



## MEMORANDUM

**TO:** City Council

**FROM:** Matthew Downing, City Manager  
Bill Robeson, Assistant City Manager/Public Works Director  
Nicole Valentine, Administrative Services Director  
Shannon Sweeney, City Engineer

**SUBJECT:** Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure

**DATE:** May 14, 2024

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### **RECOMMENDATION:**

Review and provide direction on financing options related to the top three priorities from the Community Priorities Survey Results and consider directing staff to prepare a resolution and ordinance for City Council consideration at the May 28, 2024 meeting, to place a 1% Transaction and Use (“sales tax”) measure on the November 5, 2024 ballot.

### **IMPACT ON FINANCIAL AND PERSONNEL RESOURCES:**

Historically, the City has been able to allocate on average \$6.1 million to the Police Department and approximately \$1.25 million annually towards the Pavement Management Program (PMP) that addresses streets and sidewalks. The recently Amended and Restated Joint Exercise of Powers Agreement for the Five Cities Fire Authority (FCFA) the City resulted in an anticipated average payment over the next five years of \$4.2 million annually. A new 1% local sales tax measure increase would generate approximately \$6 million annually.

### **BACKGROUND:**

At the [March 2, 2023](#), Special City Council Meeting, the City Council established four (4) major City goals for staff to prioritize for the [FY 2023-25 Biennial Budget](#). The goals were established considering the results of a community survey and input from the public and staff. The four major goals are:

## City Council

### Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure

May 14, 2024

Page 2



#### Funding

Support a thriving community through fiscal responsibility, economic development efforts, and additional and alternative revenue streams.



#### Fire Services

Implement operational and fire and emergency service delivery improvements through the Five Cities Fire Authority and complete the transition of services to Oceano due to its exit from the Authority.



#### Infrastructure

Invest in and complete critical infrastructure projects throughout the City through the strategic prioritization of projects based on available resources.



#### General Plan Update

Prioritize and complete major work efforts for the comprehensive General Plan update to provide a vision and framework for future development within the City.

On [June 13, 2023](#), the City Council authorized the publishing of a Request for Proposals (RFP) for Voter Opinion Polling and Public Education and Outreach Services. On [August 22, 2023](#), the City Council approved a professional services agreement with Clifford Moss and True North Research for these services. Voter Opinion Polling was conducted in November and December 2023. On [January 9, 2024](#), the City Council reviewed the polling results summary [report](#) from True North Research and directed staff to continue working with the consultant on a potential future revenue measure.

As part of the City's efforts to listen to the community regarding their priorities for Arroyo Grande, a Community Priorities Survey was mailed to all Arroyo Grande households on February 22, 2024. The mailer included a tear-off response option as well as an online option for completing the survey. To encourage residents' participation, video and still ads were developed and placed on various online platforms driving viewers to the online version of the survey.

On [April 23, 2024](#), the City Council reviewed the [Community Priorities Survey Results](#). As of April 23, 2024 the City received 1,444 responses to the Community Survey – 477 written and 967 online. Over 400 personal comments were also provided with the responses.

## **City Council**

### **Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 3**

On average, the top three priorities, as ranked by Arroyo Grande residents responding to the survey, were as follows:

1. Maintain fire protection services;
2. Maintain 911 response and emergency police services; and
3. Repair, pave and Maintain Arroyo Grande's 73 miles of roads; fix potholes and damaged sidewalks.

The top three priorities were calculated by taking the sum of each selection and dividing it by the number of responses received for that category. Categories with the lowest averages reflect the more important issues to the community members who responded.

The top three "1st place" priorities, by a significant margin, were as follows:

1. Repair, pave, and maintain Arroyo Grande's 73 miles of roads; fix potholes and damaged sidewalks;
2. Maintain 911 response and emergency police services; and
3. Maintain fire protection and paramedic services.

The top priorities were calculated by adding up how many rankings of "1" each category received.

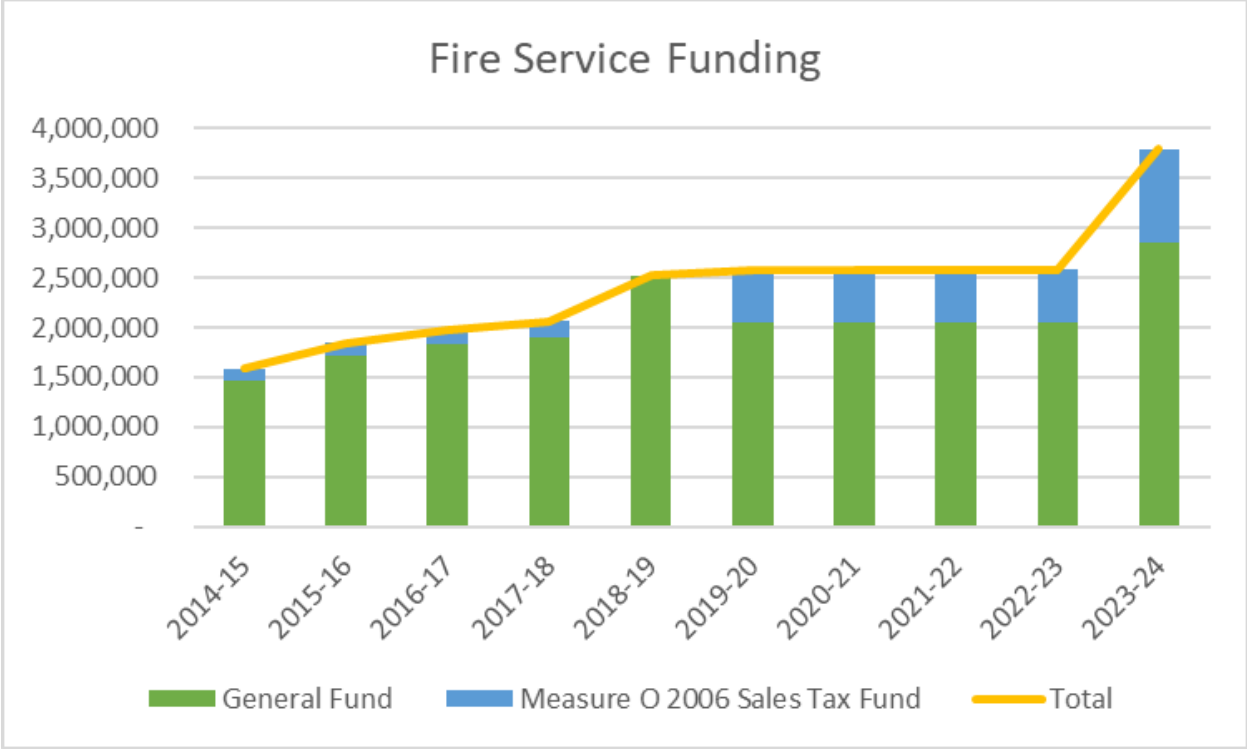
#### **Maintain Fire Protection Services**

The FCFA was formed on July 9, 2010, through a Joint Exercise of Powers Agreement (JPA) entered into by the City of Arroyo Grande (City), the City of Grover Beach, and the Oceano Community Services District (OCSD) to provide integrated and efficient fire and emergency medical services to the three communities. On June 13, 2023, the City Council approved an Amended and Restated Joint Exercise of Powers Agreement for the FCFA with a formal execution date of June 22, 2023, by the FCFA Board, and an agreement between the FCFA and the OCSD regarding short-term fire and emergency response services for FY 2023-24 while OCSD completes the San Luis Obispo Local Agency Formation Commission (LAFCO) process following their departure from the FCFA.

Over the last ten years, the City has allocated the following funds towards the FCFA to maintain lifesaving fire protection service:

**City Council**  
**Discussion of Financing Options Related to the Top Three Priorities from the**  
**Community Priorities Survey Results and City Council Direction on a Potential**  
**Sales Tax Measure**  
**May 14, 2024**  
**Page 4**

**Chart 1: Fire Service Funding**



**Table 1: Fire Service Funding**

Fiscal Year	Measure O		Total
	General Fund	2006 Sales Tax	
2014-15	1,457,448	125,000	1,582,448
2015-16	1,708,434	137,700	1,846,134
2016-17	1,840,717	140,500	1,981,217
2017-18	1,893,047	169,300	2,062,347
2018-19	2,523,661	-	2,523,661
2019-20	2,052,061	528,894	2,580,955
2020-21	2,052,061	528,894	2,580,955
2021-22	2,052,061	528,894	2,580,955
2022-23	2,052,061	528,894	2,580,955
2023-24	2,847,000	949,000	3,796,000

As indicated in Chart 1 and Table 1 above, FY 2019-20 through FY 2022-23 does not show a change in funding. The large increase in FY 2023-24 was due to the change in JPA member structure and continued investment needed in FCFA.

**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 5**

Over the last ten years, FCFA calls for service continue to increase as shown in Table 2 below:

**Table 2: FCFA Calls for Service**

<b>Calendar Year</b>	<b>Calls for Service</b>	<b>Percentage Change</b>
2013	3,366	1.63%
2014	3,575	6.21%
2015	3,762	5.23%
2016	3,714	-1.28%
2017	3,943	6.17%
2018	3,694	-6.31%
2019	3,413	-7.61%
2020	4,000	17.20%
2021	4,154	3.85%
2022	4,492	8.14%
2023	4,261	-5.14%

This data is not available specifically for Arroyo Grande calls for service, although each service area has seen a steady increase.

**Maintain 911 Response and Emergency Police Services**

The purpose of the Arroyo Grande Police Department is to maintain public peace, safeguard lives and property, and provide for a quality of life whereby those persons within the City of Arroyo Grande have a sense of security and freedom in their daily activities. To achieve these ends, the Arroyo Grande Police Department maintains the capability to provide a superior level of law enforcement and related services that are appropriate and timely. Specifically, the Arroyo Grande Police Department maintains a viable proactive organization that recognizes and effectively responds to current and future community needs and maximizes the available resources, personnel, and technology.

Over the last ten years, the City has allocated the following funds to maintain 911 response and emergency police services:

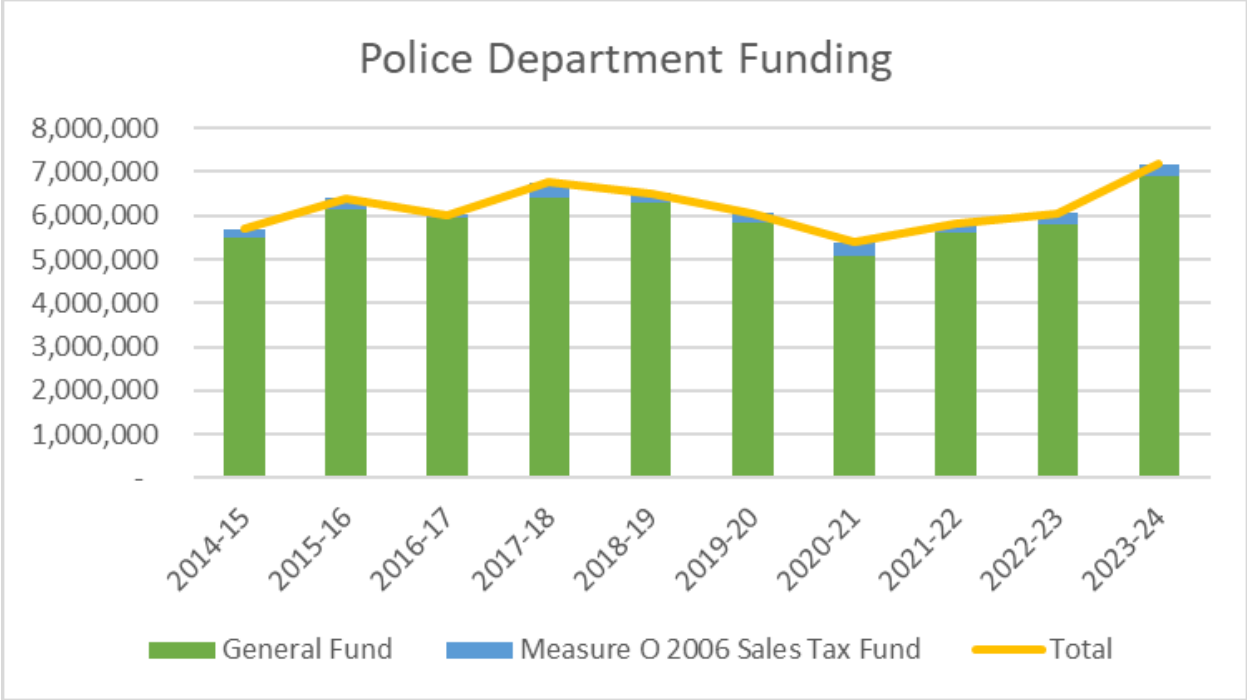
**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 6**

**Chart 2: Police Department Funding**



**Table 3: Police Department Funding**

Fiscal Year	Measure O		Total
	General Fund	2006 Sales Tax	
2014-15	5,498,126	193,000	5,691,126
2015-16	6,140,688	261,600	6,402,288
2016-17	5,950,291	71,300	6,021,591
2017-18	6,409,150	343,896	6,753,046
2018-19	6,303,739	216,804	6,520,543
2019-20	5,831,906	222,600	6,054,506
2020-21	5,089,736	292,008	5,381,744
2021-22	5,598,698	205,604	5,804,302
2022-23	5,797,299	263,100	6,060,399
2023-24	6,903,199	268,300	7,171,499

As indicated in Chart 2 and Table 3 above, the funding for the Police Department has been at a steady rate of growth for the last four years.

**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 7**

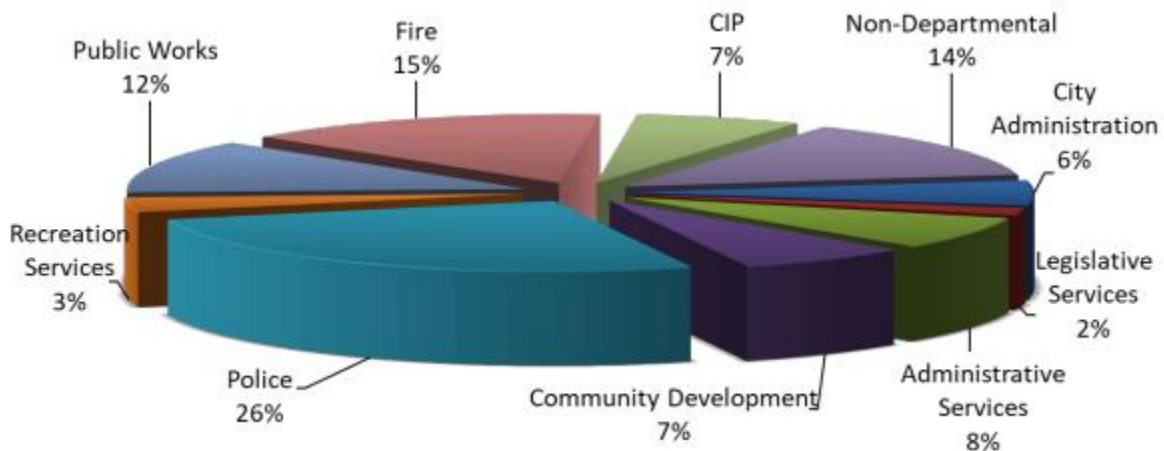
Over the last eight years, the Police Department calls for service continue to increase as shown in Table 4 below:

**Table 4: Police Department Calls for Service**

Calendar Year	Calls for Service	Incident Reports	Citations	Parking Citations	Total	Percentage Change
2015	15,986	1,858	901	134	18,879	
2016	17,137	1,844	776	214	19,971	7.20%
2017	17,295	2,024	654	298	20,271	0.92%
2018	17,507	1,903	655	771	20,836	1.23%
2019	19,292	1,850	583	152	21,877	10.20%
2020	17,997	1,660	1,022	194	20,873	-6.71%
2021	18,582	2,012	1,645	404	22,643	3.25%
2022	17,960	1,834	431	171	20,396	-3.35%
2023	17,957	1,417	2,681	36	22,091	-0.02%

As shown below, Fire and Police Services make up 41% of the FY 2023-24 budgeted Consolidated General Fund Expenditures, Police with 26% and Fire with 15%:

**Pie Chart 1: FY 2023-24 Consolidated General Fund Expenditures**



**Repair, Pave, and Maintain Arroyo Grande’s 73 Miles of Roads; Fix Potholes and Damaged Sidewalks**

On February 14, 2017, the City Council adopted the 2016 Update to the Pavement Management Plan (Plan) and endorsed the “Critical Point Management” methodology for the City’s Pavement Management Program (PMP). The Critical Point Strategy approach selects the road segments for repair or resurfacing that are at a “critical point” of

**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

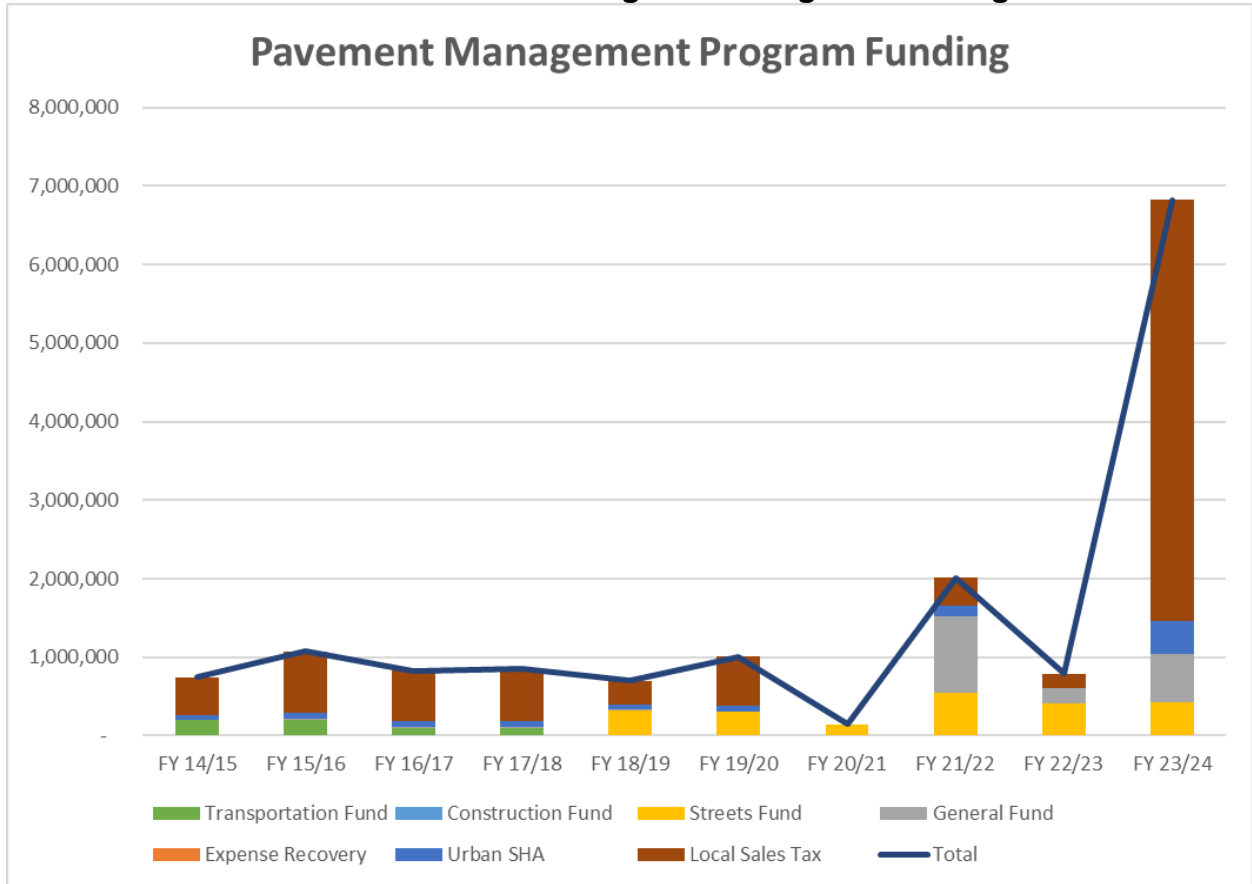
**May 14, 2024**

**Page 8**

deterioration. The critical point is a point located on the pavement deterioration graph which indicates the Pavement Condition Index (PCI) value is about to drop to a level which would trigger a more expensive maintenance or rehabilitation approach. The Critical Point Strategy is a long-range methodology that maintains and improves roadways before they slip into a PCI range that reflects costlier repairs. The PMP will annually evaluate and provide recommendations for repair and resurfacing based on this critical point approach, using the Plan as a starting point. This method, along with field evaluations is currently being used each fiscal year when considering the Street Repairs Projects.

Over the last ten years, the City has allocated the following funds towards the PMP:

**Chart 3: Pavement Management Program Funding**





**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 9**

**Table 5: PMP Funding**

Fiscal Year	Urban SHA	Expense Recovery	General Fund	Streets Fund	Construction & Transportation Fund	Measure O 2006 Sales Tax	Total
2014-15	68,829	60	-	-	200,507	476,532	745,928
2015-16	68,828	-	17,159	-	203,267	785,164	1,074,418
2016-17	69,172	-	12,620	-	100,000	649,341	831,134
2017-18	70,000	-	14,665	-	100,000	672,920	857,584
2018-19	70,000	-	4,313	328,474	-	298,305	701,092
2019-20	70,000	-	-	309,610	-	625,089	1,004,699
2020-21	-	-	-	146,328	-	-	146,328
2021-22	131,000	-	982,315	540,280	-	361,165	2,014,760
2022-23	-	-	192,263	409,192	-	192,263	793,718
2023-24	413,400	-	610,872	432,848	-	5,368,033	6,825,153

Urban SHA refers to the City’s annual allocation through San Luis Obispo County of Government’s (SLOCOG). General Fund refers to the general revenue, including Reserve Fund Balance. Streets Fund refers to the SB 1 funds. Construction and Transportation Fund refers to Local Transportation Fund (LTF) provided by the SLOCOG. Local Sales Tax refers to Measure O 2006 revenue.

**Sales Tax**

California has a State-mandated minimum sales tax of 7.25 percent. The [Local Government Guide to California Sales, Use and Transaction Tax](#) from the City’s sales tax consultant provides a detailed overview of the allocation of sales tax and how use tax is imposed in California. Counties, municipalities, and districts are allowed to increase the sales tax in their jurisdictions up to a total of 2 percent.

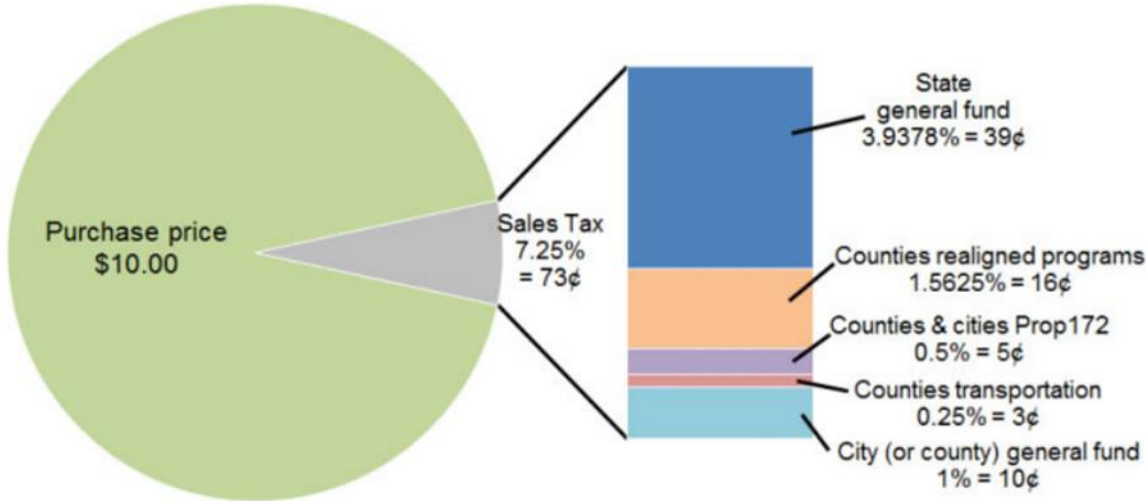
Not all sales tax revenue goes to the City. California’s base sales tax is 6%. The additional sales tax of 1.25% is called the Bradley-Burns tax, of which 1% is allocated to counties or incorporated cities to use at their discretion and the remainder 0.25% is distributed to county local transportation funds (LTFs) to support transportation programs. The following graphic provides a general breakdown of the standard 7.25% sales tax charged throughout the State and its general distribution:

**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 10**



In most areas of California, local jurisdictions have added local taxes that increase the tax owed by a seller. Sellers are required to report and pay the applicable local taxes for their taxable sales and purchases. Arroyo Grande currently has a ½ cent (0.5%) sales tax measure, Measure O-06, that was approved by the voters in 2006. This brings the total tax charged to customers purchasing items in the City of Arroyo Grande to 7.75%.

Measure O-06 passed by 50.11%, which met the majority voter approval required for establishing a local transactions and use tax. The operative date of the transactions and use tax commenced on April 1, 2007. The City publishes and distributes an annual report to each household showing the revenues and expenditures from the Measure O-06 sales tax proceeds. Additionally, the City Council is required to conduct a public hearing every five years to determine whether it is necessary for the sales tax to remain in effect.

Table 6 displays the current Sales & Use Tax Rates for the Region:

**Table 6: Regional Sales & Use Tax Rates**

City	Sales Tax Rate
Atascadero	8.75%
Grover Beach	8.75%
Morro Bay	8.75%
Paso Robles	8.75%
San Luis Obispo	8.75%
Santa Maria	8.75%
Pismo Beach	7.75%
<b>Arroyo Grande</b>	<b>7.75%</b>

**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 11**

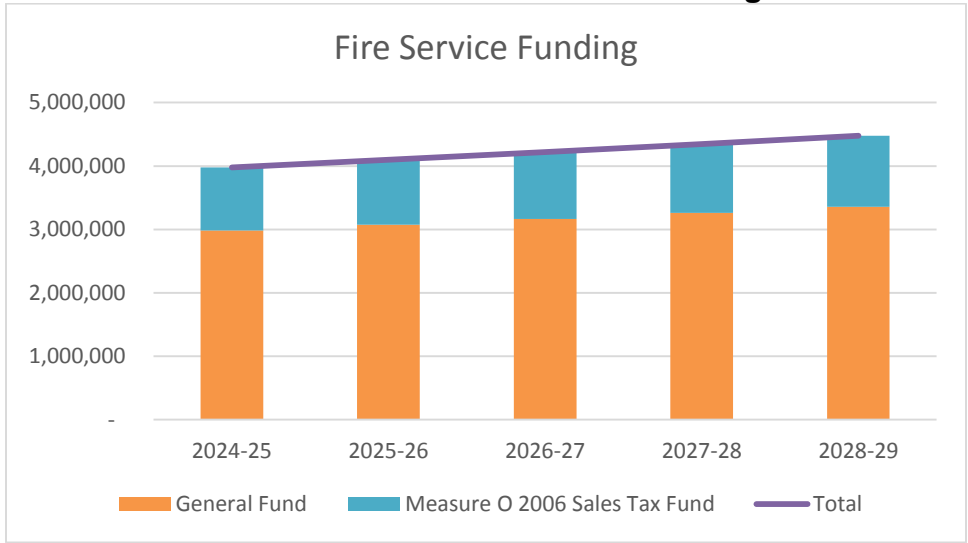
**ANALYSIS OF ISSUES:**

**Maintain Fire Protection Services**

Today’s fire service must have the personnel, training, and tools to respond to a variety of situations including medical emergencies, traffic collisions, technical rescues, structure and vegetation fires, and hazardous materials.

The projected 5-Year funding for Fire Service through FCFA for FY 2024-25 through FY 2028-29 is shown below:

**Chart 4: Future Fire Service Funding**



**Table 7: Future Fire Service Funding**

Fiscal Year	Measure O		Total
	General Fund	2006 Sales Tax	
2024-25	2,983,500	994,500	3,978,000
2025-26	3,073,005	1,024,335	4,097,340
2026-27	3,165,195	1,055,065	4,220,260
2027-28	3,260,151	1,086,717	4,346,868
2028-29	3,357,956	1,119,319	4,477,275

Measure O 2006 Sales Tax pays for only 25% of the total Fire Service costs the City provides.

**Maintain 911 Response and Emergency Police Services**

When an Arroyo Grande resident dials 9-1-1, they have likely found themselves in a situation that they can no longer manage on their own. Today’s Police Department must

**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

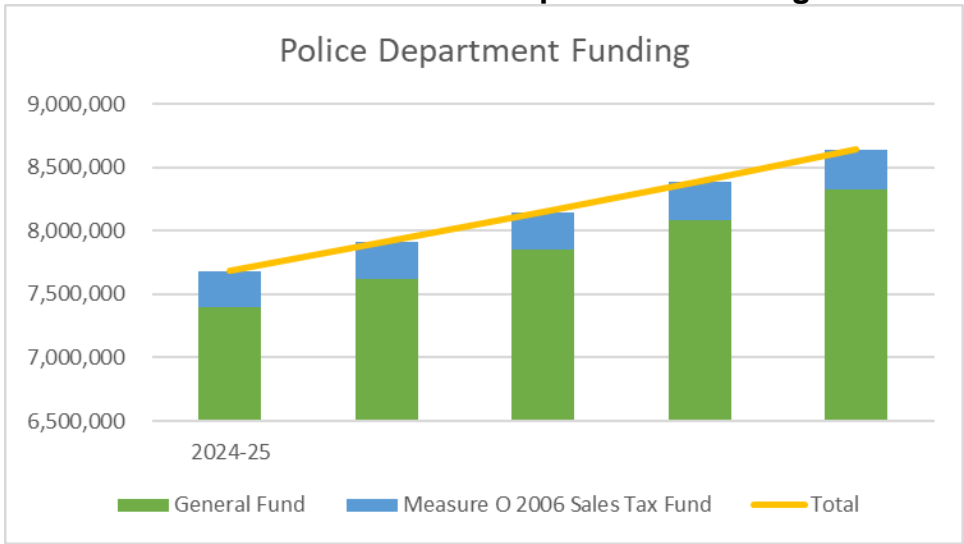
**May 14, 2024**

**Page 12**

have the personnel, training and tools to respond to a variety of situations including traffic collisions, calls related to crime such as homicide, larceny, rape, assault, arson, robbery, burglary, and vehicle theft, and calls related to homelessness.

The projected 5-Year funding for the Police Department for FY 2024-25 through FY 2028-29 is shown below:

**Chart 5: Future Police Department Funding**



**Table 8: Future Police Department Funding**

Fiscal Year	Measure O		Total
	General Fund	2006 Sales Tax	
2024-25	7,398,347	284,900	7,683,247
2025-26	7,620,297	291,900	7,912,197
2026-27	7,848,906	299,200	8,148,106
2027-28	8,084,374	306,700	8,391,074
2028-29	8,326,905	314,500	8,641,405

Measure O 2006 Sales Tax pays for approximately 4% to provide support to the Police Department including the cost of one Senior Police Officer position, the Narcotics Task Force, and the Animal Services Building Debt Services payment.

**Repair, Pave, and Maintain Arroyo Grande’s 73 miles of Roads; Fix Potholes and Damaged Sidewalks**

The City currently maintains approximately 73 centerline miles of roads representing 13,501,540 square feet of pavement with a replacement value of approximately \$408,088,527 as calculated by the City’s pavement assessment software. Despite past

**City Council**

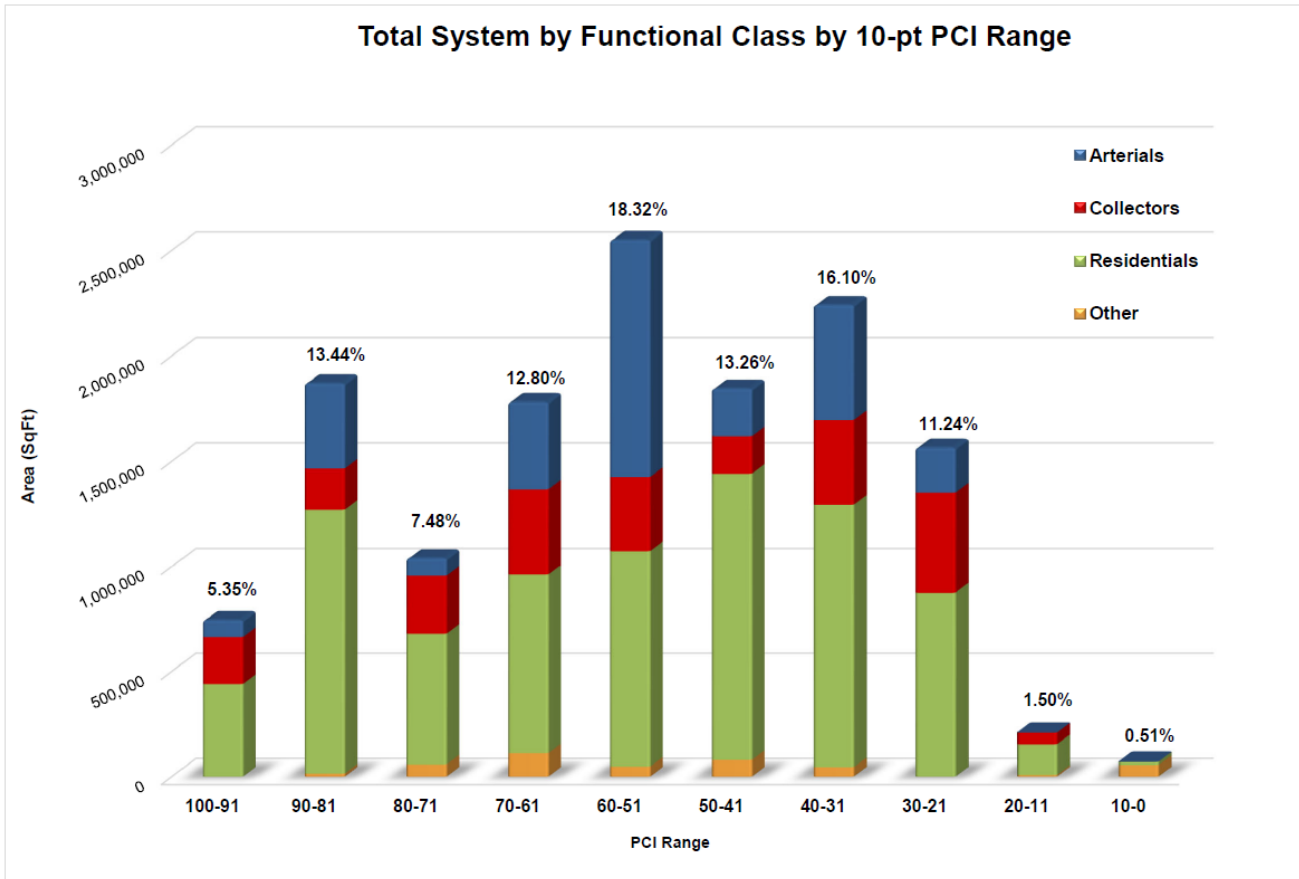
**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 13**

efforts, the condition of the City’s streets has declined. On a pavement condition scale of 0 to 100, streets now rank an average of 56, down from an average of 69 in 2016. The chart below shows the City’s pavement assessment, broken down into 10-point PCI ranges:

**Chart 6: Total System by Functional Class by 10-pt PCI Range**



The City’s pavement consultant generated five (5) scenario projections of future pavement conditions in the City and the costs to obtain and maintain those conditions over the course of ten years, which are represented graphically below in Chart 7.

**City Council**  
**Discussion of Financing Options Related to the Top Three Priorities from the**  
**Community Priorities Survey Results and City Council Direction on a Potential**  
**Sales Tax Measure**  
**May 14, 2024**  
**Page 14**

**Chart 7: 10-Year Projections**



A summary of each of the scenario projections are as follows:

- Scenario 1: Unconstrained Budget/Funds Needed to obtain Optimum PCI of 85 (\$91M for Year 1, \$4.8M/Yr Avg. for Years 2-10.)
- Scenario 2: Amount of funding to increase PCI by 5 (Avg. \$8.9M/Yr.)
- Scenario 3: Amount of funding to maintain PCI of 56 (Avg. \$7.2M/Yr.)
- Scenario 4: Impact of the current funding amount (\$1.25M/Yr.), showing that the current PCI would decline from 56 to 36, a 20 point overall drop in 10 years.
- Scenario 5: Represents the impact to the PCI if Zero dollars are spent.

Optimum PCI refers to the highest PCI level that the overall network can achieve within the given “Budget Needs” time frame. The charts that follow illustrate the consequences to the City’s overall weighted PCI and Deferred Maintenance Amount (costs for street repairs that get delayed or rescheduled into the future due to budget limitations), based on the scenario projections.

**City Council**

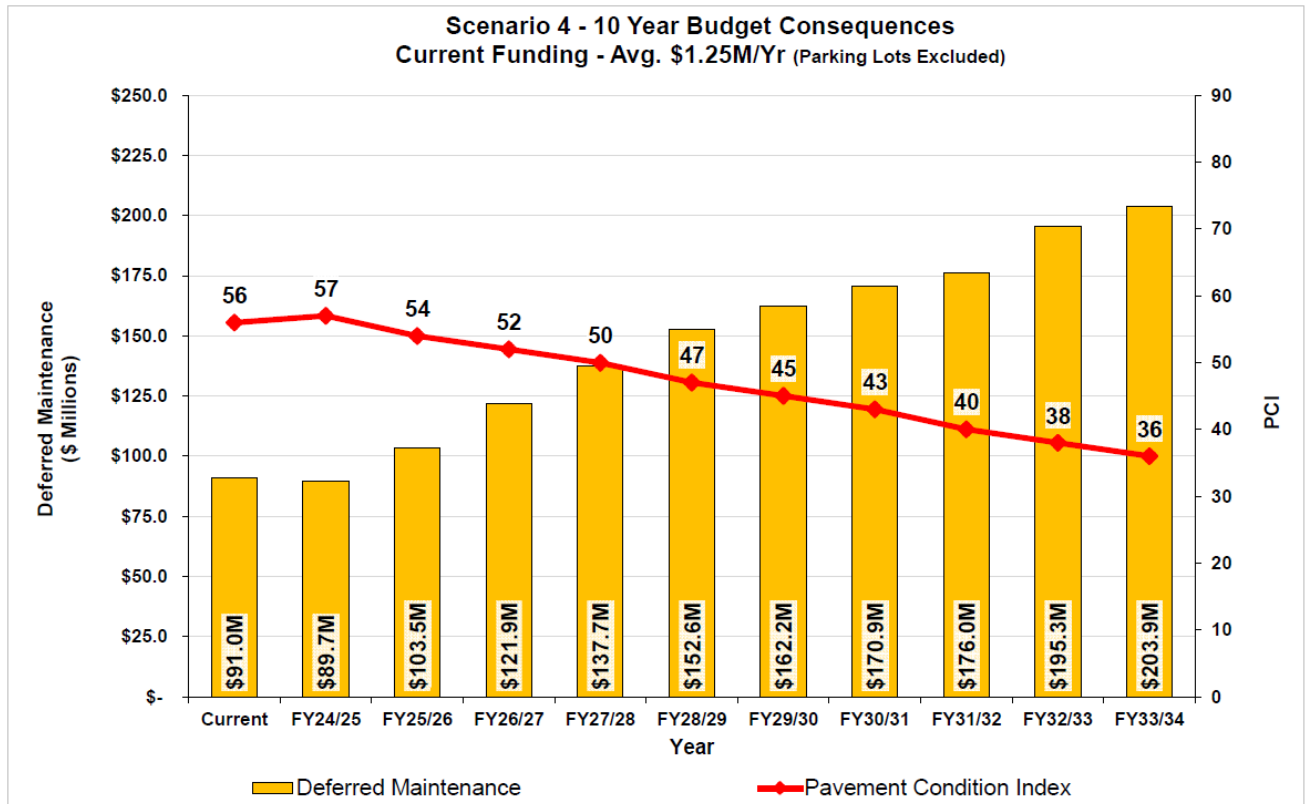
**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 15**

At the current funding level of \$1.25 million per year, it is predicted the PCI of the entire system will continue to deteriorate from 56 to 36 (Fair condition to Poor), a 20 PCI point drop over the next 10 years. Additionally, the backlog of deferred maintenance will grow from \$89.7 million to \$204 million, an increase of 127%. A PCI of 36 falls within the Poor Condition category. An example of a 36 PCI is Linda Drive, between Brisco Road and Oceanview School. Streets that have fallen into the Poor Condition Category require more expensive repair treatments such as light to heavy rehabilitation as opposed to lower cost light to heavy maintenance treatments. In addition, when repairs are deferred, they fall into a deferred maintenance backlog that creates a vicious cycle. As necessary repairs are postponed, streets start to deteriorate requiring more expensive repair treatments.

**Chart 8: PCI Scenario 4**



Based on the identified needs and current funding sources available to the City for its pavement maintenance, staff believes there are no long-term options available that can overcome the condition and replacement cost of the City's streets without a new and significant source of income for street repair.

## City Council

### Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure

May 14, 2024

Page 16

#### Financing Options - Types of Municipal Debt

##### General Obligation Bonds

General Obligation Bonds (GO Bonds) are municipal bonds that provide a way for local governments to raise money for projects (e.g. streets and roads) that may not generate a revenue stream directly. GO Bonds require voter approval of a new revenue source (property taxes) to pay debt service. These bonds are secured by the full faith, credit, and taxing power of the municipality, which typically results in the lowest possible interest rates for financing a capital project, which is the primary advantage of borrowing money by issuing GO bonds. These types of bonds are approved by a 2/3rd voter approval and paid from an additional property tax levied on property owners.

Another advantage of using GO Bonds to finance capital projects is the generally lower cost of issuance, when compared to most other methods of financing capital projects. This is because the legal structure for the issuance of GO Bonds is less complex than most other financing methods. Cities borrow funds to pay for infrastructure with a long useful life, rather than using current cash. In the case of public assets like a street, paying for it over time provides “intergenerational equity.”

##### *Pros/Cons of GO's Bonds*

- **Pros:**
  - Lowest Cost
  - Does not rely on existing General Fund resources
  
- **Cons:**
  - Long lead time, usually 9-12 months
  - High voter hurdle, requires 2/3 voter approval
  - Limited flexibility of use of proceeds
  - Property owners are paying for the use of the City instead of users paying

##### Lease Revenue Bonds

Lease revenue bonds (LRBs) are another form of debt financing public agencies often use to fund capital projects, including street and road upgrades. To utilize LRBs the City would establish a separate public financing entity that would issue the bonds and collect lease payments from the City in an amount sufficient to cover the debt service payments. LRBs usually finance the construction of facilities, including office buildings, correction facilities, courthouses, and streets and are secured through an encumbrance on a City building or facility. However, unlike revenue bonds that use money generated by the project itself (e.g. a bridge toll or water system project) to make the debt service payments, facilities funded by LRBs often do not have a dedicated funding source. For this reason, the issuance of LRBs are often paired with a new funding source (e.g. new sales tax measure) sufficient to cover the debt service.



**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 17**

*Pros/Cons of LRBs*

- **Pros:**
  - City Council approval of bond issuance, although voter approval could be necessary based on the funding source (Sales Tax Measure)
  - Quick implementation
  - Very flexible/widely available
  
- **Cons:**
  - General Fund obligation
  - Encumbrance of facility
  - Requires a new funding source, such as a voter approved sales tax measure

After reviewing the two Bond options available, the LRBs appear as the logical choice with a new form of revenue like a sales tax measure to fund the payment of this obligation. City staff worked with an independent municipal advisor to provide potential terms and bonding amounts. Below is table 9 comparing a 30-year and 20-year term LRB:

**City Council**  
**Discussion of Financing Options Related to the Top Three Priorities from the**  
**Community Priorities Survey Results and City Council Direction on a Potential**  
**Sales Tax Measure**  
**May 14, 2024**  
**Page 18**

**Table 9: 2025 Lease Revenue Bond**

**City of Arroyo Grande**  
**2025 Lease Revenue Bonds**  
**Preliminary Analysis**  
**April 22, 2024**



Lease Revenue Bonds (1)	Public Offering
Par Amount	49,010,000
Original Issue Premium	1,814,890
Project Fund	49,931,993
Estimated Total Cost of Issuance (2)	892,896
Arbitrage Yield (3)	4.10%
All-In True Interest Cost (3)	4.31%
Final Maturity	4/1/2055
Average Fiscal Year Debt Service	2,997,711
Total Debt Service	89,931,345

*(1) Preliminary analysis assumes an A+ U/L rating, bond insurance, surety policy and a closing date of April 2, 2025.*

*(2) Includes (if applicable) bond counsel, disclosure counsel, municipal advisor, underwriter's discount, trustee, rating, bond insurance, title, surety policy, and miscellaneous.*

*(3) Based on current market rates. Pricing is preliminary and subject to change with market conditions.*

To move forward with this option, the City could place a 1% local sales tax measure on the November 2024 ballot; staff estimates that the proposed sales tax measure would generate an estimated \$6 million annually in additional revenue. The estimated 1% local sales tax of \$6 million is based on doubling the current Measure O-06 0.5% sales tax totals of approximately \$3 million annually.

Use of LRBs for Streets Repair

Based on the information in Table 8 above, staff worked with the City's pavement consultant to review scenarios that used the 30-year term LRBs of approximately \$49 million, with a debt service payment of approximately \$3 million, leaving a remaining \$3

## **City Council**

### **Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 19**

million for annual ongoing infrastructure maintenance. Scenarios A through D below depict costs and PCI projections for the next 15 years.

To create Scenario A, the following funds were included in the first 5 years of projections:

- \$49 million received from the issuance of LRBs +
- \$3 million in revenue per year for 5 years from the new 1% local sales tax +
- \$1.25 million from Measure O 2006 Sales Tax Funds revenue

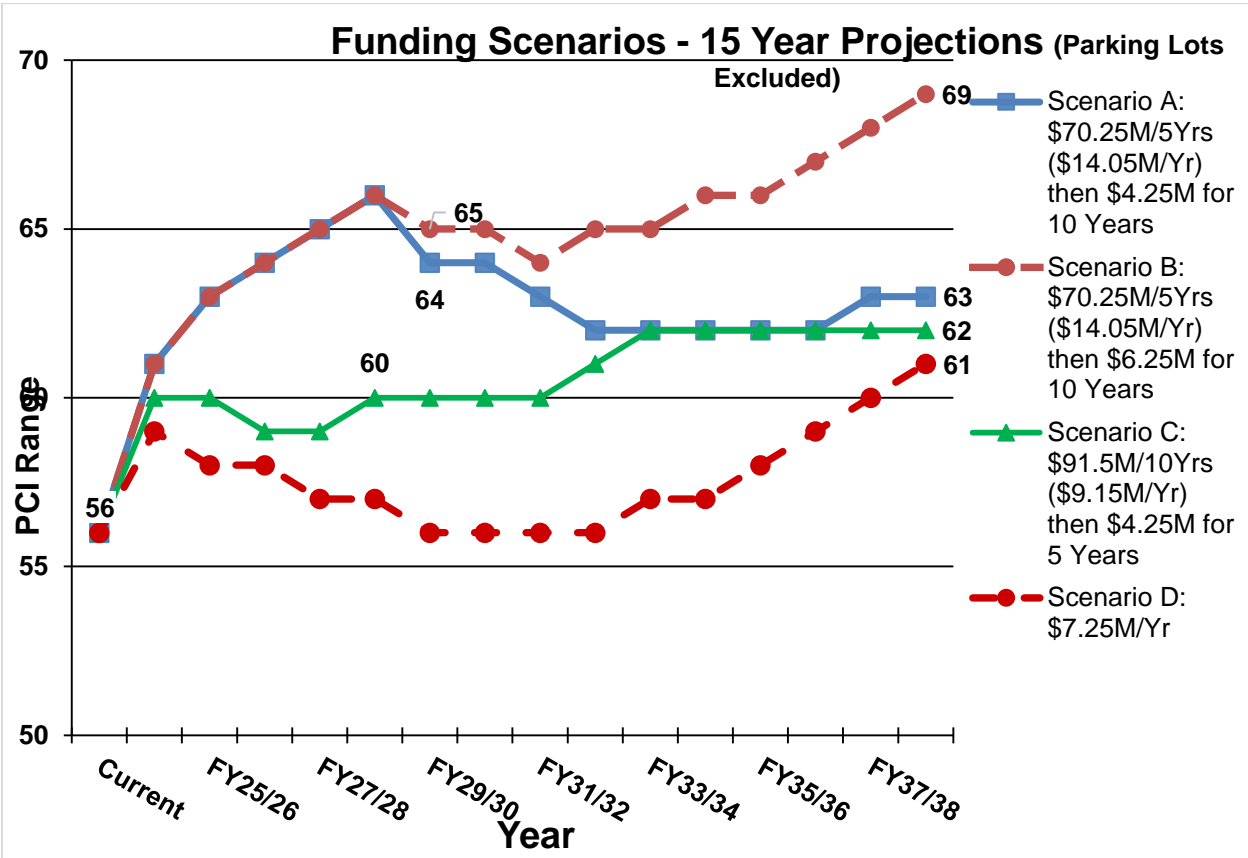
This would bring the total spent in the first 5 years of streets repairs to \$70.25 million (\$49 million in LRBs funding + \$3 million/year in new 1% local sales tax for 5 years + \$1.25 million in Measure O 2006 Sales Tax Funds for 5 years). In the years after the initial 5-year spending plan, the City would be able to allocate a total of \$4.25 million annually to pavement maintenance (\$3 million in new 1% local sales tax + \$1.25 million in Measure O 2006 Sales Tax Funds). This scenario is depicted as Scenario A in Chart 9 below.

Scenario B depicted in Chart 9 below uses the same first 5-year projections as Scenario A, but includes an estimated \$5 million in annual maintenance after the first five years. This scenario is provided for information purposes to depict the anticipated PCI level with an additional \$1.25 million for annual maintenance. The City does not currently have an anticipated revenue source for a full \$5 million in annual maintenance.

Scenario C depicted in Chart 9 below used the 30-year term LRBs of approximately \$49 million spent on street repairs over the course of 10 years rather than 5, along with debt service payments of approximately \$3 million per year, leaving a remaining \$3 million for annual ongoing infrastructure maintenance for the last 5 years of the projection. Under this scenario, the total spent in the first 10 years of streets repairs would be \$91.5 million (\$49 million in LRBs funding + \$3 million/year in new 1% local sales tax for 10 years + \$1.25 million in Measure O 2006 Sales Tax Funds for 10 years). In the years after the initial 10-year spending plan, the City would be able to allocate a total of \$4.25 million annually to pavement maintenance (\$3 million in new 1% local sales tax plus \$1.25 million in Measure O 2006 Sales Tax Funds).

Scenario D depicted in Chart 9 below projects PCI levels that would result from the use of \$6 million from a new 1% sales tax measure plus \$1.25 million in revenue from Measure O 2006 Sales Tax Funds. This scenario would not include revenue from LRBs or any other long term debt solution.

**Chart 9: 15 Year PCI Projections**



A summary of each of the scenario projections are as follows:

- Scenario A: \$70.25 million ramp up over 5 years, with \$4.25 million annual maintenance after that – overall cost over the 15-year period of \$153,750,000
- Scenario B: \$70.25 million ramp up over 5 years, with \$6.25 million annual maintenance after that – overall cost over the 15-year period \$173,750,000
- Scenario C: \$91.5 million ramp up over 10 years, with \$4.25 million annual maintenance after that – overall cost over the 15-year period \$111,250,000
- Scenario D: \$7.25 million over 15 years – overall cost over the 15-year period \$108,750,000

Based on this analysis, it does not appear to staff that LRBs are the best option for the City. While the influx of revenue from LRBs would allow the City to increase the average PCI from 56 to 66 by FY 2028-29, it is estimated that the City would need to invest significantly more money than would be available even with a new 1% sales tax measure. As a result, the City’s average PCI would yet again degrade in the out years of the 15-

## **City Council**

### **Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 21**

year projection while at the same time requiring the City to make ongoing debt service payments for at least an additional 15 years. At this time, staff would recommend the City Council move forward with placing a 1% local sales tax measure on the November 2024 ballot for voter consideration. If approved by the voters, the City Council would then have the opportunity to consider using a significant portion of the increased annual revenue of approximately \$6 million dollars directly towards Fire Service, the Police Department, and Streets Infrastructure Maintenance consistent with State law. This could enable the City to maintain road conditions using the Critical Point Strategy approach.

#### **Sales Tax Measure**

The City has the authority to raise revenues by the adoption and imposition of taxes. (Gov. Code §§ 50075.) To make a change to any general tax rate, the change must be approved by the voters. Proposition 218, approved in 1996, requires that all City tax election measures be placed on the same election when City Council Members are selected unless a financial emergency is declared. The next City Council election is scheduled for November 5, 2024. Subsequent City Council elections are held every two years. To place a tax measure on the November 5, 2024, ballot, 2/3 of the City Council (at least four members) must approve a Resolution ordering the submission to the qualified electors of the City a measure relating to the establishment of a local transactions and use tax and an Ordinance adding Chapter 3.23 to Title 3 of the AGMC regarding a transactions and use tax. Additional Resolutions are also required regarding the filing of written arguments. Once placed on the ballot, the measure must be approved by 50% +1 votes of voting residents of the City. If passed by the City Council and the electorate, the tax would be effective no sooner than the first day of the first calendar quarter, commencing more than 110 days after the adoption of the ordinance. Therefore, the tax would be effective no sooner than April 1, 2025.

#### Advantages and Disadvantages of Sales Tax Measure

As with most policy actions, enacting an increase to the sales tax has advantages and disadvantages.

Some arguments in favor include:

- Unlike property taxes, sales taxes are paid by a greater distribution of the population, including travelers, tourists, homeowners, renters, employees, and businesses in the City;
- Sales taxes are not paid on many basic necessities such as rent, groceries, sales of items paid for with food stamps, prescription medicine and certain medical devices, and services;
- Sales taxes are paid based on consumption (those who can afford to spend more pay more), and they are paid incrementally instead of in a lump sum;
- Because the tax is established by a vote of the local electorate, it cannot be taken by the State;

**Item 12.a.**

## City Council

### Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure

May 14, 2024

Page 22

- The sales tax would generate additional revenue to maintain the City's Police Services, Fire Services, and Roads Infrastructure, which staff believes are a critical component of a functioning community;
- All other jurisdictions in the Region, excluding Pismo Beach and the unincorporated County, have an additional 1% sales tax in their City; therefore staff believes:
  - There is no competitive advantage shown for having a lower sales tax rate;
  - Arroyo Grande citizens make many purchases outside of the City and may be paying a higher rate already, while none of that tax supports services in Arroyo Grande.

Some arguments against include:

- Additional taxes reduce the discretionary income of those shopping in Arroyo Grande;
- Tax increases are not generally perceived positively by the citizenry and may erode trust in local government;
- This is a general tax and there is no guarantee on how the additional revenue will be spent.

#### Potential Impact on Local Sales

The actual amount of proposed increase in the sales tax appears minimal when compared to the actual cost of a product sold. For example, for every \$100 spent on taxable goods, the increase would result in an additional \$1.00 paid by the consumer. Sales tax data trends show that an increase in the sales tax rate of one cent has no noticeable effect on the amount of taxable goods consumers buy. In other words, in other jurisdictions where the sales tax has been increased, the businesses did not see a decline in sales because the sales tax rate had been increased. The City's sales tax consultant does not believe that an increase of one cent in the sales tax rate in Arroyo Grande will affect local business sales volumes.

It is estimated that a 1% sales tax would generate approximately \$6 million annually for Arroyo Grande that cannot be taken by the State.

#### Sales Tax Options

If the City Council decides to move forward with a sales tax measure, it will require decisions on the following key issues in order to draft the measure:

- Amount of Increase – Staff recommends that 1% be proposed as the local sales tax amount as the City could utilize that 1% to address deteriorating infrastructure needs. The City has statutory authority to impose a sales tax at a rate of 0.125 or a multiple thereof. (Rev. & Tax. Code § 7285.9.)
- Local Sales Tax Allocation Report – It is important that the public be able to see where the funds are being spent to give assurance that they are being spent

**Item 12.a.**

**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 23**

properly. To ensure accountability, Measure O 2006 included a provision requiring the City to publish and distribute an annual report to each household on the revenues and expenditures from the sales tax proceeds. Staff recommends providing a Local Sales Tax Allocation Report.

- **Sunset Clause** – Sunset clauses state that a tax measure ends or “sunset” after a certain period of time. Sunset clauses can be perceived as beneficial because the tax is temporary and voters retain control over the tax. They are particularly popular when the tax will be used for a project of limited duration or to fund one-time expenditures. In this case, while the need to repair and maintain the City’s roads and infrastructure is ongoing, staff recommends that a sunset clause be added to the measure. A sunset clause was included in the polling and as part of the public outreach that staff has done in support of the City Council’s direction, it has become clear that a sunset clause would help build public trust. The City would collect the sales tax for a period of time, spending the funds as directed and then would need to place it back on the ballot in order to continue collection of the funds.

**Next steps**

In order to place the local sales tax measure on the November 5, 2024, ballot, the City Council will need to adopt a Resolution placing a measure on the ballot prior to the Registrar of Voters (ROV) deadline of June 18, 2024. In order to provide staff enough time to submit the proper paperwork and related resolutions and ordinances to the ROV, a decision should be made by the May 28, 2024, City Council meeting. Below is a timeline of events associated with a potential sales tax measure.

**City Council**  
**Discussion of Financing Options Related to the Top Three Priorities from the**  
**Community Priorities Survey Results and City Council Direction on a Potential**  
**Sales Tax Measure**  
**May 14, 2024**  
**Page 24**

May 28, 2024	1)	Adopt Resolution Calling and giving notice of the November 5, 2024 General Municipal Election
	2)	Adopt Resolution Requesting that the SLO County Board of Supervisors consolidate the City's General Municipal Election with the Statewide General Election (EC 10403);
	3)	Adopt a Resolution adopting regulations for candidates pertaining to candidate statements
	4)	Adopt Resolution ordering the submission to the qualified electors of the city of a certain measure relating to Transaction and Use Tax at the General Municipal Election to be held on Tuesday, November 5, 2024, as called by Resolution No. ____
	5)	Introduce Ordinance – Transaction and Use Tax
	6)	Adopt Resolution setting priorities for filing written arguments regarding measure and directing the City Attorney to prepare an impartial analysis
	7)	Adopt Resolution providing for the filing of rebuttal arguments
June 25, 2024	Adopt Ordinance – Transaction and Use Tax (Required by State Dept of Tax & Administration, but subject to voter approval)	
July 19, 2024	Last Day for Filing Arguments Impartial Analysis for measure due from City Attorney	
July 20 – July 29, 2024	10-day Public Examination Period for Arguments and Impartial Analysis	
July 30, 2024	Last Day to File Rebuttal Arguments	
July 31 – August 9, 2024	10-day Public Examination Period for Rebuttal Arguments	
By August 9, 2024	Last day to file final ballot measure documents (Arguments, Impartial Analysis, with County Clerk/ROV for inclusion voter information guide	

**ALTERNATIVES:**

The following alternatives are provided for the Council's consideration:

1. Receive a presentation regarding Financing Options related to the top three priorities from the Community Survey Results and direct staff to prepare a ballot measure for the November 5, 2024, consolidated election seeking a 1% Local Transaction and Use Tax ("Sales Tax") increase, to be provided at the May 28, 2024, City Council meeting;
2. Receive a presentation regarding Financing Options related to the top three priorities from the Community Survey Results and do not direct staff to prepare a ballot measure for the November 5, 2024, consolidated election seeking a 1% Local Transaction and Use Tax ("Sales Tax") increase; or
3. Provide other direction to staff.

**ADVANTAGES:**

Seeking an additional 1% sales tax will enable the City to significantly increase its investment in existing programs and infrastructure needs. A new 1% sales tax will bring the City on par with the other cities in the County and allow the City to reinvest the



**City Council**

**Discussion of Financing Options Related to the Top Three Priorities from the Community Priorities Survey Results and City Council Direction on a Potential Sales Tax Measure**

**May 14, 2024**

**Page 25**

increased revenue in existing programs and critical infrastructure necessary to safely move goods and services throughout the City. Sales taxes are paid by visitors to the City and not just residents, ensuring that costs are distributed to those who use the City's facilities and services. Increased sales taxes paid by customers within the City will be retained and reinvested within the City, providing a greater benefit to residents and businesses.

**DISADVANTAGES:**

If the voters approve a new 1% sales tax measure, costs for certain goods will increase within the City. Even with the revenue from a new 1% sales tax measure, the City's average PCI is anticipated to remain at current levels or increase only slightly over the course of 15 years. Additional funding sources are still needed to address the City's deferred and ongoing maintenance of existing streets infrastructure.

**ENVIRONMENTAL REVIEW:**

The discussion and direction sought by the City Council as part of this item is not a project subject to the California Environmental Quality Act ("CEQA") because it has no potential to result in either a direct, or reasonably foreseeable indirect, physical change in the environment. (State CEQA Guidelines, §§ 15060, subd. (c)(2)-(3), 15378.)

**PUBLIC NOTIFICATION AND COMMENTS:**

The Agenda was posted at City Hall and on the City's website in accordance with Government Code Section 54954.2.