# **MEMORANDUM**

ATTORNEY WORK PRODUCT
ATTORNEY-CLIENT PRIVILEGE

To: Sandy Briggs, Library Services Director, City of Woodland

**FROM:** Best Best & Krieger LLP

**DATE:** November 16, 2009

**RE:** Library Funding Options

# **BACKGROUND INFORMATION**

The City of Woodland is currently evaluating its options for raising revenue for the Woodland Public Library. As a municipal library, the library is operated by an appointed board of trustees. However, funding for the library comes out of the City's general fund, with the board having no control over the amount of funding allocated. In light of the current economic climate, the City has reduced library funding. To ensure the City's library remains a valuable resource for City residents, the City is evaluating its options for increasing library funding.

# **QUESTION PRESENTED**

What revenue measures may be enacted to increase library funding?

# **BRIEF ANSWER**

Generally, there are three types of revenue measures that the City could implement: a general tax, special tax, or a general obligation bond. Imposing or increasing general or special taxes requires voter approval, as does issuing a general obligation bond. Specifically, all general taxes must be approved by 50% of the voters while special taxes require a two-thirds vote. The specific types of general or special taxes the City could impose are discussed below. Although assessments are an alternative means of generating revenue for public facilities, it is unlikely that an assessment district could be created to fund the library.

ATTORNEYS AT LAW

### **ANALYSIS**

#### Free Use of Municipal Libraries

As an initial matter, municipal libraries are subject to special rules that prevent the City from imposing user fees on patrons to fund library services. In light of the public nature of municipal libraries, Education Code section 18960 requires that municipal libraries remain free to "inhabitants and nonresident taxpayers." Unless a patron violates a library rule or regulation, he or she may not be charged for using library services. Accordingly, the City cannot simply impose a user fee to increase library funding.

PROP. 218 REQUIREMENTS

# A. General and Special Taxes.

Before examining specific types of available funding mechanisms, it is important to note the substantive and procedural limitations imposed by Proposition 218. Among other things, Prop. 218 limits the power of local governments to impose taxes, which are classified as either general or special. (Cal. Const., article XIIIC, §§ 1-2.) Prop. 218 distinguishes between a general and special tax based on the purposes for which the revenue raised will be used. A general tax funds "general governmental purposes." (Cal. Const., article XIIIC, § 1(a).) By contrast, revenue from a special tax supports "specific purposes." (Cal. Const., article XIIIC, § 1(d); See Government Code, § 53717 [authorizing cities to impose special taxes consistent with Prop. 218 for library services].)

Prop. 218 imposes unique procedural requirements on the enactment of general and special taxes. General taxes must be approved by a two-thirds vote of the City Council and a majority vote of the voters. An election on a general tax must be consolidated with the regularly scheduled general election for City Council members unless the City Council unanimously declares an emergency.

Special taxes must be approved by a majority of the Council and a two-thirds majority of the electorate. (Government Code, § 53724.) An election regarding a special tax may be consolidated with a general, primary or regularly scheduled local election. However, the election may also be held on any other date permitted by law. In this case, the City must pay for the cost of the election.

These different voter thresholds create challenges for local agencies. On one hand, it is numerically easier to obtain a simple majority vote. On the other hand, it may be easier to generate sufficient public support for a special tax as voters can identify with a clearly identifiable purpose for the levy (i.e., public safety, a library or a sports arena). To avoid this problem, local governments sometimes utilize the "Measure A and B" approach. In this case, the local agency places two measures before the voters: Measure A-a general tax and Measure B-an advisory measure requesting the local legislative body use funds raised by Measure A for a specific purpose. As you may remember, Sacramento County recently used this approach in its

ATTORNEYS AT LAW

attempt to secure funding for a new Sacramento Kings arena. <sup>1</sup> It is important to remember that while this approach may help garner voter support, the advisory measure is not legally binding. Even if the City passed a general tax increase with a corresponding advisory measure requesting that funds be used for the library, a future City Council could decide that funds should be allocated differently.

### B. Assessments.

Prop. 218 also constrains local governments' ability to impose special assessments. (Cal. Const., article XIIID, § 2.) An assessment is defined as "any levy or charge upon real property by an agency for a special benefit conferred upon the real property." To qualify as a special benefit, the property must receive a benefit from the service being funded that is above and beyond the general benefits conferred on all property within the City or to the public at large. (Cal. Const., article XIIID, § 2(i).)

The California Supreme Court recently clarified what qualifies as a "special benefit" under Prop. 218. In *Silicon Valley Taxpayers Association v. Santa Clara County Open Space Authority* (2008) 44 Cal.4th 431, the court considered whether an "open space" assessment complied with Prop. 218. The court concluded that it did not, in part, because the assessment did not provide a special benefit to the assessed parcels. The benefits of the assessment, namely preserving open space and corresponding recreational and qualify of life benefits, were benefits enjoyed by the public at large and not special benefits accruing to the assessed parcels.

In the present case, an assessment is probably not a viable potential revenue source for the library. The benefit from the library received by the parcels that would be subject to the assessment is most likely not any different from the general benefit received by all parcels within the City or by the general public. While not necessarily legal support for the conclusion that library services may not be funded by an assessment, a California Library Association fact-sheet regarding 2004 library-related local ballot measures identified a number of proposed tax increases to fund library services but not a single proposed assessment for these purposes.<sup>2</sup> In fact, two of the proposed taxes were parcel taxes designed to replace expiring assessments.<sup>3</sup> This is likely due to the issues identified above. Accordingly, the City would most likely be limited to imposing a general or special tax to fund library services.

1

<sup>&</sup>lt;sup>1</sup> These measures were known as Measure Q and R. (See http://www.smartvoter.org/2006/11/07/ca/sac/meas/.) While the measures were soundly defeated in that case, the underlying approach is still valid.

<sup>&</sup>lt;sup>2</sup> See http://www.cla-net.org/events/newsletter/oct04\_measures.php. However, one of the measures was related to an assessment to pay for bonds used to finance library facilities under the state Library Bond Act of 2000. This would not be applicable in the present case. Similarly, the Mello-Roos Community Facility District Act of 1982 allows community facility districts ("CFD") to provide library services if a special tax is approved by the district's voters. (Government Code, § 53313(c).) It is important to note that the City could not form a CFD to provide library services at their current level. CFDs may not be formed to supplant services that are already provided to the district. (Government Code, § 53313.)

<sup>&</sup>lt;sup>3</sup> These were Measure X in the City of Sacramento and Measure S in San Jose. (See http://www.clanet.org/events/newsletter/oct04\_measures.php.)

ATTORNEYS AT LAW

#### POTENTIAL REVENUE SOURCES

In light of the constraints noted above, below is a discussion of each of the potential revenue measures the City may consider enacting to support the library. Unless otherwise noted, each of the following measures could be imposed as a general or special tax.

# A. Transactions and Use Tax (Sales Tax).

A transactions and use tax is a tax that increases the sales tax within the City. There are actually two components to sales tax. The first is the standard state sales and use tax. This is currently 8.25%, .75% of which the City receives. The second is a local transactions and use tax. Under the auspices of a special statute that applies only to Woodland, the City currently imposes a .50% transactions and use tax. (See Revenue and Taxation Code, § 7286.52.) The City could increase the transactions and use tax in .25% increments up to 2% total. (See Revenue & Taxation Code, §§ 7251.1, 7262.3.) Accordingly, the City could increase the transactions and use tax up to an additional 1.5% to fund the library.

## B. Utility Users Tax.

The City may impose a tax on utilities such as gas, electricity, telephone, water and cable television. (Government Code, § 37100.5.) This tax is actually paid by the utility customer and may be targeted at specific types of utilities or levied on all utilities (i.e., telephone, electricity or both).

### C. Transient Occupancy Tax.

The City may tax a person staying thirty (30) days or less in hotels, motels and similar lodgings, including mobile homes. (Revenue and Taxation Code, § 7280 *et seq.*) Although the tax is collected by the operator, the tax is imposed on the guest.

## D. Parcel Tax.

The City may levy a parcel tax to support the library. A parcel tax is an annual tax which is based on either a flat per parcel rate or rate which varies depending on use or size and/or number of units on each parcel. (See Government Code, § 53087.4.) Prop. 218 most likely requires that a parcel tax be adopted as a special tax. (Cal. Const., article XIIID, § 3.)

### E. Business License Tax.

The City could impose a business license tax on businesses operating within the City. (Gov. Code, § 37101; Bus. & Prof. Code, §§ 16000 *et seq.*) A business license tax is different from a business license fee. A fee compensates the City for its costs of issuing and administering a business license program and is not intended to raise revenue for the City. A business license tax is imposed to raise revenue. Currently, the City's municipal code authorizes the City to impose both business license fees and taxes. (See WMC, §§ 13-1-7; 13-1-15.) While

\_

<sup>&</sup>lt;sup>4</sup> Please note that a transactions and use tax is actually calculated slightly differently from a sales and use tax. Basically, the jurisdiction where the sale took place always receives the sales and use tax. However, the jurisdiction where the goods are delivered to the customer receives the transaction and use tax.

ATTORNEYS AT LAW

it is not entirely clear, it appears that the City currently imposes a combined business license fee and tax. The applicable business "fee" for most businesses increases as the number of employees or amount of annual revenue increases. For example, the City currently imposes a \$52 per year fee on retail businesses within \$100,000 or less in annual gross sales and \$762 per year for retail businesses with sales of \$4,000,001 or more. Under the definitions noted above, any portion of the applicable fee for each that exceeded the City's actual cost of administering the business license program would be a business license "tax." As it seems unlikely that the City's actual costs of administering the business license program for large retailers are \$710 more than for small retailers, the City is likely currently imposing a business license tax. The City could increase this tax to generate revenue for the library.

## F. Municipal Occupations Tax.

While the City may not levy an income or payroll tax, it may levy a tax upon employees measured by their gross income received within the City. (See Revenue & Taxation Code, § 17041.5.) If the City decides to impose this tax, it must ensure that the tax does not discriminate against non-residents. (Government Code, § 50026.) The tax should also not be graduated or allow deductions typical of an income tax. (Weekes v. City of Oakland (1978) 21 Cal.3d 386.)

In *Weekes*, the city imposed a "business license fee" that required all employees to pay one percent of all income earned in the city in excess of \$1,625 per quarter with a credit for self-employed persons paying the traditional business license tax imposed on businesses within the city. The court determined that the tax was not an income tax but a valid municipal occupations tax. Essentially, the court concluded it was similar to a traditional business license tax. Instead of taxing businesses based on their gross receipts, the city taxed employees based on their gross income. The "business license fee" was a valid tax on the privilege of working within the city.

These types of taxes are relatively rare. Traditional business license taxes are much more common. However, the City could at least theoretically impose a municipal occupations tax.

### G. Development Tax.

The City could levy a development tax. This is a tax on the privilege or activity of development and/or the availability or use of municipal services. The tax is generally imposed only on new construction. The tax rate is generally based on number of units, number of bedrooms or square footage.

It is important to remember that a development tax is different from a development impact fee. These fees are generally imposed to fund the cost of City infrastructure and services that the proposed development will require. (See *Centex Real Estate Corp. v. City of Vallejo* (1993) 19 Cal.App.4th 1358, 1364.) By contrast, a development tax is a tax on the privilege of allowing development to raise general revenue for the City. (*Centex*, at p. 1364.) For example, in *Centex*, the city imposed a development tax of \$3,000 per residential unit and \$.30 per square foot for nonresidential properties. The city also imposed various development impact fees. The court noted that the development tax was separate and distinct from the development impact fees.

ATTORNEYS AT LAW

As with municipal occupations taxes, development taxes are relatively rare. In light of the current real estate market, the City may face stiff opposition to any measure that taxes the cost of development. However, the City is empowered to levy this type of tax and revenue from it could be used to fund the library.

### H. Other Excise Tax.

The City may also impose almost any other excise tax. An excise tax is essentially any tax, except a poll or property tax. The distinguishing feature of an excise tax is that the obligation to pay the tax is based upon the voluntary action of the person taxed in performing the act, enjoying the privilege or engaging in the occupation which is the subject to the tax. (See *Pesola v. City of Los Angeles* (1975) 54 Cal.App.3d 479.)

Accordingly, an excise tax is not a specific type of tax but a category of taxes. Sales and use taxes, business license taxes, utility user taxes, transient occupancy taxes, and development taxes are all types of excise taxes. For example, a development tax is an excise tax because the developer is required to pay the tax based on his or her voluntary decision to develop property. In addition, one relatively common type of excise tax not specifically discussed above is an admissions tax. An admissions tax is a tax imposed on consumers for the privilege of attending a show, performance, display or exhibition. The tax rate is generally based on either a flat rate per ticket, a percentage of the admission price, or on a sliding scale. Generally, the tax is included in the price of the ticket, collected by the ticket seller and remitted by the seller to the City.

## **CONCLUSION**

We hope this memorandum has been helpful in explaining the various types of potential revenue measures the City could enact to fund library services. Please let us know if you have any questions or need any further assistance.

ANDY MORRIS JOSH NELSON