CITY OF
LONG BEACH

Memorandum

Date: August 21, 2020

To: Mayor and Members of the City Council

From: Thomas B. Modica, City Manager

Subject: **Update on the Split Roll Ballot Measure**

The purpose of this memorandum is to provide information about California Proposition 15, the Tax on Commercial and Industrial Properties for Education and Local Government Funding Initiative, on the November 3, 2020 ballot and its potential impacts to the City of Long Beach. The measure, commonly known as "split roll," proposes to apply different tax formulas and rates for commercial and industrial properties than for residential properties, and herein will be referenced simply as the Split Roll Initiative.

Background

The structure of California's property tax system has remained relatively unchanged since 1978, following the passage of Proposition 13, which reduced and limited property tax rates on commercial, industrial, and residential properties. Proposition 13 passed with overwhelming support, receiving 62 percent of votes in favor, largely due to the growing tax burden at the time. Prior to Proposition 13, property tax rates were set cumulatively by cities, counties, and school districts. As assessed property values skyrocketed in the 1970s, so too did property tax rates. Between 1974 and 1978, the tax burden leaned heavily on the side of homeowners; residential assessments increased by 120 percent, while commercial property assessments, by comparison, rose by 26 percent. A volatile property tax system, combined with stagnant incomes and rising inflation, drove support for what many still consider to be the most lasting transformation to the State's property tax system.[1]

Proposition 13 limits the property tax rate to one percent of the purchase price on commercial, industrial, and residential properties. For each year after the original purchase date, the annual adjustment to the property tax is capped at two percent or the rate of inflation, whichever is lower. Upon a change of ownership, property tax rates are reset based on the assessed value of the property at the time of purchase. The Proposition 13 tax system, administered by counties, generates approximately $65 billion annually. Statewide, 60 percent of property tax revenue is allocated to cities, counties, and special districts, with the remaining 40 percent to schools and community colleges.

The market value of properties in the state, however, typically increases by more than two percent per year, creating a disparity between taxable assessed value and market value. Compared with the pre-1978 system, in which property tax rates fluctuated based

[1] Goldberg, Lenny. 2010. "Proposition 13: Tarnish on the Golden Dream." In *Remaking California: Reclaiming the Public Good*, edited by R. Jeffrey Lustig, 44. Berkeley, CA: Heyday Books.

on market conditions, after 1978 local governments and educational institutions have received a fraction of these revenues through the fixed system established by Proposition 13. Ever since the measure was approved, there have been numerous failed attempts to tax commercial and industrial properties at different rates than residential, in an effort to recover some of the lost revenues at the local level. And in October 2018, the Schools and Communities First campaign successfully qualified the Split Roll Initiative for the November 3, 2020 ballot.[2]

The Split Roll Initiative

The Split Roll Initiative seeks to amend the California State Constitution to require commercial and industrial properties to be taxed based on their market value beginning in 2022-23, while continuing to assess residential properties at their Proposition 13 levels. Reassessment would be phased in over three years for commercial retail properties with 50 percent or more of the property occupied by small businesses, defined as businesses that are independently owned and operated in California with less than 50 full-time employees. Exemptions include commercial agricultural land, real property used as residential property, and property owners with holdings in California valued at $3 million or less. The Initiative further eliminates the business tangible personal property tax on equipment and fixtures for small businesses, and other businesses would receive an exemption for the first $500,000 in value of their personal property. All exempted properties would continue to be taxed based on the Proposition 13 model.

Led by the Schools and Communities First campaign, the Split Roll Initiative has received registered support from the California Democratic Party, Los Angeles Unified School District, and Former Vice President Joe Biden, along with a number of other Federal, State, and local representatives. Opposition has been received by the California Chamber of Commerce, California Taxpayers Association, and California Business Roundtable, among numerous business advocacy groups. Campaign contributions in support of the measure have reached almost $20 million, while opposition has gathered more than $3 million.

Popular opinion on the matter is similarly divided. According to a survey conducted by the Public Policy Institute of California (PPIC) between April 1 and April 9, 2020, 53 percent of likely voters support the Split Roll Initiative. This demonstrates a six percent increase from a survey conducted in November 2019, which found 47 percent of likely voters in support. A series of eight surveys conducted by PPIC and one by a collaborative between the University of Southern California's Dornsife College and the Los Angeles Times finds 50.5 percent of likely voters in support of the Split Roll Initiative. And on June 19, 2020, the League of California Cities board voted to take no position on the measure.

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[2] In August 2019, the campaign announced they would begin collecting signatures for a revised version of the initiative, and on May 29, 2020, the updated version successfully qualified for the ballot, replacing the original.

Potential City Impacts

If approved by the voters, the Split Roll Initiative is projected to result in substantial revenue increases to local governments and schools throughout California. According to the Legislative Analyst's Office (LAO), annual net revenue increases in property tax statewide are estimated to range from $7.5 billion to $12 billion, dependent upon the real estate market. A portion of the revenues generated through the measure would be distributed to the State to supplement decreases in personal income and corporation taxes collected, and to counties to cover administrative costs for implementing the reassessment required by the measure. Less these costs, the LAO estimates between $6.5 billion and $11.5 billion in net increased revenue distributed among local governments and education institutions. Roughly 60 percent of this total, between $3.9 billion and $6.9 billion, is projected to go directly to counties, cities, and special districts.

Beyond this statewide estimate, however, there is no definitive method to assess the impact of the Split Roll Initiative to individual jurisdictions, and rough estimates for Long Beach vary significantly. One methodology—taking the LAO's statewide range and utilizing the City's current assessed valuation to estimate the City's share of the overall statewide total—results in a potential revenue increase from $1.3 million to $2.4 million. Alternatively, evaluating the difference between the City's property market values and the assessed valuation under the current tax system indicates the impact could be closer to $3 million. Yet another approach, offered by the Schools and Communities First campaign sponsoring the Split Roll Initiative, estimates $32 million in additional revenue to Long Beach. The methodology and assumptions used to arrive at this estimate, however, are vague, including the application of exemptions to certain properties. It also appears that the amount may be overstated and does not disaggregate the City's share from estimated shares to other entities such as educational institutions.

All three approaches above assume Long Beach will receive an amount proportional to its share of revenues under the existing tax structure. The City of Long Beach receives, on average, 22 percent of total property taxes paid by property owners in the City, amounting to $125 million in FY 19-20. Yet, we do not know how reassessments will alter the overall share of property tax revenue across jurisdictions. Since counties would be ultimately responsible for determining the taxable value of properties according to the Initiative's eligibility criteria and distributing the additional revenues among local governments, we will need to revise the projected revenues for Long Beach as further information is made available by Los Angeles County.

Staff is currently working with the County to get more details about the County's potential allocation methodology and how it might impact the City. While they do not have individual estimates for each local jurisdiction, they estimate an increase in property tax revenue for the County's General Fund of approximately $393.4 million, or 5 percent of locally generated revenues. Similar to the disparity between the City's and the Schools and Communities First campaign's estimates for Long Beach, the County's projection is substantially lower than the campaign's of $1.337 billion.

Without additional information, evaluating the actual fiscal impact to the City is problematic for several reasons. First, the allocation methodology across counties, cities, and special districts remains undefined. Many possible allocation methodologies exist, such as redistributing revenues based on percentage of assessed valuation growth within a county. Second, it is difficult to identify how exemptions will be applied to Long Beach properties, and thus how much additional property taxes will be generated, given that exemptions are not solely based on the valuation of an individual property within the City. Last, the timeline for implementation and revenue generation is unclear, due to the administrative challenges related to a statewide reassessment process for applicable commercial and industrial properties.

Next Steps

Staff will continue to monitor this issue and provide updates related to the Split Roll Initiative's impact. In addition to the Split Roll Initiative, there are 12 other propositions on the November 2020 ballot. Information on these ballot measures will be provided ahead of the November election. If you have any questions, please contact Tyler Bonanno-Curley at (562) 570-5715 or Tyler.Curley@longbeach.gov.

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