City of Palo Alto (ID # 12299)
Finance Committee Staff Report

Report Type: Action Items **Meeting Date: 6/15/2021**

Summary Title: Workplan for November 2022 Local Ballot Measure(s) & Affordable Housing Funding Referral

Title: Recommend the City Council Approve the Workplan for Pursuit of a Revenue-Generating Local Ballot Measure for the November 2022 General Election; Review and Potential Guidance to Staff on Affordable Housing Funding as Referred by the Council

From: City Manager

Lead Department: Administrative Services

Recommendation

Staff recommends that the Finance Committee recommend to the City Council approval of the workplan for pursuit of a November 2022 or other local ballot measure(s) and any additional guidance including but not limited to:

A) Affirming pursuit of a business tax, and refinement of the basis for such a tax (e.g. headcount, payroll, square footage, gross receipts, or other);
B) Affirming pursuit of a utility use-based tax;
C) Direction to proceed with refinement of estimates and evaluation of potential tax measures, including stakeholder outreach, polling and further feasibility analysis; and
D) Review of additional information regarding affordable housing funding as directed by the City Council.

Executive Summary

This report resumes the work that the staff and City Council placed on pause in March 2020 with the onset of the COVID-19 pandemic and resumes review of this as outlined as part of the Community and Economic Recovery workplan and Council priority in 2021. Throughout the past decade, the City has worked to structurally balance its long-term revenues against increasing expenses. In 2019, the City Council adopted fiscal sustainability as an annual priority and approved a workplan on that priority through CMR 10267.

As an element of the fiscal sustainability workplan, through iterative conversations with the Finance Committee and the City Council, significant work was done on developing potential business tax ballot measure. This report seeks to resume the City's work effort to identify a potential revenue-generating local ballot measure(s) and to finalize a workplan and potentially narrow the scope for staff to focus limited resources on reaching the general election scheduled in November 2022. The report includes key attachments for the Finance Committee's review and reference:

- The earlier work on this topic included an analysis of potential options for raising revenue and a summary of that work is included with this report as **Attachment A.**
- A summary of funding options for Affordable Housing is included with this report as **Attachment B.**
- A summary of prior work specifically related to the development of a potential business tax is included as **Attachment .C**
- A full list of prior CMRs on fiscal sustainability and the topic of a revenue generating local ballot measure is included with this report as **Attachment D.**

In addition to review of the past and current work, staff has provided a workplan/timeline to complete this priority with the target of consideration of a measure(s) on the November 2022 election. Consistent with past practice, staff recommends the Finance Committee will serve as the main deliberative body for the development of a potential revenue-generating local ballot measure and that updates will be taken to the City Council for review and ultimately direction to staff in addition to the appropriation of resources.

Background

The City of Palo Alto has worked towards fiscal sustainability over the past decade through a number of actions, specifically outlined in the Fiscal Sustainability Workplan of 2019. These actions included proactive funding contributions for the city's long-term liabilities for both pension and Other Post-Employment Benefits (OPEB) and strategies to structurally balance the General Fund's revenue and expenditures on an ongoing basis. This work is detailed more fully through CMR 10267 which details each of the 14 elements of the workplan to address the 2019 City Council priority of Fiscal Sustainability and CMR 11722 which adopted the City's proactive pension funding policy.

Despite this work, structurally balancing revenues and expenses on an annual basis has proven difficult. The City Council has articulated numerous needs beyond current funding levels including:

- Funding for Affordable Housing
- Funding for electrification and Climate Change Resilience and Adaptation
- Funding for Capital Needs (including but not limited to railroad grade separation alternatives)
- Funding for Delivery of Core Services – i.e. Parks, Youth Services, Community Services, Libraries, Fire and Emergency Medical Services, and Police

The economic impacts associated with the COVID-19 pandemic, and efforts to contain and mitigate the spread of the virus resulted in a $40 million gap between revenues and expenses in the FY 2021 Adopted Operating Budget, which was balanced through significant reductions in departmental operating expenses throughout the organization, significant reduction in capital investment including catch-up and keep-up costs as well as new projects, and concessions from some of the City's bargaining units.

The table below shows the amount of general fund revenues from FY 2019 through FY 2022 in the major categories. The precipitous decline seen at the end of FY 2020 continued through FY 2021 as reflected in the FY 2021 estimate column.

Table 1. Summary of General Fund Revenues: FY 2019 and FY 2020 Actuals, FY 2021 Estimate and FY 2022 Proposed

	FY 2019 – Actual	**FY 2020 – Actual**	**FY 2021 – Estimate***	**FY 2022 Proposed**
Property Tax	$47.3	$51.1	$53.17	$51.2
Sales Tax	36.5	30.6	25.03	28.2
Transient Occupancy Tax	25.6	18.6	4.8	8.4
Utility Users' Tax	16.4	16.1	14.1	14.4
Documentary Transfer Tax	6.9	6.9	6.9	7.1
Charges for Services & Licenses and Permits	35.8	31.6	29.5	32.5
All Other Revenues	57.3	54.8	55.4	63.8**
Total General Fund Revenues	**$225.8 M**	**$209.7 M**	**$188.9 M**	**$205.6 M**

* This reflects the FY 2021 estimate as shared with the Finance Committee at the outset of the budget development process; staff subsequently communicated to the Finance Committee and the City Council that it anticipated slightly higher levels at year-end depending on activity levels in certain revenue streams.
**The FY 2022 Proposed Estimate for other revenue did not include the 60/40 Split of American Recovery Plan Act (ARPA) funding, nor the final allocation of that funding. Subsequent to the issuance of the proposed budget, all other revenues have increased to $65.8 million bringing total FY 2022 Proposed Revenues to a total of $207.6 million.

As seen in Table 1, sales tax and transient occupancy tax revenues and their contributions to the General Fund were a strength in FY 2019 that helped fund the myriad of services in Palo Alto that differentiate it from other jurisdictions. Unfortunately, primarily as a result of the economic impact of efforts to contain and mitigate the spread of COVID-19, these revenues contracted and declined.

Adding to revenue challenges, in FY 2021 a local court held that a portion of the City's longstanding annual transfer of funds from the gas and electric utilities – which has funded general City services such as police, fire, parks and libraries for many decades – could not lawfully continue absent voter approval. While the court ruling is not final and may be appealed, for FY 2022 the City has prudently set aside the disputed funds in a reserve pending resolution of the issue. On the November 2022 ballot, the City could seek voter approval to confirm the longstanding transfer or could seek to replace the transfer revenues with an increase in the utility user tax or some other type of tax.[i]

The current FY 2022 Operating Budget adjusts for both the current impacts of the pending litigation as well as the recovery period due to the current pandemic and relies on one-time funding to bridge the current uncertainties and delay further service reductions beyond those approved as part of the FY 2021 Adopted Budget. However, the significant reductions taken in FY 2021 will persist on an ongoing basis unless revenues can be brought into alignment with expenses. This report represents the next step in discussions with the Finance Committee and the City Council to address structural financial needs and is the first step in resuming prior discussions regarding a business tax and potentially a utility use-based tax and how they can be brought forward for voter consideration as part of the November 2022 general election.

Discussion

As discussed in CMR 10392 charter cities have two primary mechanisms for generating revenue: 1) charging for services and 2) taxes. More information on these mechanisms, a brief summary of Palo Alto's major existing tax categories, and the potential impacts associated with pursuing changes to various tax rates are explored in greater detail in **Attachment A** of this report. Potential revenue estimates are meant to offer context at this early stage to inform the conversation with the Finance Committee and guide potential next steps. Consistent with the discussions associated with a potential business tax through FY 2019 and FY 2020, it is anticipated that these estimates are maximums and are likely to be refined downward through additional variables, exemptions, changes to the eligible bases, and other considerations as they are more fully developed.

Prior to COVID-19, the City undertook a significant work effort to discuss potential revenue generating ballot measures. Links to each of the City Manager Reports associated with the prior work effort are included in **Attachment D**. Through those discussions, staff presented a discussion of the various taxes that contribute to the General Fund and proposed using Equity, Administrability, Stability and Economic Benefits (EASE) as the framework for analysis. The EASE framework is discussed further in **Attachment A.**

Previous work on local ballot measures included three parallel paths that were pursued by staff, augmented by consultant resources, and a fourth path that was not reached during the prior effort. Staff recommends that the Committee and Council continue to use this framework as the organization resumes this work. These four paths, the consultants used, and the contractual authority were:

- Research, Analysis, and Modeling – Matrix Associates - $75,000
- Stakeholder Outreach – TBWB - $94,125
- Polling – FM3 Associates - $85,000
- Drafting Ordinance Language – N/A

The City suspended consideration of a ballot measure before the fourth element of drafting an ordinance got underway. Regardless of which local ballot measures are pursued further to place on the November 2022 ballot, it is likely that the work will once again be organized into these three focus areas and that the City Attorneys' Office will retain outside counsel to assist with drafting the ordinance language to enact the measure. More discussion of these paths is included in **Attachment C.**

In addition, staff has provided detailed information regarding affordable housing funding as referred to staff and the Finance Committee in the Housing Workplan. **Attachment B** provides a summary of funding strategies for affordable housing initiatives. Overall, staff has found that a combination of financial/funding strategies and partnerships is the most common framework for a successful affordable housing project. As noted above, the Council has identified a number of financial needs, therefore staff has included this Council referral as part of the discussion of potential local ballot measure(s) to provide the full context of potential expenses to be coupled with potential sources to fund them.

In order to reach the November 2022 ballot, a proposed workplan is detailed here for discussion and refinement with the Finance Committee and the City Council, including their respective engagement roles. It is important to narrow the scope of work as quickly as possible not only to focus limited staff resources and optimize the use of consultants but also to avoid placing too many measures on the ballot.

Governance:
To meet that timeline, staff recommends that the Finance Committee serve as the working body to assist in the review of potential revenue-generating local ballot measures for the November 2022 election and to review staff and consultant work as well as stakeholder feedback. The Finance Committee could then make its recommendations for consideration and action to the full seven-member City Council.

Finance Committee: would serve as the public body to review periodic progress reports, allowing for structured public discussion and the provision of feedback and recommendations on the review and development of a potential revenue-generating local ballot measure. Staff will manage, review, and synthesize work done in-house and by external consultants and incorporate stakeholder feedback into regular progress reports to the Finance Committee. Ultimately, the Finance Committee would recommend their preferred potential revenue-generating local ballot measure(s) to the City Council for further action.

City Council: would serve as the governing body for policy direction at key decision points. This includes direction to conduct polling, approval of alternatives to be evaluated, and decisions on what should be placed on the November 2022 ballot.

Timeline

Given the constrained timeline and resources for pursuing the placement of a ballot measure(s) on the November 2022 ballot, the aforementioned approach once again seems worth pursuing. The table below shows the aggressive timeline necessary to finalize ballot measure language and draft a potential ordinance by late Spring 2022 in order to reach the November 2022 ballot.

SCHEDULE	TASK
JUNE 2021	<u>*Finance Committee:*</u> - *Recommendation to City Council on Workplan for 2022 ballot measure(s)* - *Review and discussion of affordable housing funding and other funding needs in the context of available revenue generating strategies.* Agreement on an approach to the development of revenue estimates and options, workplan, and roles.
JULY 2021	<u>*Staff Work:*</u> Development of Agreements for consultant services (may require RFP or sole source exemption). Depending on which potential revenue-generating local ballot measures are pursued, staff will seek consultant expertise including financial analysis, modeling, additional research, stakeholder engagement and polling. No funding is currently allocated for this and staff recommends use of the "Reserve: Strategic Investments" which is currently recommended to have a balance of $750,000 in FY 2022 to fund these services.
AUGUST 2021 – SEPTEMBER 2021	<u>*City Council:*</u> - *Direction to staff on which ballot measures to pursue and allocate resources, as recommended by Finance Committee.* (tentatively to be considered in August 2021) <u>*Finance Committee:*</u> - *accept initial analysis of revenue generating proposal estimates.* Estimates to be completed internally by staff and intended to assist in informing various working groups in financial planning and focus further refined analysis. <u>*City Council award of consultant contract(s):*</u> as necessary to complete this workplan.
OCTOBER 2021	<u>*Finance Committee:*</u> - *Accept refined analysis of revenue generating proposals estimates;* - *discuss and provide guidance on initial polling and initial stakeholder outreach*. With the assistance of consultant expertise, a more in-depth review of revenue generating proposals will be presented to the Finance Committee providing more accurate financial estimates to assist in financial planning.

	Staff work: Complete initial outreach to key stakeholders *City Council:* Discuss Councilmember and community leaders and advocates roles
NOVEMBER 2021	*City Council:* - *confirmation on potential revenue generating proposals including revised revenue estimates* - *Direction to complete initial polling and initial stakeholder outreach.* Work completed with the Finance Committee to be reviewed by the full Council in order to receive input and direction on more refined steps.
DECEMBER 2021	*City Council:* - *decision on revenue generating proposal(s) to pursue.* Decision to be informed by the Finance Committee, financial analysis, polling results, and a more refined understand of potential projects and associated costs.
DECEMBER 2021 – APRIL 2022	*Staff work:* Continue stakeholder outreach, draft required legal documents, complete polling as appropriate. City Council and Finance Committee will be provided updates as necessary for status check-ins, additional rounds of polling, feedback, and policy decisions.
MAY 2022 – JUNE 2022	*City Council: approval of November 2022 ballot measure and specific measure language.* Should the City Council choose to pursue a ballot measure(s), final approval including the ballot measure language will need to be submitted to the Santa Clara County Registrar of Voters in early August 2020.

Resource Impact
Implementation of this workplan to develop revenue-generating local ballot measures will require significant resources, including internal staffing and consultant expertise as well as extensive stakeholder engagement. Depending on which ballot measure(s) the Finance Committee and the City Council direct staff to pursue, the resource needs will scale proportionately. It is important that the scope of potential ballot measures be narrowed to effectively deploy necessary resources and stay on the timeline as noted above.

To the extent that consultants are required to augment staff on topics such as research, modeling and analysis, polling, stakeholder outreach, and eventually the drafting of ballot measure and ordinance language, staff will return to the City Council for appropriation of funds and approval of contracts as appropriate. For reference, the prior single initiative was directly resourced by approximately the equivalent of 2.0 full-time dedicated staff, significant support from staff stakeholders in key departments, and consultant services support of $250,000 (until the pausing of the work). Staff have gone through resource reductions and therefore expect there will be impacts to other projects, and additional funding needed in excess of the amount used previously, consistent with the work completed in 2019 and 2020. As the Council may choose a variety of measures for analysis and consideration, funding and staff resources will increase accordingly.

Stakeholder Engagement
Staff has solicited input and feedback at multiple junctures through evaluation of a potential business tax through previous conversations with the Finance Committee, the City Council, residents, and the business community. As the scope of this work is refined, staff will work to develop a corresponding stakeholder engagement plan specifically for this effort and incorporate that into the ongoing process. Staff will include stakeholder engagement and feedback as an element of any potential revenue-generating local ballot measure workplan and will regularly report on the status of those efforts.

Conclusion and Next Steps
This report restarts the Finance Committee and the City Council guidance to staff in the pursuit of additional revenue streams to be brought forward for voter approval through the November 2022 general election. Based on prior discussions with the City Council and the Finance Committee, staff anticipates pursuing a business tax and a potential utility use-based tax. Depending on the revenue stream, the City could allocate the funds either towards specific uses or general city services to support City services, capital infrastructure needs, funding affordable housing, or other priorities per City Council direction.

The timeline, resource impact and stakeholder engagement effort will each be impacted by the decisions of the Finance Committee and the City Council and will scale according to the necessary scope of work. In order to meet the timeline to place a ballot measure on the November 2022 ballot, timeline noted above provides a guide on next steps and cadence for approvals needed by the Finance Committee and City Council.

Attachments:

- Attachment A: Options for Raising Local Revenue
- Attachment B: Summary of Affordable Housing Funding Options
- Attachment C: Overview of Prior Work on a Potential Business Tax
- Attachment D: List of Prior City Manager's Reports on Local Ballot Measure

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[i] Green v. City of Palo Alto (Santa Clara Superior Court, Case No. 1-16-CV-300760), a class action lawsuit, was filed on October 6, 2016. Plaintiffs claim that the City's gas and electric rates are taxes that exceed the cost of providing service, absent voter approval, because the rates fund annual transfers from the utilities to the City's general fund. The lawsuit seeks a refund of three years of alleged overpayments by gas and electric ratepayers and an injunction prohibiting further overpayments.

On October 27, 2020, the Santa Clara County Superior Court issued a "Statement of Decision Regarding Phase II Trial" granting the relief sought by the plaintiffs as to the City's gas ratepayers only. The court's ruling established the City's liability at $12.6 million, which the City may have to refund to gas customers after the judgment is final and all appeals, if any are filed, are resolved. Once a judgment is issued by the Superior Court, which is likely to occur during the summer of 2021, both the City and the plaintiffs may appeal. A decision by the City Council whether to appeal is likely to be made after the Council's summer break. If either the City or the plaintiffs appeal, a decision by the Court of Appeal is not expected until late 2022 or early 2023.

Because important areas of law are unsettled relevant to the City's positions on appeal, the exact exposure to the City's general fund cannot be determined with certainty at this time. In the FY 2022 budget, the City has set aside funding to cover the $12.6 million remedy the Superior

Court identified in Phase II, plus interest, as well as the estimated future reduction in the gas equity transfer, should the current Santa Clara County Superior Court decision stand. The City estimates the annual financial impact would be $8 million over the coming four years (FY 2022 – FY 2025 and an average of $4 million annually after the initial four-year period beginning FY 2026).

ATTACHMENT A

Options for Raising Local Revenue

This attachment includes information previously presented to the City Council through City Manager's Reports (CMRs) 10392 and CMR 10445, describing the City's main revenue streams and the impact of changes to those streams, as well as information regarding the potential issuance of a General Obligation (GO) bond or the imposition of a parcel tax. It also includes a brief discussion of potential changes to the basis for the Utility Users Tax. Information related to a potential business tax can be found in **Attachment B**.

As discussed in City Manager's Report (CMR) 10392, cities have two main mechanisms for raising revenues: 1) taxes and 2) fees for services. The City of Palo Alto has a Municipal Fee Schedule which it reviews annually as part of the budget process for a robust span of fees and charges. The City also has service agreements with neighboring jurisdictions for services rendered, ranging from the regional water quality control plant to the provision of fire protection and communication services to Stanford. These fees for services are governed by various state laws and contractual agreements. In some cases, fees are designed to fully cover our cost of providing services. In other cases, fees are designed to pay part of the cost of providing services, with the balance provided by tax revenues. Finally, some fees and charges lawfully exceed our costs, providing excess revenues to help fund other programs and services to residents.

Cities can also impose taxes; however adoption of, or changes to, those taxes must be approved by the voters in accordance with California law, including Propositions 218 and 26. For a general tax, a simple majority of votes cast (50% + 1 vote) is required for approval, while for a specific tax a 2/3 supermajority approval is required. By state law, cities may place a general tax before the voters only at a general municipal election, which is an election that includes open seats on the governing body. (The exception to this rule is a fiscal emergency declared unanimously by the governing body).

Tax Revenues

Property Taxes

Property taxes are the largest revenue generator for the City of Palo Alto. All taxable real and personal property is subject to a 1% basic tax of assessed value collected by local jurisdictions and school districts for general service purposes. The City of Palo Alto receives only 9.42% of the assessment, with the majority (45.61%) going to Palo Alto Unified, followed by Santa Clara County (15.93%) and ERAF (13.88%). Due to Proposition 13, the effective property tax rate is only 0.49% of assessed value – less than half of the 1% basic tax.

Potential Property Tax Rate Change

Property taxes are regulated by state laws, including voter-approved constitutional provisions such as Proposition 13. Changing the rate itself is not within a municipality's authority. However, cities can use mechanisms such as parcel taxes which are levies on parcels of property. Typically, these are set at some fixed amount per parcel and cannot be based on the value of a property. These levies can be based on lot square footage and or land use designation. Parcel taxes are usually special taxes requiring a 2/3 voter approval. Parcel taxes are levied on the property owner; however, property owners may pass on these costs to their tenants in the form of increased rent or more expensive leases.

Sales and Use Tax

Sales and Use Taxes are usually the second largest revenue generator for the City of Palo Alto, raising $30.6 million in General Fund revenue in FY2020. Sales Tax rates include state, regional, and local assessments. Currently, the City of Palo Alto has a tax rate of 9.0 percent. The City receives 1% point of the purchase, or 11.1% of each tax dollar. The remaining distribution is State of California (5.75% point), Santa Clara County (0.125% point), Santa Clara Valley Transportation District (1.625% point) and Public Safety Fund (0.5% point). As seen in Table 1 of CMR 12299, Sales Tax revenues can fluctuate significantly depending on the overall state of the economy.

Potential Sales Tax Rate Change

An increase in the Sales Tax rate of ¼ cent, or 0.25 percentage points, as a district tax, would generate approximately $4.5 million in additional revenue annually. The State of California caps local sales taxes levied by local jurisdictions at 3.0%, meaning the total percentage can be no greater than 10.25%. This tax would be equitable across businesses of the same industry, however, it does not apply to industries that are not subject to sales tax. Sales tax is widely considered to be an outdated tax structure and according to the City's consultants only applies to up to 40 percent of the economic base. This structure and the driver for it, disposable income being a significant portion this tax, is subject to economic fluctuations as well as longer term fluctuations and the consumption of goods changes in society.

Transient Occupancy Tax

Prior to COVID-19, Transient Occupancy Tax (TOT) was the third largest tax revenue generator for the City of Palo Alto, generating $18.6 million in revenue in FY 2020, down from $25.6 million in FY2019. The Palo Alto rate of 15.5% is applied to the daily rate charged by a hotel, motel, or other lodging establishment. In November 2018, Measure E was passed raising the rate from 12% to the current level of 15.5%. TOT revenues have sharply declined due to the shelter in place declared due to COVID-19.

Potential Transient Occupancy Tax Rate Change
An increase in the TOT rate would primarily impact the visitor population. A 0.5 percentage point increase in the rate from 15.5 percent to 16 percent would generate approximately $900,000 in additional revenue annually.

Utility Users Tax

Utility Users Tax generated the next largest revenue, with receipts of $16.1 million in FY20, down from $16.4 million in FY19. The Utility Users Tax is charged to all users of electricity, gas, water and telephone services. This tax is based on consumption by each respective utility. The revenue decline was due to lower consumption of both utility commodity and telephone caused by COVID-19. The electric utility revenues are comprised of approximately 70-75 percent commercial usage and 25-30 percent residential. The gas utility revenues reflect approximately 45-50 percent commercial usage and 50-55 percent residential usage. Water utility revenues are approximately 30-35 percent commercial and 65-70 percent residential. The current rate for electricity, gas and water is 5.0% and for telephone is 4.75%.

Potential Tax Rate Change

A 1 percentage point increase in the current UUT rates, bringing the electricity, gas, and water rate from 5 percent to 6 percent, and increasing the telephone rate from 4.8 percent to 5.8 percent, would generate an estimated $2.3 million in additional revenues annually. As a consumption-based tax, high volume customers bear more of the cost.

Potential On-Bill Tax for Gas and Electric Services

As noted in the staff report, the City is currently in litigation over the longstanding practice of transferring a portion of revenues from gas and electric charges, according to a formula, to the general fund to support City services such as police, fire, libraries and parks. In FY 2020, the Gas Fund transferred $6.9 million to the General Fund and the Electric Fund transferred $13.1 million to the General Fund. Of these, approximately 65% of the Gas Fund Transfer was from commercial customers, while 82% of the Electric Fund transfer was from commercial customers. No final judgment has been entered and litigation is ongoing, however, the Superior Court has entered an order upholding the electric transfer but determining that a portion of the gas transfer is unlawful absent voter approval. To resolve all legal questions about the transfers, the City could seek voter approval for the transfers in November 2022.

One form that a voter-approved equity transfer could take would be a percentage charge on gas and electric utility bills that could be used to fund general city services. The exact percentage and the amounts expected to be raised could be analyzed, discussed, and potentially tiered by volume. This could be structured as an increase to the Utility User's Tax for gas and electric, or as a separate line item tax on gas and electric services to replicate the longstanding equity transfer. Depending on the rate and structure, the tax could be cost-neutral to rate payers. In other words, rather than incorporating the , thereby lowering the initial rates, and then would be offset by a corresponding increase to the Utility Users' Tax rates.

<u>Documentary Transfer Tax</u>

Documentary Transfer Taxes generated $6.9 million in revenue for the City of Palo Alto in FY2019 and FY 2020, ranging from $3.1 million in FY 2009 to a high of $10.1 million in FY 2015. This tax is applied to the sale of real property within Palo Alto as property ownership is transferred. The State of California has a standard base rate of $1.10 per $1,000 of sale price, of which the City and County split the proceeds 50/50 which applies to general law cities. As a charter city, the City of Palo Alto has more discretion to set its rate. The City of Palo Alto currently has a non-conforming rate, meaning that it varies from the State's standard rate, currently set at $3.30 per $1,000 of sale price.

<u>*Potential Tax Rate Change*</u>

Property owners who sell their property would be impacted by an increase in the rate and would pay this tax once per sale of a parcel. Assuming approximately $9 million in annual proceeds, a $1.10 increase in the rate to $4.40 per $1,000 of the sale price would result in additional revenue of approximately $2.8 million.

Other Revenue-Generating Options – Parcel Tax and General Obligation (GO) Bond

<u>Parcel Tax</u>

The City could choose to pursue the placement of a parcel tax on the November 22 ballot, either as a general parcel tax or one specific to businesses. CMR 10445 detailed further information on Parcel Taxes and their potential applicability. That information is repeated here for ease of access.

In California, local agencies (e.g. city, school and community college district, etc.) are authorized to impose parcel taxes which require a two-third supermajority vote approval for specified purposes. For cities, parcel taxes are subject to limitations under Government Code Section 50075 et seq.

Recent decisions of the California Supreme Court and Courts of Appeal have held that voter initiatives are not subject to certain procedural requirements that apply to tax measures placed on the ballot by local governments, including the timing of elections (general municipal election or any election) and supermajority approval requirements. This area of the law is continuing to evolve. More information can be provided as needed.

Parcel taxes are levied on a property owner's property tax bill and may be a specific amount (that may escalate) or it can be based on a factor such as building square footage. The most common type of parcel tax is a fixed amount, identical for all parcels regardless of use, size, or value, and often includes a sunset provision. Per California Article XIIIA, Section 4, special taxes (like parcel taxes) cannot be *ad valorem* (based on the value of property). A parcel tax can be approved for a set period (e.g., 10 years) or it can be permanent.

> *Fixed amount parcel taxes* if applied to all property owners equally typically require owners of smaller or lower valued property to pay the same amount as owners of larger or higher valued property and therefore are referred to as regressive. A fixed parcel tax is different from an ad valorem property tax, in that it is imposed on a per-parcel basis and is not based on the AV of the property.
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> *A parcel tax based on square footage* if applied to all property owners would be more equitable on the properties that it applies to (also referred to as "progressive") since it would require owners of properties to pay proportionally based on the size of the parcel. However, this structure would most likely result in a more complex administration of the tax. As discussed in prior reports, in November 2018 the City of East Palo Alto passed a parcel tax based on square footage ($2.50 per square foot) that only applies to commercial office space that is over 25,000 square feet. This limits the scope of impacted parcels that meet these criteria, thereby theoretically limiting both the complexity of administration and the revenue generated through the tax.

In general, properties exempt from the general 1 percent ad valorem (property) tax are exempt from parcel taxes. In addition, there is a separate statute in the Government Code for school district parcel taxes (Gov. Code Section 50079 et seq.) and it differs from the more general parcel tax authority in Section 50075 et seq in two important ways: (1) School districts require a tax that applies uniformly to all taxpayers and (2) they are specifically allowed certain exemptions:

1. Persons who are 65 years of age or older.
2. Persons receiving Supplemental Security Income for a disability, regardless of age.
3. Persons receiving Social Security Disability Insurance benefits, regardless of age, whose yearly income does not exceed 250 percent of the 2012 federal poverty guidelines issued by the United States Department of Health and Human Services.

Though the above exemptions do not apply to city parcel taxes, it may be possible to include specific exemptions like these to the extent it is concluded that the exemption is reasonable based on the purposes of the tax. Further research would be necessary on this based on specific exemptions that Council and/or staff are interested in exploring.

The following table shows the City's property breakdown by land use as of 2018. For example, based on the following data, a fixed $350 parcel tax on 20,087 parcels that are eligible to be taxed would generate approximately $7 million in annual revenue. Potential revenue from an alternative methodology, such as a tax measure based on commercial square footage is described below.

TABLE A-1: Property by Land Use

Property by Land Use
Estimated Revenues Based on Fixed Tax Rate of $350 Per Taxable Parcel

	# Parcels	% of Parcels	FY 2018 Assessed Value (AV)	% by AV	Parcel Tax Revenue
Properties Subject to Parcel Tax					
Agricultural	26	0.1%	$ 15,136,270	0.05%	$ 9,100
Commercial	405	1.9%	1,875,346,761	5.8%	141,750
Manufacturing	55	0.3%	669,193,035	2.1%	19,250
Professional	550	2.6%	5,011,938,010	15.5%	192,500
Industrial	111	0.5%	1,162,901,625	3.6%	38,850
Sub-total - Commercial	1,147	5.4%	$ 8,734,515,701	26.9%	$ 401,450
Residential	18,940	89.9%	23,319,460,730	71.9%	6,629,000
Sub-total - Properties Subject to Parcel Tax	**20,087**		**32,053,976,431**	98.8%	**$ 7,030,450**
Properties Exempt From Parcel Tax					
Forest	23	0.1%	17,527,823	0.1%	n/a
Institutions (e.g. schools, hospitals, etc.)	75	0.4%	69,911,145	0.2%	n/a
Public (gov't, cemeteries, mortuaries, etc.)	363	1.7%	50,962,757	0.2%	n/a
Recreational (parks, playfields, etc.)	15	0.1%	45,587,009	0.1%	n/a
Social (churches, clubs, etc.)	54	0.3%	4,522,615	0.0%	n/a
Transportation (utly, bus, truck, streets, etc.)	18	0.1%	7,539,575	0.0%	n/a
Other (vacant, public, non-profits, etc.)	436	2.1%	178,266,617	0.5%	n/a
Sub-total - Not Subject to Parcel Tax	984	4.7%	374,317,541	1.2%	n/a
Grand Total	**21,071**		**$ 32,428,293,972**	**100.0%**	n/a

A parcel tax measure based on commercial square footage can have a simple structure like East Palo Alto's and/or a more complex tax structure based on types of properties (e.g. office, retail, industrial, etc.). The following table shows potential annual revenues, by property type, based on a $1 rentable building area per square feet parcel tax using CoStar Data. It is not intended to suggest nor provide a structure for a parcel tax. Based on the Committee's feedback and/or direction, staff can return with specific tax structure(s) and their potential revenues.

TABLE A-2: POTENTIAL PARCEL TAX REVENUES BASED ON RENTABLE BUILDING SQUARE FEET ($1 PER SQUARE FOOT)

PROPERTY TYPE	Rentable Bldg. Area (Square Feet)	Estimated Annual Revenue ($)
HOSPITALITY	1,366,278	$1,366,278
INDUSTRIAL	2,453,992	$2,453,992
OFFICE	13,304,877	$13,304,877
RETAIL	4,010,544	$4,010,544
FLEX BUILDING	4,640,212	$4,640,212
GRAND TOTAL	**25,775,903**	**$25,775,903**
EXCLUDES: GOVERNMENT, SCHOOL, PARKING GARAGE/LOT, RELIGIOUS FACILITY, LODGING/MEETING HALL, SELF-STORAGE, CONTRACTOR STORAGE YARD, CAR WASH, SHELTER, AND THEATER/CONCERT HALL.		

Compared to GO Bond Measures, in the June and November 2018 elections, the approval for City parcel tax measures was slighter better, with 75 percent passing in June 2018 and 83.3 percent passing in November 2018. In June and November 2018, there were 62 parcel tax measures with 34, or 54.8 percent, passing. For City only tax measures, 81.3 percent passed. In addition, of the 13 school parcel taxes 10, or 76.9 percent, passed. As for the sunset provision for parcel tax measures in the last three elections, most school ballot measures had them while, in a given election year, only a third to less than half of non-school measures had them.

TABLE A-3: PARCEL TAX VARIABLES & E.A.S.E.

	PARCEL COUNT	SQUARE FOOTAGE
EQUITY	For fixed (per parcel tax), results in owners of smaller or lower valued property to pay the same amount as owners of larger or higher valued property.	A rentable building square feet tax aligns the tax with both the size and potentially the property types it's assessed on which would be considered more progressive.
ADMINISTRATION	Further research is needed to understand the full administration cost for a parcel tax. What is known are as follows: (1) the University Avenue parking assessment bonds are consider a parcel tax for which the County of Santa Clara's administrative cost is 1 percent of the levy; (2) depending on the tax structure, the county might have a $16 per parcel cost which is far more expensive than the 1 percent of levy fee; staff is working with the county to understand when this is applicable. There likely will be an annual consultant cost to prepare and submit the parcel tax assessment to the county. If these revenues are used to issue bonds, then there will be costs associated with a bond's issuance and on-going management similar to the GO Bond issuance.	
STABILITY	Very stable with low volatility.	Very stable with low volatility.
ECONOMIC BENEFITS	Economic development implications of a flat, parcel tax would depend on any policy choices for exemptions. However, as noted in the discussion a flat tax would be regressive as it does not scale to size or another unit not scale to size or another of measure.	This method could be tailored to promote certain economic development objectives; however, the selected exemptions or varying tax rate scales could result in unanticipated complexities that would make the tax difficult to administrate.

General Obligation (GO) Bond

Other options that were previously discussed included the issuance of General Obligation bonds. These were also further discussed in CMR 10445 and that information is repeated here for ease of access.

A common form of long-term capital project financing is the General Obligation (GO) bond. Cities can only issue GO bonds to pay for the acquisition and improvement of real property (California Constitution Article XIIIA). Under Article XIIIC of the State Constitution, City GO bonds require a favorable two-thirds supermajority vote of the registered voters that vote on the measure. For California cities, GO bonds are secured by a promise to levy *ad valorem* property taxes (property taxes based on the value of the property) in an unlimited amount as necessary to pay debt service. Voters approve the maximum amount of debt (bonds) that can be issued. The *ad valorem* taxes levied to pay debt service on city GO bonds are in addition to the 1 percent general *ad valorem* property tax. Although the California Constitution was modified in 2000 through the enactment of Proposition 39 to allow schools, community colleges, and county education offices, under defined circumstances, to have a 55 percent popular vote threshold, City GO bonds still require a two-thirds favorable vote.

Generally, based on assessed values (AV), approximately two-thirds or more of a GO Bond assessment is paid by residential parcels and one-third by businesses/commercial parcels in the City of Palo Alto. While GO bonds can be issued for different lengths of time, the most common are 30-year bonds with 40 years being the maximum maturity duration. The City of Palo Alto has issued GO bonds for library and school infrastructure improvements. The City's net library bond issuance of $71 million currently adds $10.62 per $100,000 in AV to each property owner's tax bill, or about $106 per year for a residence appraised at $1,000,000. This is based on a FY 2020 secured property tax AV of $37.3 billion and unsecured property tax AV of $1.9 billion.

The below table reflects a range of potential GO bond issuance size, an initial assessment rate for $1 million in AV for residential/commercial properties and the unsecured property taxes and potential annual debt service payments. The term "unsecured" refers to business personal property that can be relocated and is not real estate (e.g. aircraft, boat and machinery and equipment, etc.).

TABLE A-4: POTENTIAL GO BOND ISSUANCE AMOUNT

POTENTIAL GO BOND ISSUANCE AMOUNT	Residential/Commercial (Rate for $1 M in Assessed Value/Yr)	Unsecured Property (Rate for $1 M in Assessed Value/Yr)	Estimated Annual Debt Service
$100M	$178	$203	$6.6 million
$200M	$356	$406	$13.2 million
$300M	$533	$608	$19.8 million
$500M	$888	$1,012	$32.9 million

Note: the above tax rates will be re-calculated annually based on the annual debt service and the City's total AV. Historically, the AV increases annually while the debt service remains stable resulting in the GO Bonds' tax rates declining.

The below table addresses the E.A.S.E. framework as applied to the analysis of a potential GO Bond issuance.

EQUITY	Though the GO Bond tax rate is applied uniformly against the property's Assessed Value (AV), due to Proposition 13, properties that have changed ownership will have a higher AV and corresponding burden from a GO Bond tax assessment than those properties with a lower AV.
ADMINISTRATION	The County of Santa Clara charges 0.25 percent to administer the assessment collection via the annual property tax bill. A $100M bond issuance with a $6.6M annual debt service payment would incur $16,500 in annual administrative fees by the County to collect the tax. Considerable cost and staff resources would be incurred associated with the actual bond(s) issuance and ongoing staff time would be necessary to manage the debt service and bond covenant requirement for the bond duration (e.g. 30 years) and the annual GO Bond tax rate calculation which is submitted to the county.
STABILITY	Very stable with low volatility even during a recession.
ECONOMIC BENEFITS	A GO Bond mirrors the current assessment and weight of the baseline 1% property tax assessment. The *ad* valorem levy is the same as the baseline tax structure for both the administrator and the taxpayer, therefore, minimal administrative disruption is anticipated. However, inequities associated with current regulations such as Proposition 13 as referenced above may disproportionately impact certain owners.

The Bay Area GO Bond measures considered in June and November 2018 elections had mixed results, though the majority passed, a few did not. In November 2018, there were eleven non-school GO Bond measures totaling $2.4 billion. Five passed and a total of $1.3 billion in local non-school GO Bonds were issued. In June 2018, there were three local non-school GO Bond measures and two of those measures passed, both cities in the Bay Area. Though the overall passage rates in the last two elections were high, the passage rates for measures for school GO Bonds is higher, 86 percent, than City, 62 percent.

ATTACHMENT B

Summary of Affordable Housing Funding Options

As requested by Council, this attachment provides greater detail on different options for funding affordable housing. It includes an overview discussing affordable housing and then briefly describes various options that can be used to raise revenues for this purpose. Some of the options are already in place in Palo Alto to raise funding for this purpose, while other options may be present in Palo Alto but not specifically directed to affordable housing. Other options are not yet being used in Palo Alto for affordable housing or any other purpose.

Affordable Housing Overview

The Federal Government, through the Department of Housing and Urban Development (HUD), considers housing that requires 30% or less of a household's income as affordable to that household. Once a household pays more than 30% of its income for rent or a mortgage, the household is defined as "cost burdened." Although there is debate about the appropriateness of 30% as the measurement, the proportion of households spending more or less than 30% of their income on rent is one measure of affordability of in a city or region.[1]

The Joint Center for Housing Studies of Harvard University produces maps that show cost burden across the nation.[2] In 2017, the San Jose-Sunnyvale-Santa Clara Metropolitan Statistical Area (MSA), 36% of households were cost burdened, with 17% experiencing severe cost burden. This is similar to the 37%of households cost burdened and 18% severe cost burdened by households in the San Francisco-Oakland-Hayward MSA. Severe cost burdening occurs when a household spends more than 50% of its income on housing costs.

One way to ensure more households can afford housing is by constructing deed-restricted, income-based housing. These units are typically offered for sale and for rent to lower-income households in a region. To determine if a household is lower income, the HUD assesses the median incomes of counties nationwide. Each year, HUD publishes a table for each county identifying the median income, and the incomes of extremely low-, very low-, and low-income households. The table also varies based on household size. As of April 26, 2021, the median income in Santa Clara County for a household of 4 is $151,300.

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[1] Rental Burdens: Rethinking Affordability Measures
https://www.huduser.gov/portal/pdredge/pdr_edge_featd_article_092214.html
[2] Cost Burden Maps by the Joint Center for Housing Studies of Harvard University:
https://www.jchs.harvard.edu/son2019-cost-burdens-map

Table C-1: Income by Household Size

Santa Clara County Income Table Issued by HUD April 26, 2021[3]								
	Household Size							
Income	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**
Extremely Low	$34,800	$39,800	$44,750	$49,700	$53,700	$57,700	$61,650	$65,650
Very Low	58,000	66,300	74,600	82,850	89,500	96,150	102,750	109,400
Low	82,450	94,200	106,000	117,650	127,200	136,600	146,050	155,450
Median	105,900	121,050	136,150	**151,300**	163,400	175,500	187,600	199,700
Moderate	127,100	145,250	163,400	181,550	196,050	210,600	225,100	239,650

Funding Affordable Housing
Since the rents that low-income households can afford to pay are less than the market rent, the private market does not build new housing units for these households. Instead, states, counties, and cities deploy several tools to aid in the construction of deed-restricted, income-based affordable housing. Overall, the tools represent strategies to find funding to either (1) construct the affordable housing or to (2) decrease the cost to construct and operate the housing. Below are some potential funding tools to offset the costs of affordable housing. Those marked with an * are already in place in Palo Alto but may not be specifically dedicated to affordable housing.

- General Taxes*
- Inclusionary Housing Requirements and/or Fees*
- Commercial Linkage Fee*
- Documentary Transfer Tax*
- Jobs-Housing Linkage Policy
- Enhanced Infrastructure Financing District
- Bond Measures
- Project Specific Funding
- California Community Housing Agency
- Use of Public Land and/or Land Lease

General Taxes - Tax revenues can be dedicated to affordable housing through a jurisdiction’s budget process, or a jurisdiction can choose to raise a tax and specifically dedicate it to affordable housing. The City of Palo Alto could choose to dedicate existing tax revenues to the construction of affordable housing, could ask voters to dedicate a new tax to affordable housing, or could ask voters to approve a new tax that will be dedicated to affordable housing via the legislative process (budget). Although the City currently collects taxes, none are explicitly allocated towards affordable housing. Either a general tax, requiring a simple majority for passage, or a specific tax, requiring a 2/3 supermajority to pass, could be used for affordable housing.

Below Market Rate Housing Requirements and/or Fees - The City of Palo Alto has two affordable housing programs: 1) Below Market Rate (BMR) and 2) Affordable Housing Fund. The BMR program requires housing developers to include below market rate housing units in new housing developments. The City requires that ownership projects include 15% of the units as affordable to moderate income households. Rental projects are required to pay a fee instead of including the units in the development; the fee goes into the Affordable Housing Fund to contribute to 100% affordable housing projects.

The City has explored the feasibility of increasing the inclusionary percentage above 15%. A study completed in 2020 indicated that increasing the rate must be accompanied by adjusting some development standards, otherwise a higher inclusionary rate is not feasible. The state requires that inclusionary rates above 15% must be financially feasible. Staff could return with draft legislation to adjust development standards so that more inclusionary housing is financially feasible. The changes to standards may also allow the City to require on-site BMR units for rental housing projects.

In addition, a series of recent state laws, including the state density bonus, allow developers to become eligible for certain concessions and/or permit streamlining when a certain percentage of units are affordable.

Documentary Transfer Tax - One type of tax the Council may consider for supporting affordable housing is a documentary transfer tax. A documentary transfer tax (transfer tax) is a tax imposed by the County and/or City for the transfer of property. The City could increase this tax and dedicate the revenues to affordable housing.

For example, the City and County of San Francisco passed Proposition I in 2020 by a margin of 57.55% to 42.45%. This tax raised the property transfer tax rate on commercial and residential properties valued between $10 million and $24.99 million from 2.75% to 5.5%, and on properties valued at $25 million or more from 3% to 6%. This was passed as a general tax, though by resolution the revenues were dedicated to housing related funds. The table below presents documentary transfer taxes throughout Santa Clara County to provide context on neighboring jurisdictions.

Table C-2: Documentary Transfer Tax Rates in Santa Clara County

City	General Law/Chartered	Per $1,000 Property Value (City Rate)	Rev & Tax Code Sec 11911 – 11929 County Rate	Per $1,000 Property Value (Total)
Campbell	General	$0.55	$0.55	$1.10
Cupertino	General	$0.55	$0.55	$1.10
Gilroy	Chartered	$0.55	$0.55	$1.10
Los Altos	General	$0.55	$0.55	$1.10
Los Altos Hills	General	$0.55	$0.55	$1.10
Los Gatos	General	$0.55	$0.55	$1.10
Milpitas	General	$0.55	$0.55	$1.10
Monte Sereno	General	$0.55	$0.55	$1.10
Morgan Hill	General	$0.55	$0.55	$1.10
Mountain View	Chartered	$3.30	$1.10	$4.40
Palo Alto	Chartered	$3.30	$1.10	$4.40
San Jose	Chartered	$2 M AV Exempt	$1.10	$1.10
		1.25% $1M - $3M	$1.10	$13.60
		2.5% $3M - $10M	$1.10	$26.10
		3% > $10 M	$1.10	$31.10
Santa Clara	Chartered	$0.55	$0.55	$1.10
Saratoga	General Law	$0.55	$0.55	$1.10
Sunnyvale	Chartered	$0.55	$0.55	$1.10

Commercial Linkage Fee (CLF) – Commercial linkage fees became effective in Palo Alto in 2017. A CLF is similar to other impact fees levied on new development and helps cover the cost associated with creating new or expanded public facilities to meet the additional demand created by the development. Before levying a CLF, jurisdictions are required by state law to complete a nexus study that shows the linkage between the new development and the increased demand for the facilities. The results of the nexus study establish the maximum legal fee that may be charged.

Table C-2: CLF Affordable Housing Fee Levels in Santa Clara County (per sq. ft)

Non Residential Fees by City	**Office/R&D**	**Retail**	**Hotel**	**Industrial**
Palo Alto	$36.53	$21.26	$21.26	$21.26
Mountain View*	$28.25	$3.02	$3.02	$28.25
City of Santa Clara	$20.00	$5.00	$5.00	$10.00
Cupertino	$24.60	$12.30	$12.30	$24.60
Sunnyvale**	$17.20	$8.60	$8.60	$17.20
Milpitas	$8.00	$8.00	$8.00	$4.00
Average Fees	**$22.43**	**$9.70**	**$9.70**	**$17.55**

*Mountain View: Office/R&D<10k sq. ft. pays ½ fee. Hotel/Retail <25k sq. ft. pays ½ fee

**Sunnyvale fee for Office/Industrial is ½ fee level up to 20k sq. ft. and full fee for sq. ft. above 20k

Source: siliconvalleyathome.org

Jobs Housing Linkage Policy - A jobs-housing linkage fee is similar to the commercial linkage fee, but it identifies the nexus between commercial development and housing demand. The fee then goes to support the development of housing to meet the demand created by the commercial development. The nexus study can include examining the housing demand generated by the new workforce occupying the commercial facility, but also the demand for other jobs created by the new workers. For example, a new office building may create demand for more low-wage work in the restaurant industry; and those low-wage workers need housing as well as the office workers.

Infrastructure Financing District – The Enhanced Infrastructure Financing District (EIFD) provides broad authority for local agencies to use tax increment to finance a wide variety of projects, including affordable housing, mixed-used development, sustainable development, and transit-oriented development. According to the California League of Cities:

> The EIFD provides broad flexibility in what it can fund. No public vote is required to establish an authority, and though a 55 percent vote is required to issue bonds, other financing alternatives exist. Unlike former redevelopment, this tool imposes no geographic limitations on where it can be used, and no blight findings are required. An EIFD can be used on a single street, in a neighborhood or throughout an entire city. It can also cross jurisdictional boundaries and involve multiple cities and a county. While an individual city can form an EIFD without participation from other local governments, the flexibility of this tool and the enhanced financial capacity created by partnerships will likely generate creative discussions between local agencies on how the tool can be used to fund common priorities.[3]

[3] Source: https://www.cacities.org/Policy-Advocacy/Hot-Issues/New-Tax-Increment-Tools

This tool does not necessarily collect taxes from a new source but uses the incremental tax increases in a given geography to finance infrastructure investments. Generally, tax increment financing assumes the infrastructure or investment will yield higher tax revenues in the future, allowing the district to afford the investment.

Bond Measures - Bond measures can also be used by different levels of government to fund affordable housing.

For example, the State of California put Proposition 1 on the ballot in 2018. The proposition passed and gave the state permission to borrow $4 billion to fund affordable housing construction as well as rental and home loan subsidies. These were structured as General Obligation (GO) bonds. GO bonds are described in greater detail in **Attachment A**. The money from Proposition 1 can be used to build and renovate rentals ($1.8 billion), to offer home loan assistance to vets ($1 billion), to construct additional housing in dense urban areas and near public transit ($450 million), to offer down payment assistance and other aid to low- and moderate-income homebuyers ($450 million) and to provide loans and grants for agricultural workforce housing development ($300 million). Likewise, Santa Clara County voters passed Measure A in 2016. This bond generated revenues for affordable housing in the county.[4]

Project Specific Funding – The above represent options local governments can use to generate revenues for affordable housing development. In addition to these measures, there are project specific funding sources available for affordable housing developments. For example, the Measure A monies raised by the County are allocated to specific housing projects. Federally, the Low-Income Housing Tax Credit (LIHTC) can provide funding for specific projects. Lastly, state-funded Project Home Key provides funding to create housing for unhoused persons. This funding source is allocated to specific qualifying projects.

The key point is that additional funding sources exist for affordable housing overall. These funds come from different sources and are then allocated to specific projects, not to municipalities or other agencies.

California Community Housing Agency (*Project Specific Funding)* - The California Community Housing Agency (CalCHA)[5] is the State's first public agency focused exclusively on the production, preservation and protection of middle-income housing. The "Essential Housing" model has already created over 2,000 affordable rent-restricted rental units. Founded in 2019, CalCHA is a Joint Powers Authority (JPA) created pursuant to Chapter 5 of Division 7 of Title 1 of the Government Code of the State of California. The JPA purchases existing housing and restricts the

[4] Website regarding Measure A: https://www.sccgov.org/sites/osh/HousingandCommunityDevelopment/AffordableHousingBond/Pages/home.aspx#:~:text=%E2%80%8B%E2%80%8B%E2%80%8BIn%20November,%24950%20million%20affordable%20housing%20bond.&text=The%20bond%20proceeds%20would%20contribute,approximately%204%2C800%20affordable%20housing%20units.

[5] Website: https://www.calcha.org/

homes to income-qualified households (no more than 120% of area median income). The JPA issues revenue bonds for specific projects. Revenue bonds are project specific bonds that use the revenues of a project to service any debt obligations. Cities that join the JPA have no responsibility or obligation to the bonds. *To be active within the boundaries of a local jurisdiction, the jurisdiction must join the JPA via a resolution.*

Use of Public Land and/or Land Lease – Public agencies may also utilize land owned by the agency for housing. In the Bay Area, land acquisition can be one of the most challenging and expensive parts of building housing—both affordable and market rate. If a government already owns the land, the cost of the housing can decrease significantly. Local governments often issue RFPs to work with private developers to build the housing. The development may be 100% affordable, though subsidies are required from other sources to build the housing. The development may also be a mixed income project that includes both market rate and affordable housing. Often times, with mixed income projects, the low or no-cost land is leveraged for very high amount of below market rate housing (up to 50% or more in some cases). Typically, the government agency enters into a long-term land lease (50 years, 99 years, etc.) with the developer so that the land is still retained as publicly owned. These projects are typically rental housing, and not for sale. Some work has been done to advance community land trust models that do allow ownership of the unit by an individual or family, but retain ownership of the land by a non-profit or government.

ATTACHMENT C

Overview of Prior Work Efforts related to a Business Tax

The City of Palo Alto does not currently have a Business Tax. In 2014, the City approved a Business Registration Certificate (BRC) Program, which has a $54 annual registry fee per business. Due to the impact of COVID-19 on businesses, this fee was waived for FY 2021 and FY 2022. This fee is in addition to any special assessments, such as the Downtown Business Improvement District (BID) or Downtown Parking Assessment District. The BID fees were also waived for FY 2021 and FY 2022 in light of COVID-19.

The discussion of a business tax is not new to Palo Alto. On June 22, 2009, the Palo Alto City Council voted 6-2 to put Measure A, a general tax measure on the November ballot, where it failed to meet the simple majority required for passage. 57.28% of voters voted against the measure and only 42.75% voted in favor. That measure was expected to raise $3 million a year in general fund revenues through a $75 fee on all businesses and an additional cost of $35 to $75 per employee depending on the size of the firm.

In 2016, the Council renewed talks of a business tax, but the effort was dissolved when the Finance Committee opted instead to pursue a hotel tax increase via Measure E. In 2019, by a vote of 6-1, the Council began a new effort to place a business tax on the November 2020 ballot to help support their Fiscal Sustainability priority. Significant work by staff, augmented by consultant resources, was put into the pursuit of developing a potential business tax ballot measure. This included exploration of different options ranging from headcount to square footage to gross receipts. This attachment provides an overview of the prior work efforts including the three paths that were used to organize the work so that could it proceed concurrently.

The three paths were analysis and modeling, stakeholder outreach, and polling. These three paths would likely be used to organize work on an ongoing basis in order to facilitate the necessary conversations in a prompt and timely manner.

- The analysis path consists of creating models to estimate potential revenues, refining those revenue estimates, and incorporating iterative direction on elements of the model such as tiering of rates, exemptions, or other nuances that can be altered. During the 2019 and 2020 work on a potential business tax, the City used Matrix Associates as the consultant to augment the work on analysis.

- The stakeholder outreach path consists of targeted and tailored communication to the community around the potential local ballot measure. This includes both the potential rate-payers that would be impacted by a new local ballot measure and other members of the community. During the 2019 and 2020 work on the development of a potential business tax, the City used TBWB as the consultant to facilitate stakeholder engagement.

- The polling path consists of polling voters on the specific language and elements of a potential ballot measure to inform the wording of the ballot measure and incorporate potential changes to aid the measure's passage. During the 2019 and 2020 work on the development of a potential business tax, the City used FM3 associates as the consultant to engage on polling.

Although the Finance Committee and City Council had given direction to staff to pursue a business tax based on employee headcount, that may no longer be the most viable nor administratively feasible option as a result of changes to the work environment from COVID-19. The remainder of this attachment retransmits information previously sent to the Finance Committee and City Council through CMR 10392 and CMR 10445 to restate the context for a potential business tax and present additional options for re-consideration. Subsequent City Manager Reports that more fully explore a potential employee head-count business tax are listed and available in **Attachment D.**

Limits and Constraints on Business Taxes

The City can consider any tax that is not arbitrary in its application or otherwise prohibited by state law or the constitution. Jurisdictions may only tax conduct with a constitutionally-sufficient nexus to the jurisdiction. For businesses that conduct business in multiple jurisdictions, the city's business license tax can only be applied to the portion of business transacted in the city. Business tax measures follow the same voter thresholds for a general tax or special tax and could be proposed as either.

Some businesses and occupations are exempt from local business taxation under state or federal law; these include non-profit or charitable organizations (e.g., non-profit hospitals), banks and other financial institutions that pay the state in-lieu tax, small residential care facilities, and small home childcare facilities. This list is not exhaustive or exclusive. The City can include other exemptions (e.g., small business, limited duration activity) in addition to the exemptions required under state or federal law in a proposed tax measure.

Analysis of Neighboring Jurisdictions' Business Taxes

Staff reviewed election results for cities in the Bay Area (Santa Clara County, San Mateo County, City and County of San Francisco, Alameda County, Contra Costa County, and Marin County) for business license tax measures in the past five years, that did not specifically target a type of business (such as landlords, parking lots, warehouses, sugary drinks, gaming, cardrooms, gambling, soil recycling and recycling). Over the past five years, general use business tax measures, which require a simple majority vote, have passed at the polls.

Over the past 10 years, there were a handful of examples of business tax measures in the Bay Area that did not pass. An example of a failed business tax measure was in November 2014 for the City of Milpitas (Measure E) that targeted licensed gaming establishments. Measure E would have allowed the City to tax licensed gaming establishments 10.5 percent on gaming revenues.

According to Ballotpedia.org, the following business tax measures in the Bay Area, that did not target a specific business type and failed on the ballot were in November 2009 for the City of Redwood City (Measure Y, business tax increase) and City of Palo Alto (Measure A, to establish a business tax). City of East Palo Also voters passed Measure O (a general tax) in November 2016 by simple majority which, in addition to the City's business license tax assessed on the business community at-large, added a landlord business license tax to the City's overall business tax structure.

As part of the effort in 2019, the City engaged Matrix Consulting Group (Matrix) to conduct research that will assist in development of a potential business license tax. The scope of the engagement included

- comparative research of selected Bay Area communities to understand each agency's business license tax practices regarding the development, implementation, and administration of each program; and
- to perform data analysis and modeling, based on available data resources, of the potential revenue range the City may generate if a business license tax measure were to be approved by the voters.

Comparative agencies were selected based on a few general criteria: proximity to Palo Alto, business community and population size, business industry environment, and Bay Area agencies that have brought business license tax measures to the ballot in the last few years. 2017 data from the U.S. Census was used to compare Palo Alto's industry environment to selected comparable agencies. The Business License Tax Program Comparative Assessment and Revenue Projections report completed by Matrix, which can be found as Attachment C to CMR 10445, indicated that according to U.S. Census Data for 2017, Palo Alto's business environment was comparable to the selected agencies, where professional and healthcare services are the top industry types. The U.S. Census data, however, includes business conducted in Stanford, which is primarily business in the education and healthcare segments and depending on location, these businesses would not be subject to a Palo Alto Business License Tax.

Table B-1: Employment by Industry as of 2017

INDUSTRY	***Cupertino***	***East Palo Alto***	***Mountain View***	***Redwood City***	***San Francisco***	***San Jose***	***San Mateo***	***Santa Clara***	***Sunnyvale***	***Palo Alto***
PROFESSIONAL	29%	6%	23%	14%	22%	13%	15%	21%	27%	**25%**
INFORMATION	7%	3%	13%	5%	6%	4%	5%		8%	**8%**
MANUFACTURING	22%	7%	13%	8%	4%	16%	9%	19%	20%	**13%**
EDUCATION	7%	8%	9%	9%	7%	8%	8%	8%		**14%**
HEALTHCARE	9%	12%	9%	11%	11%	12%	11%	9%	15%	**11%**
RETAIL	7%	12%	7%	10%	9%	9%	9%	8%		**5%**
HOSPITALITY	3%	14%	6%	7%	9%	8%	9%	6%	6%	**5%**
ADMINISTRATIVE		11%	3%	6%	4%	5%	6%			**2%**
CONSTRUCTION	2%	8%	3%	7%	3%	6%	5%	3%		**1%**

Professional, scientific and technical services is the largest industry segment in the City of Palo Alto. To further validate the U.S. Census data and to review average number of firms, employees and employee wages, the City obtained data from the California Employment Development Department (EDD) which excludes businesses located at Stanford. Please see the "Employment and Wages by Northern American Industry Classification System (NAICS) Code from EDD Data" table on p. 39 in the Consultant Study – page 70 of CMR 10445 - for detail of the City's 2018 number of firms, employment, total annual wages, and average employee wage, organized by Industry NAICS code. Please note that data for some industry types are suppressed from the report due to EDD's confidentiality and disclosure restrictions. Although grand totals for number of firms, employment, and annual wage is included in the report, information for an industry is redacted if the industry category 1) has less than five reported business in that industry and 2) one business comprises 80 percent or more of the total for the industry.

According to the EDD data, in 2018 the City of Palo Alto had:

> Approximately 942 professional, scientific, and technical firms (NAICS code 54), or 22 percent of total reported businesses, within the City that are dedicated to this industry type. Healthcare and social assistance and other services (excluding public administration), are the second and third largest industries totaling 854 firms (20 percent) and 495 firms (12 percent), respectively.
>
> The average employee wage data (which includes regular salary, bonuses, and sometimes stock option income) is also telling of the type of employment market within the City. The highest paid industries in the City are finance and insurance, averaging approximately $307 thousand per employee; information, averaging $296 thousand per employee; and management of companies and enterprises, averaging $242 thousand per employee.

In 2018, there was an average of 103,921 employees within City limits (excluding Stanford). Of those employees, 97,350 were non-government employees. This data is presented in the Consultant Report and the verified data from InfoGroup was used to calculate the employee head count revenue estimate.

Agency demographic information that was examined in the Consultant Study included

- population
- number of businesses;
- total revenue generated and percent total of General Fund revenues;
- business tax revenue generated compared to total agency full-time equivalent (FTE) as a benchmark unit of measure;
- whether the tax is general or specific;
- business tax structure;
- exemptions in addition to those specified in State or Federal law;
- sunset of the tax;
- annual escalator; and
- whether the tax is administered in-house or by an outside firm.

Of the agencies selected for comparison, all agencies approved ongoing taxes without sunset provisions and chose to administer the tax in-house. Each agency had varying types of tax exemptions and methods of an annual escalator for the tax. The tables below summarize the demographic and business license tax information for each selected agency and how each compare to Palo Alto as well as business tax exemptions by agency. Five of the nine selected agencies use employee head count as the tax method; all but East Palo Alto have a general tax.

ATTACHMENT C

Table B-2. City Demographic and Business Tax – General and Financial Information (As of August 2019)

CITY	POPULATION	# OF BUSINESSES	THREE LARGEST INDUSTRIES	TAX METHOD	GENERAL OR SPECIAL TAX	REVENUE / % GENERAL FUND	REVENUE PER FTE
CUPERTINO	60,777	3,800	Professional Manufacturing Healthcare	Square Foot	General	$0.8M, 1%	$4,344
EAST PALO ALTO	29,765	1,527	Hospitality Healthcare Retail	Gross Receipts	Specific	$1.2M, 4%	$10,239
MOUNTAIN VIEW	81,438	3,700	Professional Information Manufacturing	Employee Count	General	$6.0M, 4%	$9,438
REDWOOD CITY	86,685	6,275	Professional Healthcare Retail	Employee Count	General	$2.6M, 2%	$4,757
SAN FRANCISCO	884,363	242,000	Professional Healthcare Hospitality	Gross Receipts; Payroll	General	$820.0M, 9%	$26,469
SAN JOSE	1,035,000	58,000	Manufacturing Professional Healthcare	Employee Count	General	$72.2M, 6%	$11,259
SAN MATEO	104,748	7,486	Professional Healthcare Retail	Gross Receipts	General	$5.9M, 5%	$8,659
SANTA CLARA	127,134	13,000	Professional Manufacturing Healthcare	Employee Count	General	$0.9M, 0.5%	$823
SUNNYVALE	152,389	7,875	Professional Manufacturing Healthcare	Employee Count	General	$1.8M, 1%	$2,027
PALO ALTO	**66,649**	**5,496**	**Professional Healthcare Manufacturing**	**N/A**	**N/A**	**N/A**	**N/A**

Table B-3: Business Tax Exemptions by Agency

	STATE EXEMPTIONS		LOCAL EXEMPTIONS			
CITY	Non-Profit	Charitable Organizations	Public Utility	Small Business	Disabled Veteran	Low Income Rental Units
CUPERTINO	✓	✓				
EAST PALO ALTO	✓	✓				
MOUNTAIN VIEW	✓	✓	✓			
REDWOOD CITY	✓	✓	✓		✓	
SAN FRANCISCO	✓	✓		✓		
SAN JOSE	✓	✓		✓		✓
SAN MATEO	✓	✓			✓	
SANTA CLARA	✓	✓				
SUNNYVALE*	✓	✓	✓		✓	

*** BANKS AND OTHER FINANCIAL INSTITUTIONS THAT PAY THE STATE IN-LIEU TAX ARE EXEMPT FROM A LOCAL BUSINESS TAX. THE CITY OF SUNNYVALE EXEMPTS ALL BANKS AND FINANCIAL INSTITUTIONS FROM THE LOCAL BUSINESS LICENSE TAX.**

On June 18, 2019, staff received direction from the Finance Committee to model three types of business tax models: employee head count, square footage, and payroll. In addition to these structures, staff was directed to examine potential exemptions, in addition to those legally exempted, to provide the Committee with information to make informed policy decisions for the tax. The below discussion summarizes the results of the business license tax modeling from 2019 as presented in the Consultant Study, which is Attachment C of CMR 10445.

*Table B-4: Estimated Business Tax Annual Revenue**

HEAD COUNT	$3.6M using City of Mountain View's rates
SQUARE FOOTAGE	$1.0M to $3.2M using City of Cupertino's rates
PAYROLL	$15.5M to $16.5M assuming 0.1% of total payroll expense

***REVENUE ESTIMATES INCLUDE EXEMPTED BUSINESS CATEGORIES PER STATE AND FEDERAL LAW, SUCH AS NON-PROFIT AND CHARITABLE ORGANIZATIONS.**

Business Tax: Employee Head Count

Fundamentally, the employee head count business tax model applies a tax rate based on the number of people a business employs within the City's boundaries. The tax rates are commonly separated into ranges and the tax is applied based on how many people are employed by the business. In our survey of comparative agencies, employee head count is the most common business tax structure and, perhaps the simplest form business tax model.

For purposes of a headcount business tax structure, establishing a definition for an "employee" will be the foundation of this tax and can be defined as any person who works for, under the direction of, on behalf of, or as an agent of a business owner. Amidst the growing trend of non-traditional employment structures (i.e. outside consultants, employees working from sites outside of City boundaries) in information and professional services industries, establishing the definition and criteria of an employee and setting a tax around such definition will be critical.

Staff recognizes that there a wide range of datasets which identify number of employees citywide, with varying conclusions of the total number of employees in the City of Palo Alto. Several reasons may be the cause of this – inclusion of businesses located in Stanford proper, various definitions of an employee, confidentiality parameters, or how the data is collected (self-reported, mandated, audited, etc.) – just to identify a few. Site-based employment headcount and wage data, in total, is available from the EDD. Staff has previously presented employee head count totals from the American Community Survey, which totaled 97,000. InfoGroup is another data set that was utilized in the City Auditor's Office most recent audit of the Business Registry Certificate Program. The revenue estimates presented in the Consultant Report are modeled using the verified database from InfoGroup. The verified data from InfoGroup provided the most detailed information by firm at the time of the analysis.

EQUITY	*Palo Alto's top three industry types for average employee head count are healthcare/social assistance, professional, and information.* This tax model would directly relate revenue to the daily phenomena of the influx of daytime population within the City's boundaries and tax this activity as such. Equity concerns within the same type of industry are to be determined, however, businesses that are labor driven and have lower average wages will be bear a higher tax based on employee head count and such as tax will not correlate to the business' ability to pay. Examples of these industries are manufacturing, retail, social assistance, and food service/hospitality.
ADMINISTRATION	Establishing criteria that sets the definition of an employee should be included so that businesses are able to accurately report data and remit tax. Self-reported employee head count by the business owner would be the simplest method of administering this tax, however there is a higher risk that data is reported incorrectly. An alternative is to use data from the EDD and assess the tax based on this data. Data on firm size is currently being generated by the EDD. The recently passed business tax measure in Mountain View, Measure P, calculates the tax based on the employee count form the last four quarters submitted to the EDD. Structure for this tax model should define whether headcount related to from alternative employment models should be included or not be included in the assessment.

STABILITY	Tax revenue driver is directly related to how many businesses are in the City and the number of employees at each business. Depending on the policy is developed and how the tax definitions are written, the basis will be impacted as companies transition to alternative employment models (i.e. outside consultants, employees working from offsite locations outside of City boundaries), which is becoming a trend in consulting and high-tech companies.
ECONOMIC BENEFITS	Administration of the tax is simple if based on number of employees at a site address, which is already reported by businesses to the EDD on a quarterly basis; results in minimal operational disruption to the tax payor. Implications of economic development goals would be dependent on the specific structure, potential exemptions, and business classifications

Of the nine selected comparison agencies, five of the cities used employee head count as the tax method. Although total employee count for each selected agency could not be readily obtained as of the drafting of the report, a summary table of those agencies is below, similar to the table presented earlier in this report, that includes the number of businesses, tax method, exemptions, total generated revenue, and revenue per FTE:

Table B-5: Employee Headcount Agencies

CITY	# OF BUSINESSES	TAX METHOD	EXEMPTIONS	REVENUE	REVENUE PER FTE
MOUNTAIN VIEW	3,700	Base tax plus tiered incremental rate (scaled increase)	Public Utility	$6.0M	$9,438
REDWOOD CITY	6,275	Base tax plus flat tax based on employee or business type	Public Utility Veteran	$2.6M	$4,757
SAN JOSE	58,000	Tiered incremental rate (scaled decrease)	Small Business Low-Income Rental Units	$72.2M	$11,259
SANTA CLARA	13,000	Tiered flat rate (scaled increase) or flat; has cap		$0.9M	$823
SUNNYVALE	7,875	Tiered incremental rate (scaled increase)	Public Utility Veteran	$1.8M	$2,027

Generated tax revenue compared to City FTE was used as a benchmark to compare each agency’s business license tax. The cities of Redwood City and Santa Clara both use employee count as the tax method. Redwood City generates $2.6 million annually and has approximately half the number of business firms compared to City of Santa Clara. However, Redwood City generates three times the amount of business license tax revenue compared to Santa Clara. The driver of this difference is that Redwood City’s employee count model incrementally increases based on number of employees, where Santa Clara’s model is a flat tax.

The City of Sunnyvale also uses the employee head count model and, in addition to businesses that often times are exempt or receive preference from a grant perspective (such as non-profits, residential care facilities, or Veteran-operated businesses), Sunnyvale exempts banks and financial institutions and insurance brokers-agents. Like Redwood City, but unlike Santa Clara, Sunnyvale uses an incremental employee count model as opposed Santa Clara's flat tax model. This results in approximately $1.8 million in annual revenue and $2,027 in tax revenue per FTE.

City of San Jose is the largest agency, for both population and number of businesses, that uses the employee head count model. It is also the only agency that was reviewed that encourages large business by using a tiered model where the tax rate is incrementally scaled down as the business has more employees and has a total maximum cap that can be collected per year.

Business Tax: Square Footage

The square footage business tax model commonly calculates the tax based on a tiered square footage range. There are several options of how a square footage tax can be structured by either applying a single square footage rate, depending on which tier the business falls under; a flat tax based on tier; or a combination of a flat tax and square footage rate. The rates can be structured to either benefit or penalize certain commercial space sized businesses.

Real estate market analytic tools are available for purchase and provide dependable, real-time, census information that can be used as a tool for administration, regulation, and revenue forecasting purposes. The Consultant Study used verified InfoGroup data to perform tax revenue modeling and also reviewed data from CoStar, a real estate market analytical tool which categorizes commercial property into several categories (distribution/manufacturing, healthcare, hospitality, industrial, office by class, retail, specialty, and sports/entertainment) and into various subcategories. Data from CoStar (available LINK) also discloses whether the commercial space is owner occupied, leased, or sub-leased. These lease arrangements should be considered when structuring, administering, and regulating this tax model. Matrix found that the data from InfoGroup appeared to have the largest population of reported businesses within its "verified" roster.

EQUITY	If industries within the City require an average square footage that is similar to the business' competitors, the tax burden would fall equally among businesses in the same industry. This tax model would place heavier tax burden on industries that require larger square footage to operate, such as manufacturing.
ADMINISTRATION	The source of compliance data would be an actively maintained and updated third-party real estate database. Whether the commercial space is owner occupied, leased, or sub-leased, how regulation is administered, and allocation of the tax is administered by the property owner or the City should be addressed and clarified in the tax language. Examples of complex areas in this tax structure are common areas, shopping centers, franchises and how a business may define their company's site(s).
STABILITY	Tax is assessed on commercial square footage and, although some exemptions can be made to encourage certain industries to expand in the City, overall revenue growth using this model will be limited based on policy decisions related to commercial space in the City.
ECONOMIC BENEFITS	This tax model would appear to inhibit square footage growth, however depending on how the tax is structured, this model has the potential to encourage growth for targeted industries and/or business sizes and/or property types.

Of the nine selected agencies in the Consultant Study, the City of Cupertino was the only agency that used the square footage tax method for a business tax. It should be noted as discussed earlier in this report that the City of East Palo Alto recently approved a parcel tax based on a commercial square foot metric.

Table B-6: Square Footage Agency

CITY	# OF BUSINESSES	TAX METHOD	EXEMPTIONS	REVENUE	REVENUE PER FTE
CUPERTINO	3,800	Flat base rate plus tiered incremental rate (scaled decrease)	Non-Profits	\$0.8M	\$4,344

Cupertino considered a November 2018 ballot measure to restructure the City's business license tax, which was enacted in 1992, however it was decided to defer the proposed tax restricting plan to the November 2020 election. The proposed structure would shift Cupertino's business license tax from square footage to employee head count, which is consistent with most agencies selected in the Consultant Study. According to the City of Cupertino's website, restructuring the business license tax would generate approximately $10 million annually and would fund the City's transportation infrastructure and traffic congestion programs.

Business Tax: Payroll Expense

Using payroll data as the basis for a business tax is similar to the methodology of an employee headcount structure. Relevant data can be accessed through the EDD and the sensitivity of the tax resets on the composition of employees in the data but instead of the focus being the volume of employees, the focus is on how much employees earn. Based on data from the EDD, approximately half of the City's job market is in high wage sectors including information and professional services. Based on the City's business environment and economy, a tax structure based on payroll earnings would result in a progressive tax that relates the amount of tax paid by the business to the ability to pay the tax.

In considering the payroll tax model, the definition of wages should be detailed enough to determine the type of pay that should be included in the calculation of the tax. The policy choice of including earnings aside from regular wages such as overtime, commission, allowances, bonuses, stock options, and/or cash fringe benefits, should be considered when structuring the payroll tax model.

EQUITY	Wage data will include bonuses and sometimes stock options, which can drastically vary across industries and within sub-categories of an industry. Based on the industry data from EDD, the higher wages are in professional services industries which indicates the average employee wage is higher than manufacturing, retail, social assistance, and food service/hospitality industries.
ADMINISTRATION	Similar to a business tax based on employee headcount, the simplest form of administration would be self-reported by the business owner, however there is a risk that data is reported incorrectly. Data from the EDD can validate and support regulation of this tax structure. Similar to the employee headcount tax model, the payroll tax model will be impacted as companies transition to alternative employment models. Structure for this tax model should define how wages for such employees are included in the tax.
STABILITY	Tax revenue driver is directly related to how many businesses are in the City and the average employee wage. According to data from the EDD, high wage sectors in the City are information, financial activities, and professional services which is comprises half of the City's employment base.
ECONOMIC BENEFITS	Administration of the tax is simple if based on wages of employees at a site address, which is already reported by businesses to the EDD on a quarterly basis; results in minimal operational disruption to the tax payor. Depending on structure, this model has the potential to encourage growth for targeted industries and/or business sizes and/or employee types.

The City and County of San Francisco was the only city of the nine selected in the Consultant Study that uses the payroll expense tax method to assess the City's business license tax. Prior to the November 2012 election, San Francisco used the payroll expense tax as the City's tax method and was the only city in California to use the payroll expense tax method. The gross receipts method was approved by voters in November 2012, with implementation beginning 2014 over a five-year period. The Consultant Study details the structure for both the gross receipts method and payroll expense method. The table below illustrates San Francisco's payroll expense tax method.

Table B-7: Payroll Expense Agency

CITY	# OF BUSINESSES	TAX METHOD	EXEMPTIONS	REVENUE	REVENUE PER FTE
SAN FRANCISCO	884,363	Payroll phase-out over 5 years: 1.35% to 0% by end of 2019	Small Businesses	$820.0M	$26,469

ATTACHMENT D

Summary of Prior Work on Potential Revenue Generating Ballot Measures

As discussed in the body of City Manager's Report (CMR) 12299, the City of Palo Alto has been discussing its options for potential revenue-generating ballot measures through 2019 and 2020. This work was suspended at City Council direction in March 2020 in order to marshal available resources to manage through the COVID-19 pandemic. A brief timeline of the CMRs and discussions with the Finance Committee and the City Council since April of 2019, when staff was formally directed to begin working on this project by the City Council, is included below for additional context. The date, the forum of the meeting (Finance Committee or City Council), the summary title, and the CMR number are included for ease of reference.

Timeline:
4/22/2019 City Council, "2019 Fiscal Sustainability Workplan", CMR 10267

4/22/2019 City Council, "Approve Workplan for a Potential Revenue Generated Ballot Measure", CMR 10261

6/18/2019 Finance Committee, "Review, Comment, and Accept Preliminary Revenue Estimates for Consideration of a Ballot Measure", CMR 10392

8/20/2019 Finance Committee, "Evaluation and Discussion of Potential Revenue Generating Ballot Measures", CMR 10445

9/16/2019 City Council, "Evaluation and Discussion of Potential Revenue Generating Ballot Measures and Budget Amendment", CMR 10615

10/1/2019 Finance Committee, "Revised Workplan for Consideration of a Ballot Measure", CMR 10712

10/15/2019 Finance Committee, "Stakeholder Outreach, Initial Polling, and Discussion of a Potential Ballot Measure", CMR 10743

11/4/2019 City Council, "Potential Ballot Measure Polling/Outreach, Contract, Solicitation Exemption and Budget Amendment", CMR 10792

12/2/2019 City Council, "Structure and Scenarios of Initial Round of Polling for a Potential Local Tax Measure", CMR 10891

12/17/2019 Finance Committee, "Consideration, Evaluation, and Discussion of a Revenue Generating Local Tax Ballot Measure, Review of Refined Modeling, Analysis, Tax Structure and Recommendation to the City Council", CMR 10655

1/27/2020 City Council, "Update, Consideration, and Potential Direction on Possible Local Tax Measure for 2020 Election", CMR 11019

ATTACHMENT D

3/23/20 City Council, "Consideration of Analysis, Public Outreach, and Refined Polling and Further Direction on a Potential Local Business Tax Ballot Measure for 2020 Election", CMR 11161

3/23/20 City Council, "Consideration of Analysis, Public Outreach, and Refined Polling and Further Direction on a Potential Local Business Tax Ballot Measure for 2020 Election", *At-Places Memorandum*