



MEMORANDUM

TO: MAYOR AND CITY COUNCIL

FROM: JAMES B. HENDRICKSON, CITY MANAGER

SUBJECT: PROPOSITION 218 AND RE-ENACTMENT OF
FIRE SUPPRESSION BENEFIT ASSESSMENT DISTRICT

DATE: DECEMBER 17, 1999

Passage of Proposition 218 (November 1996)

Proposition 218 was passed by the voters of the State of California on November 5, 1996. Dubbed by its proponents as the "Right to Vote on Taxes" measure, this initiative constitutional amendment severely constrains local governments' ability to impose fees, taxes and assessments. It applies to all cities, counties, special districts, redevelopment agencies and school districts in the State of California.

For the City of Palos Verdes Estates, it is probably **the most** consequential measure to pass since Proposition 13 in 1978. Back then, property taxes constituted ~60% of our General Fund revenues. Proposition 13 cut these by two-thirds, in one fell swoop. It led to layoffs at City hall, the loss of the City's Fire/Paramedic unit, the inability to continue maintenance of the median islands, and the severe curtailment of office hours that the staff was available to the public. After a couple of failed attempts, the City voters eventually enacted two parcel taxes (Police/Fire/Paramedic and Streets and Parklands) to make up for some of the lost property tax revenue. Each required a minimum two-thirds vote for enactment. They were first approved in April 1980 and renewed every 4 years thereafter.

Establishment of Fire Suppression Benefit Assessment District

In August 1990, the City Council decided to consider potential substitutes to the parcel taxes to provide for more permanent financing. It appointed a Special Citizens' Advisory Committee to examine the City's finances and look at a broad range of alternatives. The Committee unanimously recommended the establishment of a Fire Suppression Benefit Assessment District to cover 100% of the cost of fire services.

The Los Angeles County Fire Department has provided fire suppression and paramedic services, enforcement of the City Fire Code and support services (such as cliff rescue, borate bombers, etc.) through a single station (located at the City Hall complex) since May 1986. The station consists of one 3-man engine company, and one 2-man paramedic rescue squad. It is staffed on a 24-hour basis seven days a week, with the following personnel.....

3 captains
3 firefighter specialists
9 firefighters

15 total

The City proceeded to notice all property owners of the proposal and the amount of assessment that each would incur. It was proposed that the assessment would be enacted for a 5-year period and serve as a substitute for the parcel taxes. The total assessment amounted to \$1,940,000 in FY 91—92, which was slightly less than the amount being raised by the two parcel taxes. At the Hearing on Protests in May 1991, the Council was presented with written protests amounting to 3.5% of the revenue to be raised. The Council voted unanimously to institute the FSBAD.

With the FSBAD scheduled to expire on June 30, 1996, the City launched a process (in September 1995) to renew the District for an additional 5 years. The Special Citizens' Advisory Committee was reconvened to review the City finances and satisfy itself that this mechanism was, in fact, needed and was still the preferred way to fund fire services. They agreed unanimously that this was the best way to proceed.

Concurrent with this process, the City negotiated a 10-year renewal of its contract with Los Angeles County Fire (covering 7-1-96 through 6-30-06).

This included some very important and significant cost containment measures and other safeguards for the City that helped stabilize costs. It incorporates an annual fee limitation based on one of two options; but in no case can the annual increase exceed 6.5% per year. It also eliminated the separate charges for fire prevention personnel. With these measures in place, the projected cost of fire service actually decreased in 96-97, and the five year rolling average annual increase has steadily decreased from 8.5% in 91-92 to 2.3% in 98-99 (see Attachment 1). The City managed to hold the assessment rate constant for 3 years in a row, and actually decreased the rate 6% in 97-98 (Attachment 2). In FY 99-00, a median sized home in the City (2,450 sq. ft.) pays \$417.53 for fire protection – which is only 3.7% higher than it paid 5 years earlier. The assessment is based on a flat-rate stand-by availability charge, plus an additional amount for each square foot of improvement on the property.

Each property owner received formal written notice of the proposed assessment for 1996-97 and the maximum allowable assessment for 2000-01. They were also advised of their right to make written protest at the formal Hearing on Protests on April 23, 1996. If the City received written protests from property owners representing more than 10% of the expected revenue, the FSBAD would have to be submitted to the voters for approval. If protests exceeded 50%, the City would be required to abandon the proposal.

In fact, the City received less than ½ of 1% formal protest. We were advised by our assessment engineers that this was the lowest level of protest they had ever experienced in the formation of any assessment district. The Council voted unanimously to re-enact the FSBAD. The levy was established for the next five years and does not become subject to the new rules for special assessments under Proposition 218 until it expires June 30, 2001.

Today, the FSBAD is an essential and integral part of the financing structure of City services. It pays 100% of the cost of the contract with Los Angeles County Fire Department for fire suppression and paramedic services. It will raise approximately **\$2.3 million** in FY 99-00. This represents **25%** of the City's Operating Budget.

Option 1: Re-enact the Fire Suppression Benefit Assessment District

Discussion. The Fire Suppression Benefit Assessment District has stood the City in good stead for the past 8-1/2 years. When first proposed as a substitute for the two parcel taxes, it was endorsed by the property owners for a 5-year period with minimal protests. When proposed for re-enactment for the ensuing 5 years (7-1-96 through 6-30-01), the level of protest diminished even further. This indicates a level of acceptance and satisfaction with the assessment. However, the process to levy a special assessment under Proposition 218, and the costs that can be recovered, is much more complicated, demanding and uncertain than the process under prior law.

Issues.

- **Eligible Costs.** The Proposition makes a clear distinction between “special benefits” and “general benefits”. Special benefits, which are recoverable through the assessment, are those that are conferred on real property (land and buildings). General benefits may not be recovered through the assessment, and must be paid from other resources of the agency.

This delineation between special benefits and general benefits has tremendous consequence to the continued viability of the FSBAD as a mechanism to pay for the L.A. County Fire contract. Expert legal opinion, and the conclusion of the assessment engineers, is that paramedic services qualify as general benefits and may not be recouped by the assessment (See Attachment No. 3) They are deemed to be services provided to people and **not** conferred on property. Paramedics comprise **39% of the cost** of the L.A. County Fire Contract (\$967,377 of \$2,472,959) in FY 99-00.

In addition, the preliminary indication is that the flat rate “standby availability” charge currently assessed on each parcel (\$173.74) qualifies as a general benefit and would be ineligible, as well. This is the only levy on a vacant parcel. In the future, all assessments on a piece of property would be based on the amount of square footage of building improvements.

- **Public Agencies (schools, state, federal government), including the City itself, are no longer exempt from the assessment.** This is a major shift from prior law and could have an added impact on the amount of money raised by the District, and the likelihood that it would secure approval. One positive side effect is that it would reduce the assessments on all other (private) properties in the City because the fire costs will be spread over a broader base. But this provision re: the assessment of public agencies could possibly motivate the School District (a major public property owner) to oppose the measure.

The City is permitted to pay the assessment on behalf of public agencies. However, this has the potential to considerably reduce the amount of revenue that would be raised. The question then arises as to where the supplemental revenue would be derived. The Assessment Engineer would have to determine what proportion (and cost) public property represents of the total assessment.

- **Notice Requirements and Voter Protests.** The City must conduct a mail ballot vote on the assessment. Each property owner is provided official notice at least 45 days prior to the Public Hearing on Protests. They are also transmitted a ballot to be mailed back, signifying their support or opposition to the proposal. The ballots cast at the election are weighed according to the amount of the assessment the property owner would pay. For example, a property owner assessed \$750 has three times the vote of a property owner \$250. The City must receive a “majority vote” from those property owners returning ballots in order to re-enact the assessment. No assessment may be imposed if a majority of those returning ballots protest, regardless of how small a number of property owners return ballots.

This reverses the process under which the assessment district is established. Previously, an election was only required if formal protest exceeded 10% of the total assessment (and a 50% or more protest forced discontinuation of the proceedings). A non-response was equivalent to support of the proposal. However, under the new rules, it is necessary to garner a majority of affirmative votes – which is an entirely different psychology.

- **Engineer's Report.** All assessments must be spread in accordance with an Engineer's Report prepared by a registered professional engineer. While not required under previous law, the City has always hired a professional engineer to do this work.

Summary. The new rules imposed by Proposition 218 not only make the process for re-enactment of the FSBAD more difficult, but make it highly questionable whether it is even worth pursuing as a financing mechanism. We now recover 100% of the costs of the annual L.A. County Fire contract, and have done so since the inception of the District in FY 91-92. But with the inability to recover paramedic costs, the loss of the standby availability charge, and the erosion of the assessment base due to the need to assess public agencies, the City would be fortunate to recoup 50% of the contract costs – about \$1.2 million a year. The remaining \$1.2 million would have to be derived from some other unknown, and unidentified, source.

Option 2. Enact a Special Tax.

Discussion. Proposition 218 defines a “special tax” as any tax imposed for specific purposes, including taxes imposed for specific purposes and placed in the General Fund. These require two-thirds voter approval to be enacted. Thus, the act of specifying the use of monies to make the measure more saleable to the electorate makes it far more difficult to pass due to the “super-majority” requirement.

A parcel tax is considered a special tax under Prop 218. A parcel tax could be presented as a flat-rate tax (applicable equally to all parcels), as a graduated tax (different rates charged to properties in different broad categories of building square footage), or as an individualized rate (a charge for each square foot of building improvements on the property).

Issues.

- **Requires two-thirds voter approval.** “General taxes” require simple majority for approval; and assessment districts require majority approval (based on the “weighted vote”). However, special taxes require 2/3 affirmative vote for approval.

- **Election Date.** An election may be set at **any** time to consider the enactment of a special tax. This provides more flexibility in the timing of an election; and ensures that it would be a “stand-alone” issue.
- **Deductibility.** We have been advised on an informal basis that a special tax may be structured more easily to qualify as a deduction for income tax purposes. If the City were to pursue this mechanism in lieu of the Fire Suppression Benefit Assessment District, we should seek a formal opinion from a tax attorney verifying that this is so. The deductibility feature is a tremendous asset in selling it to the electorate.

Option 3: Enact a General Tax.

Discussion. Proposition 218 defines a “general tax” as any tax imposed for general governmental purposes. It requires a majority vote for enactment. However, the likelihood of its success is seriously diminished if the monies are not earmarked for some specific purpose. Voters will be much more reluctant to authorize a tax for general purposes for fear that the monies will be used for services and programs they do not approve of.

One of the main reasons the City’s FSBAD has been so favorably received is because the monies are used solely and exclusively for fire services. They are placed in a separate fund and reserved for this explicit purpose. Fire service is recognized as a critical and essential local government service that must be funded in some fashion.

The principal general taxes levied by California cities are: (1) utility users tax, (2) business license tax, (3) transient occupancy tax. Unfortunately, it would be difficult to use any one of these as a substitute for the FSBAD. The City already levies a 10% utility users tax (with an amount equivalent to 100% of the proceeds transferred to the Capital Improvement Fund to address the City’s infrastructure needs). To recoup an additional \$2.4 million to pay for the fire contract costs would require that we more than double the tax – to 20%+. The City business license tax only generates \$195,000 a year. Raising that to \$2.4 million a year would place an unfair and harsh burden on a single class of taxpayers. Finally, the City has no hotels or motels upon which to levy a transient occupancy tax. No monies would be derived from this source.

An additional option we have researched carefully is the documentary transfer tax (real property transfer tax). Cities and counties are permitted to impose a tax on the transfer (ownership) of real estate with a value exceeding \$100. The established rate is \$1.10 per \$1,000, which is shared 50/50 between the City and the County. Over the past 3 fiscal years, the City has derived between \$115,000 and \$147,000 a year from this source. Several cities in the State charge in excess of the \$1.10 per \$1,000 rate.....

- Redondo Beach = \$3.10
- Santa Monica = \$4.10
- Los Angeles, Culver City, Hayward = \$5.60
- Alameda = \$6.50
- San Leandro = \$7.10
- Palm Springs = \$11.10
- Berkeley, Oakland = \$16.10

The tax receipts are volatile, depending on the state of the economy and the housing resale market. However, our analysis indicated that if the City were to levy a rate equivalent to 1% of the value of the sale (the same as Palm Springs), we could recoup a substantial portion of the revenue we now derive from the FSBAD.

Unfortunately, all the cities that levy a rate in excess of the standard are charter cities. The City Attorney carefully researched whether Palos Verdes Estates, as a General Law City, was empowered to exceed the \$1.10 rate. She concluded that we are prohibited by Government Code Section } 53725 from doing so. There appears to be no mechanism to avoid the effect of this law (See attachment No. 4).

Issues.

- **Requires majority vote for enactment.** A new, favorable wrinkle to the voter approval requirement was created by a 1998 Appellate Court decision in Coleman v. Santa Clara County. In that case, the County of Santa Clara placed a sales tax measure on the ballot as a general tax to be deposited in the General Fund. On the same ballot, the County submitted an advisory measure which sought the electorate's advisory approval on a spending strategy

for the revenues that would be raised. Both ballot measures passed by a simple majority. The Jarvis/Gann Taxpayers Association challenged the tax increase as a special tax necessitating two-thirds voter approval. The court disagreed by ruling that the tax increase on the ballot was clearly intended as a general tax increase, and the advisory ballot measure was just that, advisory, and not binding. The California Supreme Court has declined to review the decision, so it is final. (The only caveat is that this election took place the same day Proposition 218 was on the ballot, and technically, was not yet in effect).

This approach could be of considerable significance if the City were to place a general tax increase measure on the ballot accompanied by an advisory measure indicating that the monies would be utilized to pay the costs of fire service. This lowers the threshold requirement for passage of the measure. The difficulty will be in devising a general tax measure that can be utilized for this purpose. ✓

- **Election Constraints.** An election must be consolidated with a regularly scheduled municipal election for members of the City Council. The next such election is scheduled for March 2001. If the measure failed, another general tax election could not be scheduled until March 2003. One exception in law – a measure can be placed on a special election ballot if the Council unanimously determines that an emergency exists.

JBH:s
Attachments