



Council Agenda Report

To: Mayor Grisanti and the Honorable Members of the City Council

Prepared by: Elizabeth Shavelson, Deputy City Manager

Reviewed by: Joseph Toney, Assistant City Manager

Approved by: Steve McClary, Interim City Manager

Date prepared: June 20, 2022

Meeting date: July 11, 2022

Subject: Potential Transaction and Use Tax Measure

RECOMMENDED ACTION: 1) Receive report on potential Transaction and Use Tax; 2) Direct staff to bring back resolutions to submit the question to the voters, setting priorities for arguments and rebuttals; 3) Direct the City Attorney to prepare an impartial analysis; and 4) Consider directing staff to hire a consultant to educate Malibu residents regarding the potential ballot question.

FISCAL IMPACT: No additional appropriation is required to bring back resolutions and prepare an impartial analysis. There is adequate funding for the costs associated with adding a ballot measure to the November 8, 2022 General Election ballot including in the Adopted Budget for Fiscal Year 2022-2023 in Account No. 100-7007-5150 (City Clerk - Elections). An estimated additional appropriation of \$30,000, for Account No. 100-7003-5100-00, may be needed to hire a consultant and provide educational materials.

WORK PLAN: This item was included as Item No. 6.c. in the Adopted Work Plan for Fiscal Year 2022-2023.

DISCUSSION: On November 8, 2021, Council considered recommendations from the Administration and Finance Subcommittee regarding potential revenue-generating measures and directed staff to explore tax measures for District Sales Tax, Documentary Transfer Tax, and Parking Occupancy Tax related to valet parking.

On April 25, 2022, staff provided the Council with information on the three potential tax measures it had identified. Council discussed the information presented and directed staff to bring back more information regarding the following measures:

- 1) a Transient Occupancy Tax Measure
- 2) a 0.50% Transaction and Use Tax Measure
- 3) the process to become a Charter City so that the City can implement a Documentary Transfer Tax

On May 23, 2022, Council considered the additional information staff presented on the potential tax measures as requested. At the meeting, Council indicated that it was interested in learning more about a potential transaction and use tax (TUT) measure and, in particular, the Council was interested in learning more about how residents feel about a potential TUT measure.

On June 13, 2022, the Council approved Amendment No. 1 to the City's professional services agreement with FM3 Research to conduct research to assess support for a potential 0.50% TUT measure with a sample size of up to 250 Malibu voters likely to cast a ballot in November 2022. Since that time, FM3 has developed questionnaire, prepared the sample and begun to reach out to potential respondents, and conduct interviews online and via telephone. At the time of this report, FM3 is still gathering data and anticipates that it will have completed its data collection and analysis and be prepared to present its findings at the July 11 City Council Meeting.

As the final deadlines to place a question on the November 2022 ballot approach, Council is asked to consider the community survey information from FM3 to be presented at the July 11 meeting and consider whether or not to direct staff to bring back resolutions to submit the question to the voters, setting priorities for arguments and rebuttals, and direct the City Attorney to prepare an impartial analysis regarding a potential 0.50% TUT.

Background

In Fiscal Year 2020-21, in recognition of the continuing economic impacts of the COVID-19 pandemic and the Council's priority to help homeowners rebuild after the Woolsey Fire, the Council established a General Fund Designated Reserve for Fiscal Year 2021-22 Operating Expenditures in the amount of \$6.5 million. On June 28, 2021, Council adopted the Annual Budget for Fiscal Year 2021-22 which included the use of \$3.8 million from the \$6.5 million General Fund Designated Reserve for Fiscal Year 2021-22 operating expenditures. At the time of budget adoption, the projected Fiscal Year 2021-22 General Fund revenues were estimated to be less than General Fund expenditures and the Council was concerned that the projected revenue shortfall might continue into future fiscal years.

Since June 2021, many City revenue sources have recovered more quickly than anticipated, while other sources were not significantly impacted. On January 24, 2022,

the Council adopted Resolution No. 22-07 amending the Adopted Budget for Fiscal Year 2021-22. The Mid-Year Budget Amendment included an \$5.66 million increase in General Fund Revenue. As a result of this significant increase in General Fund Revenue, the draw down from the Designated Reserve initially reflected in the Adopted Budget for Fiscal Year 2021-2022 was no longer required and was eliminated. The \$6.5 million remains designated for contingencies.

On June 13, 2022, the Council adopted the budget for Fiscal Year 2022-23. While the City's budget is currently balanced and the reserves are strong, the City is anticipating having to face significant revenue impacts and potential increases in expenditures in the near-term. There will likely be revenue and expenditure impacts associated with the proposed implementation of additional short-term rental regulations, the opening/staffing of the Malibu Sheriff's Substation (yet to be discussed and determined) and economic factors that indicate a significant potential downturn in the economy. These anticipated changes to the City's revenues and expenditures could be mitigated by the revenue generating measures such as the potential 0.50% TUT that Council is considering.

Anticipated Revenue and Expenditure Impacts

Short-Term Rental Regulations

On November 23, 2020, the City Council adopted Ordinance No. 472, the Hosted Short-Term Rental (STR) Ordinance, to establish provisions to regulate short-term rental of property citywide which include, but are not limited to, requiring the presence of an onsite host during short-term rentals, primary residency requirements and multifamily restrictions. The Hosted STR Ordinance is intended to supersede the short-term rental regulations and permit program currently in place. The Hosted STR Ordinance regulations cannot go into effect until the associated amendments to the City's Local Coastal Program and Land Use Plan are certified by the California Coastal Commission (CCC). The Hosted STR Ordinance and the associated Local Coastal Program Amendment (LCPA) 19-003 are currently being reviewed by the CCC staff.

On June 13, 2022, Council discussed the Hosted STR Ordinance and the status of LCPA 19-003 and declined the CCC's invitation to further weaken the Hosted STR Ordinance. The CCC has until early November 2022 to schedule the public hearing and take action on the City's proposed ordinance but may act earlier.

In Fiscal Year 2020-21 the City received \$5.3 million (audited) in transient occupancy tax from private residential rentals, it is anticipated to receive \$5.0 million from this revenue source in Fiscal Year 2021-22 and it is projected to receive \$5.0 million from this revenue source in Fiscal Year 2022-23. The implementation of the Hosted Short-Term Rental Ordinance will have a significant impact on this revenue. Although, the full impact of this TOT revenue reduction is not known at this time, preliminary loss estimates are \$2.0 million to \$3.0 million.

Malibu Sheriff's Substation

The Santa Monica College (SMC) Malibu Satellite Campus Project is currently in construction and is anticipated to be substantially complete in Fall 2022. As part of the project, SMC is building a 5,700 square foot Sheriff's substation. The City has been in discussion with Los Angeles County and the Los Angeles County Sheriff's Department regarding the potential staffing for the proposed substation. A variety of staffing scenarios have currently been requested. According to one preliminary estimate, it could cost up to approximately \$4.0 million annually to staff the facility without jail operations. This cost would be in addition to the amount the City is currently paying for the Sheriff's services it receives out of the Lost Hills Sheriff's Station. While a portion of these proposed costs may be borne by the County, the majority may be the responsibility of the City depending on the negotiated agreement. Ongoing discussions are underway with the County and Sheriff's Department to evaluate staffing levels and costs so that more detailed information can be provided to the Council and presented to the community for input.

Gann Limit

In 1979, California voters approved Proposition 4 with the goal of keeping state and local government spending, including school spending, capped at 1978–79 levels, adjusted for changes in population and inflation. Proposition 4 created Article XIIIB of the State Constitution, a state law that requires the state and local governments to adopt an annual appropriation limit. This limit, also referred to as the "Gann Limit," establishes a limit on the proceeds of taxes that may be appropriated for spending in a given fiscal year. The limit allows the City's spending of tax proceeds to increase only by population growth and cost-of-living factors from the base year of 1978-1979. In June 1990, Proposition 111 was passed which changed the way the limit is calculated and enabled cities to increase the limit annually in two ways. First, by a percentage equal to the increase from the preceding year in county or city population (whichever is greater); and second by an amount equal to the change in per capita personal income in California or the change in the assessment roll the preceding year due to the addition of local nonresidential new construction (whichever is greater). The calculations also allow for exclusions of certain costs to the appropriations subject to the limit including but not limited to debt service, qualified capital outlay and the costs of complying with a federal mandate.

The City establishes the appropriation limit each fiscal year. On June 13, 2022, the Council adopted Resolution No. 22-23 establishing the appropriations limit of \$31,507,804 for Fiscal Year 2022-23. The appropriations included as part of Adopted Budget for Fiscal Year 2022-23 were \$3,347,683 under the limit. HdL Companies' revenue estimate of \$2.88 million from a 0.50% TUT is within this limit. If a new tax measure were approved by voters, the City will need to continue to monitor this going forward.

District Sales Tax – Transaction and Use Tax

The City has the authority to levy a district sales tax commonly referred to as a local transaction and use tax (TUT) for general purposes pursuant to Revenue and Taxation Code section 7285.9. A city may levy, increase, or extend a TUT for general purposes at a rate of 0.125% or a multiple thereof, if the ordinance proposing the tax is approved by a 2/3 vote of the entire City Council and the tax is approved by a majority vote of the City's qualified voters. The City's authority to impose a TUT is subject to the rate limitation specified in statute.

Currently, the allowable sales tax in Los Angeles County is capped at 10.25%. Given that the current sales tax for Malibu is 9.5% (California at 7.25% plus Los Angeles County at 2.25%), Malibu could implement a district tax of up to 0.75% if approved by voters.

On April 25, 2022, Council directed staff to focus on a TUT rate of 0.50%. As of April 1, 2022, 51 out of the 88 cities in Los Angeles County have a district tax in place. The City's sales tax consultant, HdL Companies, has prepared a memo highlighting the differences between local tax allocation and district tax allocation (Attachment 1).

TUT is calculated differently than general sales and use tax. While sales tax is generally allocated to the jurisdiction where the sale is negotiated or the order is taken, revenues from voter-approved TUT are allocated to the place of first use. The City of Malibu can expect to receive transactions tax revenue from normal sales tax-generating businesses like retail stores, service stations, and restaurants. Both visitors and residents alike will pay for the transactions tax on goods that are consumed or taken possession of at the place of business within the City of Malibu. In addition, any purchases shipped or delivered into a Malibu address from outside the City (e.g., business supplies, medication supplies, industrial equipment, construction equipment, furniture, appliances, etc.) will generate additional transactions tax revenue.

However, as the transactions tax relates to registered vehicles, boats and motorcycle purchases, the tax will only be paid by Malibu residents and businesses regardless of where the purchase was made. If a Malibu resident purchases a vehicle from an auto dealer outside the City of Malibu, the auto dealer will collect and remit the City's transactions tax.

In Fiscal Year 2021-22 the City anticipates \$4.5 million in revenue from Sales and Use Tax. With voter approval, the City could implement a district TUT of up to 0.75%. HdL Companies estimates that a 0.50% TUT is estimated to yield approximately \$2.88 million annually.

To better understand how this revenue would be generated and who would bear the cost, HdL Companies examined the City's market area and analyzed the extent to which the potential TUT revenues would be generated from residents versus non-residents. According to HdL Companies, 73% of the proposed TUT revenue would be generated by non-residents. This is driven by the City's restaurant and hotel sector and is a higher percentage than most municipalities. As a comparison, approximately 80% of the City's Sales and Use Tax revenue is generated by non-residents. The report is provided as Attachment 2. HdL Companies reexamined its analysis in response to questions raised during prior discussion but made no changes to the report.

Required Voter Approval for Tax Measures

A TUT tax measure requires voter approval to be enacted. The requirements for voter approval depend on the purpose of the tax funds. A general tax to go into the City's general fund and be used for general City purposes requires a simple majority of voters (50% + 1). A special tax in which funds will be dedicated for a specific purpose requires a two-thirds supermajority (66.67%) of voters to pass. Voting on a general tax measure must be held as part of a consolidated general election that includes election of members of the governing body. Malibu's next consolidated general election is scheduled for November 8, 2022. Special taxes may go on the general election ballot, a special election ballot, or an all-mail ballot.

Given the timing of the next consolidated election and the threshold for approval, it is recommended that, if the Council desires to move forward with a tax measure, the City pursue a general tax that can be used for general City purposes.

November 8, 2022 General Election Deadlines and Next Steps

On June 13, 2022, Council adopted Resolution No. 22-20 calling and giving notice of the holding of a General Municipal Election to be held on Tuesday, November 8, 2022, for the election of certain officers and adopted Resolution No. 22-21 requesting the Board of Supervisors of the County of Los Angeles to consolidate a General Municipal Election to be held on November 8, 2022, with the Statewide General Election.

In order to get a tax measure on the November 8, 2022 ballot, the City Council must adopt a resolution to submit the question to the voters. The resolution must be submitted to the County Clerk by August 12, 2022. The latest regular meeting at which the Council could adopt such a resolution is August 8, 2022. A supermajority of the Council (4/5 vote) is required to adopt a resolution placing a general tax measure on the ballot.

In addition, the Council may adopt a resolution setting the priorities for filing written arguments and directing the City Attorney to prepare an impartial analysis showing the effect of the measure on the existing law and operation of the measure is required. The

analysis shall not exceed 500 words and would be printed preceding the arguments for and against the measure. The impartial analysis must be filed by August 19, 2022 and there must be a review period.

California election law also allows for rebuttal arguments. The rebuttal process only applies if the City Council adopts rebuttal provisions no later than the day on which the election is called. On July 9, 2018, the Council adopted Resolution No. 18-46 providing for the filing of rebuttal arguments for measures submitted to the voters at municipal elections from that date forward.

If Council wishes to move forward with a potential TUT measure and directs staff to bring back these required resolutions the first regular meeting that Council could consider these items is August 8, 2022. Given the pending deadlines for the November 2022 election, August 8, 2022 would be the last opportunity for Council to adopt the resolutions necessary for the November 2022 election. If, at that time, Council would like to make changes to the resolutions it would have to forgo placing the measure on the November 2022 ballot.

In addition, if Council wishes to educate voters on the ballot initiative, then a consultant will be needed to assist with the outreach effort. The outreach will be for educational purposes only and is not allowed to include any advocacy, it will only be to supply voters with information.

ALTERNATIVES: Council could direct staff to continue to monitor the City's finances and the impact of a potential TUT measure and bring this item back for consideration as part of a future election cycle.

ATTACHMENTS:

- 1) HdL Companies memo regarding Local Tax Allocation vs. Transaction (District) Tax Allocation
- 2) HdL Companies report on Resident/Non-Resident Analysis

LOCAL TAX ALLOCATION VS. TRANSACTION (DISTRICT) TAX ALLOCATION

Under the Bradley-Burns Uniform Local Sales & Use Tax Law, most retail sales are deemed to occur at the retailer's place of business in this state, if that is where the sale is negotiated. Exceptions may include certain auctioneers, vending machine operators and construction contractors. If the retailer has more than one place of business in this state, the sale is deemed to occur at the location where the principal negotiations take place. Generally, the local one percent tax is allocated to the jurisdiction where the retailer's place of business is located and the local use tax is allocated indirectly through the countywide pools where the property is used.

For the purposes of distributing the district tax, the tax generally follows the merchandise. That is, the tax is generally distributed to the district where the goods are delivered (and presumably used). In order for the retailer to be responsible for collecting district tax, one of the following conditions must be met:

- A. The retailer has a business location in the district, and the sale and/or delivery occur at the location.

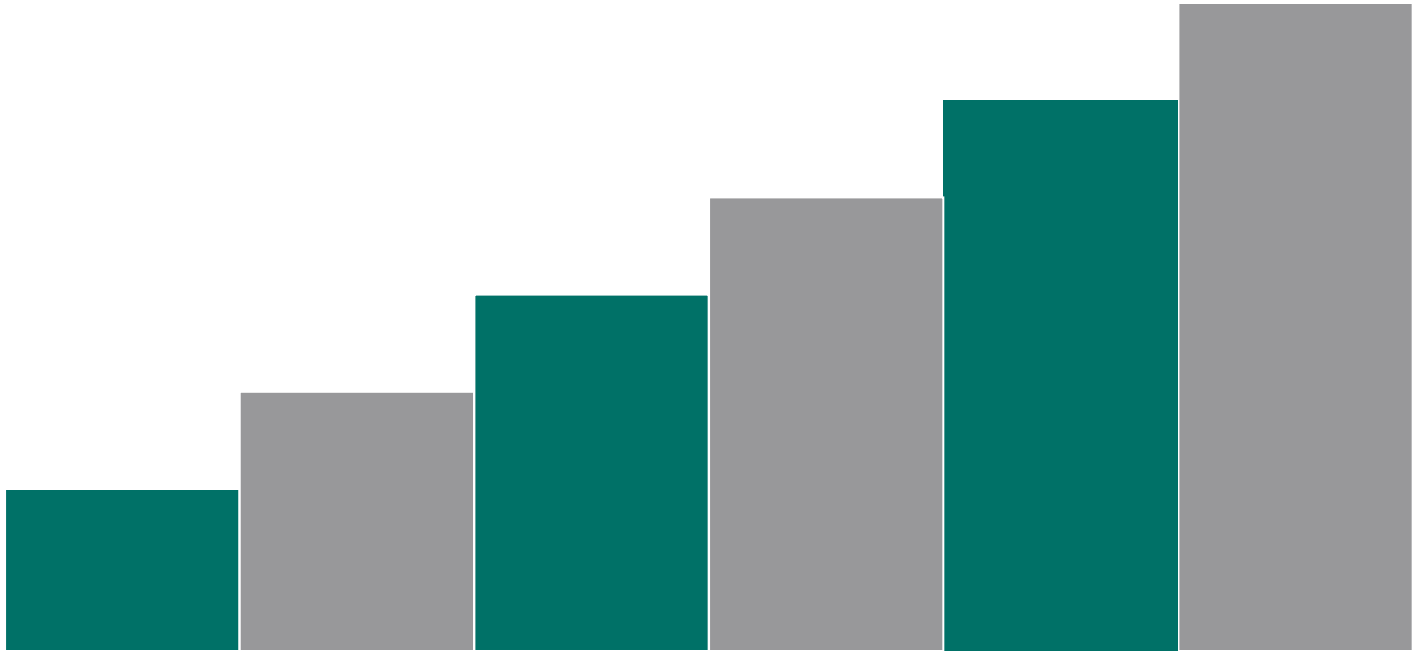
OR

- B. The retailer is engaged in business in the district as defined by one of the following:
- a. The retailer has any kind of representative operating in the district for purposes of making sales or taking orders
 - b. The retailer delivers goods to the buyer using their own vehicles or trucks
 - c. The retailer leases or sells vehicles, undocumented vessels or aircraft that will registered within the district.

Local agencies attempt to draw a correlation between local sales and use tax and transactions and use tax collected in their city/county. Since the factors determining whether a transaction is subject to local sales and use tax differ from those that indicate whether the same transaction is subject to transaction and use tax, it is not always possible to establish a direct correlation between the two.

Examples:

- ❖ City A has a .5% district tax. A retailer has a place of business within the city. Customers purchase goods on a cash and carry basis. The retailer is responsible for collecting and remitting both the local 1% tax and the .5% district tax, both are allocated to City A.
- ❖ City A has a .5% district tax. A resident in City A purchases an appliance from a retailer located in City B. The retailer has only one location in the state, and agrees to deliver the merchandise to the buyer's home. The local tax is allocated to City B. The retailer is obligated to collect and remit the district tax for City A only if he uses his own vehicle for the delivery, which creates nexus. If the goods are delivered by common carrier, which includes FedEx or UPS, the retailer is not considered to be "engaged in business" in City A and not liable for any district tax.
- ❖ City A has a .5 district tax. A retailer has a brick and mortar store in City A, but ships property to a buyer in City B, which has no district tax. The retailer collects only the state and local tax applicable to City A, but no district tax.
- ❖ City A has a .5% district tax. An out of state retailer has no place of business in this state, but does have home based sales representatives that call on customers within City A. Goods are shipped to California customer from an out of state location. The local 1% is allocated to the countywide pool based on place of use, and the retailer must collect the district tax which is allocated to City A.
- ❖ City A has a .5% district tax. City B has a 1% district tax. A retailer located in City A sells and delivers goods to a customer located in City B. The retailer uses their own truck for the delivery. The seller is required to collect the local tax on behalf of City A and the district tax for City B.



Development Driven by Data

City of Malibu Resident/Non-Resident Analysis

Overview

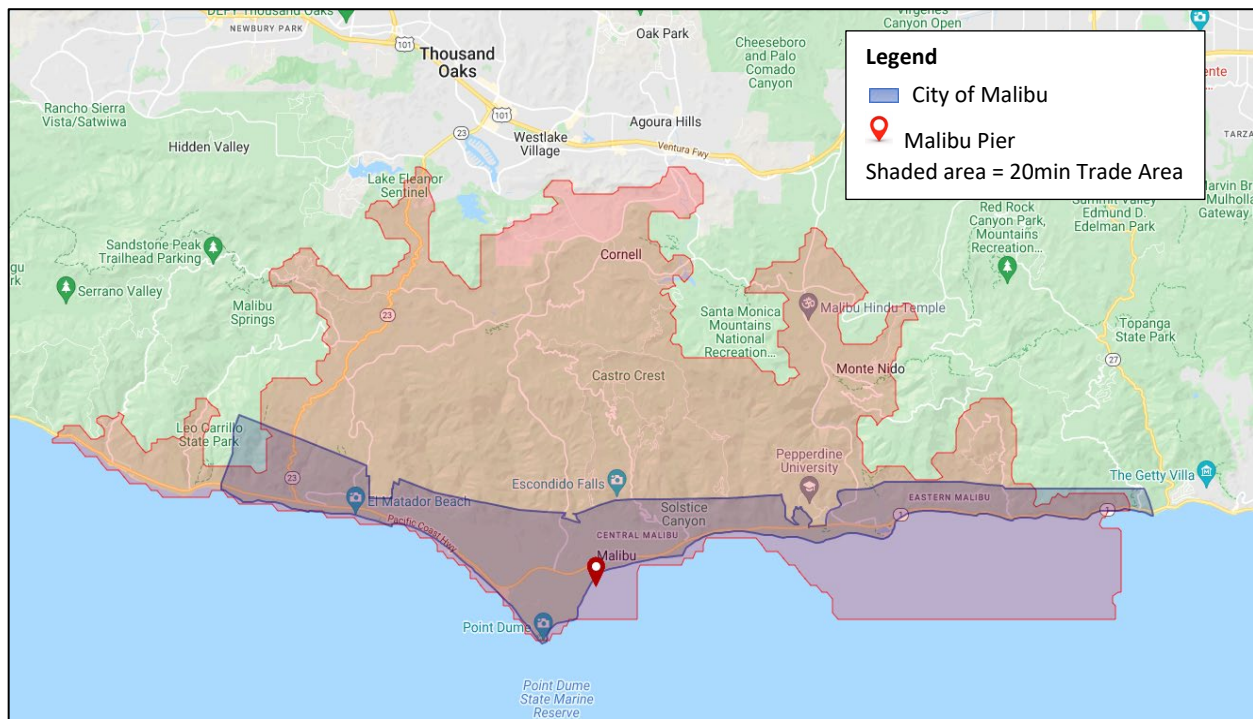
Malibu is a beach city situated along the Santa Monica Mountains in Los Angeles County, stretching 21-miles long of scenic beauty along the Pacific coast and is easily accessible, via Pacific Coast Highway 1.

The City of Malibu was incorporated in 1991 and it has an approximate population of 12,330 with an impressive daytime population increase, almost doubling the city's population to 24,368 during the daytime. Malibu is home to celebrities and multiple famous beaches including, Zuma Beach, El Matador Beach, Leo Carrillo State Beach and Malibu Lagoon State Beach, which makes it an ideal location for restaurants and hotels.

Proximity to Pepperdine University and Getty Villa Museum (all within 5-10 minute drivetime) attract college population, professional population as well as tourists from outside the city. Below is a summary of the market analytics, for City of Malibu and trade area within a 20-minute drive.

	City of Malibu	20-Minute Drive Time
Population	12,330	15,256
Households	4,859	5,271
Average HH Income	\$275,888	\$258,481
Daytime Population	24,368	25,074

The economy of Malibu employs approximately 9,451 (Source: SiteSeer Demographics) people in specialized industries such as Educational Services, Health Care & Social Assistance and Retail Trade. The largest industry category in the City of Malibu is Educational Services, providing employment to approximately 17% of the total workforce within the City of Malibu.



Non-Resident Spending Summary

The City has requested an estimate of the approximate amount of sales and use tax revenue generated by residents versus non-residents. Hereafter, individuals and businesses residing and located within the city will collectively be referred to as residents. While individuals and businesses residing and located outside of the city will collectively be referred to as non-residents.

The table below summarizes the results of the analysis based on Fiscal Year 2020-21, showing 80.1% of the 1% Bradley Burns Sales Tax is estimated to be paid by non-residents. Such a tax is generally assessed based on where the sale is negotiated or the place where the order is taken. Because Transactions and Use Taxes (TUT) are charged in accordance with where purchased goods are delivered or placed into use, HdL's estimate for the percentage of a TUT that would be paid by non-residents is slightly lower at approximately 73.0% due to the businesses that primarily market and sell their goods and services to buyers and businesses outside the City's jurisdictional boundaries.

Economic Segment	Bradley Burns 1% Sales & Use Tax	Transactions & Use Tax
	Non-Resident	Non-Resident
Autos & Transportation	29.4%	13.4%
Building & Construction	21.1%	63.8%
Business & Industry	58.1%	20.5%
Food & Drugs	86.1%	86.1%
Fuel & Service Stations	55.7%	55.7%
General Consumer Goods	64.9%	30.3%
Restaurants & Hotels	101%	101%
Estimated Generated Revenue	80.1%	73.0%

Estimated % of Sales Tax Revenue Generated from Non-Residents

The figures shown above were obtained utilizing a variety of methodologies customized to each economic segment. These methodologies consider the mix of businesses located in the City, per-capita-sales within the City versus the per-capita-sales across Los Angeles County, as well as factoring average income population and trade area daytime- population for the designated trade areas previously described as a percentage of those categories within the City.

Analysis Summary

Sales Tax Revenue for the City of Malibu by Business Categories in Calendar Year 2020:

- The Autos & Transportation sector makes up 3.1% of the Bradley Burns Sales Tax revenue.
- The Building & Construction sector makes up 3.2% of the Bradley Burns Sales Tax revenue.
- The Business & Industry sector generates 5.0% of city's total 1% Bradley Burns Sales Tax revenue.
- The Food & Drugs sectors makes up 10.7% of the Bradley Burns Sales Tax revenue.
- The General Consumer Goods sector makes up 23.7% of the Bradley Burns Sales Tax revenue.
- The Fuel & Service Station sector brings in 7.9% of the Bradley Burns Sales Tax revenue.
- The Restaurants & Hotel sector brings in 45.7% of the Bradley Burns Sales Tax revenue.

It is worth noting that the Restaurants & Hotels sector produced almost half the total Bradley Burns Sales Tax revenue for City of Malibu in 2021 with significantly higher per capita sales, more than five times the per capital sales level of Los Angeles County. This is supported when reviewing the Consumer Demand & Market Supply Assessment, the Restaurants & Hotels segments reflect an average of \$3.6M in supply surplus while fulfilling close to \$35M worth of consumer demand.

Additionally, General Consumer Goods sector produced almost 1/4 of the total Bradley Burns Sales Tax revenue for City of Malibu, and it also has a significantly higher per capita sales, more than two times the per capital sales level of Los Angeles County. This is supported when reviewing the Consumer Demand & Market Supply Assessment, the General Consumer Goods segments reflect an average of \$22M in supply surplus while fulfilling close to \$58M worth of consumer demand.

Conclusion

Local tax is the general term for sales and use taxes imposed under the Bradley Burns Uniform Sales and Use Tax Law. The basic statewide sales and use tax rate is divided between the State, the local jurisdiction (City or county of place of sale or use) and the local transportation fund (County of place of sale or use). Whereas, when implemented District Taxes are imposed locally under the Transaction and Use Tax Law (TUT). The tax rate in a locality that imposes a TUT will have a higher tax rate than the statewide rate, depending on the district taxes that apply.

City of Malibu is attracting a healthy number of outside consumers into the city, showing that non-residents visiting the city, commuting employees and vacationers are exponentially increasing sales tax revenue, especially in Restaurants & Hotels and General Consumer Goods sectors. To that end, it is estimated that in Malibu 80.1% of the Bradley Burns (local tax) sales tax revenue and 73.0% of Transaction & Use Tax (TUT) revenue is generated by non-residents