SANTA BARBARA COUNTY
BOARD AGENDA LETTER

Clerk of the Board of Supervisors
105 E. Anapamu Street, Suite 407
Santa Barbara, CA 93101
(805) 568-2240

Agenda Number:	
Prepared on:	16 March 2001
Department Name:	County Administrator
Department No.:	012
Agenda Date:	3/20/01
Placement:	Departmental
Estimate Time:	2 Hours
Continued Item:	NO
If Yes, date from:	

TO:	Board of Supervisors
FROM:	Michael F. Brown County Administrator
STAFF CONTACT:	William Chiat (568-3407) Director of Organizational Effectiveness
SUBJECT:	Goleta Incorporation Revenue Neutrality Agreement

Recommendation(s):

That the Board of Supervisors:

1. Receive a staff presentation and recommendations on the Revenue Neutrality Agreement for the incorporation of the proposed City of Goleta;
2. Adopt the proposed Revenue Neutrality Agreement reached with Goleta*Now!* for Module A;
3. Adopt in principle the proposed Revenue Neutrality Agreement for Module A+B pending action by LAFCO; and
4. Provide direction to staff as appropriate.

Alignment with Board Strategic Plan:

This recommendation is primarily aligned with Goal #1: An Efficient Government Able to Respond Effectively to the Needs of the Community; Goal #3: A Strong, Professionally Managed County Organization; and Goal #6: A County Government that is Accessible, Open, and Citizen-Friendly.

Executive Summary and Discussion:

The incorporation of Goleta is governed by the Cortese-Knox Local Government Reorganization Act of 1985. Under §56845, the Local Agency Formation Commission (LAFCO) may not approve a proposal for incorporation unless it finds the revenues transferred to the new city are "substantially equal" to the expenditures for services transferred. This is not the case with Goleta, as concluded by the initial fiscal analysis. There are significantly more revenues transferred than service costs in both incorporation options under study by LAFCO (Module A and Module A+B).

Nonetheless, the Act provides LAFCO the ability to approve an incorporation that does not meet the above test if it finds either: 1) the County (and all of the subject agencies) agrees to the transfer; or 2) the negative fiscal effect has been adequately mitigated. The chief proponents of the incorporation have represented the interests of the proposed new city in the negotiations.

Revenue Neutrality Negotiations

Since late October, County staff has been meeting with the proponents to craft a revenue neutrality agreement for your Board's review that assures both the fiscal feasibility of the new city and minimizes the negative fiscal impact to the County. On 25 September 2000 your Board adopted Principles of Revenue Neutrality (see box). The principles were also adopted by Goleta*Now!* and provided the foundation for the negotiations and the proposed agreement.

For the last three months staff and the proponents have been meeting in often twice weekly sessions to fully understand all the issues and develop creative solutions that respect the adopted principles. Though tempting to focus on positions, the negotiation teams worked hard to keep these negotiations interest-based. In the end the agreement discussed below was developed based on the interests of both parties.

In addition to the principles of revenue neutrality, three other goals were identified by the negotiation team. Those included:

- Funding for on-going countywide services for the residents in the new city
- Defined time period for a mitigation payment
- Sharing in future risk and opportunity

Principles of Revenue Neutrality For Goleta Incorporation

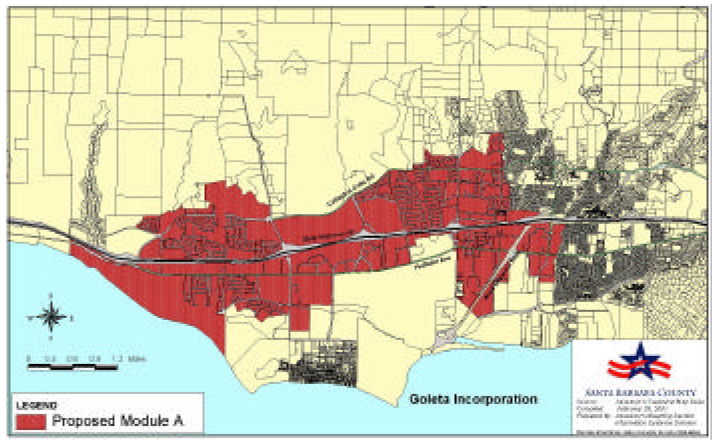
These principles are intended to allow LAFCO to make the required findings that the City is fiscally feasible and has prudent reserves, and negative fiscal impacts to the County are adequately mitigated. These principles are intended to:

1. Assure the initial fiscal feasibility of the City.
2. Minimize potential negative impacts on the County resulting from incorporation.
3. Not decrease the service levels of either the City or the County.
4. Provide incentives for future annexations to the City of Goleta.
5. Avoid litigation.

"*Revenue neutrality*" is a term only loosely defined in the legislation. Staff has studied most of the other incorporations consummated under this legislation and found that the neutrality agreements reached in each circumstance were significantly different. Further, there is no case law to help define what is considered neutral. As staff has previously indicated to your Board, however, in almost all cases the counties tended to transfer some additional revenues to the new city over the cost of the services transferred in order to insure the fiscal feasibility of the new city. This is required in large part due to the administrative costs which result from adding another government without a corresponding transfer of service or revenue to fund those costs from the County. These costs typically include such areas as city administration, city attorney, finance department, city council and clerk, elections, and department directors. Conversely, your Board has discussed the benefits of creating a new City of Goleta, and the value of local governance and decision-making. Therefore staff has approached this negotiation with the notion of flexibility in assuring both the fiscal feasibility of the city and the fiscal impact to the County.

Negotiated Revenue Neutrality Agreement

The revenue negotiation teams (County staff and the chief proponents) were placed in an unusual situation by LAFCO. Typically the negotiations would focus on a single option advocated by the incorporation proponents. In the case of Goleta, LAFCO asked that agreements be developed for both the *GoletaNow!* proposal (Module A), and a second option adding UCSB/Isla Vista (Module A+B). The proponents have long argued not to include UCSB/Isla Vista (Module B) in the proposal, and understandably, were reluctant to participate in the development of an agreement which included Module B. In discussing this situation with the LAFCO staff, it was decided to negotiate the agreement for Module A, and then LAFCO staff and County staff would apply the same components to create a revenue neutrality agreement for Modules A+B. That outcome is discussed later in this letter.



The draft Revenue Neutrality Agreement is included with this letter as Attachment 1 for your Board's consideration. Key provisions of the agreement include:

1. ***Revenue Sharing for Countywide Services***. The County will continue to provide countywide services to the residents of Goleta after incorporation. It was agreed that the residents should participate in the funding of those services. Therefore the agreement calls for 50% of the property tax that would accrue to the new city from Module A and 30% of the sales tax that would accrue to the new city from Module A to continue to accrue to the County—in perpetuity—for the cost of these services. There is no cap on the growth of these funds. In the first year, that equates to approximately $3.3 million allocated to the County.

2. ***Mitigation Payment***. With the revenue sharing described in #1 above, there remains a gap of approximately $2.2 million between the revenues transferred to the new city and the cost of services transferred. The agreement calls for a mitigation payment to be made for 10 fiscal years following incorporation. This will be accomplished through revenue sharing during the 10-year period where the County receives an additional 20% of the sales tax from Module A and 40% of the transient occupancy tax (TOT) from Module A facilities. Together these amount to the approximately $2.2 million. In addition it was agreed that the County would not share in any increase to the TOT that results from a) any new facilities which are built subsequent to the date of incorporation; or 2) any increase in the TOT tax rate which the city might impose.

The first two components of the agreement are based on sharing of revenue sources in order that both entities share risk. Property tax is the most stable revenue source, and under this agreement both the County and the new city retain 50% of the property tax. Sales tax and TOT can fluctuate greatly depending on the economy. Under this agreement both the new city and the County will benefit if they increase, and share the risk if they decrease. Pending the release of the final Comprehensive Fiscal Analysis (CFA) next month, the County has developed a spreadsheet to analyze the fiscal results of this agreement. The analysis for Module A is included with the Board letter as Attachment 2.

3. ***First Year Service Repayment***. Cortese-Knox requires the County to continue to provide services to the new city for the remainder of the fiscal year following incorporation. The proponents are currently considering a 1 February 2002 incorporation, thus requiring the County to provide services for five months. The cost is approximately $2.1 million. During that five months, the revenue sources begin accruing to the new city. The Comprehensive Fiscal Analysis (CFA) had

anticipated the new city would reimburse the County for the cost of those services over five years (approximately $420,000/year). The analysis of the new city's budget, however, indicated that while it would still have a reserve, it would run at a deficit for several of its early years. Therefore the agreement calls for the County to forgive the first year transition service repayment.

4. ***Deferral of a Portion of First-Year Mitigation Payment***. The agreement calls for the County to defer payment of $1.5 million of the first year mitigation payment to year 11. The deferral is interest free. This provision, along with previous provisions, assures the new city will have a projected minimum fund balance of $1.5 million during the ten years in the analysis. This general fund balance is projected to be in excess of $3 million by the end of the tenth year.

5. ***Contract Services***. The city will contract with the County to provide Sheriff law enforcement, public works, and parks maintenance services. Those contracts will initially run for five fiscal years, and then an annual renewal at the discretion on the new city and the County. The provision results in a significant savings to the new city by reducing the department indirect costs which the new city would have to mitigate if they choose not to contract.

6. ***Property***. County-owned roads, lands, parks, and open spaces—including Los Carneros Park and Santa Barbara Shores—will transfer to the new city. The County agreed to work with the new city to transfer its sublease of the Goleta Community Center. The agreement calls for the new city to assume the remaining Santa Barbara Shores debt payments. Properties remaining with the County include fire stations and Flood Control District property.

7. ***Fire District***. The Fire Department is not affected by this incorporation and will continue to provide its existing services as a fire district. The County will retain ownership or easements for the fire properties in the incorporation. The agreement calls for the fire district to receive a new tax allocation factor, if it accrues to the County as a result of this incorporation, for increased services in the Goleta Valley.

8. ***Redevelopment Agencies***. The new city will include a Redevelopment Agency (RDA). The agreement calls for the existing Old Town Goleta RDA project area to be transferred (assets and liabilities) to the new city. The Isla Vista project area will remain with the County RDA. The property in Storke Ranch will continue to contribute its tax increment to the IV RDA even though it will be in the new city. The agreement calls for no RDA expansion of the existing project area or new RDA project areas within the new city during the first 10 years after incorporation.

9. ***Housing-Related Programs***. The new city will become a member of the various housing program consortia, at a minimum, through the current program or contract periods. These include the HOME and McKinney programs and the CDBG consortium. This will ensure that the County and participating cities will not lose any existing funding and the County and participating cities will remain eligible for the anticipated significant increase in CDBG monies next year after designation as an urban county by HUD.

10. ***Transition Loan***. The County will provide the new city with a loan of up to $100,000, at the Treasurer's pool interest rate, to assist with transition costs between the time of election and when it begins to receive its own revenues.

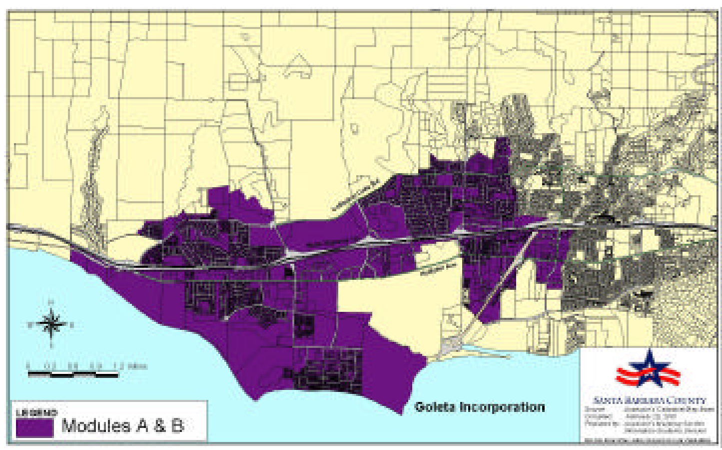
Fiscal Impacts on the County

In most respects the agreement mitigates much of the fiscal impact on the County. It is difficult to estimate the exact fiscal impact on the County, as the agreement calls for sharing percentages of various revenue sources. In general, it is anticipated that for the first ten years the cost impact to the County is between $400,000 and $600,000/year. This is in part because of the forgiveness of the first year services, but also because more revenues will be transferring to the new city than service costs. Some of this difference will be offset by ancillary revenues the County will receive because cities and counties in California share different pots of monies. Much of this impact will accrue to the County in the early years of incorporation. It is likely the County will use its strategic reserve to help buffer the impact on operating departments.

At the conclusion of the tenth fiscal year after incorporation, the impact to the County will increase significantly. At that time the mitigation payment will end (20% of the sales tax and 40% of TOT). That amount is currently approximately $2.2 million, and will have grown over the ten years. The County has ten years to prepare for this reduction in revenues.

Revenue Neutrality for Modules A+B

LAFCO asked that the CFA and revenue neutrality discussions contemplate a second option of Module A+B. This would add UCSB and Isla Vista with Module A as the new City of Goleta. As previously described, County staff and the proponents did not negotiate a specific revenue neutrality agreement for this option. However the agreement for Module A is designed in such a way as it can be readily applied to an A+B configuration. The provisions in the agreement are applicable to this option.



Attachment 3 provides the resulting fiscal analysis of Module A+B. In this case, the County transfers more municipal services than revenues. Therefore there is no 10-year mitigation payment as in Module A. However the population is significantly higher, as will be the costs of on-going countywide services. Therefore the agreement calls for 50% of the property tax from Module A+B and 48% of the sales tax from Module A+B to continue to accrue to the County—in perpetuity—for the cost of these services.

Because Module B is a large municipal service area for the County and due to the large number of people in a relatively small area, a new city in this configuration would retain significantly more revenues than Module A alone. In addition, the new city would receive substantially higher subventions from the state than Module A. The fiscal impact to the County would remain relatively similar as described previously. However, the new city would have substantially higher reserves at the end of each fiscal year. Staff estimates that under this scenario, the new city will have over $15 million in general fund reserves by the end of the tenth year. Because of the large number of residents in IV/UCSB and the relatively few road miles added, there is a significant increase in the road fund reserve. Module A+B shows a road fund balance of nearly $17 million by the 10^{th} year. The fiscal impact to the County is approximately the same as with Module A.

Staff recommends that your Board adopt the Module A+B revenue neutrality agreement in principle only. Were LAFCO to select Module A+B for the boundaries of the new city, a revised agreement would be required. Staff recommends that your Board take a more detailed review of that agreement prior to final approval.

Options and Next Steps

The Cortese-Knox Act provides your Board with three options.

1. ***Approve this agreement***. Should your Board approve this agreement, LAFCO would be able to make a finding pursuant to §56845 that the County agrees to the transfer even though revenues transferred exceed service costs transferred. LAFCO staff will integrate the agreement into the terms and conditions of the incorporation. Once approved by LAFCO the entire package will be sent to the voters for approval in November.
2. ***Approve in part or with modifications***. Your Board may approve part of the agreement and/or seek modifications in the agreement. Staff would then need to meet with the chief proponents and attempt to negotiate a resolution. Should an agreement then be reached, staff will return to your Board for approval or rejection of the agreement. At this stage of the incorporation, time is of the essence in order to achieve a November election.
3. ***Reject this agreement***. Should your Board reject the agreement, LAFCO has the responsibility to develop its own methods to mitigate the fiscal impact on the County. LAFCO terms and conditions will be presented to the voters as part of the incorporation election, and if successful, would be imposed on the County. Your Board would not be involved in the decision. Should your Board object to the mitigation imposed by LAFCO your Board may appeal for a review by the State Controller and/or seek other legal remedies. In either case, this option is likely to delay the cityhood election.

LAFCO has already set its final schedule to hear and consider the incorporation proposal. Key next steps and dates in the process include:

- 12 April 2001 — LAFCO consideration of Negative Declaration and the preferred eastern boundary
- 26 April — LAFCO consideration of the proposal and terms and conditions, including the findings of revenue neutrality and final incorporation boundaries
- 3 and 10 May — LAFCO continuation of previous consideration, if necessary
- 3 July — Final date for Board to hold and conclude protest hearing
- 6 November — Election
- 1 February 2002 — Incorporation

Mandates and Service Levels:

The County of Santa Barbara is obligated by the Cortese-Knox Act to negotiate an agreement with the proponents to achieve revenue neutrality.

Fiscal and Facilities Impacts:

There are significant fiscal impacts to the County that may result as a consequence to adopting this agreement. Those impacts are discussed above in the section entitled “Fiscal Impacts to the County”.

Attachments:

1. Draft Revenue Neutrality Agreement
2. Fiscal Analysis for Module A
3. Fiscal Analysis for Modules A+B

Concurrence:

County Counsel
Auditor-Controller

c: Auditor Controller
LAFCO Executive Officer
Goleta*Now!*