

Finance MEETING

3/28/2022

☒ Received Before Meeting

1

POTENTIAL REVENUE GENERATING LOCAL BALLOT MEASURE

Further Refinement

Finance Committee

March 28, 2022

www.cityofpaloalto.org/fiscalsustainability



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OVERVIEW

Council Direction and Work Plan

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- Staff continues to implement the workplan associated with pursuit of consideration of potential local ballot measures for the November 2022 general election

Updates since January 2022 for discussion tonight

- Summary and progress report on the Community and Stakeholder Engagement Plan,
 - Second poll (Attachments A and B), Online and mailed feedback survey (Attachment C), Business and community focus groups (Attachment D);
- Components of a ballot measure(s)
 - Business license tax, discussion on ordinance status,
 - Measure to affirm the Gas Funds Transfer draft ballot question and ordinance (Attachment E); and
- Business license tax additional analysis

COUNCIL DIRECTION & STATUS

The Council moved to direct staff to:

- ★ A. *Pursue preparation of a square footage business license tax with the following characteristics as recommended by the Finance Committee:*
 - i. *Continue to review the rates, adding option 3 (flat fee of \$50 for first 5,000 square feet occupied and apply a monthly tax rate per square foot beyond the 5,000 threshold) as a starting point;*
 - ii. *Exemptions for businesses subject to the Transient Occupancy Tax and grocery stores;*
 - iii. *Annual escalator uses CPI as a basis;*
- ✓ B. *Develop a proposal for voter ratification of the existing gas General Fund Equity Transfer and eliminate the UUT option, with the exploration of whether to cap growth of the transfer to be explored via polling;*
- ✓ C. *Amend the workplan to three polls, with the second poll developed and executed by the City's polling consultant, and the third to test potential ballot language; and*
- ✓ D. *Launch the Community and Stakeholder Engagement Plan, as outlined in the staff report.*

January 24, 2022 (Passed 6-1, Tanaka no)

WORKPLAN: JANUARY 2022 AND BEYOND



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March 2022

Community and Stakeholder Engagement

Finance Committee

- Results of second round polling and progress report of Community and Stakeholder Engagement Plan
- Ballot question(s) for proposed tax measures
- Fourth round of analysis for the BLT

April 2022

Council

- Results of Community and Stakeholder Engagement
- Fiscal Sustainability and Spending plan discussion
- Review preliminary draft ballot questions and measure language
- Review outline of final poll & direct staff to execute

May 2022

Staff Work

- Final round of polling
- Refining of ballot measure language and ballot question

June 2022

Council

- Results of final polling report to Council
- Final approval of November 2022 Ballot Measures

FINANCE COMMITTEE DELIBERATIONS TONIGHT

- Receive results of second round polling and progress report of the Community and Stakeholder Engagement Plan for consideration.
- Recommend Council direct staff to finalize the draft ballot question and ordinance language for the Gas General Fund Transfer measure.
- Recommend Council decide on final core characteristics of sq ft business license tax:
 - i. Refine implementation of “Option 3”
 - ii. Finalize characteristics (e.g. monthly rate, exemptions, CPI) based on polling and community input
- Recommend Council direct staff to execute third round of polling based on draft ballot language and refined business license characteristics.



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COMMUNITY & STAKEHOLDER ENGAGEMENT PLAN

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COMMUNITY SURVEY ONLINE & MAIL-IN

358 responses (174 online and 184 mail in)

Highly ranked priorities:

- Maintaining basic services
- Repairing streets/roads
- Investment in community-owned assets
- Adding public safety services such as police, fire, and emergency medical
- Funding affordable housing and homeless services

Thank you to the community for this input!





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Updating Palo Alto Voter Views of Potential Ballot Measures

*Key Findings of a Survey of Palo Alto Voters Conducted March 8-14,
2022*



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Survey Methodology

Dates	March 8-14, 2022
Survey Type	Dual-mode Voter Survey
Research Population	Likely November 2022 Voters in Palo Alto
Total Interviews	427
Margin of Sampling Error	(Full Sample) $\pm 4.9\%$ at the 95% Confidence Level (Half Sample) $\pm 6.9\%$ at the 95% Confidence Level
Contact Methods	 Telephone Calls  Email Invitations  Text Invitations
Data Collection Modes	 Telephone Interviews  Online Interviews

(Note: Not All Results Will Sum to 100% Due to Rounding)



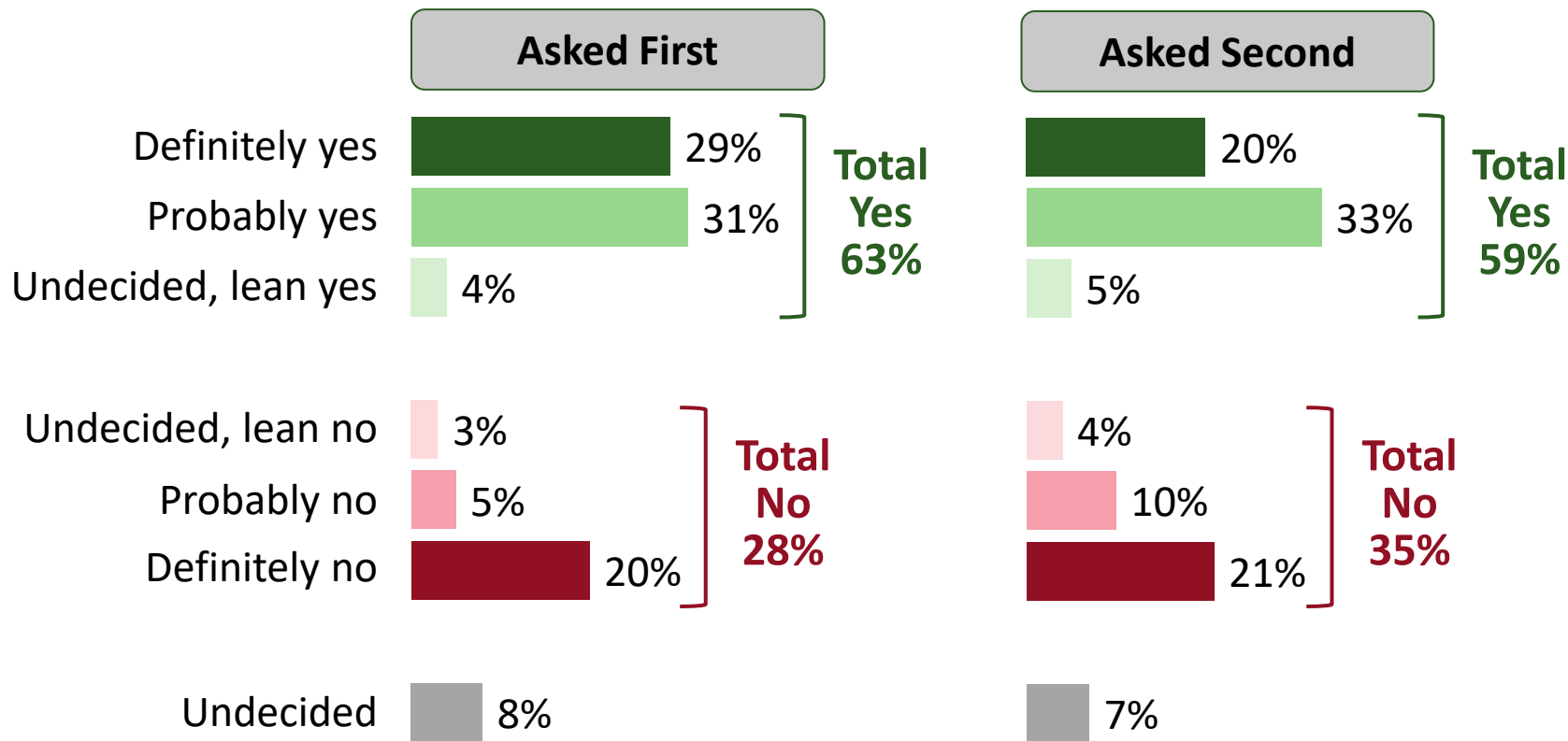
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Voter Views of Ballot Measure Concepts

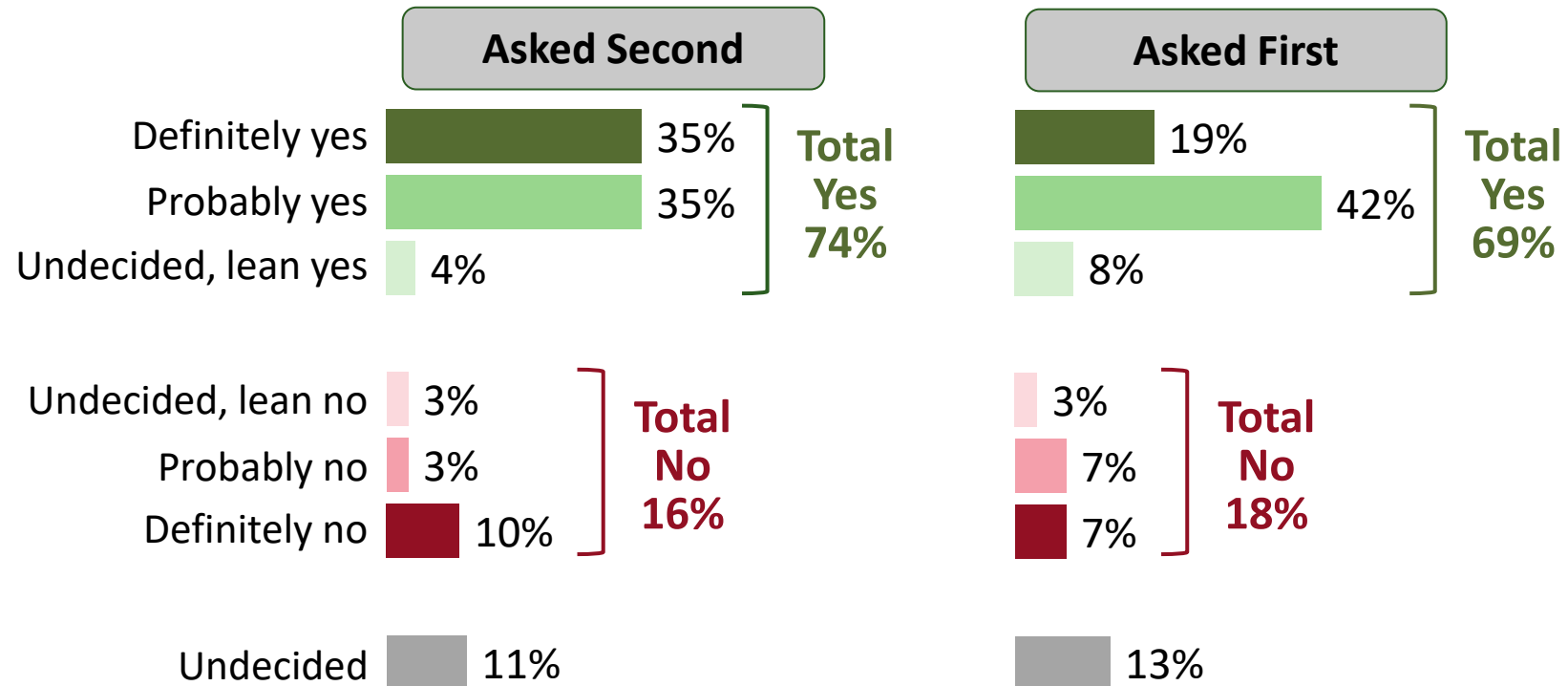
About three in five support a business license tax conceptually.

The measure would deal with a business license tax. This measure would create a business license tax on commercial property in the city of \$50 per year for the first 5,000 square feet occupied, plus 12 cents per square foot per month for space occupied over 5,000 square feet, adjusted annually for inflation. The funds would pay for City services such as police, fire and emergency medical services, affordable housing and support for the unhoused, parks and recreation, transportation, the City's climate action plan, and other public services.



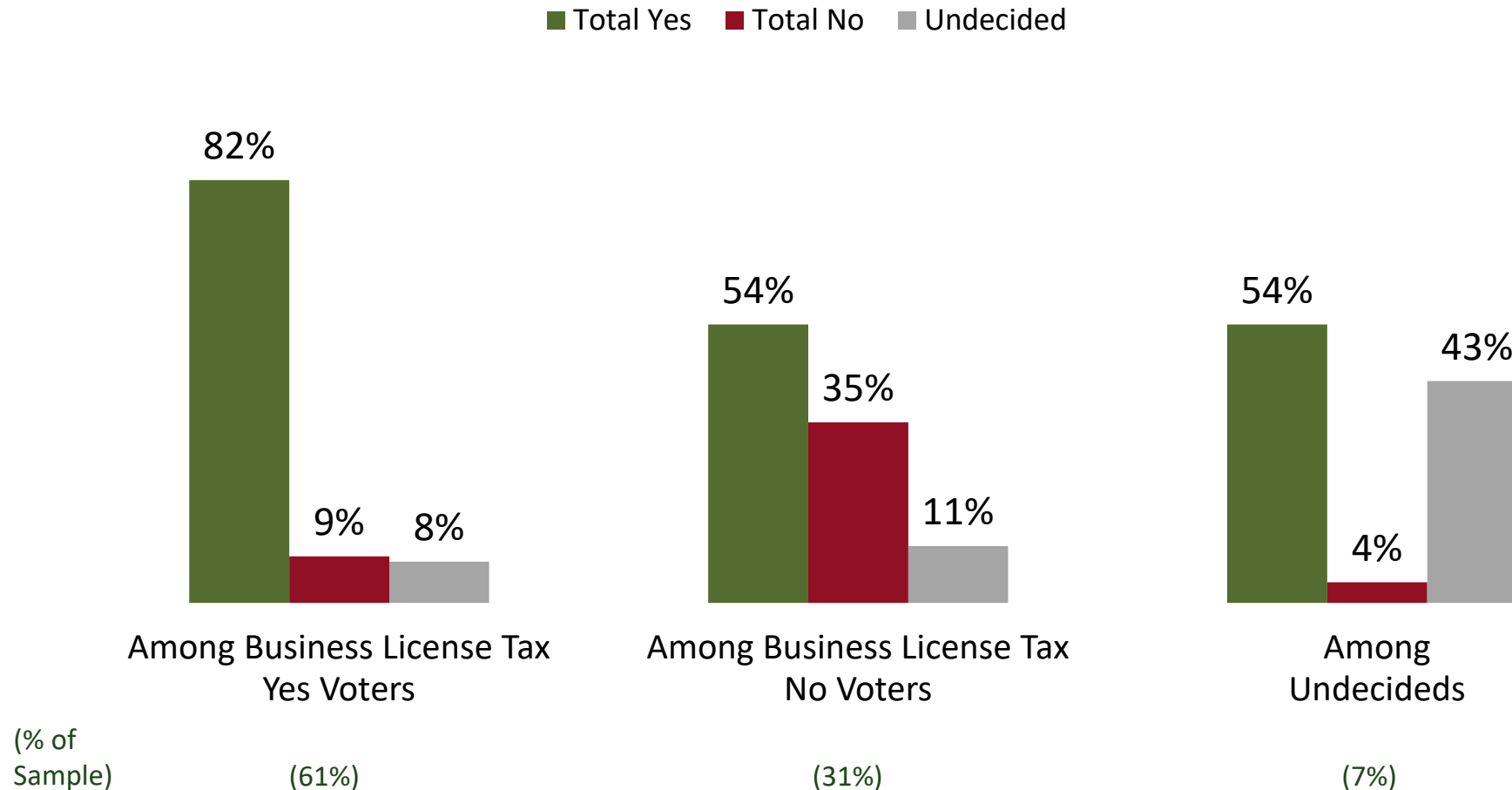
The utility fund measure has support from at least seven in ten voters.

The **FIRST/SECOND** measure would deal with utilities. As you may know, the City of Palo Alto provides natural gas service to residents and businesses. As part of its routine budget practices, the city annually transfers some money from the utility fund to the general City budget which maintains core services. This measure would confirm the existing practice of transferring not more than 18% of City of Palo Alto Utilities' gross annual sales of gas, providing over \$7 million annually to needed investments like police, fire and emergency medical services; affordable housing and support for the unhoused; parks and recreation; transportation; the City's climate action plan; and other public services. This measure would not increase utility rates.



A majority of those voting “no” on the business license tax support the utility measure.

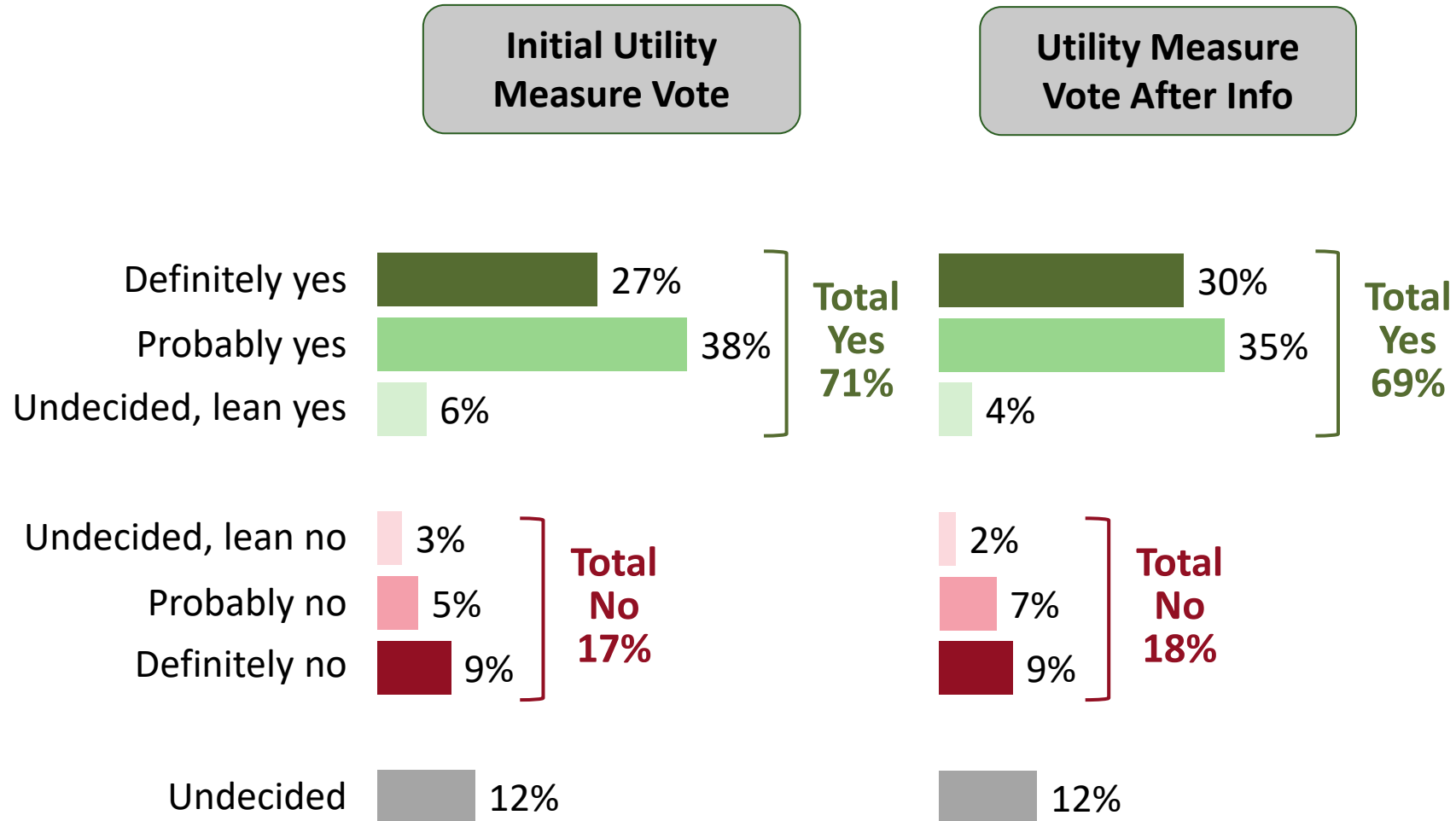
Initial Utility Measure Vote by Initial Business License Tax Vote



Next, voters were provided more context on the utility fund measure.

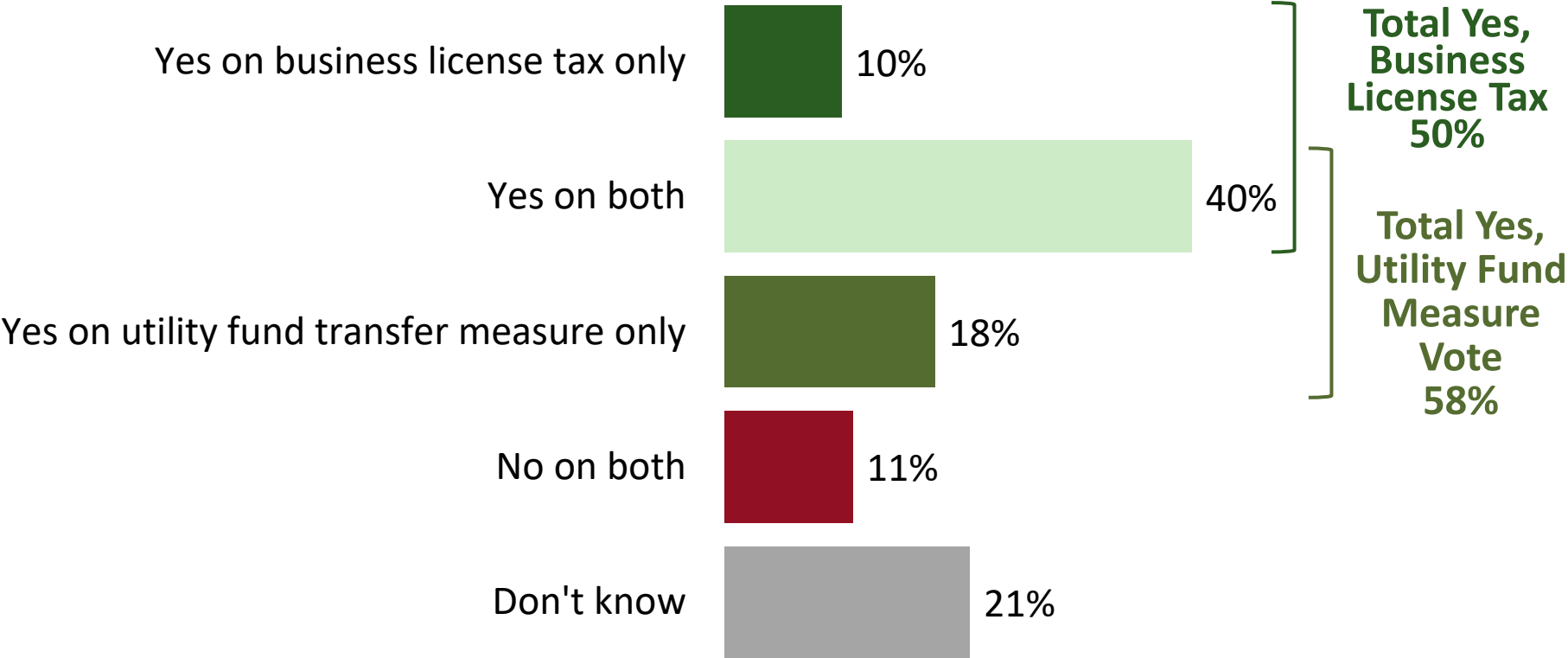
Investor-owned utilities like PG&E that provide natural gas service transfer some funds from their utility to shareholders. Cities like Palo Alto that own their own utilities do not have shareholders, so many cities instead transfer some funds from the utility to pay for City services like police, fire, transportation, parks and other public services. Palo Alto received voter approval for these kinds of transfers in its municipal Charter in 1950; however, this practice has been challenged legally, and voter approval may be required for it to continue. As a result, the City may place this measure to reconfirm this practice on the November ballot.

This did not shift patterns of support.



In a head-to-head test, two in five said they would vote “yes” on both measures.

If both of these measures were on the same ballot, would you vote “yes” on both, for just one, or for neither?





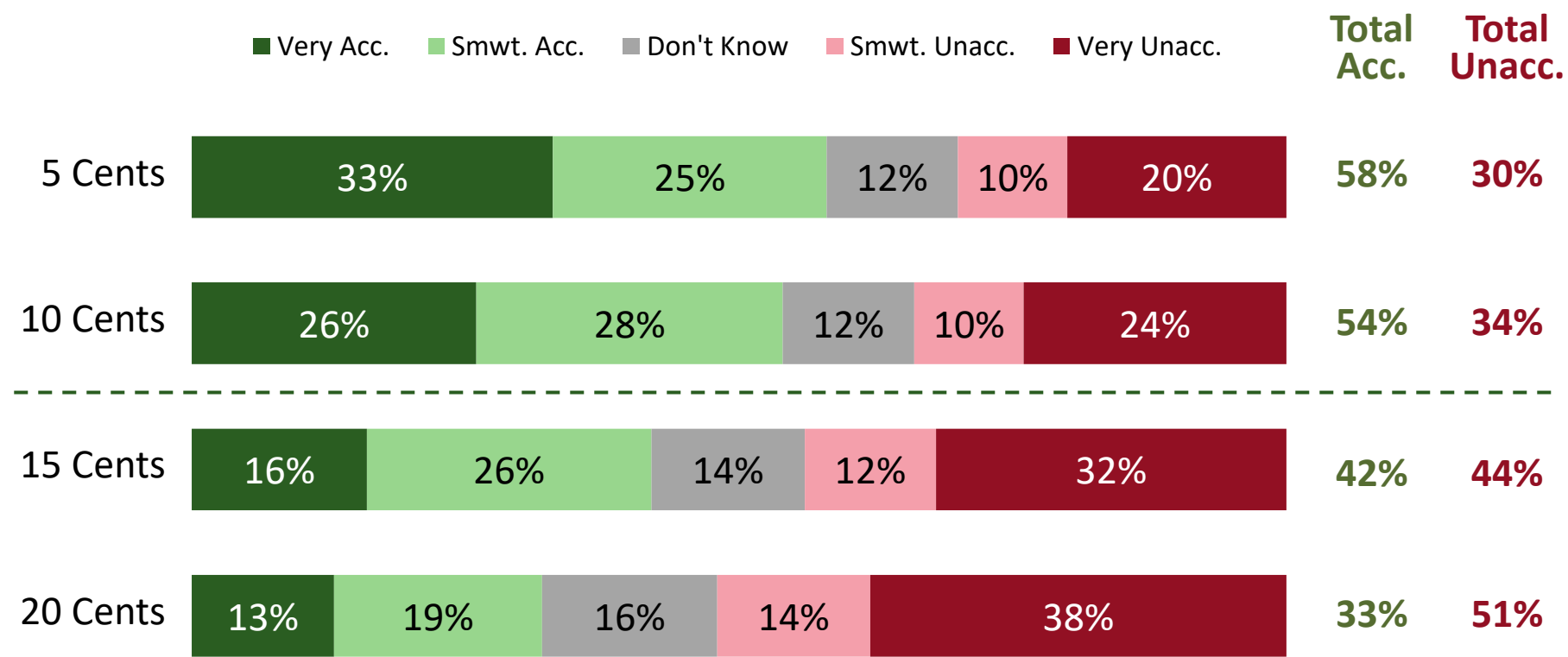
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Structuring a Business License Tax

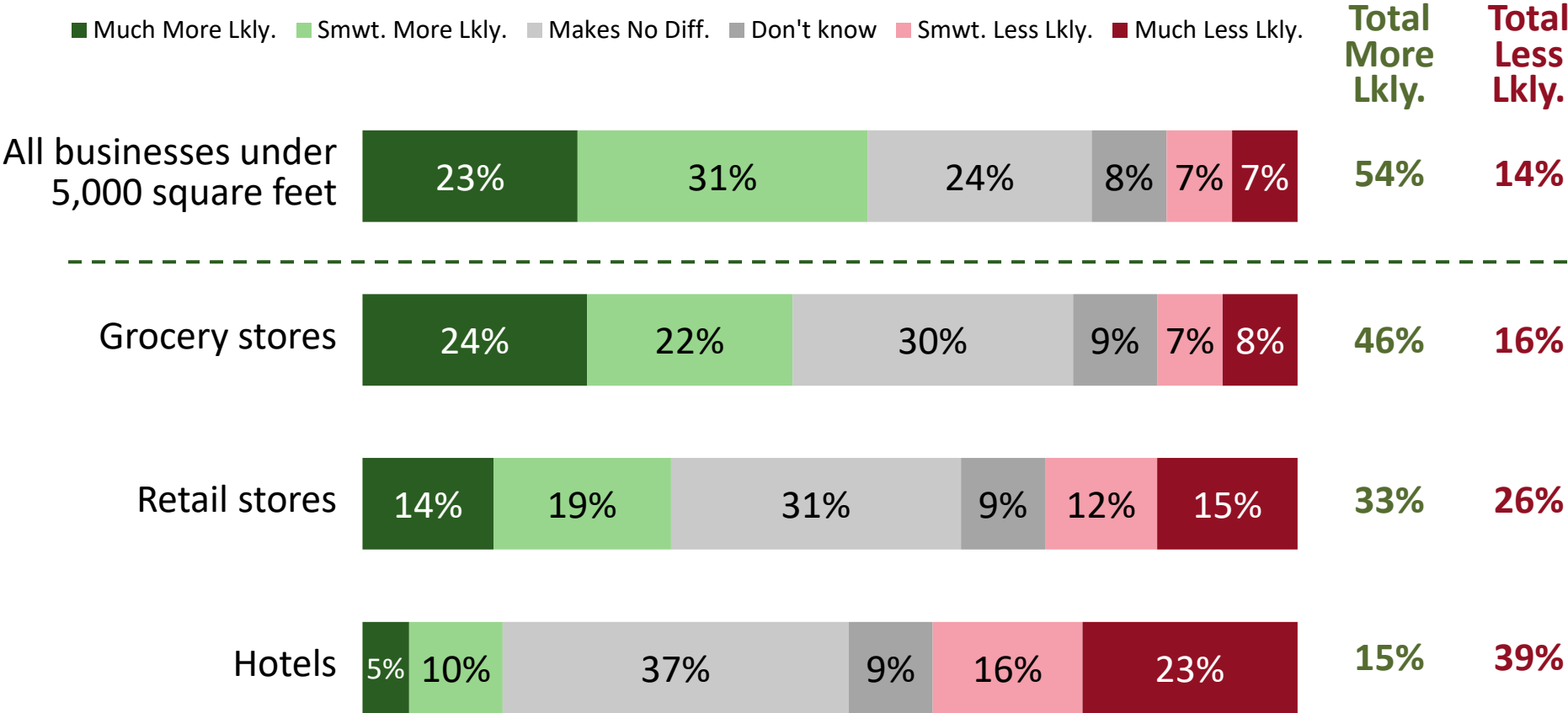
Majorities are comfortable with a rate that would increase rent by 10 cents per square foot.

The structure of this measure has not been finalized. Currently, average monthly rents for businesses range from \$4.10 to \$6.40 per square foot per month for retail and industrial space and \$7.10 to \$8.50 per square foot per month for office space. Would a measure that increased monthly business rent by roughly ___ per square foot be an acceptable or unacceptable amount?

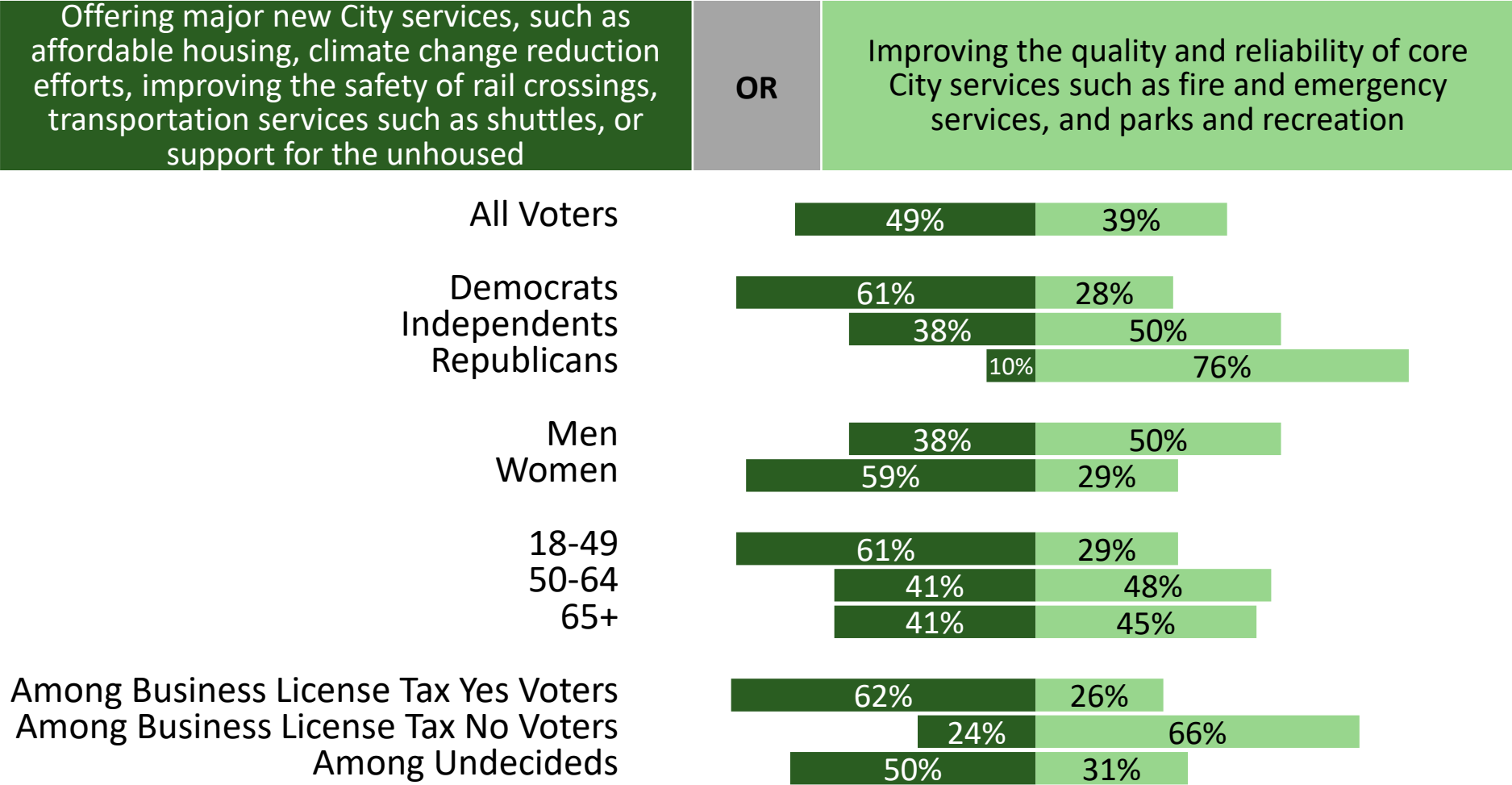


Exemptions for small-square-footage businesses are a plus; an exemption for hotels is more of a minus.

If it were written to exempt _____ from the tax, would you be more likely to support it or less likely to support it? If it makes no difference, you can tell me that instead.

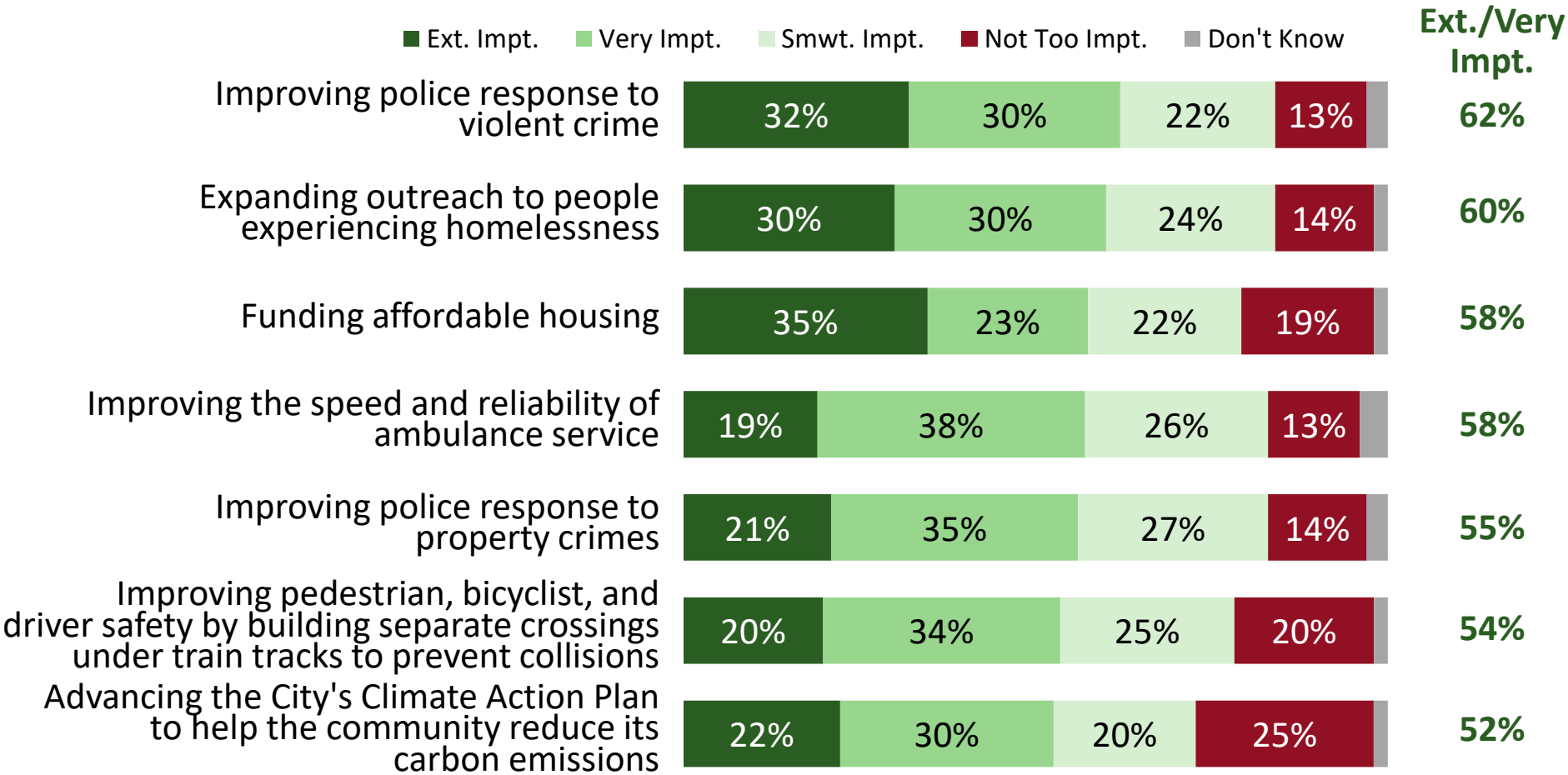


Voters are split on their desired focus for new revenue, with a strong preference for major new investments among Democrats.

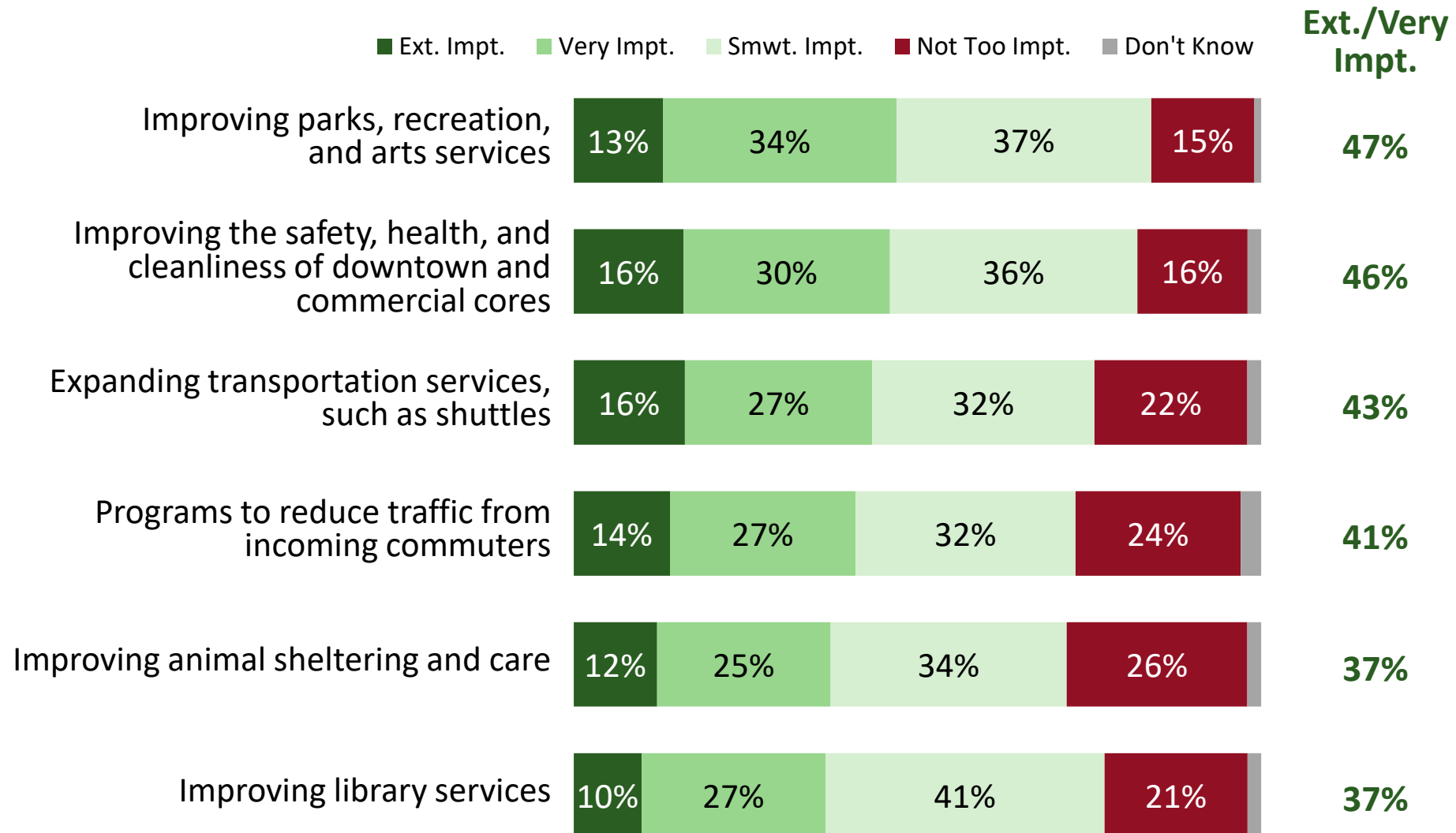


Improvements to public safety, homelessness and housing services are seen as most important.

I am going to read you a list of more-specific ways in which funds generated by a tax could be spent. Please tell me how important each item is to you personally: extremely important, very important, somewhat important, or not too important.



Voters value library services, animal sheltering, and transportation with less intensity.



Support Messages Tested

(Ranked in Order of Effectiveness)

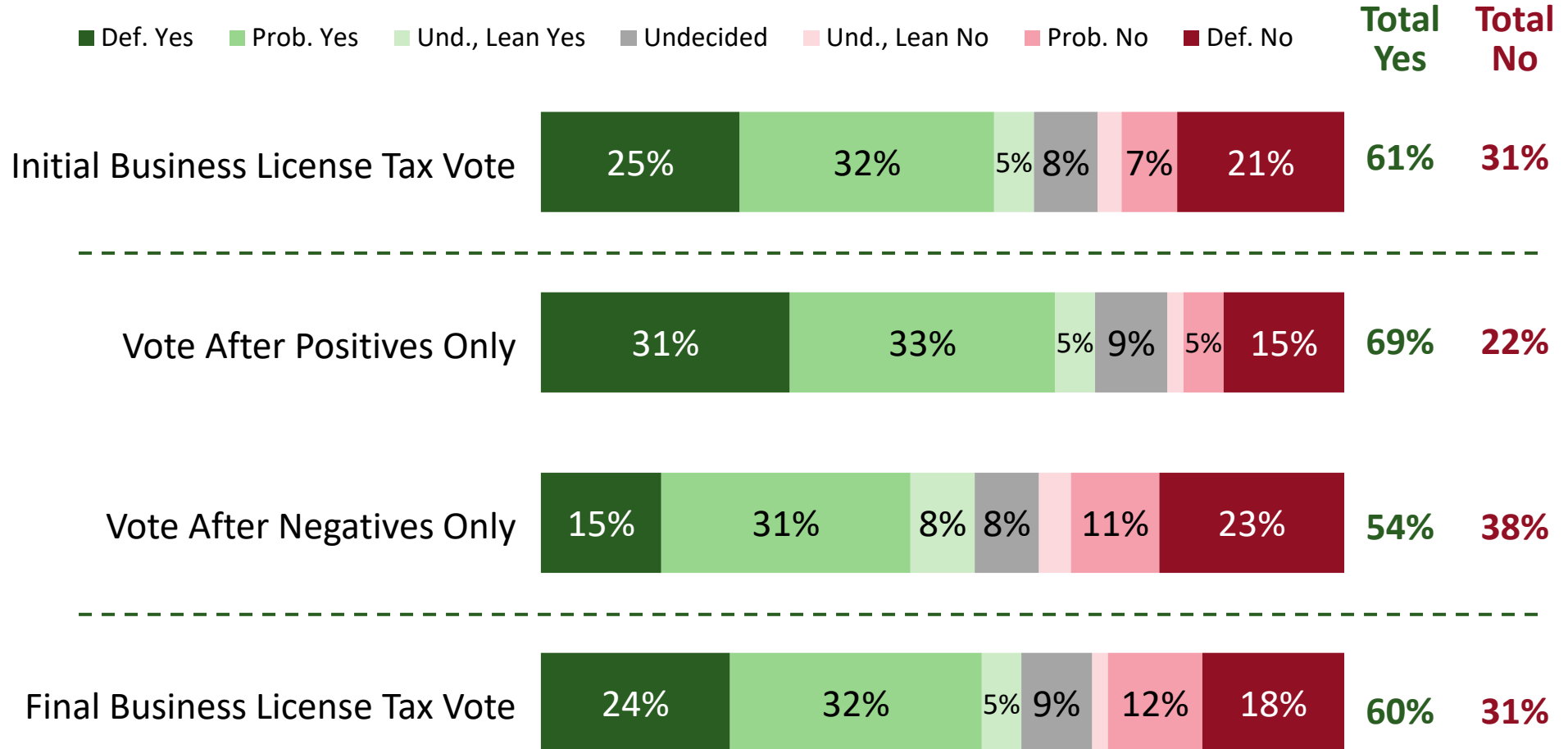
46%	(FAIR SHARE) Palo Alto currently registers businesses of all sizes for \$50. That means a mom-and-pop coffee shop pays the same as a tech company with thousands of employees. This measure is a sensible way to ensure large businesses pay their fair share for the services the City provides and that their employees enjoy, like road repairs and police and fire protection.
31%	(COMPARISON) Palo Alto does not have a business license tax, unlike most communities in California. Several nearby communities have significant taxes on business, such as East Palo Alto's tax of \$2.50 per square foot annually on commercial office space over 25,000 square feet and San Francisco's business tax of \$2.85 to \$5.60 per \$1,000 of gross receipts annually. This tax would align Palo Alto's tax system with those of other cities in the area.
30%	(TAX BASE) This measure is not a tax on homeowners or shoppers, but on the city's largest businesses. Sales taxes continue to decline in Palo Alto, and by diversifying the City's tax base with a thoughtfully designed business license tax, we will be better able to weather future financial crises without having to raise taxes on everyday residents.
27%	(ACCOUNTABILITY) This measure will be subject to strict accountability provisions like annual financial audits; full public disclosure of all spending; and a requirement that all funds be spent locally in Palo Alto. This will ensure funds are used efficiently, effectively, and as promised.
23%	(SAFETY) The recent economic downturn had significant impacts to funding for police and emergency services. Recently the community has seen increases in property crimes impacts to fire and emergency medical services. This measure would provide funding for police and emergency services to address these issues.

Opposition Messages Tested

(Ranked in Order of Effectiveness)

34%	(LOOPHOLES) Just like any tax, this will fall hardest on small and medium businesses already struggling with labor shortages, inflation, and high commercial rent. Meanwhile, the largest companies will find creative loopholes to get out of paying their fair share.
33%	(INFLATION) The cost of living is out of control and inflation is on the rise. With the price of groceries and gasoline increasing and an interest-rate hike on the way, now is simply not the time to be raising taxes.
32%	(RECOVERY) COVID-19 restrictions have already pushed many local businesses to slash hours or even close. The last thing we need to do is drive up prices with a tax that hurts local businesses just as we start to recover.
31%	(WASTE) Given the amount of money we already pay in city, county, and state taxes, and the amount we pay for expensive employee pensions, salaries, and healthcare benefits, City government simply needs to tighten its belt, work together, and do a better job with the dollars they already have.

A majority supports the measure throughout exposure to pro and con messages.





Conclusions

Conclusions

- The mood of the city continues to be mixed, as it is in many cities around region. A slim majority rates City government's performance as "excellent" or "good" (51%).
- Three in five back the business license tax concept we tested, which – pending a more detailed exploration of a more specific concept and associated ballot language – has consistent majority support.
- Voters are comfortable with a measure that would increase average monthly rent for businesses by up to 10 cents per square foot. They are more likely to support a measure that exempts small-square footage businesses, and are less likely to support one that exempts hotels.
- A measure ratifying utility fund transfers polls at 71%; support remains high when voters hear a more detailed explanation.
- Voters are divided on whether they would prefer new revenue be dedicated to major new investments or to improving existing services – however, those who support the BLT are more likely to favor new investments.
- Voters are most enthusiastic about allocating funding toward public safety, affordable housing, and outreach to the unhoused.

For more information, contact:



OPINION
RESEARCH
& STRATEGY

1999 Harrison St., Suite 2020
Oakland, CA 94612
Phone (510) 451-9521
Fax (510) 451-0384

Dave Metz

Dave@FM3research.com

Miranda Everitt

Miranda@FM3research.com



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COMMUNITY & STAKEHOLDER ENGAGEMENT PLAN

Business & Community Focus Groups



Communication/Engagement Objectives

- Design and execute a multi-disciplinary engagement and communications process to support this project
- Utilize a full range of multi-disciplinary approaches that include:
 - Successful integration of expertise and approaches with Executive Team/FM3 Research
 - Engaging stakeholders in facilitated focus groups to express/collect viewpoints
 - Approaches that embrace all types of engagement/communications methods to collect additional input and report on that input, including online surveys, interactive/report-back mailings, social media information, embedment into routine City communications vehicles, and paid digital media
- Provide information and recommendations to City staff and Council for policy and ballot measure decisions

Stakeholder Focus Groups

- Outreach and Recruitment
 - Extensive outreach via email and regular mail to Palo Alto business and community organizations
- Five Focus Groups Conducted (February 22 – March 17)
 - Four with business community stakeholders (27 participants)
 - One with community stakeholders (6 participants)
- Participation
 - All who expressed interest in participating were accommodated
 - Three focus groups were cancelled and two rescheduled due to low attendance

Focus Group Purposes and Outcomes

- A. Educate stakeholders about Palo Alto's Fiscal Sustainability Strategy for 2022 and the funding options currently under consideration
- B. Elicit feedback on City service priorities that are important to the business community and community at-large
- C. Elicit feedback on the two ballot measures that the City Council is considering for voters in November 2022:
 - 1) Measure to affirm Gas Funds Transfer and
 - 2) Adopt a new Business License Tax (BLT)

Overall Results

- Support for Gas Funds Transfer:
Either support or neutral based on lack of familiarity
- Support for Business License Tax:
Either conditional support or no support

BLT Focus Group Feedback

- No cap on the CPI - Concern that the tax will continually increase.
Participant Suggestions: Cap the CPI or cap the total amount to be paid
- No sunset - Concern that there is no specified end date, especially without a CPI cap
Participant Suggestions: Designate an end date
- Not the right time - Concern that the tax will impede businesses recovery from COVID; disincentive to attract new businesses
Participant Suggestions: Postpone placing tax on ballot
- Need a funding plan - Concern how the revenue will be allocated (i.e. General Fund).
Participant Suggestions: Specify how revenue will be allocated to benefit the business community and community

Next Steps

- Listening Session: Tuesday, March 29, 6:00pm
- Second round of focus groups:
April – May to elicit more targeted feedback
- Update with results to be presented to Finance Committee and City Council



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COMPONENTS OF A BALLOT MEASURE

Draft Ballot Question & Ordinance

COMPONENTS OF A BALLOT MEASURE

For each local measure, the official ballot includes :

- a letter designation generated by the County Registrar of Voters;
- the ballot question (a clear, accurate statement that describes what the measure will do, not to exceed 75 words);
- space for voters to mark their vote for or against.

In advance of the election, registered voters receive a Voter Information Guide that includes:

- An impartial analysis of the measure prepared by the City Attorney;
- the full text of the measure; and
- arguments for and against.

MEASURE TO AFFIRM GAS FUNDS TRANSFER

Initial draft ballot question:

“Shall the measure affirming the City of Palo Alto’s past practice of annually transferring from the City’s gas utility an amount up to ____% of the gross revenues of the gas utility to the City’s general fund for general government use, to be paid for by the retail gas rates and providing approximately \$_____ annually until ended by voters, be adopted?”

Areas of Input:

1. Percentage of gross revenues to transfer
2. Uses to note in ballot measure question

MEASURE TO ESTABLISH A BUSINESS LICENSE TAX

Staff is actively working on key elements of the draft ordinance, specifically definition of:

- Business
- Square footage and how to measure
- Grocery stores or supermarkets



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BUSINESS LICENSE TAX

Additional Analysis

SQUARE FOOTAGE BUSINESS TAX – OPTION 3

Option 3:

Tiered Rates After Square Footage Threshold, exempting grocery stores and hotels

- Flat fee for first 5,000 sf (\$50/year) and apply monthly rate/sf beyond threshold
- Est. gross revenues \$11M to \$43M
(estimate, does not include cost for administration)

These figures reflect the following:

- Proposed exemption of grocery stores and hotels (est. exemption of 38 properties)
- Grocery assumed 139,580 sq ft.
- Hospitality assumed 1.4 million sq ft.
- Reduced gross revenue est. 8%, from original range of \$12M to \$47 M

Second round polling reflects majority support for

- a tax rate up to 1.5% of rent (approx. \$0.10/sf monthly, \$1.25/sf annual)
- exemption for businesses less than 5,000 square feet will more likely gain support

SQ FT BASED TAX CALCULATIONS

Range of rates / square foot applied on sq. ft.
5,001:

From \$0.05/SF (0.7% rent incr.)
to \$0.20/SF (2.9% rent incr.)
(monthly, % based on ~\$6.96/sf)

**Table 2: Business License Tax Scenario
(Exempt Grocery Stores and Hotels)**

	5,000 sf	30,000 sf	100,000 sf
\$0.05/sf per mo.	Exempt	\$1,250	\$4,750
\$0.10/sf per mo.	Exempt	\$2,500	\$9,500
\$0.15/sf per mo.	Exempt	\$3,750	\$14,250
\$0.20/sf per mo.	Exempt	\$5,000	\$19,000

**Characteristics for Committee review
and recommendation to Council for
direction to staff:**

- Exempt the first 5,000 square feet of space occupied by a business, deemed as “small”
- Exemption for grocery stores
- Exemption for hotels
- CPI
- Administer Business Registry Certificate (BRC) Program concurrently with potential business license tax @ current rate of \$50/yr

MAJOR COMPONENTS FOR CONSIDERATION

★ Finance Committee focus area

Structure

- ✓ Tax Method(s)/Unit of Measure
- ✓ General/Specific & Passage Rate
- ✓ Legally Required Exemptions
- ★ Exemptions by Council Policy

Revenue & Modeling

- ★ Taxation Level
- ★ Rate Structure (flat or tiered)
- ★ Avg. Annual Fee
- ★ Tax Rate per Unit

Administration

- Data Sources
- E.A.S.E.
- Administration/
Staffing Levels

DRAFT FINANCE COMMITTEE MOTION

The Finance Committee recommends Council:

- A. Accept the results of the second poll and progress report of the Community and Stakeholder Engagement Plan
- B. Review and provide feedback on the initial draft of the ballot question and draft ordinance language ratifying the Gas General Fund Transfer, including the changes below:
 - i. 18% of gross revenue
 - ii.
- C. Direct staff to pursue preparation of a square footage business license tax with the following characteristics:
 - i. Implement the intent of “Option 3” by exempting the first 5,000 square feet of space occupied by a business,
 - ii. Apply a monthly rate of \$___ beginning at square foot 5,001,
 - iii. Administer the BRC Program requiring all businesses that occupy less than 5,000 square feet to register at a rate of \$50 per year,
 - iv. Annual escalator ... [using CPI as a basis ____], and
- D. Direct staff to execute the third round of polling based on draft ballot language and refined business license tax calculations



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