COUNTY ADMINISTRATIVE OFFICE
COUNTY OF MONTEREY

MEMORANDUM

DATE: March 28, 2024

TO: Board of Supervisors

FROM: Sonia M. De La Rosa, County Administrative Officer

SUBJECT: Options to Enhance the County's Financial Condition in FY 2024-25 and Future Fiscal Years

On March 12, 2024, the County Administrative Office (CAO) presented the countywide financial forecast to the Board of Supervisors (Board). The forecast indicated continued growth in discretionary revenues. However, the growth is not sufficient to keep up with the increased costs of doing business.

As indicated during the March 12th Board Meeting, all ongoing discretionary revenue has been allocated to departments; therefore, the Board directed staff to identify and research options to enhance revenues or reduce expenditures to address the forecasted deficits in FYs 2024-25 through 2026-27. The revenue enhancement options are detailed below, and implementation will likely necessitate hiring a consultant to help the County maneuver the requirements for every option to identify the most practical approach for the Board's consideration.

Revenue Enhancement Options

Transaction ("Sales") Tax Rate Increase per Revenue & Taxation Code ("R&T" section 7285, et seq.)

Sales tax is the additional amount paid based on a percentage of the selling price of goods and services purchased. This tax is collected and sent to the state and local governments.

- Process: An increase in the unincorporated sales tax rate requires a ballot measure to be brought to voters. The measure could request the voters to approve a general district tax (R&T, section 7285) which would require a majority vote or a special tax (R&T, section 7285.5) which would require approval by two thirds vote. If approved as a general tax, revenues could be for general government purposes, but if approved as a special tax, the funds would be restricted for the specific purpose stated in the ballot measure. If successful, revenue will likely be available in the fourth quarter of FY 2024-25.
- The existing unincorporated sales tax rate is 7.75%, which is one of the lowest in the region. Of this total, 7.25% represents the minimum amount charged at the state level and 0.50% is a district tax. District taxes are imposed under the Transactions and Use Tax Law (R&T, section 7285, et seq.) and are added to the statewide base tax rate of 7.25%. Local taxes are imposed under the Bradley-Burns Uniform Local Sales and Use Tax Law. Local taxes are imposed in every city and county in California at a uniform rate of 1.25%, which is a component of the statewide base sales and use tax rate (7.25%).
- The distribution of the 7.25% tax receipts are as follows:
    - 3.94% to the State's General Fund
    - 0.50% to the Local Public Safety Fund to support local criminal justice activities
    - 0.50% to Local Revenue Fund to support local health and social services programs (1991 Realignment)
    - 1.06% to Local Revenue Fund 2011

    - 0.25% to local transportation funds
    - 1.00% to county operations
- The distribution of district taxes of 0.50% for the County are as follows:
    - 0.125% to the Monterey-Salinas Transit special district.
    - 0.375% to the Monterey Transportation Safety Transactions and Use Tax
- Timing: A ballot measure could be presented to the voters as early as the November 2024 general election if a ballot measure is fully reviewed and approved by the Board and submitted to Monterey County Elections by August 9, 2024.
- Once approved by the voters, the Board would have to consider an ordinance to implement the increased sales tax rate. If adopted, the ordinance is not operative until the first day of a calendar quarter, or prior to the first day of the first calendar quarter, commencing more than 110 days after the adoption of the ordinance (R&T, section 7265).
- Once approved, county staff must coordinate with the California Department of Tax and Fee Administration. (R&T, section 7270).
- Financial Impact: This option could yield an increase of an estimated $3.1 million for an increase of 0.25% (8% rate) or $12.4 million for a 1% increase (8.75% rate). If approved, the County will also have to pay the state and administrative fee of up to $175,000 to implement the new sales tax for the County.

Establish a New Utility User Tax

The County does not currently have a utility user tax (UUT). This tax is an “excise” or “privilege” tax imposed on a person using utility services. A county may levy a UUT on the consumption of electricity, gas, water, sewer, telephone, telegraph, and cable television services in the unincorporated area.

- Process: Establishing a new UUT requires a ballot measure to be presented to the voters for approval and a change in the County Code through the adoption of an ordinance and required time to institute the tax after approval.
- Timing: A measure could be presented to the voters as early as the November 2024 general election if a ballot measure is fully reviewed and approved by the Board and submitted to the elections department by August 9, 2024. The measure could request the voters to approve a general tax which would require a majority vote or a special tax which would require approval by two thirds vote. If approved as a general tax, revenues could be for general government purposes, but if approved as a special tax, the funds would be restricted for the specific purpose stated in the ballot measure. Revenue will likely be available in the fourth quarter of FY 2024-25 or first quarter of FY 2025-26.
- Once approved by the voters, the Board would have to consider an ordinance to implement the tax.
- Financial Impact: Estimating the financial impact will require hiring a consultant to analyze the potential financial impact as this will depend on the specific areas of the ordinance that will be amended. The Treasurer’s Office would require added resources to develop and administer the collection of this new tax.

Increase the Existing Transient Occupancy Tax

Transient Occupancy Tax (TOT) is a tax imposed under the authority of R&T, section 7280. The tax is levied as a percentage of the rent charged to transient guests in hotels/motels, including properties rented through short-term rental services like Airbnb.

- Process: This would require a measure to be approved by the voters. If this approach is followed, the County’s TOT ordinance will have to also be updated.
- Timing: A measure could be presented to the voters as early as the November 2024 general election if a ballot measure is fully reviewed and approved by the Board and submitted to the elections department by August 9, 2024. The County’s existing TOT is a general tax. Staff would recommend any measure presented to the voters continues as a general tax, revenues could be for

general government purposes, but if approved as a special tax, the funds would be restricted for the specific purpose stated in the ballot measure. Revenue will likely be available in the fourth quarter of FY 2024-25 or first quarter of FY 2025-26.

- Once approved by the voters, the Board would have to consider an ordinance to amend Chapter 5.40 of the Monterey County Code.
- Financial Impact: The current rate is 10.5%. If the County were to increase the rate by 0.25% it could bring additional $608,000 annually, if increased by 2% it could bring an added $4.8 million annually. This amount represents the County's share of the increase (65.81%) as the current policy would redirect 25% to the Road Fund and 9.19% to the development set aside.

Amend contribution policy to Development Set-Aside
The County's Development Set-Aside (DSA) is a program established by the Board of Supervisors which promotes economic development, tourism, filmmaking, and cultural arts activities that strengthen the County's economic base. On an annual basis, to fund this program, the Board considers whether to provide a share of its TOT to four community organizations: The Monterey County Convention and Visitors Bureau (MCCVB), the Arts Council for Monterey County, the Monterey County Film Commission, and the Monterey County Business Council (MCBC). These organizations submit annual marketing plans outlining specific programs and tasks in support of economic development. If the Board decides to fund the program, the County enters into annual agreements with these agencies to implement the plans.

TOT is a county general tax, currently set at 10.5%, on hotel room revenues at all short-term stay hotels and accommodation rentals. On an annual basis for numerous years, the Board allocated a percentage of the **growth** to three organizations (MCCVB, the Arts Council and the Film Commission); however, in recent years the Board has annually allocated the contribution to three of the organizations based on a percentage of the County's TOT from the prior audited fiscal year. The percentages for the MCCVB, the Arts Council and the Film Commission have been 6%, 1.98% and .95%, respectively. MCBC has received a flat amount of $100,000. However, in difficult budget years, the County has capped or lowered its contributions to these organizations.

- Process: In this budget year, the Board can decide to hold the contribution levels at the same levels as the revenue provided in FY 2023-24 (capped at $2.8 million), return to the original practice of allocating only a percentage of the growth, or decide to use the tax for other purposes.
- Timing: This could be approved as part of the budget hearings and the revenue will be available immediately on July 1, 2024.
- Financial Impact: If the Board decided to maintain the level of funding in FY 2024-25 the same as in FY 2023-24 (with the cap), the County could have approximately $720,000 more funds to provide services in the community. The Board can alternatively decide to only allocate a percentage of the growth and to provide services in the community.

<u>**Decrease Expenditures**</u>
Suspend or lower the supplemental unfunded accrued liability contribution program
The supplemental accrued liability program was established by the Board in June of 2021. Under this program a policy was established to help address the growing unfunded accrued liability (UAL) for the County's pension plan. The County contracts with the California Public Employees' Retirement System (CalPERS) to provide retirement benefits for permanent county employees, and each year, the County receives actuarial valuation reports, which identify the employer contribution rates for the following year, as well the UAL. The UAL has grown significantly due to changes in wages, reduced earnings, changes in demographics, and policy changes enacted by the CalPERS Board, such as reductions to the assumed discount rate and shorter amortization schedules for these liabilities. The latest actuarial report for the valuation dated June 30, 2022, estimates the UAL for the County plan at $947.5 million.

Under the County's existing plan and policy, the target is to bring the pension plan funded status to 100% of the Actuarial Accrued Liability related to the County's pension plans with the goal to accumulate sufficient assets to fund all projected benefit payments. The UAL supplemental plan has accumulated over $100 million since its inception. If the plan is suspended and the resources for this plan are allocated to other ongoing expenditures, the County would consider reinstatement of the program as part of the review of the year end fund balance.

- Process: The Board can decide to implement by directing staff to suspend or lower the supplemental unfunded accrued liability contribution by a majority to vote during the budget process or during any regularly scheduled Board meeting.
- Timing: This could happen as part of the budget hearings for FY 2024-25.
- Financial Impact: If the Board approves this change, $10.9 million in discretionary funds would be available for ongoing services as of July 1, 2024. This would result in a suspension or lowering of the supplemental unfunded accrued liability contribution to be revisited at year-end.

One-time Funding Options

Redirect funds from the Compensated Absences Assignment

The compensated absences assignment was established by the Board to provide funding to the County when ongoing revenues are insufficient to cover the costs of accrued benefits payable to employees separating from the County.

- Process: The Board can make this decision by directing staff to use a portion of these one-time funds for a different purpose.
- Timing: This could happen as part of the budget hearings for FY 2024-25.
- Financial Impact: The compensated absences assignment has $12.7 million available. The payments for compensated absences (payouts or employees leaving employment with the County) in FY 2023 are estimated at $5.9 million. Similar amounts could be payable on an annual basis depending on employee turnover.

Conclusion

Implementation of any of these options will require further research and Board consideration, but this memo provides the major points to consider as the County moves forward with its FY 2024-25 budget process. As part of this process, the County Administrative Office will be presenting a balanced recommended budget in late May 2024 which could incorporate any of these potential solutions if feasible.

In addition, development of the Recommended Budget is a collaborative effort between the County Administrative Office and all departments, with overall direction provided by the Board. If some options in this report are implemented, they will require coordination with various internal and external stakeholders.

Please contact me if you have any questions.