

League of California Cities ❖ October 18, 2019

Death, Taxes and Other Unavoidables: A California Municipal Finance Update

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The California Local Government Finance Almanac

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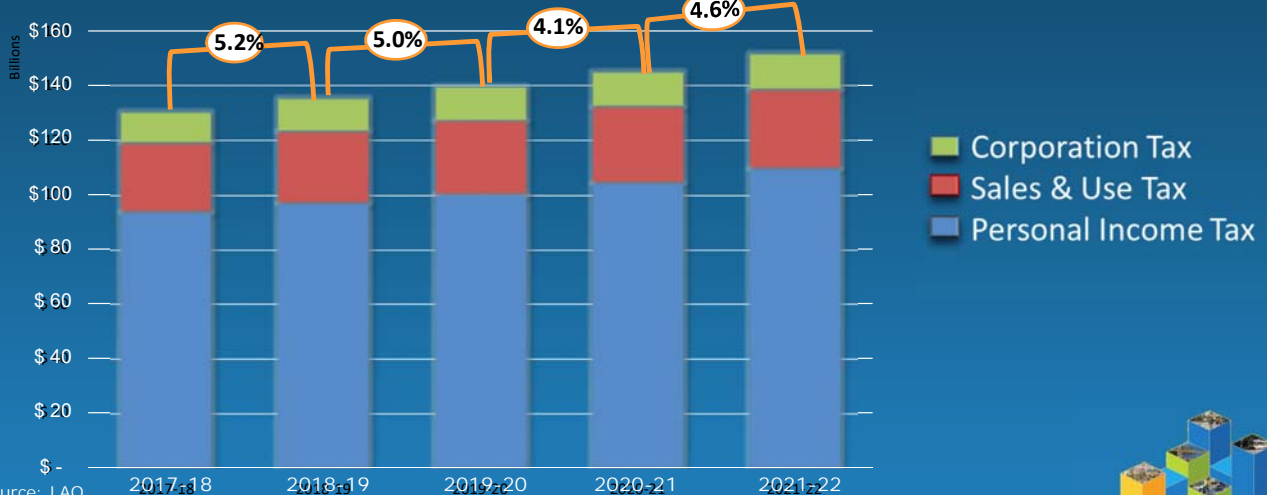
Stuff to Talk About ...

- State Fiscal Condition and Outlook
- Diagnosing Financial Health
- Sales Tax
- Local Streets and Roads Funding

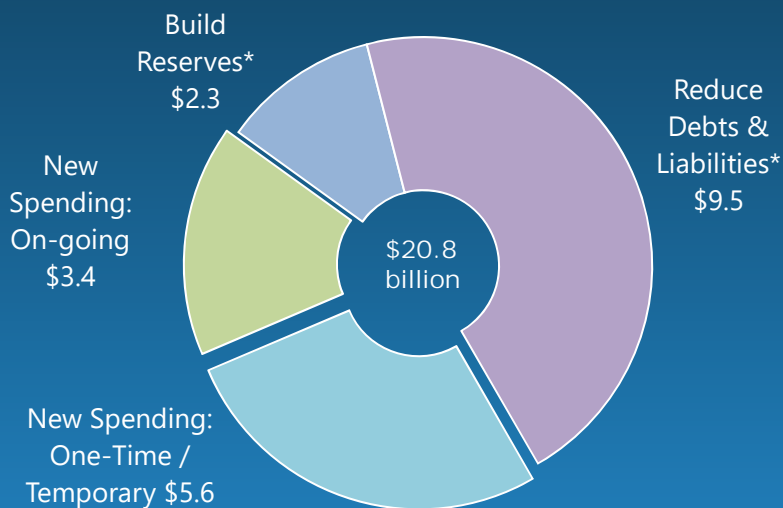


State Revenue Outlook Good ... until it's NOT

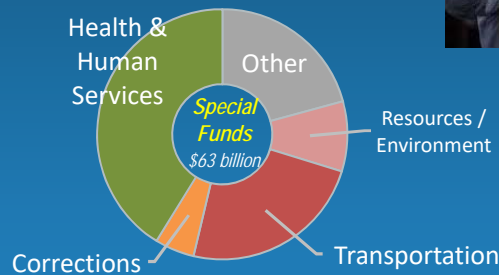
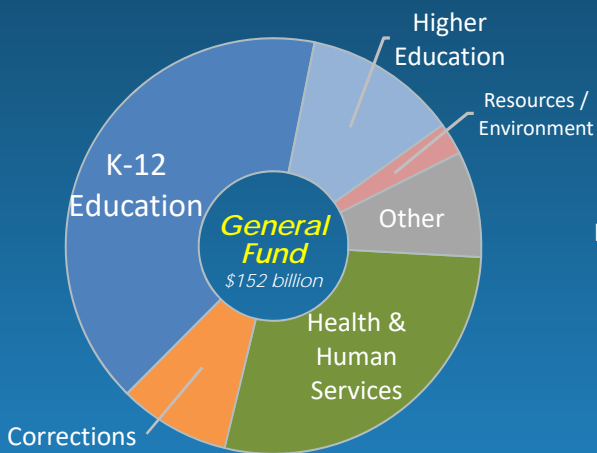
Big Three Tax Revenues



Use of Discretionary Resources



California State Spending Plan 2019-20 Budget Agreement

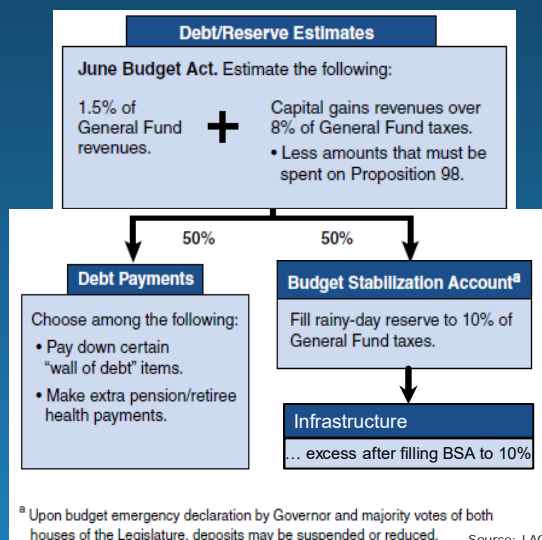


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Proposition 2 Rainy Day Fund & Debt Reduction



FY2019-20
Governor's Proposed (May Rev)

Required
\$4.4 Billion

Debt
reduction
\$2.2

BSA Reserve \$ 2.2
Prior balance 14.3
Total BSA \$16.5 B

SFEU Reserve \$1.4
SafetyNet Reserve \$0.9
Public School System Stabilization Acct \$0.4

Total Reserves \$19.2 Billion
at end of 2019-20

Source: LAO May 2019

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Paying Down Debts

millions	Paydown
Budgetary Borrowing	
Loans from Special Funds	\$ 2,169
Prop98 Settle-up	687
Undo Payroll and CalPERS payment deferrals	1,680
CalPERS Borrowing Plan	390
State Retirement Liabilities	
State Employee Pensions (CalPERS)	3,000
School Employee Pensions	
Local Districts' share	2,300
State share	1,117
State Retiree Healthcare (OPEB)	260
UC Retirement Plan	25
Total	\$ 11,628



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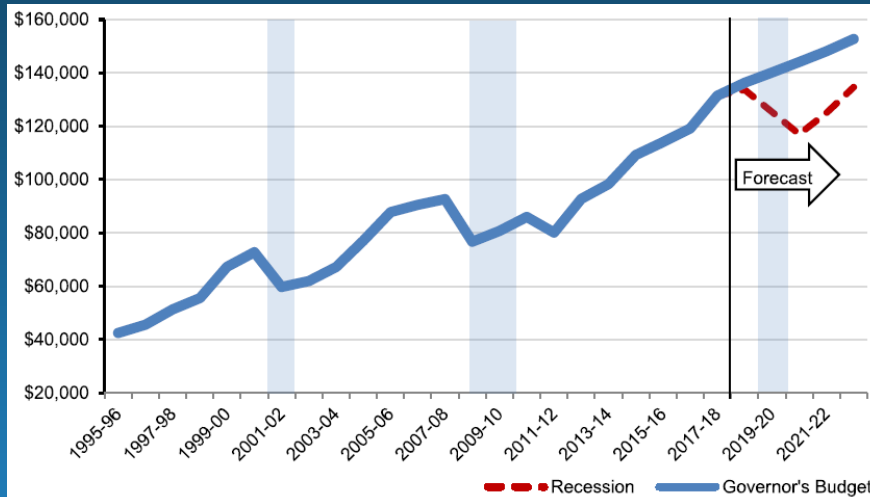
Source: Budget Conference Committee

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Recession Scenario: \$70 billion loss over 3 years

California State General Fund (Dollars in Millions)



Source: Governor's Proposed Budget

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A recession in 2019-20 could result in a ~\$70 billion \$ loss and ~\$40 billion budget deficit over three years.

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A Brief Look at the California City Financial Condition and the California Municipal Financial Health Diagnostic Tool



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The California Municipal Financial Health Diagnostic



Financial Health Indicators - Summary Checklist

Measures	1. Net Operating deficit / surplus. There are no recurring general fund operating deficits. General revenues are sufficient to meet the net general revenue demand of programs.	
	2. Fund balance. Reserves are sufficient over multiple consecutive years and in compliance with adopted policy.	
	3. Capital Asset Condition. The city is keeping pace with the aging of its capital assets.	
	4. Liquidity. Cash and short-term investments are sufficient to cover current liabilities (including short-term debt and accounts payable within 60 days).	
	5. Fixed costs & labor costs. Fixed costs (including debt service and other contractual obligations), salaries and benefits are stable or decreasing over multiple years relative to reasonably expected revenue growth.	
	6. General fund subsidies of other funds. Any general fund subsidies other enterprises or special funds are sustainable and in compliance with adopted policy.	
Practices and Conditions	7. Constraints on budgetary discretion. The city council's authority to make budget changes is not excessively constrained by charter, contract, or law.	
	8. Balancing the budget with temporary funds. The use of reserves, selling assets, deferring asset maintenance to balance the general fund has been limited, prudent and in compliance with adopted policy.	
	9. Balancing the budget with borrowing. The use of short-term borrowing, internal borrowing or transfers from special funds to balance the general fund has been limited, prudent and in compliance with adopted policy.	
	10. Balancing the budget by deferring employee compensation costs. Pension liabilities and other non-salary benefits have been determined, disclosed and actuarially funded in compliance with adopted policy.	
	11. Balancing the budget with backloaded debt service payments. Debt service payments have not been "backloaded" into future years.	
	12. Funding operating costs with non-recurring revenues. Ongoing operating costs are being funded with ongoing rather than temporary revenues (e.g., from development, etc.)	
	13. Timeliness and accuracy of financial reports. Financial Reports are being filed on time. (CAFR, Annual Audit, State Controller's Financial Transactions Report)	
	14. Service level solvency. Public service levels meet the standards and needs in this community.	

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The Importance of Good Financial Policies

Use of temporary funds

Reserves, fund balance

Short-term borrowing

Interfund transfers

Payment of Employee comp costs (pension, OPEB)

Pay-as-you-go financing

Debt management and affordability

Long Range Financial Planning

Essential Element of Financial Strength: Multi-Year Budget Forecasting

Financial

- ✓ Improves understanding of major revenue and expense budget drivers
- ✓ Identifies structural budget issues

Strategic

- ✓ Promotes long-term view
- ✓ Informs policy decisions e.g. impact on reserves, budget sustainability



Evolving Sales & Use Tax

Wayfair SCOTUS decision
and AB147 (Burke)



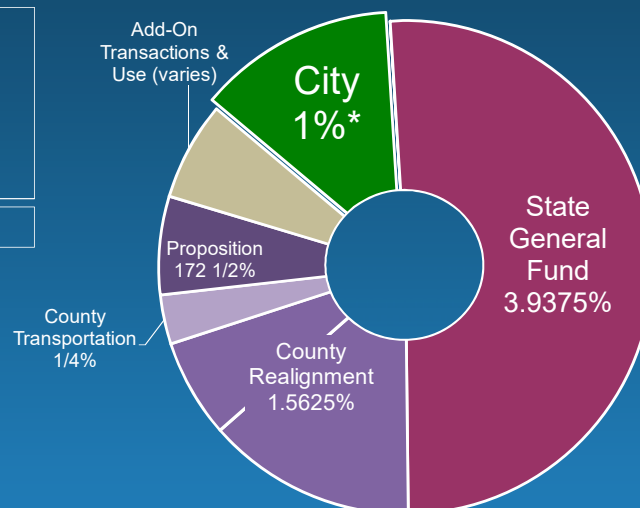
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Where Your Sales Tax Goes

City*	1.00
County TDA	0.25
Prop172 Safety	0.50
County Realign	1.5625
State GenFund	3.9375
Total Base	7.25 %
+ Add-on TrUTs	



* For taxable sales in unincorporated areas, the local 1% rate goes to the county.

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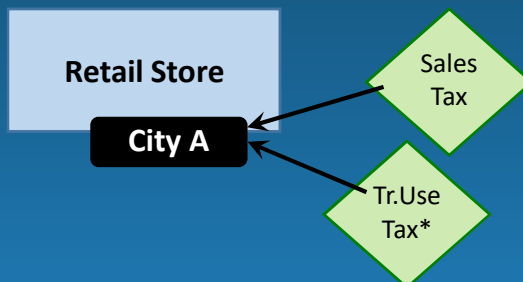




“Over the Counter” Transaction

Seller's
Place of
Business

Buyer
Receives
at ...



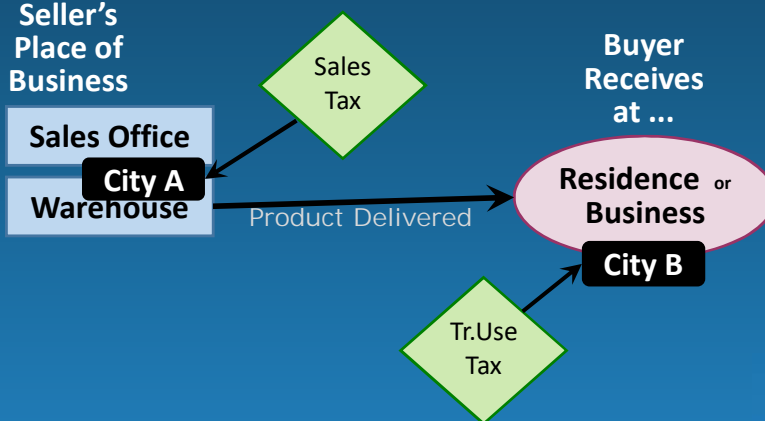
*Transactions and Use Tax, also called “District Tax” or “Add-on sales tax” ... varies.



Remote (Online) Sale Seller with *In-State* Presence

Seller's
Place of
Business

Buyer
Receives
at ...





Remote (Online) Sale Out-of-State Seller

Seller's
Place of
Business

Sales Office

Warehouse

Out of State

City D E X Y Z

Countywide pool

Use
Tax

Buyer
Receives
at ...

Residence or
Business

City B

Product Delivered

Tr.Use
Tax

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South Dakota v Wayfair, Inc.

- ✓ Overrides *Quill Corp. v. North Dakota* - which held that a state cannot require seller with no physical presence in state to collect/remit taxes on goods the seller ships to consumers in state.
 - Physical presence rule of *Quill* is outdated, unnecessary and puts businesses with physical presence at a competitive disadvantage.
- ✓ Sellers with significant business within a state may be required to collect/remit taxes, despite not having physical presence in the state.
- ✓ Kennedy: South Dakota's system provides
 1. Safe harbor for limited business in state (\$100,000 or 200 transactions)
 2. Not retroactive
 3. Streamlined Sales & Use Tax Agreement: uniform administration, definitions, rates, rules and free software.

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AB147 (Burke) re South Dakota v Wayfair, Inc.

- ✓ Any retailer must register with CDTFA and collect California Sales (Use) Tax except if:
 - \$500,000 or less of combined taxable sales for delivery in California during the preceding year.
- ✓ Marketplace sellers (who must register) must collect for all transactions.
- ✓ Any retailer who is required to register must also collect applicable local *transactions and use taxes* on all sales.

Economic Development Subsidies

SB 531 (Glazer) Prohibits future sales tax agreements between local agencies and retailers with a warehouse, sales office, or fulfillment center that results in a shift of sales taxes from another jurisdiction.

Status: *Vetoed.*

AB 485 (Medina) Requires important transparency and information regarding agreements between local governments and businesses that public tax dollars.

Status: *Signed.*

Housing, Economic Development: Legislation

SB 5 (Beall/McGuire/Portantino) A city, county, or JPA would be eligible for additional property tax if project contains:

- affordable housing,
- transit-oriented development,
- infill development,
- revitalizing and restoring neighborhoods, and
- planning for sea level rise.

\$200 million /year

Status: Vetoed.

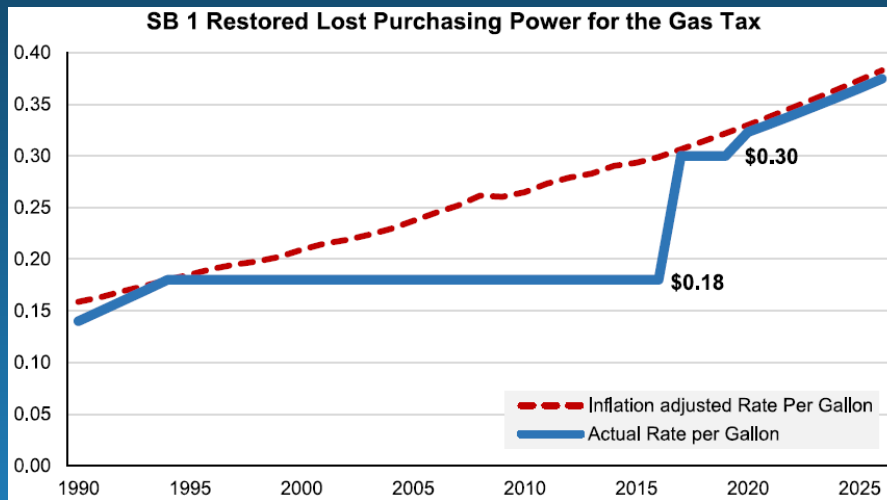


Critically Needed Transportation Funding Arrives:

SB1: The Road Repair and Accountability Act of 2017



The Road Repair and Accountability Act of 2017



Source: Governor's Proposed 2018-19 Budget Summary Figure INT-06

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Road Repair and Accountability Act Revenues



Effective July 1, 2019

Price-based Gas Tax
 reset rate
 @17.3¢
 Now 11.7¢ @7/1/17
 +\$1.1 billion/year

*inflation adjusted
 starting 7/1/2020*

Effective Nov 1, 2017

Gasoline Excise Tax
 increase by 12¢
 +\$1.8 billion/year

*inflation adjusted
 starting 7/1/2020*

Effective Nov 1, 2017

Diesel Excise Tax
 increase by
 20¢/gal
 +\$730million/year

*inflation adjusted
 starting 7/1/2020*

Gas Excise Tax (HUTA) base rate

*inflation adjusted
 starting 7/1/2020*

Effective Jan 1, 2018

Transportation Improvement Fee
 \$25 to \$175/year
 depending on auto value
 +\$1.6 billion/year

*inflation adjusted
 starting 7/1/2020*

Effective Nov 1, 2017

Diesel Sales Tax
 +4.00% to 5.75%
 +\$300 million/year

Beginning 2017-18 over 3 yrs

State GF Loans Repaid
 \$706 million
 one time incl. \$225 m to TCRF

*inflation adj.
 7/1/2021*

Effective July 1, 2020

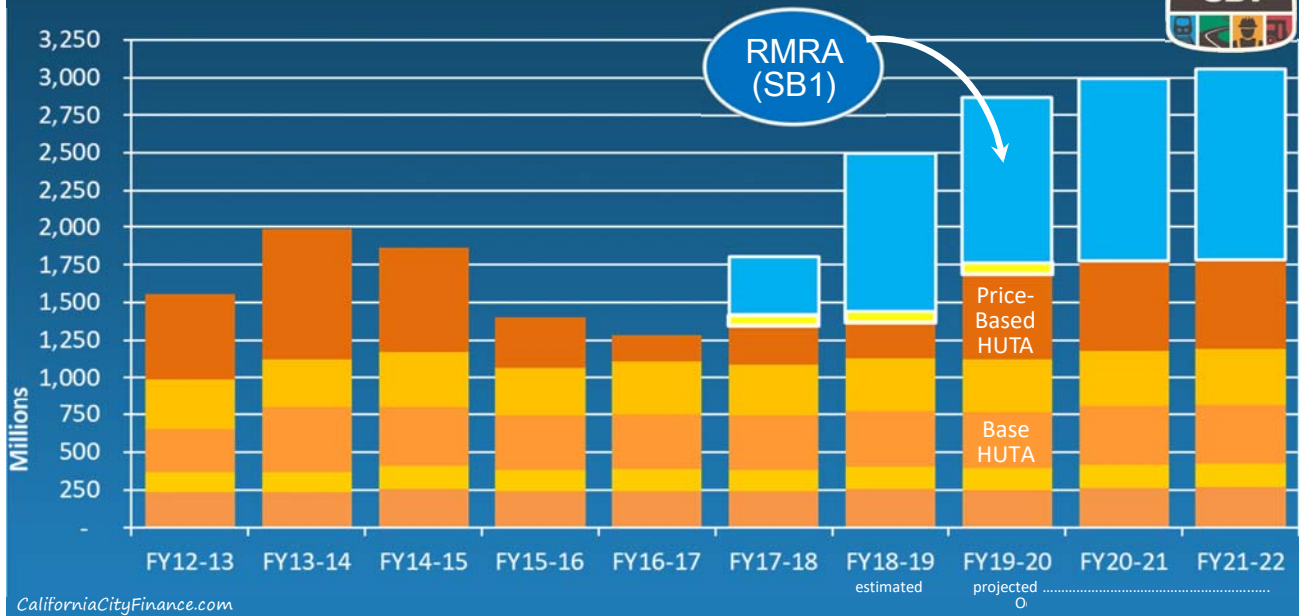
ZEV Registration Fee

\$100/yr on 2020 models / later

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Local Streets and Roads Revenues



City Annexations and Incorporations: Property Tax in Lieu of VLF

AB 213 (Reyes) Restores critical funding to cities annexing areas from the Vehicle License Fee by providing Property Tax in Lieu of VLF – just like all cities and counties received in the VLF swap of 2004.

Status: *Two year bill.*

AB 818 (Cooley / Quirck) Restores critical funding to incorporating cities from the Vehicle License Fee by providing Property Tax in Lieu of VLF – just like all cities and counties received in the VLF swap of 2004. **Status:** *Two year bill.*



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