A Municipal Finance Update
Municipal Finance Institute
December 2014

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CaliforniaCityFinance.com  The California Local Government Finance Almanac
The State of the State:
A City View of the 2014-15 State Budget
Historical Composition of State General Fund Revenues

Source: LAO
2014-15 Budget State General Fund and Realignment Fund Revenue

- Personal Income Tax, $72,201, 59%
- Corporation Tax, $9,482, 8%
- Insurance Tax, $2,435, 2%
- Vehicle License Fee, $2,071, 2%
- Realignment Sales Tax, $9,569, 8%
- Other/Transfers, $2,050, 2%
- Sales & Use Tax, $23,420, 19%
- Source: LAO, Dept of Finance

- Big Three Revenues Up 7.9% (PIT, CUT, CIT)
- Overall Gen Fund Revenues up 5.1%
- But some is one time
- LAO projects 3.7% revenue growth for FY2015-16
Proposition 30 Temporary Revenues

Will There be a Revenue Cliff?

<table>
<thead>
<tr>
<th>Year</th>
<th>Personal Income Tax</th>
<th>Sales and Use Tax</th>
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<tbody>
<tr>
<td>2011-12</td>
<td>$3</td>
<td>$0</td>
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<tr>
<td>2012-13</td>
<td>$4</td>
<td>$1</td>
</tr>
<tr>
<td>2013-14</td>
<td>$5</td>
<td>$2</td>
</tr>
<tr>
<td>2014-15</td>
<td>$5</td>
<td>$1</td>
</tr>
<tr>
<td>2015-16</td>
<td>$5</td>
<td>$1</td>
</tr>
<tr>
<td>2016-17</td>
<td>$5</td>
<td>$1</td>
</tr>
<tr>
<td>2017-18</td>
<td>$6</td>
<td>$0</td>
</tr>
<tr>
<td>2018-19</td>
<td>$4</td>
<td>$2</td>
</tr>
<tr>
<td>2019-20</td>
<td>$3</td>
<td>$0</td>
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</table>
California’s Big Three Revenues
Personal Income Taxes, Sales Taxes, Corporate Taxes

![Bar chart showing revenue for personal income tax, sales and use tax, and corporation tax from 2013-14 to 2019-20.]

- **Personal income tax**
- **Sales and use tax**
- **Corporation tax**

- **Prop30 Temporary Sales Tax**
- **Prop30 Temporary PersIncTax**

The chart illustrates the revenue for each tax category over the years, with a recent shift indicating the impact of Proposition 30.
2014-15 Budget
State General Fund and
Realignment Fund Spending

- Health & Human Svcs: $29,162
- K-14 Education Prop98: $46,548
- Mental Health, Support Svcs: $9,330
- Corrections: $9,073
- Law Enforcement, Trial Court: $2,296
- UC/CSU/Student Aid: $8,056
- ERB Payment: $1,606
- Legisl Judicial Exec: $1,392
- CalSTRS: $1,486
- Infrastructure Debt: $5,446
- Resources & Environment: $7,517

Source: LAO, Dept of Finance
Historical State Spending by Program Area
General Fund and Special Funds - as a % of Calif Personal Income

**Health and Human Services**

- Prop13

**K-12 Education**

- Prop13

**Transportation**

**Corrections**

Source: LAO
California’s Fiscal Outlook

Risks

- Threat of Recession. It’s inevitable.
- Federal Challenges
  - + 2 year delay in prison cap OK
  - + Avoided debt ceiling problems
- Health Care Costs. Medi-Cal is budget’s 2nd largest program.
- Natural Disasters: draught, fires, flood, earthquake.
- Debts and Liabilities. In addition to budgetary debt:
  - $218 billion state retirement-related unfunded liabilities
  - $65 billion deferred maintenance
  - $9 billion unemployment insurance
- Capital Gains (10% of General Fund tax revenues) volatile, affected by stock market behavior.
2014-15 State Budget Highlights

- Economic Recovery Bonds paid off by end of 2014-15
- Pay down operating budget debt by $10.6 billion
  - Additional $1.8 billion paydown to schools and city/county mandate costs owed if revenues exceed forecast. To be determined in May 2015.
- Initiates plan to address CalSTRS unfunded liabilities
- Increases K-12 education funding 10% over 2013-14
- Infrastructure Investments: $1.2 billion

2014-15 Approved State Budget General Fund Budget Summary

<table>
<thead>
<tr>
<th></th>
<th>2013-14</th>
<th>2014-15</th>
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<tbody>
<tr>
<td><strong>Resources</strong></td>
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<tr>
<td>Prior Year Balance</td>
<td>$2,429</td>
<td>$3,905</td>
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<td>Revenues and Transfers</td>
<td>$102,185</td>
<td>$105,488</td>
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<td>Total Resources Available</td>
<td>$104,614</td>
<td>$109,391</td>
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<td><strong>Expenditures</strong></td>
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<tr>
<td>Non-Proposition 98 Expenditures</td>
<td>$57,980</td>
<td>$63,526</td>
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<td>Proposition 98 Expenditures</td>
<td>$42,731</td>
<td>$44,462</td>
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<td>Total Expenditures</td>
<td>$100,711</td>
<td>$107,988</td>
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### Eliminating the “Wall of Debt”

<table>
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<tbody>
<tr>
<td>Deferred payments to schools and community colleges</td>
<td>$10.4</td>
<td>$6.4</td>
<td>$6.1</td>
<td>$0.0</td>
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<td>Economic Recovery Bonds</td>
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<td>5.2</td>
<td>3.9</td>
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<td>Loans from Special Funds</td>
<td>5.1</td>
<td>4.9</td>
<td>3.9</td>
<td>2.9</td>
<td>0.0</td>
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<td>Unpaid mandated costs to local govts, schools, colleges</td>
<td>4.3</td>
<td>4.9</td>
<td>5.4</td>
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<td>Underfunding of Proposition 98</td>
<td>3.0</td>
<td>2.4</td>
<td>2.4</td>
<td>1.8</td>
<td>0.0</td>
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<tr>
<td>Borrowing from local governments (Proposition 1A)</td>
<td>1.9</td>
<td>1.1</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
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<tr>
<td>Deferred Medi-Cal Costs</td>
<td>1.2</td>
<td>2.0</td>
<td>1.8</td>
<td>1.7</td>
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<td>Deferral of state payroll costs from June to July</td>
<td>0.8</td>
<td>0.7</td>
<td>0.8</td>
<td>0.8</td>
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<td>Deferred payments to CalPERS</td>
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<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
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<td>Borrowing from transportation funds (Proposition 42)</td>
<td>0.4</td>
<td>0.4</td>
<td>0.2</td>
<td>0.1</td>
<td>0.0</td>
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<td><strong>Total</strong></td>
<td><strong>$34.7</strong></td>
<td><strong>$28.2</strong></td>
<td><strong>$24.9</strong></td>
<td><strong>$13.1</strong></td>
<td><strong>$0.0</strong></td>
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</table>

For FY2014-15...

- Pay down remainder of school deferrals: $6.2 billion
- Pay off Economic Recovery Bonds early: $1.6 billion
- Repay special funds: $1.6 billion
Local Government Issues in the 2014-15 State Budget

Mandate cost reimbursement. $100 million toward paying down the $900 million owed to counties, cities and special districts for pre-2004 mandate claims. Full payment due by 2021.

- $73 million counties, $25 million cities, $2 million special districts
- Specific allocation to be determined (State Dept of Finance, State Controller)
- Up to $800 million additional repayment if revenues come in above adopted estimates. To be determined in 2015 May revision.

Local mandates once again made “optional” so as to avoid costs.

- Public Records Act, Open Meetings Act are now mandatory but not reimbursable due to voter approved state measures (Prop 42, Prop 30).
- Local Agency Ethics Training mandate was NOT suspended.
Local Government Issues in the 2014-15 State Budget

- **Municipal Law Enforcement grants** to $40 million** from $27.5 million (began in 2012 with Prop30)
- State law enforcement grant program continued. 
  *(funded since 2011 from VLF shifted from cities)*
  - COPS Frontline Law Enforcement at same level (SLESA)
  - Jail Detention Facility Grants (in lieu of booking fees)
- **Highway Users Tax (HUTA)** +$242 million including
  - $100 million loan repayment (of $337m) +$142 million (Str&Hwy§§2104-2107)
  - Half to counties, half to cities ($121 million) on population (Str&Hwy§2105)
- Multi-Family Housing grants. $100 million
- Cap & Trade: $872 million
Proposition 2 (2014) Reserves

Key Components

- Annual required deposit
  - 1.5% of General Fund Revenues plus
  - Capital gains income tax revenues over 8.0% of annual General Fund revenues

- Use half to pay down debt
  - Half must remain in “rainy day” account

- Increases Budget Stabilization Account (BSA) target to 10%

- Limits ability to suspend contributions or make withdrawals from BSA
Municipal Revenues in Moderate Recovery

Property Tax Revenues - Cities

Source: Computations by Michael Coleman from data from CA State Board of Equalization (revenues), CA Dept of Finance (Population), CA Dept of Industrial Relations (CPI)
Municipal Revenues in Moderate Recovery
Sales Tax Collections

Source: California State Board of Equalization (Sales Tax), CA Dept of Finance (Population), CA Dept of Industrial Relations (CPI)
The Cost of Doing Business

CalPERS Payments on the Rise

Average Employer Contribution Payments

Percentage of Payroll

Average Annual Employer Contribution Percentage of Payroll


Safety (police, fire) plans

Miscellaneous plans
The Cost of Doing Business
CalPERS Payments on the Rise

Projected CalPERS Employer Contribution Payments

Example City #1

Police and Fire
3% @ 50

Miscellaneous
2.5% @ 55

Rates up half again or double since 2009

Source: Bartel Associates
The Cost of Doing Business
CalPERS Payments on the Rise

Projected CalPERS Employer Contribution Payments

Example City #2

Source: Bartel Associates
The Cost of Doing Business
CalPERS Payments on the Rise

Employer Contribution Forecasts Have Changed

Safety (Police and Fire) Plan
Employer Contribution Rates

Source: City of Woodland
The Cost of Doing Business
CalPERS Payments on the Rise

Employer Contribution Forecasts Have Changed

MISCELLANEOUS Plan
Employer Contribution Rates

Source: City of Woodland
The Cost of Doing Business

Retiree Health Care Costs & other OPEB*

huge unfunded liabilities for many agencies

➢ Number of retirees continues to rise
➢ Retirees living longer
➢ Healthcare costs continue to rise

Alameda County Cities 2013 Task Force Study
✓ OPEB liabilities are often unfunded
✓ Unfunded liabilities are 7% to 140% of General Fund
✓ Among the 14 Alameda County cities
✓ OPEB* costs increased 45% over 5 years (2008-2013)

*Other Post Employment Benefits
Going to the Local Voters

- School Bond, 112
- City General Tax, 88
- City Parcel or Special Tax, 21
- Special District G.O.Bond, 2
- County G.O.Bond, 1
- Special District Tax, 19
- County Parcel or Special Tax, 8
- School Parcel Tax, 8
- School Bond 2/3, 1

55% Vote

2/3 Vote

Majority Vote

- Record 268 local tax and bond measures
- 113 School bonds totaling $11.7 Billion
- 90 pass = $9.2 Billion

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# Going to the Local Voters

## Local Revenue Measures November 2014

<table>
<thead>
<tr>
<th>Measure</th>
<th>Total</th>
<th>Pass</th>
<th>Passing%</th>
</tr>
</thead>
<tbody>
<tr>
<td>City General Tax (Majority Vote)</td>
<td>88</td>
<td>61</td>
<td>69%</td>
</tr>
<tr>
<td>County General Tax (Majority Vote)</td>
<td>6</td>
<td>2</td>
<td>33%</td>
</tr>
<tr>
<td>City Special Tax or G.O. bond (2/3 Vote)</td>
<td>23</td>
<td>14</td>
<td>61%</td>
</tr>
<tr>
<td>County Spec. Tax, G.O. bond (2/3 Vote)</td>
<td>9</td>
<td>4</td>
<td>44%</td>
</tr>
<tr>
<td>Special District 2/3</td>
<td>21</td>
<td>10</td>
<td>48%</td>
</tr>
<tr>
<td>School Parcel Tax 2/3</td>
<td>8</td>
<td>8</td>
<td>100%</td>
</tr>
<tr>
<td>School Bond 2/3</td>
<td>1</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>School Bond 55%</td>
<td>112</td>
<td>90</td>
<td>80%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>268</strong></td>
<td><strong>189</strong></td>
<td><strong>71%</strong></td>
</tr>
</tbody>
</table>
Going to the Local Voters

- SalesTax MajVote: 32 Passing, 10 Failing
- ParcelTax 2/3vote: 20 Passing, 13 Failing
- BusinessTax: 14 Passing, 6 Failing
- UtilityUsersTax MajVote: 11 Passing, 4 Failing
- HotelTax MajVote: 4 Passing, 10 Failing
- SalesTax 2/3vote: 5 Passing, 8 Failing
- G.O. Bond 2/3vote: 3 Passing, 8 Failing
- PropTransf Tax MajVote: 1 Passing, 1 Failing
- $1AbandonedVehTax2/3: 1 Passing, 1 Failing
- UtilityUsersTax 2/3 vote: 1 Passing, 1 Failing
Bad Brew in Troubled Cities

- Over-reliance on land development revenue
- Over-reliance on redevelopment revenues
- Risky financing schemes
- Unsustainable and Intractable employee compensation, especially public safety pension and retiree health care
- Unsustainable Decline in Core Revenues
- Ceding of management and policy choices to others
- Fear & Denial
- Toxic relationships
Are Incorporations and Annexations Extinct?

Pernicious Effects of the VLF-Property Tax Swap of 2004
The VLF-Property Tax Swap of 2004

VLF Backfill

$4.4 b*

Cities & Counties

Property Tax in Lieu of VLF

$4.4 b

State General Fund

$4.4 b

Schools

* in FY2004-05
The Lack of VLF Replacement Makes New Cities Fiscally Unviable

City of Jurupa Valley General Fund

- VLF: "Bump" declines to zero over 5 yrs
- Swapped for PropTax in 2004
- If incorporated before 2004 swap
- After Swap
- Actual (after SB89 shift)

- SalesTax
- Property Tax
- Franchise Fees
- Licenses/Permits

$0.0 $5.0 $10.0 $15.0 $20.0 $25.0 $30.0

- $0.0
- $5.0
- $10.0
- $15.0
- $20.0
- $25.0
- $30.0

Denied PropTax-in-lieu-of-VLF that all other cities get
The Lack of VLF Replacement Makes many Annexations Fiscally Unviable

Annexation of Inhabited Area

VLF

Swapped for PropTax in 2004

VLF AB1602 Special

VLF

VLF

Denied PropTax-in-lieu-of-VLF that all other areas of city get

 Millions

$1.8

$1.6

$1.4

$1.2

$1.0

$0.8

$0.6

$0.4

$0.2

$0.0

If incorporated before 2004 swap

w/AB1602 VLF patch (assumed in annex process)

Actual (after SB89 shift)