ALAMEDA-CONTRA COSTA TRANSIT DISTRICT

STAFF REPORT

MEETING DATE: 9/23/2020 **Staff Report No.** 20-370

TO:	**AC Transit Board of Directors**
FROM:	**Michael A. Hursh, General Manager**
SUBJECT:	**Resolution in Support of Schools and Local Communities Funding Act**

ACTION ITEM

RECOMMENDED ACTION(S):

Consider adoption of Resolution No. 20-048 in support of Schools and Local Communities Funding Act (Proposition 15). [Requested by Vice President Ortiz - 9/9/20]

STRATEGIC IMPORTANCE:

Goal - Financial Stability and Resiliency
Initiative - Financial Efficiency and Revenue Maximization

The resolution in support of Schools and Local Communities Funding Act (Proposition 15) is intended to provide formal support for a measure that potentially provides additional revenues for the District.

BUDGETARY/FISCAL IMPACT:

The Schools and Communities First Initiative have estimated that Proposition 15 could generate up to $29 million annually for the District. Staff is not able to independently verify that number due to the complicated nature of commercial property tax valuation and revenue distribution. Using relative shares and increases based on county-level property tax information, staff calculated an increase of at least $10 million and up to $18 million annually.

In addition, the measure specifies that the legislature identify a phase-in period of at least two years starting in FY 2022-23. Properties with majority small business occupancy would have the new valuation deferred until at least FY 2025-26. Based on these milestones, staff estimates the District would not see additional revenue until FY 2023-24, with the amount rising over the following few or more years.

BACKGROUND/RATIONALE:

Market assessment of commercial property valuation would increase property tax revenues. Upon full implementation, the measure's shift of most commercial and industrial properties to market value assessment could increase annual property taxes paid for these properties by $8 billion to $12.5 billion. The amount of revenue raised in a given year would depend heavily on the strength of the state's real estate markets, since the commercial property valuation is based on market value. As a result, this new revenue stream would fluctuate more from year to year than property tax revenues have historically.

Current Conditions

Local Governments Levy Taxes on Property Owners. California local governments-cities, counties, schools, and special districts-levy property taxes on property owners based on the value of their property. Taxed properties include real property-land and buildings-and business personal property-machinery, computers, and office equipment. Property taxes raise around $65 billion annually for local governments, about $2 billion of which is attributable to business personal property. Statewide, about 60 percent of property tax revenue is allocated to cities, counties, and special districts, while the remaining 40 percent is allocated to schools and community colleges.

Counties Administer the Property Tax. County assessors determine the taxable value of property, county tax collectors bill property owners, and county auditors distribute the revenue among local governments. Statewide, county spending for property tax administration exceeds $600 million each year.

Property Taxes Are Based on a Property's Purchase Price. Each property owner's annual property tax bill is equal to the taxable value of their property multiplied by their property tax rate. Property tax rates are capped at 1 percent plus smaller voter-approved rates to finance local infrastructure. A property's taxable value generally is based on its purchase price. When a property is purchased, the county assessor assigns a value to the property-often its purchase price. Each year thereafter, the property's taxable value increases by 2 percent or the rate of inflation, whichever is lower. This process continues until the property is sold and again is taxed at its purchase price. In most years, the market value of most properties grows faster than 2 percent per year. As a result, under this system the taxable value of most properties is less than their market value.

California Taxes Individual Income and Corporate Profits. California levies a personal income tax (PIT) on the income of state residents, as well as the income of nonresidents derived from California sources. California also levies a corporation tax on the profits of corporations.

Property Owners Can Deduct Property Tax Payments from Taxable Income. State law allows property owners to deduct property tax payments from their taxable income for the purposes of calculating PIT and corporation tax payments. This reduces their tax bills.

State Constitution Governs State Spending on Schools and Community Colleges. The State Constitution requires the state to provide a minimum amount of annual funding for schools and community colleges, known as the "minimum guarantee." The minimum guarantee tends to grow with the economy and number of students.

Proposal for Schools and Local Communities Funding Act (Proposition 15).

Assess Commercial and Industrial Property at Market Value. The measure requires commercial and industrial properties, as well as vacant land not intended for housing, commercial agriculture, or protected open space to be taxed based on their market value, as opposed to their purchase price. A property's market value is what it could be sold for today. The measure's shift to market value assessment is phased in over a number of years beginning in 2022-23. For properties in which the majority of space is occupied by small businesses-defined as businesses that own California property and have 50 or fewer employees-the shift to market value taxation would not begin until 2025-26 or a later date set by the Legislature.

Properties owned by individuals or businesses whose property holdings in the state total less than $3 million (adjusted for inflation biannually beginning in 2025) are exempt from market value taxation. These properties would continue to be taxed based on purchase price. Similarly, residential properties would continue to be taxed based on purchase price.

Exempt Lower Value Business Personal Property. The measure exempts from taxation the first $500,000 in value of a business's personal property. Additionally, the measure exempts from taxation all personal property of small businesses-as defined above.

Allocate New Revenues to Local Governments and Schools. The measure allocates most new revenue resulting from the measure to cities, counties, special districts, and schools. Before allocating funds to local governments, the measure requires a portion of the new revenues be allocated to (1) the state general fund to compensate for any reductions in PIT and corporation tax revenue resulting from the measure (as discussed below) and (2) counties to cover their costs of administering the measure. Of the remaining funds, roughly 60 percent is allocated to cities, counties, and special district, with each entity receiving an amount proportional to the share of property tax revenues in their county that they receive under existing law. The remaining roughly 40 percent would be allocated to schools and community colleges generally according to the same per -pupil formulas the state uses to distribute most other funding for these entities. This allocation would supplement the existing funds schools and community colleges receive under the state's constitutional minimum funding requirement.

Fiscal Effect

Business Personal Property Exemption Would Decrease Property Tax Revenues. The measure's new business personal property exemptions likely would reduce property tax revenues by several hundred million dollars per year.

Allocation of Net Increase in Property Tax Revenues. On net, after the aforementioned exemptions, the measure would increase statewide property tax revenue by $7.5 billion to $12 billion annually in most years. From this revenue, the measure first allocates funding to cover:

- **Decreased Income Tax Revenues.** By increasing property tax payments for commercial and industrial properties, the measure would decrease taxable personal and corporate income and, in turn, decrease state PIT and corporate tax revenues. This decrease in PIT and corporate tax revenues could be as much as several hundred million dollars annually.

- **Increased County Costs for Property Tax Administration.** The measure creates significant new administrative responsibilities for counties, particularly county assessors. These new responsibilities could increase county property tax administration costs by hundreds of millions of dollars per year ongoing.

Of the remaining $6.5 billion to $11.5 billion, roughly 60 percent would be allocated to cities, counties, and special districts and roughly 40 percent to schools and community colleges.

Short-Term General Fund Costs. Counties likely will incur administrative costs related to the measure before new revenue is available to cover their costs. The measure requires the state to provide loans to counties to cover these initial costs-possibly in the hundreds of millions of dollars-until new revenue is available, at which time the state loans would be repaid.

ADVANTAGES/DISADVANTAGES:

Advantages: Adopting a resolution in support of Schools and Local Communities Funding Act (Proposition 15) would provide formal support to the measure, which could provide approximately $10 - $18 million annually to the District.

Disadvantages: There are no foreseen disadvantages of adopting a resolution in support of Schools and Local Communities Funding Act (Proposition 15).

ALTERNATIVES ANALYSIS:

The AC Transit Board of Directors could choose not to adopt the resolution.

PRIOR RELEVANT BOARD ACTION/POLICIES:

None

ATTACHMENTS:

1. Resolution
2. Full Text of Proposition 15
3. Proposition 15 Fact Sheet

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