

Agenda Report

April 28, 2003

TO: CITY COUNCIL
FROM: CITY MANAGER
SUBJECT: **OPPOSITION TO AB 1221: TAXATION (STEINBERG AND CAMPBELL)**

RECOMMENDATION:

It is recommended that City Council:

1. Oppose AB 1221 (Steinberg and Campbell) unless the legislation is tied to a constitutional amendment that protects local revenue in the future; and,
2. Authorize the Mayor to send letters to the appropriate authorities conveying Pasadena's position on this matter.

BILL SUMMARY:

AB1221 would substitute local sales tax revenue (.5%) with property tax revenue of an equal amount beginning in fiscal year 2005.

BACKGROUND:

The intent of the bill is to reduce "fiscalization of land use" where cities unilaterally pursue commercial land use at the expense of a more balanced land use policy because commercial property produces local revenue. Commercial development is currently the only land use that generates enough new revenue to cover the cost of providing services for the new use.

As more and more cities are accused of "chasing sales tax," it has also created disincentives for regional cooperation. Large sales tax generators can be the subject of heated competition and often are enticed to move from one city to the next by offers of shared sales tax revenue. In the end, local government revenues are reduced and individual cities may lose a significant economic base as other cities "raid" their retail sector.

The authors of the bill believe that AB1221 will eliminate incentives to focus on retail development, resulting in better local land use policy and, more specifically, an environment more conducive to the development of housing at all levels of affordability.

In addition, the switch could result in increased revenue to cities since AB 1221 allows property tax revenues to local governments to grow with the property tax base in the community. Research shows that property tax has had a much stronger growth trend over the last 20 years and has been less volatile than sales tax.

Despite the potential benefits, opponents of the bill believe it would open cities to another dangerous raid of local government revenue. In 1992 the State shifted a significant amount of property tax revenue from local governments to schools districts. In the current fiscal year, impacts of this shift total \$5.3 billion in lost revenue to cities, counties and special districts, with an impact of \$3 million to Pasadena alone. Since the inception of the shift, local governments have lost more than \$44 billion and Pasadena more than \$30 million. In addition, there are currently several pending proposals to shift redevelopment funds to school districts as a means to balance the State budget.

Without constitutional protection, local governments could face further shifts in property tax revenue but would not be able to make up the difference through an enlarged sales tax base.

Impacts on Pasadena

Pasadena has adhered to its General Plan and Specific Plan principals and has not made decisions based on revenue. A sales tax sharing agreement has not been approved in over five years. However, these decisions are ultimately putting a strain on the city budget as demands for service have increased without associated increases in revenue.

Pasadena's three largest revenue sources are sales tax, property tax and utility users tax. Under current law, the city receives 1% of every retail purchase that takes place within its jurisdiction for a total of \$27 million in revenue and approximately 22% of every property tax dollar resulting in \$18.5 million in revenue.

Over the past four years, property tax has increased at an average rate of 7%, while sales tax revenue has increased an average of 5.6%. While it is not clear how these revenue sources may increase or decline in the future, it serves to provide a basic context for analysis. If these trends were to continue, the city would benefit from the larger growth of the property tax.

In addition, analysts have predicted which cities would fare best under AB1221 and identified a series of criteria. Pasadena generally meets those criteria, including:

- a. Do not have substantial amounts of property in open redevelopment areas;
 - b. Are not on the brink of realizing revenue from new large sales tax generators;
 - c. Anticipate mixed residential and commercial growth in the future; and
 - d. Are predominantly built-out.
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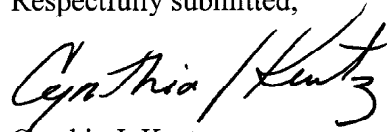
Bill Status

AB 1221 passed out of the Assembly Local Government Committee on April 23 on a vote of 6 to 1. The bill will be heard next by the Assembly Revenue and Taxation Committee. The League of California Cities opposes the bill unless amended to require a constitutional amendment to protect local revenue in the future.

FISCAL IMPACT

AB1221 would reduce sales tax revenue by \$13.5 million and increase property tax million by a like amount in the first year. If constitutionally protected, the revenue swap could result in increased revenues to the city in future years.

Respectfully submitted,



Cynthia J. Kurtz
City Manager

Approved by:



Jay M. Goldstone
Director of Finance

Concurrence:



Richard J. Bruckner
Director of Planning and Development