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Staff Report for Overview of Various Revenue Measures Currently Being Explored for the November 2016 Ballot

**SUMMARY AND RECOMMENDATIONS**

The City Manager recommends that the City Council review, discuss, and provide direction to staff regarding up to three potential local revenue measures currently planned for the November 2016 ballot.

**BACKGROUND**

In November 2010, San Leandro voters authorized Measure Z, a local ¼-cent sales tax revenue measure that was designed to temporarily stabilize the City budget in the midst of the Great Recession. Measure Z provided a reliable, voter-approved funding source for public safety and other essential City services for seven years. As Measure Z was approaching expiration, San Leandro voters authorized its extension at a half-cent rate for 30 years through passage of Measure HH in November 2014. The primary purpose of Measure HH was to preserve *current* City service levels for a range of public services, including public safety and anti-gang programs, library, and programs serving children and youth, as well as various other City programs and services. In conjunction with Alameda County Measure BB, Measure HH also assists with the City’s significant street and road repair needs.

While Measure HH allows the City to maintain existing service levels, the City continues to face a growing backlog of new and emerging needs that cannot be sufficiently addressed through existing revenue sources. Such needs include major renovations to aging public safety infrastructure (e.g. police and fire protection facilities), deteriorating playground and park equipment in need of replacement, human services challenges related to the homeless and other at-risk and low income

community members, and community interest in enhanced artistic and cultural amenities.

Although local sales tax receipts this past year were robust, they are inherently volatile in that they generally rise and fall in direct correlation with broader regional economic cycles. There is inherent risk that if the economy slows down or contracts in future years, the City's revenue base could similarly face steep declines, thereby causing the need for future budget cuts and associated disruptions in service levels. In order to maintain sustainability in the City's budget, there can be significant public benefits from a diversified revenue base.

To address these factors, at the direction of the City Council Finance Committee, City staff are exploring various potential new local sources of revenue, which per State law require voter authorization. Those measures include:

- 1) a medical cannabis business tax of up to 10% of gross receipts;
- 2) an increased transient occupancy tax of up to 14%; and
- 3) A modified business license tax that would reduce fees for small businesses, while charging up to 10% of gross receipts for parking lots, and also charging \$100 per 1,000 square feet of real property that is used for warehouse businesses.

These potential revenue sources align with previously adopted City Council goals and policy priorities, as outlined below. Furthermore, these new revenue sources would not directly impact the vast majority of San Leandro residents.

#### Overview of Potential Cannabis Business Tax

Now that the City has issued its first cannabis dispensary permit, and a second permit is expected to be issued soon, the City has an opportunity to derive an important new source of revenue from these businesses. Similar to many other communities that have permitted such businesses, staff recommends that the Council consider asking voters to authorize a new tax based on the cannabis dispensaries' annual gross receipts. Given that the specific rates of such taxes vary by jurisdiction, coupled with the rapidly evolving legal and regulatory landscape surrounding cannabis businesses, staff recommends that the Council explore structuring the ballot question such that the tax amount would be "up to" 10% of gross receipts, which would allow the City flexibility to modify the rate over time up to that maximum 10% threshold. Staff also recommends that the tax be structured such that it would apply to any business involving the use of any component of the cannabis sativa plant. To the extent that the adult use of cannabis becomes legal following this November's election and/or if the Council were to decide in the future to allow other ancillary cannabis-related businesses to operate in the community (such as laboratory testing, bakeries, or THC/CBD extraction), this tax could provide an important new revenue stream to the City.

Given that no permitted cannabis dispensaries are currently open in San Leandro, there is inherent uncertainty in how much revenue could be derived from such a tax. However, based upon revenue estimates provided by Harborside San Leandro as part of its application materials for the first dispensary permit, staff estimates that this revenue measure could potentially generate approximately \$500,000 per year if the tax were initially set at a rate of between 5% and 7% of gross receipts. For comparison purposes, the City of Oakland currently charges a tax of 5% of gross receipts on cannabis businesses and San Jose voters authorized a tax of up to 10% of gross receipts, but the City currently charges just 7%.

#### Overview of Potential Increase in Transient Occupancy Tax

The City's current transient occupancy tax (TOT) is set at 10%, which is charged to travelers when renting overnight accommodations of a limited duration in a hotel, inn, tourist home or house, motel or other lodging. Other communities in the region have established even higher rates, including the cities of Oakland and San Francisco, each of which presently have TOT rates of 14%. In addition, the redevelopment of the San Leandro shoreline area is expected to result in the creation of at least one new hotel in San Leandro, which could provide an important source of additional TOT revenue in the future. The City of San Leandro currently receives approximately \$500,000 in total annual tax receipts from its three hotels, which could increase to \$700,000 if the rate were expanded to 14%.

### Overview of Potential Modifications to Business License Tax

The proposed modifications to the business license tax have been designed to better align the City's business license tax rates with Council priorities to support local small businesses, while also incentivizing the productive use of the City's industrial areas. More specifically under this scenario, the per-employee component of the current business license tax for small businesses with three or fewer employees would be eliminated. This change would reduce the total fee for small business by approximately \$30 to \$300, depending on the size and type of the business.

Additionally, the tax rate for warehouse space would be modified to \$100 per 1,000 square feet of space, rather than based on the number of employees. The rationale for this proposed change is that warehouses in the City's industrial area tend to take up large areas of land, generate substantial impacts on local streets through truck and delivery traffic, and tend to generate limited business license revenue and economic benefit to the community because they generally employ few workers. By modifying the business license tax rate to be based on square footage, staff believes that property owners would be incentivized to utilize industrial properties for more productive uses that create more jobs and associated economic benefits for the community. Further, warehouse businesses would be more likely to be paying their fair share, relative to other business types.

Lastly, the City's current annual business tax rate that is applied to parking lots (such as those providing long-term parking for Oakland International Airport) is currently set at a flat fee of \$125 plus \$37.25 per parking space. In comparison, the rate that is applied to similar businesses in Oakland is currently set at 18% of gross receipts. As such, staff recommends that the City Council review and discuss a revenue measure to set the tax at up to 10% of gross receipts, which would still place parking lot businesses in San Leandro at a competitive advantage as compared to their counterparts in Oakland.

Staff estimates that the above modifications to the City's business license tax could generate up to \$800,000 annually, while also reducing the fee burden for over 2,000 San Leandro small businesses.

### Public Opinion Survey

Per the direction of the City Council Finance Committee, staff initiated a contract with a third-party consultant for the development and execution of a public opinion survey designed to gauge community service priorities as well as the potential viability of the aforementioned revenue measures. The telephonic and email survey of 500 likely San Leandro voters is complete and the results of this survey are being finalized. Staff expects to present the results at the July 5<sup>th</sup> City Council meeting.

### **Next Steps**

Based upon the direction provided by Council at tonight's meeting as well as the results of the public

opinion survey, staff recommends bringing forward resolutions for measures that present ordinances to authorize all or a portion of the above tax measures as part of the November 2016 ballot. Tentatively, staff envisions bringing this ordinance forward for the Council's consideration at the July 18<sup>th</sup> City Council meeting.

**Fiscal Impacts:**

If adopted by voters, conservative estimates indicate the proposed tax measures could generate approximately \$1.5 million to \$1.8 million per year in new General Fund revenue.

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