsibilities, with each being accountable to taxpayers for its own programs.
- Cities require a greater share of the property tax and other reliable, discretionary revenues in order to finance local services to property.
• Counties require additional funding if they are to fulfill their state-mandated and traditional roles.

Related League Housing, Community and Economic Development policy:
• Support the establishment of a secure, balanced, and discretionary local revenue base necessary to provide the full range of needed services and quality land use decisions.

Comments:
• The California Association of Realtors®, the sponsor of this measure, which they describe as the “Property Tax Fairness Initiative,” advocates that existing law results in the following problems:
  o Seniors cannot afford to move, because they would face increases in their property taxes compared to what they currently pay.
  o Many disabled people are trapped in inadequate homes and efforts to move to a more suitable property are often impossible due to the prospect of paying increased property taxes.
  o Disaster victims are penalized when they seek to move out of their disaster-stricken county, because many counties have opted to not accept out-of-county transfers.
  o The existing process results arbitrary and limited property tax protections from a confusing patchwork of county laws (where only 11 out of 58 counties have opted to accept out-of-county transfers).

The Realtors® maintain that is measure will produce the following benefits:
  ✓ Seniors will have the freedom to downsize and move closer to family.
  ✓ The severely disabled can move to more practical homes.
  ✓ Disaster victims will have an opportunity to move anywhere in the state.

Additional policy benefits include:
  ✓ Unlocking the existing housing market by providing more opportunities for home ownership when seniors and others sell their existing properties.
  ✓ Increased property taxes to jurisdictions where the properties are sold.
  ✓ Increased economic activity and additional local revenue triggered by other actions that occur in conjunction with a home sale, including additional household spending like building renovations, new furniture, carpeting and other purchases.

See Full Fact Sheet Attached:  https://www.cacities.org/Resources-Documents/Policy-Advocacy-Section/Legislative-Resources/Fact-Sheet-8_V1-4-(002).aspx

• Opponents to this measure, include the California State Association of Counties (CSAC). CSAC is concerned about the significant revenue losses for local governments and the removal of the existing county choice to accept out-of-county transfers. The fact that only 11 out of 58 counties have opted to allow transfers from other counties reflects existing concerns for protecting local revenue, including city
revenue, within those counties. This measure not only removes the existing county option, it would significantly expand the financial impact resulting in up to $2 billion in annual losses for local agencies.

- The policy argument that likely resonates the most with this proposal is whether it would help free up housing stock by providing additional incentives to seniors to sell and move. This proposal will likely trigger some activity, but how much it tips the balance is debatable. It’s also debatable whether it is worth $2 billion annually in local revenue to find out. In today’s tight housing market, having more homes for sale may moderate price increases in areas where seniors are selling, but perhaps increase prices in areas where seniors are moving to. Since this incentive is not limited to lower income individuals or those seeking to downsize it could create additional challenges for first-time homebuyers who may be competing with seniors able to make cash offers with accumulated equity and have an additional advantage of paying lower property taxes.

- When the League has opposed similar proposals in the Legislature, the following additional policy arguments were made:
  
  o Prop. 13 already gives all Californian’s a significant property tax break by capping property taxes at one percent of assessed value. Thirty-three other states have higher property tax levels. Also, most other states also annually reassess property values, but in California increases cannot exceed two percent.
  
  o Local governments already do not receive enough property tax revenue from housing to offset service costs, this would make it even harder for housing to “pencil out” for cities.
  
  o The existing tax break that is provided to seniors is appropriately targeted to those looking to downsize to a dwelling of equivalent or lesser value. This measure would give tax incentives to wealthier individuals looking to buy more expensive homes; such activity should not be subsidized by other taxpayers. Furthermore, it is unclear why an individual who is already eligible to move their property tax base year to another dwelling of equal or lesser value should be allowed to “double down” and receive an additional discount per the new formula in this measure; such changes expand inequities among taxpayers.
  
  o Property taxes are not the only financial reason affecting a decision to move. Other costs associated with selling and buying property need to be factored in. Property tax is capped at one percent of home value, but Realtor fees associated with the same transaction average six times that (six percent).

- Legislative Discussions: There are currently ongoing discussions in the Legislature over whether an alternative measure can be negotiated. June 28 is the deadline for the Legislature to place measures on the ballot.
Support-Opposition: (as of 06/04/2018):

Support: Major organizations supporting include: California Association of Realtors (Sponsor), The African American Farmers of California, American Legion - Department of California, California Chamber of Commerce, Californians for Disability Rights, Inc. CDR, California Senior Advocates League, Howard Jarvis Taxpayers Association, Latin Business Association, National Guard Association of California, Nisei Farmers League. For a full list of endorsing organizations and individuals see HERE.

Opposition: California State Association of Counties, California Professional Firefighters, California Special Districts Association (League staff was unable to confirm other opponents).

Staff Recommendation: Opposition
League policy is to protect local revenue, and the League has opposed similar proposals when they were introduced in the Legislature. Per the Legislative Analyst’s analysis this measure could result in annual losses for local agencies of up to $2 billion annually. All California homeowners already receive a significant tax break from Prop. 13, and the existing property tax reduction for seniors and other qualified individuals when they move to a dwelling of equal or lesser value is appropriately targeted.

Committee Recommendation:

Board Action: