

Agenda Report

APRIL 30, 2001

TO: City Council

FROM: Cynthia J. Kurtz, City Manager

SUBJECT: Opposition to Senate Bills 62x and 69 and Assembly Bills 14 and 120 and Future Legislation that Impact Pasadena's Authority to Levy the Utility User Tax

RECOMMENDATION

It is recommendation that the City Council oppose Senate Bill 62x (SB62x) – Utility user's tax: gas and electricity, by Senator Poochigian; Senate Bill 69 (SB69) – by Senators McClintock and Haynes; Assembly Bill 14 (AB14) by Assembly Members Matthews and Havice and Senator Poochigian; and Senate Bill 120 (SB120) - Assembly Member Matthews

BACKGROUND

Currently 156 cities and six counties levy utility user taxes on the consumption of electricity, gas, water, sewer, telephone, telegraph, and cable television services. Charter cities can levy utility user taxes under their constitutional power over municipal affairs, while general law cities receive their authority from State statute.

Over the last 20 years, utility user tax (UUT) revenues have become more important to cities and counties, ranging from 1% to 32% of a city's general fund revenue. For Pasadena, UUT revenues represent approximately 19% of its external revenues, while the statewide average is approximately 16%.

Cities and counties levy UUT on the dollar amount of a utility bill, not on the number of kilowatts or gas therms consumed. As electricity and natural gas prices climb or fall, so does the utility bill, and thus the utility user tax revenue.

Each of these pieces of legislation would require every local jurisdiction that levies a UUT on gas or electricity to base its tax rate for residential and small commercial customers on a per unit usage basis and not on the price per unit. With the exception of SB69, the usage rate cannot exceed the effective per unit usage rate paid by consumers in January 2000. SB69 sets the usage rate at a level not to exceed the effective per unit usage rate paid by consumers in January 1999.

SB62x includes legislative declarations that basing a utility user's tax on usage will reduce the potential for excessive tax increases and will encourage reduced consumption. Further, SB62x declares that the regulation of the utility user's tax on gas and electricity is a matter of statewide concern because of rising consumer energy costs.

DISCUSSION

While the intent of these pieces of legislation may be noble, the result is another attack on local revenues by the State Legislature. In this case, it appears that the State is attempting to fix mistakes made during deregulation of the electric utility industry on the backs of local government.

Nowhere in the legislation does the State acknowledge that local government utility costs are also rising. In many instances, the increased utility user tax revenues generated by the higher energy and gas rates helps to offset this higher utility costs without jeopardizing other valuable city services. In addition, nowhere in the original deregulation legislation did the legislature raise concerns about the dropping UUT revenues if deregulation had been successful. Finally, nowhere in SB62x does the legislature take into account those cities that maintain their own electric utility and the positive steps taken to minimize the negative affects of past State legislation. These efforts by the Pasadena City Council have resulted in only minimal rate increases, a small fraction of the 46% rate hike recently approved by the California Public Utility Commission.

Just recently, the City received its annual update on the projected energy market by Henwood. While these projections suggest higher utility rates than previously projected, they are still at or below the energy rates in affect prior to deregulation. As such, the Henwood study suggests that the State may be feeling the affects of a short-term problem. If this is the case, the State's suggestion to change how utility user tax rates are applied addresses a short-term problem with a long-term solution, definitely ill-conceived.

In addition, the proposed legislation is another example of how the State continues to jeopardize cities and counties ability to fund local services. Time and time again, cities find ways to improve efficiencies, expand services and meet the needs of residents and time and time again the State finds ways to take control over local revenues to cover its inability to manage its resources and affairs. Just two years ago the State took another local revenue, the Vehicle License Fee (VLF). While the State backfilled this revenue with a portion of its enormous surplus, that surplus should have been used to fulfill the State's commitment to return lost property tax revenues. Now because of the State's energy crisis, the State has depleted its surplus and now the backfill of the VLF is in jeopardy. If the State is unable to backfill lost VLF revenues, the City of Pasadena stands to lose over \$3 million annually. This is on top of the \$3 to \$4 million it lost annually in property taxes.

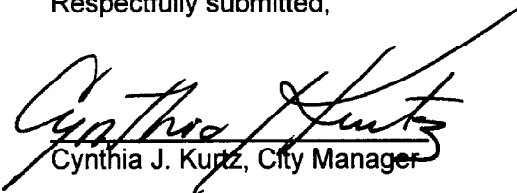
A final issue raised but unanswered is whether or not the State legislature can even impose its will on charter cities in this matter. The California Constitution gives charter cities the power to control their own municipal affairs. The Constitution, however, does not define "municipal affairs," leaving the courts to interpret the phrase. The courts distinguish between municipal affairs and issues of statewide concern. The courts

usually include local taxes with the meaning of municipal affairs, reasoning that local taxes produce local revenues that pay for local services. SB62x asserts that utility user's taxes are an issue of statewide concern and that charter cities must comply with the new legislation. It has been suggested that the real test of whether the Legislature can force charter cities to change their utility user's taxes will come in the courts.

FISCAL IMPACT

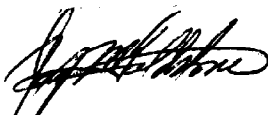
While none of the proposed legislation would prohibit cities and counties from levying a utility user's tax, changing the tax base effectively caps the resulting revenues. Regarding the bills included in this report, supporters' claim that they will not reduce revenues to cities and counties, however, contrary to this claim, it will over time. Historically, Pasadena has relied upon a general growth in the utility user tax revenue to cover the increasing costs of providing services. Under these bills, unless customers use more gas and electricity, taxing on usage leaves little room for revenue growth. At roughly 19% of the City's general fund revenue, the difference between a 3% growth in utility user tax revenue on electric and gas related consumption versus no growth represents a loss of nearly \$275,000 annually. This loss would grow each year.

Respectfully submitted,



Cynthia J. Kurtz, City Manager

Approved by:



Jay M. Goldstone
Director of Finance
