



MEMORANDUM

TO: City Council

FROM: Whitney McDonald, City Manager
Timothy Carmel, City Attorney
Nicole Valentine, Administrative Services Director

SUBJECT: Consideration of Placing a Local Transactions and Use Tax (“Sales Tax”) Measure on the November 8, 2022 Ballot

DATE: May 24, 2022

SUMMARY OF ACTION:

Adoption of the proposed Resolutions and Introduction of the Proposed Ordinance will enable the voters to determine through the November 8, 2022 General Municipal Election whether to enact a local transactions and use tax (“sales tax”) that would provide general revenue to the City.

IMPACT ON FINANCIAL AND PERSONNEL RESOURCES:

If approved by the voters, the proposed sales tax measure would generate approximately \$5.6 million in additional annual revenue. As a general tax, the proceeds would be deposited into the General Fund and may be used for any lawful purpose, as designated by the City Council, including being allocated towards maintaining the City’s streets, sidewalks, and stormwater infrastructure, as well as for other underfunded City programs and services. Funding for the November 2022 General Municipal Election has been included in the Biennial Budget for Fiscal Years 2021-23 in the amount of \$28,000, and is anticipated to cover costs associated with printing the ballot measure in the Sample Ballot booklet. It is recommended that the City engage the services of a consultant to support public outreach and information regarding the proposed sales tax measure in an amount not to exceed \$25,000, which would be covered through existing consultant services budgets included in the adopted Biennial Budget.

RECOMMENDATION:

1) Adopt the proposed Resolution ordering the submission to the qualified electors of the City a measure relating to the establishment of a local transactions and use tax (hereinafter referred to as a "sales tax") at the General Municipal Election to be held on Tuesday, November 8, 2022, as called by Resolution; 2) Introduce the proposed Ordinance adding Chapter 3.23 to Title 3 of the Arroyo Grande Municipal Code regarding a transactions and use tax; 3) Adopt the proposed Resolution setting priorities for filing a

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written argument regarding a City measure and directing the City Attorney to prepare an impartial analysis of the measure; 4) Adopt the proposed Resolution providing for the filing of rebuttal arguments for City measures submitted at municipal elections; and 5) Approve the argument to be submitted in favor of the measure.

BACKGROUND:

On May 28, 2019, the City Council discussed the City’s revenue and potential opportunities to increase revenue in the face of rising business costs. At that time, the staff report recognized the work of previous assessments of unfunded or severely underfunded needs for core City infrastructure, including pavement (roads and parking lots), sidewalks, drainage facilities, parks, and government buildings (Attachment 9). These assessments indicated that, at the time, the City needed to invest an additional \$2.4 million annually to maintain existing facilities. It was also noted that this investment would still result in a decrease in the pavement condition index (PCI) of the City’s existing street infrastructure over time and that an additional \$1.16 million would be needed to keep the PCI at 70 and avoid larger maintenance costs in the future. Together, these needs totaled over \$3.5 million in unfunded annual infrastructure maintenance in May 2019.

Following discussion on May 28, 2019, Council directed staff to seek more information about community surveys and the ballot measure process for a potential local sales tax increase. Further information was provided regarding community survey options on August 13, 2019, and Council authorized the City Manager to select a professional research firm to conduct a statistically valid voter opinion survey of Arroyo Grande voters. On January 28, 2020, Council received a presentation of the community survey results from True North Research (Attachment 8). The survey conducted by True North Research evaluated community interest in a local (City of Arroyo Grande) sales tax revenue measure. The survey consisted of a statistically valid sample of residents (541 residents were surveyed) to objectively evaluate the viability of passing a local ballot measure and to understand voter’s preferences for the funds raised. The survey found that Arroyo Grande voters, at that time, have a high opinion of the quality of life in the City and that they value the services they receive from the City. Together, according to the survey, these sentiments translated into “solid natural support (57%)” for establishing a one percent local sales tax to provide funding for general City services.

In the survey, when presented with a list of services that could be funded by the sales tax measure, voters were most interested in using the money to:

- Maintain local streets and repair potholes.
- Repair and maintain public buildings and infrastructure including sidewalks, curbs, flood prevention infrastructure, and storm drains.
- Maintain parks and recreation facilities including Soto Sports complex, courts, fields, playgrounds, and community centers.

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- Provide fire protection and emergency medical response services, including police patrols, drug and crime prevention, fire, emergency medical, and 9-1-1 emergency response.
- Maintain street, sidewalk, and pothole maintenance.
- Address impacts from homelessness.
- Maintain parks, recreation, childcare, and senior programs.

At its June 23, 2020 meeting, the City Council received a comprehensive presentation regarding a proposed revenue measure to address the City’s future funding needs and provided direction to staff to prepare a proposed 1% (increasing from 7.75% to 8.75%) local sales tax revenue measure for the November 3, 2020 ballot (Attachment 7). On July 14, 2020, the City Council considered placing the Local Transaction and Use Tax Measure on the November 3, 2020 Ballot. Extensive Council discussion ensued and, ultimately, Council did not direct pursuit of a measure at that time, primarily due to the unknown financial impacts on the City’s residents as a result of the COVID-19 pandemic.

On April 27, 2021, the City Council considered and established goals and priorities for incorporation into the upcoming Biennial Budget. The adopted goals and priorities were included within the Fiscal Years 2021-23 Biennial Budget and addressed three broad categories:

- Investing in the Future
- Investing in City Infrastructure and Facilities
- Investing in People.

Within the “Investing in City Infrastructure and Facilities” category, an item was included to “identify and pursue short- and long-term funding mechanisms, such as a sales tax measure, for pavement maintenance and other infrastructure maintenance needs.”

At its April 26, 2022 meeting, the City Council received a comprehensive report and presentation regarding the City’s pavement, sidewalk, and stormwater infrastructure maintenance needs and options for financing those needs, including a potential general revenue sales tax measure. (Attachment 6). As explained in the staff report, in February 2022, the City contracted with Pavement Engineering Inc. (PEI) to update the City’s Pavement Management System. The final report was received on April 21, 2022, and presented to the City Council at its April 26, 2022 meeting.

The City currently maintains approximately 67.5 centerline miles of roads representing 13,922,291 square feet of pavement with a replacement value of approximately \$313,566,000 as calculated by StreetSaver. The City has a comprehensive Pavement Management Plan (PMP) and, on February 14, 2017, the City Council endorsed the “Critical Point Management” methodology for the City’s Pavement Management System (PMS). The Critical Point Strategy approach selects the road segments for repair or resurfacing that are at a “critical point” of deterioration. The critical point is a point located

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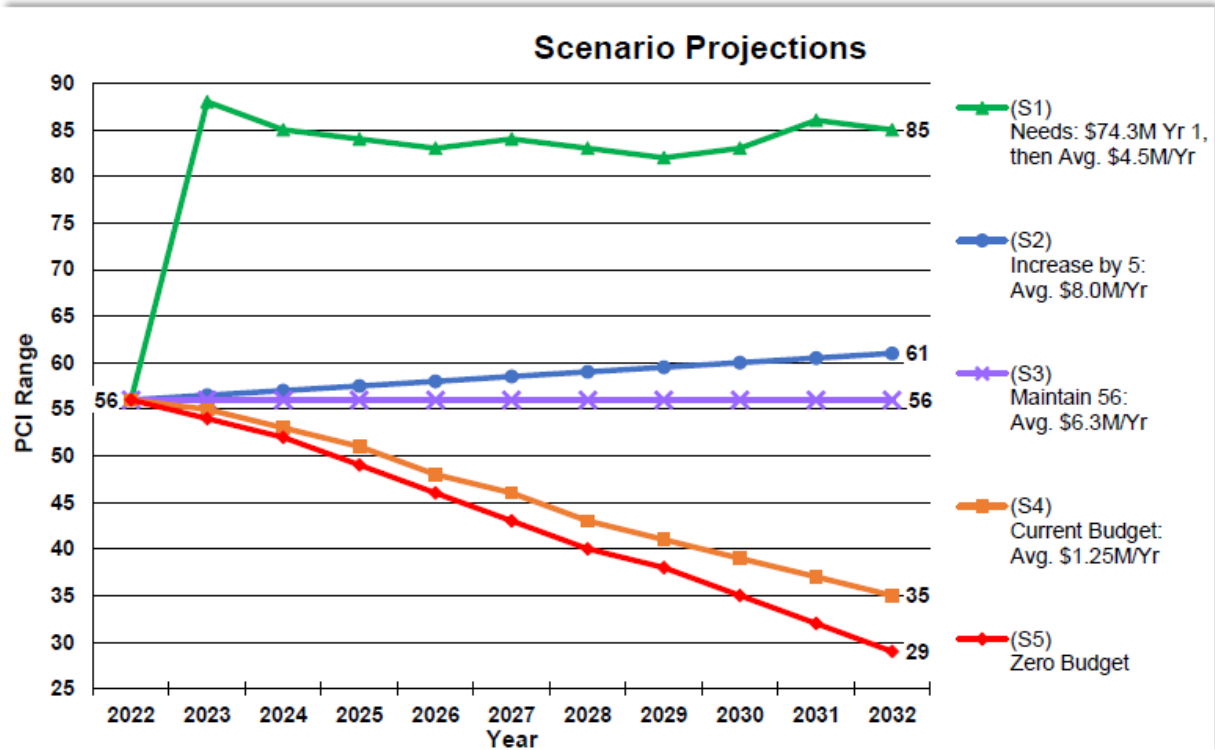
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on the pavement deterioration graph which indicates the Pavement Condition Index (PCI) value is about to drop to a level which would trigger a more expensive maintenance or rehabilitation approach. The Critical Point Strategy is a long-range methodology that maintains and improves roadways before they slip into a PCI range that reflects costlier repairs.

As reported in the 2022 Pavement Management Program Update, despite past efforts, the condition of the City’s streets has declined. On a pavement condition scale of 0 to 100, the City’s streets now rank an average PCI of 56, down from an average PCI of 69 in 2016. As explained in the April 26, 2022 staff report, in order to maintain an overall PCI of “Fair” (PCI range of 51 to 70), approximately \$6.25 million is needed annually to maintain the City’s current pavement PCI. However, the City has historically only been able to allocate approximately \$1.25 million annually to pavement maintenance from its existing revenue sources.

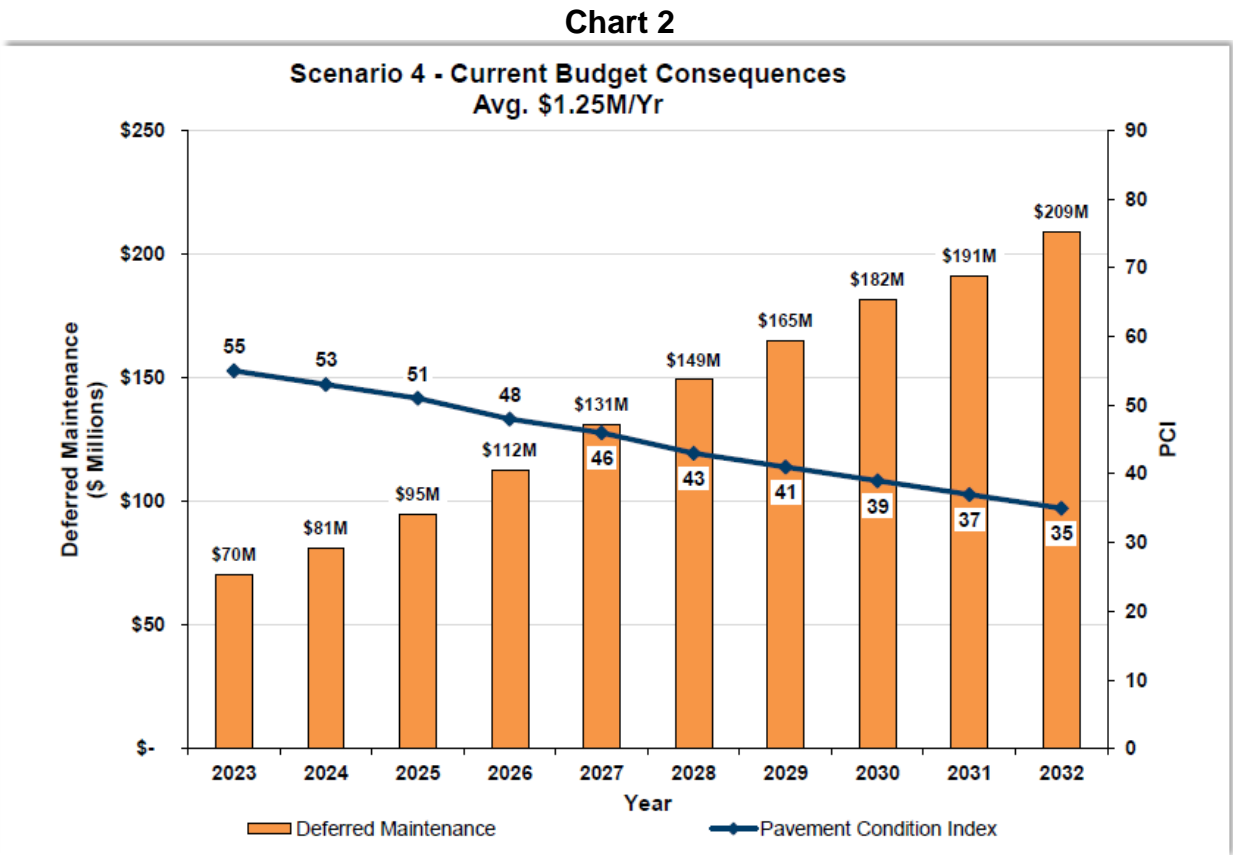
PEI generated five (5) scenario projections of future pavement conditions in the City and the costs to obtain and maintain those conditions over the course of ten years, which were presented in the April 26, 2022 staff report as follows:

Chart 1



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At the current funding level of \$1.25M/Yr., it is predicted the PCI of the entire system will continue to deteriorate from 56 to 35, a 21 PCI point drop over the next 10 years, and the backlog of deferred maintenance will grow from \$70 million to \$209 million, an increase of 197%. A PCI of 35 falls within the Poor Condition category. An example of a 35 PCI is Brighton Avenue, between Courtland and North Elm Street. 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. The outcome of this situation was depicted in the April 26, 2022 staff report as follows:



Funding for the City’s annual street repairs program is provided through a combination of state, regional, and local funding sources, including local sales tax revenue. In 2006, Arroyo Grande voters approved Measure O-06, creating a half percent local transactions and use tax and bringing the overall sales tax rate in Arroyo Grande to 7.75%. This half cent sales tax currently generates approximately \$2.5 million annually. The revenue from this measure has been used to fund street and park improvements, public safety services, drainage improvements, City facilities, and transportation projects. To ensure

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accountability, Measure O-06 required: 1) the City to publish and distribute an annual report to each household on the revenues and expenditures from the sales tax proceeds; and 2) a review and public hearing by the City Council every five years to determine whether the sales tax is necessary to remain in effect. The City has completed these steps since Measure O-06 was approved and went into effect in April 2007. The most recent 5-year report covering the period of July 2016 through June 2021 and the public hearing to consider continuation of the local sales tax will be conducted at the May 24, 2022 City Council meeting (the same date as this item).

Based on the identified needs and current funding sources available to the City for its pavement maintenance, it was explained in the April 26, 2022 staff report that 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.

Additionally, the April 26, 2022 report described ongoing and deferred maintenance needs for the City's sidewalks and stormwater infrastructure. In 2016, City Public Works staff completed a deferred maintenance assessment that identified each sidewalk segment in need of repair and estimated a total cost of \$1,346,250 to repair all sidewalk defects in the City. Since 2016, the City has been able to allocate an average of \$120,000 annually to sidewalk repairs. Funding for sidewalk repairs is provided almost entirely from local sales tax revenue, with occasional funds (e.g. up to \$50,000 in FY 2018-19) provided by regional State Highway Account (SHA) grant.

Similarly, stormwater infrastructure repairs are not paid for through the City's Water and Wastewater Enterprise Funds and have, instead, been funded through the CIP Budget using local sales tax revenue. The City's existing stormwater infrastructure requires constant repair, replacement, and maintenance. According to a 2016 assessment of the City's existing drainage facilities, \$238,000 is needed annually to complete necessary improvements to avoid costly failures and areas of flooding. On average, the City has been able to allocate \$100,000 to these improvements. Additionally, the City has approximately 2.57 miles of existing corrugated metal pipe (CMP) facilities, which are aging and will require lining or replacement before they fail. It is estimated that lining of the City's existing CMPs will cost approximately \$4 million. Although the City has allocated \$500,000 in American Rescue Plan Act funding toward CMP lining, it is anticipated that an additional \$3.5 million is needed to complete the lining. The April 26, 2022 staff report explained that revenue from a new sales tax measure will enable the City to better fund these needed improvements.

Staff's presentation provided during the April 26, 2022 discussion also included a description of the distinction between a special tax and a general revenue tax. While a general revenue measure raises revenue for general government purposes and is subject to a majority (50% +1) vote for approval, a special tax earmarks the funding for a specific or single purpose and is subject to a 2/3rds (66.66%) vote for approval. According to

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information provided by California City Finance, results of 2020 local sales tax measures in California included the following:

- 14 City Special Tax Measures – 6 passed (42.8% passage rate)
- 132 City General Tax Measures – 108 passed (82.8% passage rate)

By comparison, Measure O-06 passed with 50.11% approval. It was noted that significant assistance from the public would be needed to advocate for passage of a special tax to meet the 2/3rds approval threshold.

Additionally, staff recommended that a potential new 1% sales tax measure include the following provisions that provide accountability and transparency, consistent with the practices included in Measure O-06:

- Publication of an Annual Local Sales Tax Allocation Report
- Public hearing to determine ongoing necessity for the tax every 5 years

Following consideration and discussion of the presentation on April 26, 2022, the City Council provided direction to staff to prepare a proposed 1% (increasing from 7.75% to 8.75%) local sales tax revenue measure for the November 8, 2022 ballot.

ANALYSIS OF ISSUES:

The City Council has received information and discussed the City’s revenue and potential opportunities to increase revenue in the face of rising costs. The revenue from a new 1% local sales tax measure would be deposited into the General Fund and may be used for any lawful purpose, as designated by the City Council, and may be allocated towards maintaining the City’s streets, sidewalks, and stormwater infrastructure, as well as for other City programs and services. If approved, the proposed sales tax measure would generate approximately \$5.6 million annually and is intended to augment the existing Measure O-06 local sales tax fund created in 2006. City staff met recently with HdL, the City’s Sales Tax Consultant, to review the October through December 2021 actual sales tax revenues received and to discuss projections for the remaining fiscal year. HdL provided Measure O-06 projections for FY 2021-22, which are now expected to be \$2,797,000. With this updated information, City staff have included language in the proposed measure to reflect an estimated \$5.6 million ($\$2,797,000 \times 2 = \$5,594,000$) in additional revenue to the City if the voters approve the measure. This updated estimate is an increase of \$600,000 compared to the total anticipated revenue discussed at the April 26, 2022 Council Meeting.

Funding received from a new sales tax measure would allow the City to expand its increasingly underfunded Capital Improvement Projects (CIP) and public facility maintenance funds including the City’s Annual Street Repairs Program, Annual Concrete (Sidewalks) Repairs Program, and maintenance of storm water and drainage systems, as well as provide funds for other City programs and facilities.

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The potential additional funding for these important annual projects would result in more miles of street rehabilitation, more sidewalk repairs and more rehabilitation of aging storm drain piping.

Structure of the Sales Tax Measure

Following discussion at the April 26, 2022 meeting, the Council provided feedback and direction regarding a proposed 1% general sales tax measure to address the City’s future funding needs for critical City infrastructure, including maintenance and repair of streets, sidewalks, potholes, stormwater and drainage facilities, as well as other underfunded City programs and facilities.

In order to place a tax measure on the November 8, 2022 ballot, a 2/3 vote of the City Council (at least 4 members) must approve the proposed Resolutions and Ordinance. Revenue and Taxation Code Section 7285.9 authorizes the City to increase a transactions and use tax for general purposes, and provides that the ordinance proposing the tax is to be approved by a two-thirds vote of all members of that governing body and the tax also has to be approved by a majority vote of the qualified voters of the City voting in an election on the issue. Likewise, for general taxes, Government Code Section 53724(b) provides that the ordinance or resolution proposing the tax has to be approved by a 2/3rd vote of the legislative body.

The proposed measure includes provisions for citizen review of reported revenue and expenditures to establish accountability and transparency, which is important when structuring government operations to maintain trust and efficiency. First, consistent with Measure O-06 funds, the measure will require the City to mail to every household an annual report of prior year expenditures and proposed expenditure of the additional sales tax proceeds for the following year. Second, the City Council will be required to conduct a review and public hearing every five (5) years to determine if the sales tax is still necessary. If other funding sources became available to replace the sales tax revenue, the City Council would have the authority to reduce or eliminate the local sales tax amount.

Ballot language has also been prepared to comply with the requirements of law. Elections Code Section 13119(b) and (c) provides as follows:

(b) If the proposed measure imposes a tax or raises the rate of a tax, the ballot shall include in the statement of the measure to be voted on the amount of money to be raised annually and the rate and duration of the tax to be levied.

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(c) The statement of the measure shall be a true and impartial synopsis of the purpose of the proposed measure, and shall be in language that is neither argumentative nor likely to create prejudice for or against the measure.

Accordingly, the following language has been developed for the ballot measure, which is also limited to only 75 words:

To provide funding for general governmental use in Arroyo Grande, including maintenance and repair of streets, sidewalks, stormwater and drainage facilities, and for other City programs and facilities, shall an ordinance establishing a one percent sales tax be adopted, providing approximately \$5,600,000 annually until ended by the City Council and requiring annual reports on revenues and expenditures, and review and public hearing by the City Council every five years on its necessity?

The proposed Ordinance, Resolutions, and Ballot Argument have been prepared and are included with this report for consideration (Attachments 1-5). It is recommended the Council introduce the Ordinance, adopt the Resolutions, and approve the Ballot Argument as presented for placement on the November 8, 2022 ballot. It should be noted that, if successfully introduced, the Ordinance will be considered for adoption at the June 14, 2022 City Council meeting.

ALTERNATIVES:

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

1. Adopt the Resolutions, introduce the Ordinance, and approve the Ballot Argument pertaining to the placement of a ballot measure on the November 8, 2022 ballot;
2. Modify and adopt the Resolutions and introduce the Ordinance and/or make changes to and approve the Ballot Argument; or
3. Provide other direction to staff.

ADVANTAGES:

Adoption of the proposed Resolutions and Ordinance, and approval of the Ballot Argument will meet the provisions required by the California Elections, Revenue and Taxation, and Government Codes for submitting to the voters a measure relating to the establishment of a local sales tax in the City.

DISADVANTAGES:

There are no identified disadvantages related to proposed actions as they are required by State law in order to place a measure on the ballot.

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ENVIRONMENTAL REVIEW:

No environmental review is required for this item.

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. A notice regarding the placement of a measure on the November 2022 ballot will be published pursuant to the timeline prescribed by the Elections Code.

Attachments:

1. Proposed Resolution – Ordering the Submission to Electors
2. Proposed Ordinance
3. Proposed Resolution – Setting Priorities for Filing Arguments
4. Proposed Resolution – Filing of Rebuttal Arguments
5. Proposed Argument in Favor of Measure
6. April 26, 2022 Staff Report and Attachments
7. June 23, 2020 Staff Report and Attachments
8. January 28, 2020 Staff Report and Attachments
9. May 28, 2019 Staff Report and Attachments