

REVENUE AND TAXATION POLICY COMMITTEE HIGHLIGHTS

Friday, January 18, 2019

Sacramento Convention Center, 1400 J Street, Rm. 204, Sacramento

ATTENDANCE

Members: Olivia Valentine (V. Chair), Deborah Baird, Robert Biery, Michael Brownrigg, Nancy Carroll, Rolando Charvel, James Davis, Ryan Dunn, Juan Garza, John Gillison, Barbara Halliday, Jenny Haruyama, Loella Haskew, Mike Hennawy, Brian Johnson, Randon Lane, Mina Layba, Sashi McEntee, Russell Melton, Glenn Miller, Joseph Muller, Stephanie Nguyen, Laura Parisi, William Pattison, Michael Perciful, Marcus Pimentel, James Purtee, Amanda Rigby, Doug Robertson, Sylvia Robles, Laura Rocha, Ed Sachs, David Sander, David Sheasby, Greg Sparks, Niroop Srivatsa, Fred Strong, Anthony Suber, Kuldip Thusu, John Trujillo, Luis Uribe, Jim Vanderpool, Joe Vinatieri, Scott Voigts, Bertral Washington, Maya Williams, Jim Zervis

League Partners: Rob Braulik, Tracy Vesely

Staff: Dan Carrigg

I. State Budget and General Briefing

Olivia Valentine, Vice Chair, League Revenue and Taxation Policy Committee, gave a brief introduction to the general session. After her welcome, she introduced League President Jan Arbuckle and League Executive Director Carolyn Coleman who welcomed the Committee members to the general session. League lobbyists, then gave a condensed version of the following presentation, prior to the arrival of two special guest speakers: Governor Newsom's Cabinet Secretary Ana Matosantos and Chief Deputy Cabinet Secretary for Executive Branch Operations Jason Elliott.

Deputy Executive Director/Legislative Director, Dan Carrigg, gave a brief overview that highlighted the importance of the League's 2019 Strategic Goals, and discussed both the state budget and legislative issues. Mr. Carrigg then introduced Michael Coleman, the League's Fiscal Policy Advisor, to discuss the Governor's January budget.

Mr. Coleman gave a short PowerPoint presentation on the 2019-20 January Governor's budget. Governor Newsom's proposed state budget includes \$144 billion in General Fund spending and when combined with proposed special fund and bond proceed allocations, totals \$209 billion. Mr. Carrigg explained that while general fund expending has increased, Governor Newsom was being fiscally prudent. The budget proposal increased the Rainy Day Reserve to \$15.3 billion, paying down a total of \$4.1 billion state pension liabilities, allocating an additional \$700 million to a social safety net reserves and \$2.3 billion in general reserves. Mr. Coleman warned that former Governor Brown warned of a looming recession and that the state needs to be prepared for a downturn. Also discussed the makeup of the current state Legislature, including that the Democrats now have a "super-duper" majority in both legislative houses. For more information about the impacts of the budget on cities, please review the [League's analysis](#), and information on Mr. Coleman's website [here](#). Mr. Coleman then gave Dan Carrigg the floor.

Mr. Carrigg elaborated on some of the line items included in Governor Newsom proposed budget. This included homelessness funding, mental health, and disaster recovery. Mr. Carrigg also explained the new ballot initiative process where ballot measure sponsors can now pull measures from the ballot in exchange for legislative deals. Then Mr. Carrigg introduced the League's lobbyists to discuss their respective issue areas.

Jason Rhine, League Assistant Legislative Director, focused on the housing affordability and availability challenges throughout the state. Mr. Rhine noted that housing legislation is a high priority for the Governor, Legislature, and the League this year. He noted that if achieved, Governor Newsom's goal of producing 3.5 million housing units by 2025 would create an unprecedented level of housing production in the state. Additionally, Mr. Rhine encouraged members to be active in advocating for legislation that will help local governments address their housing challenges while preserving appropriate local control functions.

Dane Hutchings, League Legislative Representative, briefed members on issues related to governance, transparency, and labor relations. He briefly discussed sexual harassment prevention legislation that would provide rebuttable presumptions and joint-several liability with contractors. Mr. Hutchings also mentioned divestment measures, the Governor's plan to extend paid family leave, and the pending outcome of the "Cal-Fire" case. He stressed that cities are struggling with increasing costs and securing additional flexibility for cities is a priority.

Charles Harvey, League Legislative Representative, gave an update on various public safety related issues including cannabis and cannabis deliveries, drones, police use of force, and gun legislation. On the topic of cannabis, Mr. Harvey noted that the recently authorized Bureau of Cannabis Control regulations authorizing cannabis deliveries in any jurisdiction in the state would be harmful to cities and will take effect in the spring. In addition, Mr. Harvey discussed the topic of police use of force and the likely re-introduction of a police use of force bill from last year, which was authored by Assembly Member Weber.

Erin Evans-Fudem, League Legislative Representative, highlighted evolving environmental and community issues that will be big in 2019. Ms. Evans-Fudem discussed the programs and proposed funding allocations in the cap-and-trade program. She explained how those programs would continue to be a priority for cities. In addition, Ms. Evans-Fudem discussed the importance for cities to engage in discussions about organic waste recycling regulations, disaster relief and wildfire response legislation, the ramifications of the PG&E declared forthcoming bankruptcy, and clean drinking water legislation.

Rony Berdugo, League Legislative Representative, discussed transportation, communications, and public works. Chief among them was the concept Governor Newsom proposed to tie transportation dollars from Senate Bill 1 (Beall, 2017) to housing production. Mr. Berdugo also summarized the recent Federal Communication Commission's ruling that preempts cities' ability to site telecommunications infrastructure. This proposal is similar to SB 649 (Hueso, 2017) that was vetoed by Governor Brown in 2017 and garnered over 320 opposition letters from cities.

Lastly, Dan Carrigg briefly talked about issues related to revenue and taxation. Mr. Carrigg informed the general session about the *Wayfair* court case and bills that could affect city sales tax. Mr. Carrigg then welcomed Governor Newsom's Cabinet Secretary Ana Matosantos and Chief Deputy Cabinet Secretary for Executive Branch Operations Jason Elliott to begin their presentation.

Special Presentation and Discussion with Governor's Representatives:

Ms. Matosantos and Mr. Elliott spoke to the general session about Governor Newsom's budgetary and legislative priorities this year. Some of these items included, housing, transportation, and healthcare. Ms. Matosantos stressed that the administration wants to work with the League and local governments on a variety of issues. Mr. Elliott talked about his decade of city service in San Francisco and how he wants to work with local governments to implement Governor Newsom's agenda. Then Ms. Matosantos and Mr. Elliott took questions from the general membership. The questions from the general session ranged, but included disaster and emergency response, implementation of the *Wayfair* decision, addressing homelessness, and tying transportation dollars to

housing production. It was encouraging to hear Ms. Monasatnos say that cities should not be blamed or punished for things they do not control when it comes to the production of housing. After they took numerous questions, the general session was adjourned and policy committees commenced.

II. Welcome and Introductions

Committee Vice Chair Olivia Valentine, Council Member, Hawthorne welcomed the Committee and asked members to introduce themselves.

III. Public Comment

No public comment.

IV. Overview of Parliamentary Procedures and Roberts Rules

Dan Carrigg, Deputy Executive Director/Legislative Director, referred members to a handout on the parliamentary procedures. Members were assured that a representative of the City Attorney's department and committee staff will assist, if needed.

V. Committee Orientation

Dan Carrigg provided a brief explanation of the League's policymaking process, including the role of the Committee in making recommendations to the League Board and the collaborative process between Committee members and staff on preparing meeting agendas.

VI. League Strategic Goals for 2019

Dan Carrigg introduced the 2019 strategic goals and explained the process of establishing the goals. He then stated that the goals also influence scheduling presentations/speakers for the Committee.

VII. Review of Existing Policy & Guiding Principles

Dan Carrigg explained the importance of the guiding principles document as the foundation of League advocacy positions. The League's Existing Policy can be found [here](#).

VIII. Additional Discussion on State Budget Proposal

Mike Coleman, Fiscal Policy Advisor, League of California Cities and Dan Carrigg, went over the [Legislative Analyst's Office Nov. Fiscal Outlook](#), the [Governor's Budget](#), and the [League's Summary of Governor's Budget](#).

IX. Expected Rev. & Tax Issues in 2019 Session (Wayfair, Tax Reform, etc.)

Colin Grinnell, Staff Director, Senate Governance and Finance Committee and Carlos Anguiano, Principal Consultant, Assembly Revenue and Taxation Committee presented to the Committee on issues related to AB 147 (Burke), potential tax reform and the implications of the split roll initiative that has qualified for the 2020 ballot. The Committee asked the two speakers several questions and engaged in thoughtful conversation.

X. State Legislative Update

Dan Carrigg discussed two pieces of legislation that would reinvest in tax increment financing and bring back a form of redevelopment. These measures are [SB 5 \(Beall\)](#) and [AB 11 \(Chiu\)](#). For more background on the need for local tax increment tools see the linked [Western City Article](#).

AB 147 (Burke)

The Committee then discussed AB 147 (Burke), legislation to implement the *Wayfair* decision. Many of the questions the Committee had on this topic were answered in the previous presentation. After discussion, the Committee unanimously voted to recommend a **Support** position on AB 147 (Burke). This measure will improve state and local collection of use tax from out-of-state sales, and is an improvement over CDTFA's proposed implementation of *Wayfair*. Fixing the district tax collection problem is a huge benefit to local governments with district taxes.

AB 213 (Reyes)

Dan Carrigg briefly discussed the introduction of AB 213 (Reyes), a League-sponsored measure. The bill would restore funding to approximately 140 cities that had annexed inhabited territory in reliance on previous financial incentives, then suffered significant fiscal harm when those funds were swept away due to the passage of SB 89 (2011). The bill also offers similar incentives to support future annexations of inhabited territory to improve services to affected residents. More information can be found here: Background on city loss of VLF ([Western City Article](#)). Cities were encouraged to send support letters on this legislation.

City Manager Working Group Legislative Recommendations

After discussing the City Manager Working Group Legislative Recommendations and the extensive work done by the League's Policy Committee and more recently by a working group of 30 city managers, the Committee unanimously voted to **Approve** the positions recommended by the working group.

The recommendations are as follows:

Step One:

- Further Limiting Rebate Agreements: The consensus of the Group was that:
 - Sales tax rebate agreements involving online retailers should be prohibited going forward. They are inappropriate because they have the effect of encouraging revenue to be shifted away from numerous communities and concentrated to the benefit of one.¹
 - Any type of agreement that seeks to lure a retailer from one community to another within a market area should also be prohibited going forward. Existing law already prohibits such agreements for auto dealers and big box stores.²
- Shift Use Tax from Online Sales, including from the *South Dakota v Wayfair* Decision Out of County Pools: The Group's recommendation is based first on the principle of "situs" and that revenue should be allocated to the jurisdiction where the use occurs. Each city and county in California imposed a Bradley Burns sales and use tax rate under state law in the 1950s. The use tax on a transaction is the rate imposed where the purchaser resides (the destination). These use tax dollars, including new revenue from the *South Dakota v Wayfair* decision, should be allocated to the destination jurisdiction whose Bradley Burns tax applies and not throughout the entire county.³
 - Shift of these revenues, from purchases from out of state retailers including transactions captured by the *South Dakota v Wayfair* decision, out of county pools to full destination allocation on and after January 1, 2020.⁴

¹ Amend Section [53084.5](#) of the Government Code (that contains existing prohibitions on rebates of Bradley Burns sales taxes) to specifically prohibit: Future sales tax rebate agreements between local agencies and retailers involving any sales tax revenue from the sale of products that are ordered either online or by another means and delivered to purchasers in the territorial jurisdiction of another city or county.¹

² Amend [53084](#) of the Government Code to prohibit agreements that involve the relocation of any retailer. (Section [53084](#) of the Government Code already prohibits the use of "any form of financial assistance" to a vehicle dealer (within 40 miles) and big box retailer (within 25 miles) which closes one location then open another within one year in a market area.

³ Dated (former BOE) policies have allocated these use tax dollars into county wide pools. Revenues in county pools are distributed in accordance with a jurisdiction's pro-rata share of sales tax within a county.

⁴ Reflects working group agreement to shift these use taxes to destination more immediately, while the CDTFA looks at sales tax allocation issues. The group is also concerned about the future corporate plans of Amazon which accounts for nearly half of all online revenues. The fulfillment centers located in state are not legally owned by Amazon, and thus Amazon continues to collect use and report use taxes under "affiliate nexus" rules. These revenues are distributed via county pools in proportion to other taxable sales among the agencies within each county. Absent a

- Allow more direct reporting of use taxes related to construction projects to jurisdiction where the construction activity is located by reducing existing regulatory threshold from \$5 million to \$100,000.
- Request/Require CDTFA Analysis on Impacts of Sales Tax Destination Shifts: After discussion of numerous phase-in options for destination sourcing and allocation for sales taxes, the group ultimately decided that a more complete analysis was needed to sufficiently determine impacts. Since the two companies most cities rely on for sales tax analysis, HdL and MuniServices, were constrained to modeling with transaction and use tax (district tax) data, concerns centered on the problem of making decisions without adequate information.⁵ Since the California Department of Tax and Fee Administration (CDTFA) administers the allocation of local sales and use taxes, it is in the best position to produce an analysis that examines:
 - The impacts on individual agencies of a change in sourcing rules. This would likely be accomplished by developing a model to examine 100% destination sourcing with a report to the Legislature early in 2020.
 - The model should also attempt to distinguish between business-to-consumer transactions versus business-to-business transactions.
 - The model should analyze the current number and financial effects of city and county sales tax rebate agreements with online retailers and how destination sourcing might affect revenues under these agreements.

Step Two:

Conditions for considering a Constitutional Amendment that moves toward destination allocation:

Absent better data on the impacts on individual agencies associated with a shift to destination allocation of sales taxes from CDTFA, the Group declined to prescribe if/how a transition to destination would be accomplished; the sentiment was that the issue was better revisited once better data was available.⁶ In anticipation that the data would reveal significant negative impacts on some agencies, the group desired that any such shift should be accompanied by legislation broadening of the base of sales taxes, including as supported by existing League policy including:

- Broadening 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.

XI. Adoption of 2019 Work Program

In addition to helping the League achieve its strategic goals, the Committee will also focus on the following:

- Remain informed on developments associated with the upcoming Cal Fire ruling, and engage where necessary on legislation and administrative activity at CalPERS affecting pensions and other post-employment benefits.
- Advocate for appropriate implementation of the Wayfair decision to expand collection of use tax from remote sales.
- Monitor and engage on state budget developments, including proposals that may affect local government or provide funding opportunities.
- Support efforts to restore more robust forms of tax increment financing.

shift to destination allocation, should Amazon take title to these fulfillment centers there would be a significant concentration of local sales tax revenue in those communities.

⁵ While all members of the group want to avoid undue harm to specific agencies, some were also concerned that some prior phase-in proposals were not aggressive enough and the changing economy required faster transition. The group also discussed allowing those under existing rebate agreements to “opt out” and remain on full origin sourcing rules until when they expired or by a fixed date at the end of a phase-in period.

⁶ The group is also aware that legislators could introduce proposals in 2019 affecting tax reform and/or destination allocation, which could influence the policy discussion.

- Engage in tax reform discussions that may develop at the state level, using League policies as guidelines.
- VLF and New Incorporations/Annexations: Sponsor legislation to address the fiscal viability of new incorporations and annexations of inhabited areas.
- Remain on alert for proposals that could undermine local revenue, affect funding for infrastructure, or shift costs and responsibilities.
- Continue to monitor and protect vital local revenues including the transient occupancy tax, and utility user's tax.
- Remain informed and take action, where necessary, to prohibit additional state mandates funded or unfunded.
- Monitor issues associated with the California Department of Tax and Fee Administration.

Next Meeting: March 29, Hilton Orange County/Costa Mesa, 3050 Bristol Street, Costa Mesa