

2014-2015

OPERATING BUDGET

GANN LIMIT



Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Jennifer A. Maguire

SUBJECT: SEE BELOW

DATE: June 10, 2014

Approved

Date

6/10/14

SUBJECT: ADOPTION OF A RESOLUTION IN COMPLIANCE WITH ARTICLE XIII B OF THE CONSTITUTION OF THE STATE OF CALIFORNIA AND AS MODIFIED BY PROPOSITION 111 AND SB 88 ELECTING THE POPULATION AND INFLATION FACTORS AND ESTABLISHING THE FISCAL YEAR 2014-2015 APPROPRIATION LIMIT

RECOMMENDATION

It is recommended that the City Council adopt a resolution taking the following actions with respect to the City's 2014-2015 "Gann Limit":

- (1) Elect the per capita income index as the inflation factor for 2014-2015 on a provisional basis, with the option to adjust the Limit, if necessary, once the non-residential assessment data is available from the County Assessor; and
- (2) Elect the City population growth index as the population factor for 2014-2015; and
- (3) Establish the Fiscal Year 2014-2015 Appropriation Limit at \$936,545,078 in compliance with Article XIII B of the State Constitution.

OUTCOME

The establishment of the 2014-2015 Appropriation Limit ("Gann Limit") is necessary to comply with Article XIII B of the State Constitution.

BACKGROUND

California voters approved an initiative on November 6, 1979 that added Article XIII B to the State Constitution. The provisions of this article place limits on the amount of revenue that can be appropriated by all entities of government. The Appropriation Limit is based on actual appropriations during the 1978-1979 fiscal year, as increased each year using specified population and inflationary growth factors.

The original legislation implementing the provisions of Article XIII B became effective January 1, 1981. In accordance with that legislation, the governing body of each government jurisdiction must, by resolution, establish its annual Appropriation Limit for the coming year (prior to July 1) at a regularly scheduled meeting or noticed special meeting.

The original Article XIII B (Proposition 4) and its implementing legislation Chapter 1205/80 were modified by Proposition 111 and SB 88 (Chapter 60/90). Significant changes imposed by Proposition 111 include the following:

- The provision of a choice in methodologies for determining the annual inflation factor between (1) growth in California per capita income, or (2) growth in non-residential assessed valuation due to new construction within the City.
- The provision of a choice in methodologies for determining the annual population growth factor between (1) City population growth, or (2) County population growth.
- Regulations allowing the exclusion of “qualified capital outlay” expenditures from the calculation of the Limit.
- Provision of a process for avoiding tax refunds if a city falls sufficiently below the Limit in the next fiscal year. The revised language provides two years, beyond the second year, to refund any remaining excess during which jurisdictions can seek to obtain a successful override vote.

ANALYSIS

The State Constitution (Article XIII B) specifies that the Appropriation Limit restricts the amount of revenue that can be appropriated. Not all revenues are restricted by the Limit, only those that are “proceeds of taxes”. The majority of the major General Fund revenue sources (Sales Tax, Property Tax, Utility Tax, Business Taxes, Telephone Line Tax) are classified as proceeds of taxes, and are, therefore, subject to the Limit. Special fund revenue sources subject to the Limit generally include local construction tax revenues. Each revenue source is reviewed annually for classification as subject to, or exempt from, this Limit.

Appropriation Limit Adjustment Factors

In addition, proceeds of taxes may be spent on several types of appropriations that do not count against the Limit. The law allows a city to spend tax proceeds on voter-approved debt, costs of complying with court orders and federal mandates, with certain restrictions, and expenditures for qualified capital outlay. Appropriations for these excludable categories do not count against the Limit.

As a result of Proposition 111, the City is required to choose between two annual inflation factors and two population growth factors.

The choice offered for the annual inflation factor is the greater of (1) the growth in California per capita income or (2) the growth in non-residential assessed valuation due to new construction within the City. The data necessary to calculate the increase in non-residential assessed valuation is not currently available from the County Assessor. Until such information is available, it is recommended that the City approve the 2014-2015 Appropriation Limit on a provisional basis using the inflation factor of California per capita income.

The choice offered for the annual population growth factor is the greater of the growth in City or County population. The California State Department of Finance provided the 2013 population growth rates for both the City of San José and County of Santa Clara at 1.72% and 1.50%, respectively. Based on these growth rates, it is recommended that the City Council approve the 2014-2015 Appropriation Limit using the City's population growth factor.

Calculation of the 2014-2015 Appropriation Limit

The application of the annual growth factors to the 2013-2014 Limit result in a 2014-2015 Limit of \$936,545,078:

2013-2014 Appropriation Limit	\$ 922,831,397
Inflation factor	X 0.9977
Population factor	<u>X 1.0172</u>
2014-2015 Appropriation Limit	<u>\$ 936,545,078</u>

Based on these calculations, the City Attorney, as required by the State Constitution, has prepared a resolution for City Council consideration that would establish the 2014-2015 Appropriation Limit for the City of San José at \$936,545,078.

Appropriations Subject to the Limit

The amounts in the City's 2014-2015 Proposed Budget subject to the Limit (net proceeds of taxes) total \$648,178,846, which represent 69% of the Appropriation Limit. This amount is approximately \$288 million below the required Limit:

2014-2015 Appropriation Limit	\$ 936,545,078
2014-2015 Appropriations Subject to Limit	<u>(648,178,846)</u>
Amount Under Limit	<u>\$ 288,366,232</u>

When the annual budget is prepared each year for the City of San José, the appropriations subject to the Appropriation Limit are typically well below the Appropriation Limit as shown below:

Fiscal Year	Appropriation Limit	Appropriations Subject to the Limit*	Amount Under Limit
2013-2014	\$923 million	\$600 million	\$323 million
2012-2013	\$864 million	\$510 million	\$354 million
2011-2012	\$821 million	\$515 million	\$306 million
2010-2011	\$790 million	\$458 million	\$332 million
2009-2010	\$798 million	\$458 million	\$340 million

* Actual data used for 2009-2010 through 2012-2013; Proposed Budget data used for 2013-2014.

Over the last five years, and including 2014-2015, the City's appropriations subject to the Appropriation Limit have remained well below the Appropriation Limit, with these appropriations totaling between 57% and 69% of the Appropriation Limit. Given the size of this gap, it is unlikely that the City will exceed the Appropriation Limit in the upcoming years without significant changes to the City's tax structure.

EVALUATION AND FOLLOW-UP

At the end of the 2014-2015 fiscal year, the Finance Department will reconcile actual revenues and expenditures to ensure compliance with the Gann Limit.

PUBLIC OUTREACH

- Criterion 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- Criterion 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**
- Criterion 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

HONORABLE MAYOR AND CITY COUNCIL

June 10, 2014

Subject: Adoption of a Resolution Establishing the Fiscal Year 2014-2015 Appropriation Limit

Page 5

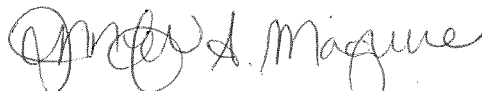
While the recommended actions do not meet any of the above criteria, this memorandum will be posted on the City's website for the June 17, 2014, Council Agenda.

COORDINATION

This memorandum was coordinated with the City Attorney's Office.

CEQA

Not a project.

A handwritten signature in black ink, appearing to read "Jennifer A. Maguire". The signature is cursive and somewhat stylized.

JENNIFER A. MAGUIRE

Deputy City Manager/Budget Director

For questions, please contact Margaret McCahan, City Manager's Budget Office, at (408) 535-8132.

PAGE IS INTENTIONALLY LEFT BLANK