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Staff Report for City Council Consideration of Placing Three Ballot Measures on the November 2016 Ballot Asking Voters to Authorize New General Fund Revenue

SUMMARY AND RECOMMENDATIONS

The City Manager recommends that the City Council:

- 1) By motion, adopt by two-thirds vote the attached resolution placing a measure on the November 8, 2016 ballot asking San Leandro voters to levy an ongoing tax of up to 10% of gross receipts on cannabis businesses in the City
- 2) By motion, adopt by two-thirds vote the attached resolution asking San Leandro voters to authorize a modification of the ongoing business license tax to reduce fees for small businesses, charge up to 10% of gross receipts for parking lots, and charge \$100 per 1,000 square feet of real property that is used for warehouse and distribution businesses
- 3) By motion, adopt by two-thirds vote the attached resolution asking San Leandro voters to authorize an increase in the ongoing transient occupancy tax charged to hotel guests from 10% to 14%
- 4) Adopt by majority vote the attached resolution appropriating \$65,000 from the City's General Fund Economic Uncertainty Reserve in order to provide funding for public outreach and informational efforts related to the above measures in advance of the November 2016 election

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 programs, services for 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, sales tax is an inherently volatile source of revenue that will generally rise and fall in direct correlation with broader regional economic cycles. Should the economy slow down or contract 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. A diversified revenue base is essential to maintain the sustainability of the City's budget.

To address these factors, at the direction of the City Council Finance Committee, City staff began exploring various potential new local sources of revenue which, per State law, require voter authorization. An overview of these measures was presented to the City Council at its June 20, 2016 meeting. Those measures include:

- 1) A medical cannabis business tax of up to 10% of gross receipts;
- 2) 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; and
- 3) An increased transient occupancy tax of up to 14%.

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, as they would be paid by a select number of businesses and people from out of town. Should the Council decide to move forward with the above measures, staff recommends that the City Council adopt by resolution the attached ordinances which would bring forward corresponding ballot measures for local voter consideration on the upcoming November 2016 ballot.

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 by the City Council on July 18, 2016, the City has an opportunity to derive an important new source of revenue from these businesses. Similar to many other communities that have permitted the operation of cannabis businesses, the recommended tax in San Leandro would be 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 the cannabis industry, the proposed ballot question has been structured such that the tax amount would be “up to” 10% of gross receipts. The proposed language would allow the City flexibility to modify the rate over time up to that maximum 10% threshold. The draft ordinance has also been structured such that it would apply to any business involving the use of any component of the cannabis plant. If the adult use of cannabis becomes legal following this November’s election and/or if the City Council were to decide in the future to allow other ancillary cannabis-related businesses to operate in the community (e.g. laboratory testing, cultivation sites, or extraction facilities, among others), this tax would apply, providing an important new revenue stream to the City.

Given that no permitted cannabis dispensaries are yet operating in San Leandro, there is uncertainty as to 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 7%.

Overview of Potential Modifications to the 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 City Council priorities to support small businesses located in San Leandro, while also incentivizing the productive use of the City’s industrial areas.

Small Business Discount:

As currently structured in the attached draft ordinance, the per-employee component of the business license tax for small San Leandro businesses with three or fewer employees would be eliminated. Currently, these businesses pay a flat fee of \$128.20, plus a per-employee fee that varies by business type. The per-employee fee would be waived for all small businesses.

This modification would result in a tax reduction for approximately 2,300 small businesses located in San Leandro and an estimated decrease in business license tax revenue of \$250,000 annually.

Warehouse Rate Change:

Additionally, the proposed draft ordinance would modify the tax rate applied to warehouse and distribution businesses. They are currently charged a flat fee of \$128.20, plus a per-employee fee. The draft ordinance would charge them \$100 per 1,000 square feet of building space. The rationale for this proposed change is to better align the business license fee with the impact of such businesses, much of which comes from the physical size of their business rather than the number of employees. Warehouse and distribution businesses cause heavy wear on local streets through truck and delivery traffic, but generate relatively few jobs and limited business license revenue or sales tax. By modifying the business license tax rate to be based on square footage, the tax would better reflect such businesses’ impacts on City infrastructure and services. The estimated additional business license revenue to be generated from this change in collection methodology is \$450,000 annually.

Parking Lot Range Change:

Lastly, the proposed draft ordinance would modify the business tax rate that is applied to parking lots

(such as those providing long-term parking for Oakland International Airport). Currently, parking lots pay a flat fee of \$128.20, plus \$38.50 per parking space. The draft ordinance would charge such businesses a rate of 10% of gross receipts. In comparison, the rate in the City of Oakland is currently set at 18.5% of gross receipts. The proposed rate would enable the City of San Leandro to capture additional revenue while still providing parking lot businesses in San Leandro a competitive advantage over those located in Oakland. The estimated additional business license revenue to be generated from this change in collection methodology is \$600,000 annually.

In summary, staff estimates that the above modifications to the City's business license tax which align the taxes collected with the economic priorities of the City could generate up to \$800,000 annually, while simultaneously reducing the tax burden for approximately 2,300 small businesses located in San Leandro.

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 located within San Leandro. Other communities in the region have established 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. If voters authorize the expansion of the TOT tax from 10% to 14%, an additional \$200,000 in revenue could be realized by the City, with the potential for greater increases in the future as new hotels are constructed.

Overview of 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 501 likely San Leandro voters has been completed and the results of the survey were presented to the City Council at its July 5, 2016 meeting. A copy of the report summarizing the results of that survey is provided as an attachment to this report.

Survey Results

The survey's results indicate strong informed support from survey respondents for all of the above potential revenue measures. More specifically, 72.2% of survey respondents indicated that they would "definitely" or "probably" support the cannabis business tax; 64.3% of survey respondents indicated support for the Business License Tax modifications; and 64.7% of respondents indicated support for the proposed modifications to the TOT tax. As part of the survey, respondents were also asked about various community priorities that could benefit from new funding, and the following topics received the highest support:

- Provide shelters for abused women and children
- Fix potholes and repair City streets
- Improve 9-1-1 emergency response times
- Attract new businesses and create jobs in San Leandro
- Enhance safety net programs for homeless and at-risk adults and children

Proposed Ballot Questions:

If the City Council should decide to place the above measures on the November 8, 2016 ballot, the following draft ballot language is recommended to be used. It is important to note that this language has been reviewed and is recommended by the City's public opinion survey consultant, is approved by the City Attorney, and also meets the specific legal and technical requirements of the Elections Code. Lastly, this is the specific language that was used in the community survey to gauge public support, outlined above. Staff therefore recommends that no changes be made to the proposed ballot language. Following placement on the ballot, the City Council may also authorize the Mayor or a subcommittee of the City Council to file an argument in favor of the measure and a rebuttal to an argument filed against it, and to work with an independent campaign committee or other third-parties on the preparation of the argument and rebuttal. The draft ballot language for each of the measures is as follows:

CANNABIS BUSINESS TAX MEASURE:

To maintain and enhance the City of San Leandro, with funding that cannot be taken by Sacramento, including: social services, public art, programs that celebrate diversity, multilingual programming and other general city services, shall the City of San Leandro levy an ongoing tax of up to 10% of gross receipts of cannabis (marijuana) businesses in the city, providing \$500,000 annually, requiring independent citizen oversight, financial audits, and that all funds stay in the City of San Leandro?

YES NO

BUSINESS LICENSE TAX:

To maintain and enhance the City of San Leandro, with funding that cannot be taken by Sacramento, including: enhancing City infrastructure and general city services, shall the City of San Leandro modify the ongoing business license tax to reduce taxes for small businesses, charge 10 percent of gross receipts for parking lots, and charge \$100 per 1,000 square feet of warehouse and distribution space, providing \$800,000 annually, requiring independent citizen oversight, and all funds stay in San Leandro?

YES NO

TRANSIENT OCCUPANCY TAX MEASURE:

To maintain and enhance the City of San Leandro, with funding that cannot be taken by Sacramento, including: enhancing library programming for children, more space for books, reference materials and public access computers, enhancing parks and infrastructure, and other general City services, shall the City of San Leandro increase the ongoing transient occupancy tax charged to hotel guests from 10% to 14%, providing \$200,000 annually, requiring independent citizen oversight, financial audits, and all funds staying in the City of San Leandro?

YES NO

Public Outreach

If the City Council decides to proceed with asking voters to adopt the above-referenced measures, staff also recommends that as part of its actions, the Council appropriate \$65,000 from its economic uncertainty reserve for various outreach efforts in advance of the November 2016 election. Such efforts could include development of online and mailed informational materials that explain the factual details of the proposed revenue measures. Similar to the outreach efforts that were conducted in advance of Measure HH, a significant component of these costs is driven by the cost of postage for the anticipated informational mailer. These materials and outreach efforts could also provide

additional information about the types of community services and other policy priorities that could be funded with the new revenue should voters ultimately decide to authorize the measures. A resolution authorizing a \$65,000 appropriation has been attached to this staff report for the Council's consideration.

Fiscal Impacts and Spending Priorities Discussion:

If adopted by voters, conservative estimates indicate the proposed tax measures could generate approximately \$1.5 million per year in new ongoing General Fund revenue. If the proposed measures are approved by voters, staff also recommends that the City Council consider budgeting portions of the new funds derived from those measures towards the following programs and service priorities, which survey responses indicate are of highest priority to community residents:

- Fixing potholes and repairing city streets
- Improving 9-1-1 emergency response times
- Attracting new businesses and creating jobs in San Leandro
- Enhancing safety net programs for homeless and at-risk adults and children
- Making improvements to the Mulford-Marina Branch Library, including: providing space for a children's area; children's story times; homework center; up-to-date reference materials, books, audio-visual materials and periodicals; public access computers; a community room; and free Wi-Fi
- Providing a police operations center that meets current seismic safety codes and will survive an earthquake and be up and running in a disaster
- Enhancing walking and running trails in San Leandro parks
- Providing traffic calming measures to improve traffic safety
- Connecting to the Bay Trail and Bay Water Trail in San Leandro
- Providing programs that celebrate diversity in San Leandro
- Providing multilingual outreach
- Providing free Wi-Fi hotspots throughout the City
- Enhancing public art including sculptures and murals

In addition, if the City Council were to adopt the attached resolution authorizing funding for public outreach efforts, it would result in \$65,000 in net costs to the General Fund.

Submittal Requirements

The three attached Resolutions for the proposed ballot measures include blank spaces for certain dates related to the submittal of the approved ordinances, deadlines for the impartial analysis and ballot arguments, and designation of Mayor/Councilmembers to provide the arguments in favor of the measures. The submittal deadlines will be clarified by staff at the July 18 City Council meeting. Staff requests that the City Council provide direction on the individuals authorized to provide written arguments in favor of the measures.

Budget Authority

Staff recommends City Council approve appropriation of \$65,000 from the General Fund Economic Uncertainty reserves to account number 010-12-020-5120 for public outreach efforts in fiscal year 2016-17.

Attachments:

- Summary of Community Survey Results

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