CITY OF
LONG BEACH

Office of the City Manager
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June 11, 2024

Honorable Mayor and City Council
City of Long Beach
California

RECOMMENDATION:

> Recommendation to receive and file a presentation regarding research on potential revenue measures and receive direction from the Mayor and the City Council regarding the placement of revenue measures on the November 2024 ballot. (Citywide)

DISCUSSION

The City of Long Beach (City) is facing tough future financial realities which will need to be addressed. State and local deficits, in addition to the end of one-time federal recovery dollars, mean that the City needs to consider alternative revenue growth strategies. In 2023, as a result of the Mayor's State of the City Address and later by Council action, City staff were tasked with research on viable potential measures to grow the City's revenue. First in March 2024, the City Council received a briefing on the City's General Fund fiscal outlook and the impact of oil on future revenues. Then in May 2024, the Mayor and City Council received a presentation on 52 ideas as part of Grow Long Beach to expand current revenues over the next several years through Economic Development efforts. However, these ideas alone will not be enough to prevent expected service reductions over the next three years. The way we are funding services is changing, with oil revenues no longer a revenue source that can or should be relied on in the future.

To help offset declining local revenue due to the state's scheduled oil production phase-out, and to maintain general City services, staff has begun evaluating a number of different proposals that could generate additional revenue to close the projected $45 million gap over the next three years.

This item provides an opportunity for staff to present a number of different potential revenue generating options and their impact on taxpayers and receive input from the Mayor and City Council.

Fiscal Projection and Grow Long Beach

On March 19, 2024, staff provided a study session on the City's fiscal outlook and FY 25 proposed budget development. The presentation outlined the core enhancements and efficiencies that have helped advance the City's 2030 Strategic Vision without increasing the projected General Fund shortfall. The City has also made great strides to implement the Elevate '28 Infrastructure Investment Plan to revitalize the City's infrastructure, prepare for the 2028 Olympic and Paralympic Games, and continue to improve and enhance City parks, major corridors, and visitor-serving areas. However, with the end of one-time investments through the Long Beach Recovery Act later this year and forecasted declines in revenues related to local oil production, it is essential that the City consider additional revenue measures to further advance key priorities, projects, and initiatives.

As presented at the study session, the projected FY 25 shortfall is $23.5 million, including carryover from FY 24's $8.8 million structural shortfall solved on a one-time basis using Long Beach Recovery Act funding. The three-year shortfall (FYs 25 – 27) is currently projected at $45 million. Due to the projected structural shortfall and limited current resources, priorities to maintain operations and execute priorities within the 2030 Strategic Vision may not be able to be funded in FY 25 without one-time resources like the Long Beach Recovery Act.

With a shifting legislative landscape and the City's commitment to address climate change, it is clear oil production is not in the City's future. Depending on fossil fuels as a long-term revenue source to support core City services is no longer feasible nor fiscally prudent. Starting in FY 25, the City will reduce annual planned structural support from oil proceeds and related taxes down to $0 by FY 30. Annual oil revenue received above the budgeted levels will be available for one-time uses and/or future oil well abandonment.

In order to secure the City's financial future and continue delivering the essential services our community depends on, staff outlined a plan to grow the City's economy in new and more sustainable directions on May 14, 2024. Staff presented 52 economic development strategies as part of the Grow Long Beach Initiative aimed at expanding and diversifying the local economy. In an effort to expand the City's tax base and good-paying job opportunities to offset projected oil production revenue declines, the City's Grow Long Beach Initiative centers around strategies to bolster key industry sectors in Long Beach.

In addition to the strategies proposed in the Grow Long Beach Initiative, staff has begun researching alternative revenue options that could be placed on the November 2024 ballot for voter consideration.

Dedicated Regional Sales Tax Measure for Housing and Homelessness

In November 2024, voters will consider whether to approve a measure that would increase the sales tax in Los Angeles County to provide additional funding for homelessness prevention and services, as well as affordable housing. The proposal, backed by United Way of Greater Los Angeles and a broad coalition of advocacy groups, would repeal and replace Measure H, the current quarter-cent sales tax approved by voters in 2017, with a half-cent sales tax estimated to produce $1.2 billion annually to fund homeless services, affordable housing, and other support like rental assistance countywide. 60 percent of the revenue through this measure would go to homelessness services, while 35.75 percent would go to the Los Angeles County Affordable Housing Solutions Agency (LACAHSA), an agency created through state legislation to advance affordable housing investment in the region.

Assembly Bill 1679 passed in 2023 authorized this proposed sales tax increase to exceed the current cap, meaning that if this measure passes, Long Beach's new sales tax would be 10.75 percent total. As a Continuum of Care and a member of LACAHSA, Long Beach would receive significant direct allocations through this proposal for affordable housing and homelessness programs. Long Beach has a dedicated seat on the LACAHSA Board, and next year Mayor Rex Richardson will be the Chair of the Board.

Additionally, in Long Beach it would have a significant revenue impact on the City. In addition to providing a new and stable revenue source for housing and homelessness, it would also allow the City's Measure A to return to the full one percent ahead of schedule. Currently the City does not realize the full 1 percent sales tax authorized by voters, due to the 10.25 percent cap. If Measure H is repealed, Measure A can return to the full 1 percent, generating $12 million in FY 25 and the full $24 million in FY 26. This could be spent on public safety or infrastructure.

Proposed Long Beach Revenue Ideas

Utility Users Tax (UUT) Power Plant Exemption Elimination

One area that staff have focused on has been revenues that will not be paid for by the vast majority of taxpayers in our City. The City could expand the utility users tax to remove exemptions for powerplants in the City with virtually no impact on ratepayers The City Auditor has performed significant research in this area and found that Long Beach residents derive marginal benefit from electricity generated at the Alamitos Energy Center (AEC), and little to no benefit from electricity generated by the Haynes plant, but incur a much greater price in environmental consequences. Amending the Municipal Code to remove the AEC's and LADWP Haynes Utility Users Tax exemption is just a small step towards evening out the cost-benefit equation. The estimated $15 million in annual revenue generated by removing the UUT exemption could be used to fund a variety of general services, including maintenance of trees and parks, enhancing library facilities and services, and improving marine and beach water quality.

Located at 690 N Studebaker, the AEC was built in the 1950s by Southern California Edison (Edison) and through its six natural gas-fired generating units, was capable of producing 1,940 megawatts of electricity. In 1997, as part of the State's deregulation of the power industry, Edison sold the AEC to Applied Energy Services Corporation (AES), a publicly traded for-profit company with power plants in operation across the world. Other power plant purchases by AES from Edison included locations in Huntington Beach and Redondo Beach.

Located across the San Gabriel River from the AEC and within the City sits the Los Angeles Department of Water and Power (LADWP) Haynes Generation Station. Built in the 1960s, the station currently operates ten natural gas-fired generators capable of generating 1,666 megawatts of electricity. LADWP is a vertically integrated power system which owns and operates the majority of its generation, transmission, and distribution systems. The electricity generated at Haynes is used to power homes and business serviced by the LADWP – for its own customers located within the City of Los Angeles.

The Long Beach Municipal Code Chapter 3.68 imposes a UUT for users of electricity, telecommunications, water, and gas. Section 3.68.040 describes the Gas Users Tax, which is imposed on every person in the City using gas in the City which is delivered through mains or pipes at a rate of 5 percent of the charges made and paid by the person paying for such gas.

Subsection C of the Gas Users Tax carves out exceptions for certain uses, including charges made for gas to be used in the generation of electrical energy by an electrical corporation or governmental agency. The City Attorney's Office, both historically and presently, has opined that AES qualifies for the gas UUT exemption based upon the municipal code's language, as written.

This language in the municipal code dates back 30 years to 1994 and has not been revised despite dramatic changes in the utilities industry. At the time the municipal code exemption for Gas Users Tax was made, Edison was a public utility and the owner of the plant. It was thought that a municipal code exemption for Edison was appropriate since the City was already assessing residents a User Utility Tax on electricity delivered by Edison, and that taxing the natural gas to make the electricity would have been a double taxation. Despite the 1997 sale of the AEC from Edison to AES and the change in the energy marketplace, the municipal code has not changed, and the same exemption still applies to AES.

To advance this proposal, Subsection C (2) of Long Beach Municipal Code Section 3.68.040 could be revised as follows:

> *There shall be excluded from the base on which the tax imposed in this Section is computed: (1)charges made for gas which is to be resold and delivered through mains or pipes; ~~(2) charges made for gas to be used in the generation of electrical energy by an electrical corporation or governmental agency;~~ and (~~3~~2) charges made for compressed natural gas used for motor vehicle fuel.*

Real Property Transfer Tax

Furthermore, in recent years, cities have considered and passed increased real property transfer taxes applied on the sale of real property. For example, the City of Los Angeles' Measure ULA, which was approved by voters and went into effect on April 1, 2023, imposes an additional tax on the real property transfer tax on all documents that convey real property within the city over $5 million. Revenues generated through Measure ULA are used to fund affordable housing projects and provide resources to residents at risk of homelessness. Similarly, Long Beach could consider increasing its real property transfer tax to generate additional revenue.

Unlike property taxes that are paid by voters every single year, Real Property Transfer Taxes are only paid upon sale of the property. The majority of Long Beach residents are renters, and this would not be paid by renters. Homeowners would not pay the tax unless they sold their home. The tax is structured so that the seller pays the tax, not the buyer, therefore it is not factored into the overall price and comes out of the proceeds of the sale. The market sets the overall asking price of the house – once the sale price is agreed to and the sale commences, the tax is applied at the end with the seller responsible for paying for the tax.

This tax would primarily be paid by:

1. Investors who purchase and then sell property, with the tax coming from the proceeds of the sale;

2. Property owners who are selling their property to leave Long Beach, with the tax coming from proceeds of the sale; and,
3. Long Beach property owners who are selling their property and investing in another property in Long Beach, which would be paid from the growth in property value.

There are two different concepts for applying an additional transfer tax. One option would be to align with the City of Los Angeles rate and increase the real property transfer tax assessed against sellers to $5.60 per $1,000 of property value, generating approximately $16 million annually. This has the potential to generate about $16 million in the first full year of implementation. The tax paid for the sale of the average single-family home in this scenario would be $3,864.

A second approach would be to adopt a two-tiered system applying a tax of $3.30 per $1,000 of value transferred for the first $1 million in property value and $5.60 per $1,000 of value above $1 million. This would be a more progressive model, taxing the average property in Long Beach at a lesser amount, and increasing the tax for those properties over $1 million, which would have greater ability to absorb the tax from the proceeds of the sale. A possibility under this scenario would be to create a rebate program for families selling to immediate family members, so as to allow properties to be transferred to children without the application of the increased tax. This scenario would generate approximately $12 million annually for the City. The tax paid for the sale of the average single-family home in this scenario would be $1,889.

It should be noted the amount generated by the real property transfer tax is largely influenced by the real estate market and interest rates, and trends which can be highly volatile so the projection could increase or decrease depending on those conditions.

Business License Tax Increase

Currently Long Beach has a lower Business License Tax (BLT) than several cities in the region. Several cities charge a gross receipts tax which is a percentage of total gross receipts. Long Beach assesses a flat fee, and then a per employee charge. The tax varies based on the type of industry. The average business license tax paid by all Long Beach businesses is $321 a year. If doubled, this would bring in about $15 million per year in new revenue. This has the potential to be passed on to customers both within and outside Long Beach, as the business would likely try to recoup the cost of the business license tax.

Electric Franchise Fee

Most cities charge the electric company a fee to have the exclusive right to provide power in their service area. Long Beach currently has on the books a 1.66 percent franchise fee for electric power that is paid by Edison to the City. Several cities charge between 2 percent and 5 percent for this fee. If Long Beach were to increase the fee up to 5 percent, that could generate significant revenues. This would be paid for by all rate payers, with the franchise fee typically being included and passed along in the bill. For Long Beach residents, if the fee were increased to 5 percent, this would result in an average bill increase of $29.60 over the course of a year, or $2.47 a month. This would result in about $21.5 million in new revenue per year. As it is an average amount and based on usage, rate payers with low usage would pay less, and ratepayers with higher usage would pay more.

This matter was reviewed by Principal Deputy City Attorney Rich Anthony on May 30, 2024, and by Finance Director Kevin Riper on May 29, 2024.

TIMING CONSIDERATIONS

City Council action is requested on June 11, 2024, to ensure sufficient time to review potential revenue opportunities for the City to consider on the November 2024 ballot.

FISCAL IMPACT

The direct fiscal impact of a City Council decision to place revenue-raising options on the November ballot is estimated at a one-time payment to Los Angeles County of between $150,000 to $180,000 each. The potential General Fund revenue impact of the revenue-raising options, if placed on the November ballot and approved by the voters, would vary based on the options placed before voters. As noted above, depending on the measure selected, new annual revenue could range from $12 to $24 million. The potential revenue impact is based on current data and will be subject to annual economic and market conditions.

Future City Council action would be required to place any proposed revenues measures on the November 2024 ballot. The fiscal impact of these proposals is dependent on the type of proposal that is approved. In order to place anything on the ballot, City Council direction would be needed by August 6, 2024. City staff will continue to research these proposals and receive Council and community input and return by August 6 with an additional detailed proposal for discussion.

SUGGESTED ACTION:

Approve recommendation.

Respectfully submitted,

Thomas B. Modica
City Manager