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REPORT MAY 2016

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# Back in the Black

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A fiscal strategy for  
investing in  
San Jose's future

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PROJECT CHAIR  
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[www.spur.org/sjfiscalstrategy](http://www.spur.org/sjfiscalstrategy)

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## EXECUTIVE SUMMARY

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The City of San Jose needs more money. Although the “capital of Silicon Valley” has the highest median household income of any major city in the country,<sup>1</sup> years of budget cuts and staffing reductions have left the city in a precarious position, struggling to provide an appropriate level of public services with the resources it has. Compared to peer cities in Santa Clara County and around California, San Jose has less revenue per capita from the two largest sources of local government revenue: sales and property taxes. This public-sector scarcity stands in stark contrast to the region’s wealth and San Jose’s considerable affluence, as measured by high property values and household incomes.

It doesn’t have to be this way. While there are some deeply rooted causes behind the city’s fiscal distress, San Jose has options. The purpose of this report, developed collaboratively by SPUR and Working Partnerships USA, is to provide a road map for San Jose to achieve the resources necessary to deliver high-quality public services.

This report identifies the following findings about San Jose’s fiscal condition:

1. San Jose experienced acute fiscal strain and an imbalance of short-term revenues and costs between fiscal years 2002–03 and 2010–11 based on objective metrics of fiscal duress.
2. A number of factors contributed to the city’s fiscal challenges. They included economic events such as the dot-com crash and the Great Recession, which were compounded by the city’s decision to increase pension benefits. San Jose also recovered from these recessions more slowly and more modestly than most other Bay Area cities, leaving it with fewer resources for providing services to its large population.
3. The city weathered its fiscal strain by making major cuts in staffing and service levels, as well as drawing down its reserves and assets. The cuts were significant, affected employee morale and resulted in a loss of expertise. The cuts also negatively impacted the quality of life for residents as police response times increased, roads deteriorated, and libraries, parks and recreation centers were shuttered or understaffed.
4. San Jose’s service costs have been competitive with other large cities, especially its low spending on public safety.
5. San Jose’s overall fiscal health is shaped by many factors outside its direct control, such as state restrictions on property and sales taxes, high voter thresholds for new taxes, macroeconomic forces such as recessions and the pattern of business growth in the South Bay that put San Jose further from the geographic center of Silicon Valley than many of its neighbors.
6. San Jose’s fiscal health is also affected by factors it controls directly, such as past pension policy decisions. Another is the city’s history of annexation, land conversions and largely sprawling development, which has left it with a significant amount of housing compared to its job base, a large and costly road network to maintain, and lower property taxes per acre compared to denser cities in the Bay Area. Starting in the 1980s, San Jose also financed a good portion of its development through its former redevelopment agency, which borrowed roughly \$2 billion in property tax revenue. The costs of paying off that debt will deny revenues to the city, school

<sup>1</sup> San Jose’s median household income is nearly \$84,000 per year (average 2010 to 2014 in 2014 dollars) compared with the national average of \$53,500. Compared to the other large cities, San Jose’s income is higher: San Francisco (\$78,000), Washington D.C. (\$69,000), Seattle (\$67,000), San Diego (\$66,000), Austin (\$55,000), Boston (\$54,500), New York City (\$53,500), Oakland (\$53,000), Denver (\$52,000), Los Angeles (\$50,000), Sacramento (\$50,000), Chicago (\$48,000), Phoenix (\$47,000), San Antonio (\$46,000), Houston (\$46,000), Dallas (\$43,000), and Philadelphia (\$37,500). See: U.S. Census, <http://www.census.gov/quickfacts/>

districts, the county and other agencies for decades to come. This debt, combined with the limited return on redevelopment agency projects in the form of secondary revenue streams (sales taxes from retail sales, new business taxes, etc.) have limited San Jose's current tax revenues.

7. These internal and external factors have left San Jose at a comparative disadvantage. Compared to the other large cities in California, San Jose has relatively low per capita property tax revenue. Compared to large cities in Santa Clara County, San Jose is last in per capita sales tax revenues.
8. Given this history, the city's dwindled resources and its low revenue levels, San Jose will have trouble making new investments and keeping pace with rising costs. Should costs rise unexpectedly or should another recession hit, San Jose would be more vulnerable than it was before the Great Recession because it has fewer unrestricted resources to draw from and fewer costs and services to cut.
9. To mitigate its risk to future downturns and to increase services, San Jose needs to attract investment as well as increase revenues.
10. While the past shaped where San Jose is today, important market and demographic shifts may begin to work in the city's favor going forward. San Jose remains one of the few communities willing to accept both job and housing growth, which should position it to attract growing firms and new residents.

Our recommendations to strengthen San Jose's fiscal condition fall into four categories:

**Strategy 1: Expand the city's tax base through strategically attracting investment and supporting economic growth.**

1. Support dense mixed-use development in walkable, transit-supported areas.
2. Maintain restrictions on the conversion of key employment lands to residential uses.
3. Provide additional resources to the economic development and planning departments to facilitate private investment and economic growth.

**Strategy 2: Increase local resources through well-designed revenue measures for *specific* purposes.**

4. Implement a citywide retail strategy.
5. Identify opportunities to increase local fees to the levels recommended in San Jose's user fee study.
6. Pass new general obligation bonds to pay for deferred maintenance, particularly roads.
7. Expand the use of economic development and investment tools such as community facilities districts, enhanced infrastructure financing districts and business improvement districts.

**Strategy 3: Increase local resources through well-designed revenue measures for *general* purposes.**

The following is a menu of potential taxes for San Jose to consider raising. The city should carefully evaluate and select those that align with its goals and constituencies.

8. Update, restructure and modernize the business tax.
9. Increase the local sales tax by one-quarter cent (0.25 percent).
10. Increase the Utility User Tax.
11. Adopt a parking tax.
12. Pass a "soda tax" on sugar-sweetened beverages.

13. Increase San Jose's real estate transfer tax and allow some of the incremental growth to support General Fund activities.
14. Pass a parcel tax dedicated to General Fund activities.
15. Increase the disposal tax on solid waste.

**Strategy 4: Reform the public finance system to provide more flexibility and to support the regionalization of revenues and services.**

The responsibility for reforming the system of public finance in California goes well beyond San Jose and will require connecting with leaders from cities throughout California who have been affected by the limitations of the state's finance laws.

16. Make adjustments to property taxes and Proposition 13.
17. Broaden and revise the state and local sales tax.
18. Reform the state and/or federal gas tax.
19. Lower voter thresholds for general obligation bonds, particularly for housing.
20. Pursue revenue sharing across Santa Clara County and consider tying it to housing production.
21. Explore opportunities to regionalize services by providing key services to neighboring jurisdictions on a contract basis.

Ultimately, San Jose will need to grow investments and resources to align its ongoing costs and revenues, to invest strategically in essential and new services, to update declining infrastructure, and to continue attracting residents, businesses and visitors with a strong economy and a high quality of life.

# How to Think About the Fiscal Health of Cities

Cities are a reflection of the Jeffersonian maxim that “government is best which is closest to the people.”<sup>2</sup> In fact, the services provided by city governments most directly contribute to the quality of life for a city’s residents, businesses and visitors. And the quality of those services is directly tied to the fiscal health of the local government. Well-maintained parks and streets, reliable public safety, open libraries and even the capacity to plan for future growth are all contingent on a city having a strong tax base, a high-quality workforce and well-managed budget and financial processes. When a city is in fiscal trouble, as San Jose was during the 2000s, the services and the benefits they provide hang in the balance.

How can San Jose, which experienced such major fiscal strain, grow its tax base and make investments for its future? Answering this requires an understanding of three key issues:

## **First, how do San Jose’s finances work?**

To understand how a city works requires understanding not only its budget but also its overall finances. How does it generate revenue from its residents, businesses and visitors? How does it use that revenue to fund the services its constituents need and want? The balance of what is taxed and what is paid for, what is bought and what is sold, is an art rather than a science. Broadly, it is determined by the unique needs and preferences of those who live, work and play in a city and by the services that a city prioritizes to attract new people and growth.

## **Second, what is San Jose’s fiscal challenge?**

Many cities face fiscal trouble from time to time. Understanding the nature of San Jose’s fiscal challenge requires an analysis of objective indicators to characterize the problem and arrive at a tailored set of solutions. Broadly, three indicators characterize a state of fiscal strain: 1) a city cannot pay upcoming bills on time, 2) fiscal year costs are higher than revenues or 3) a city cannot pay long-term bills well into the future.

## **Third, what long-term factors have shaped San Jose’s underlying fiscal health?**

Cities constantly make decisions within a set of constraints. Cities are subject to many forces largely beyond their control and to the consequences of their own policy decisions and choices made over many years. Understanding these factors, and categorizing them as external or internal, is key to tailoring solutions to San Jose’s specific condition.

*External forces include:* the state constitution and statutes that control how cities can collect revenues from sources like property and sales tax and how they can levy taxes, assessments and fees; business and economic cycles; regional competition and the clustering of economic activity and growth outside a city’s borders.

*Internal decisions include:* city area, density and land use patterns over time; finance strategies to fund development (such as the use of redevelopment tools); economic development strategies; revenue and expenditure decisions, and the financial balancing of the two.

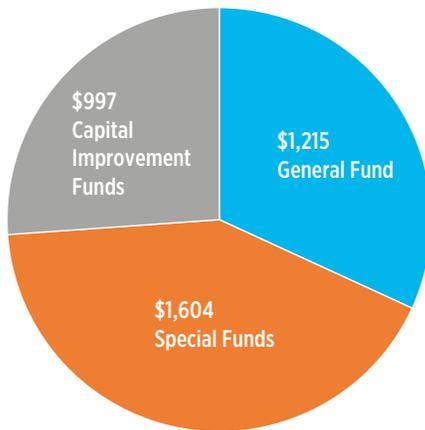
The broader goal of this report is to help San Jose become not only fiscally strong but also one of the most economically dynamic and livable cities in the United States.

<sup>2</sup> President Johnson attributed this sentiment to Jefferson in his March 16, 1965, message to Congress. See: <https://www.nytimes.com/books/98/04/12/specials/johnson-voting.html>

# How Do San Jose’s Budget and Finances Work?

San Jose is a diverse city with just over 1 million residents and more than 413,000 jobs across the public and private sectors.<sup>3</sup> Each year, San Jose’s residents, businesses, mayor, city council and city staff prioritize and formalize a budget. The budget is a forward-looking plan of what services and capital improvements to fund, as well as how to pay for them.

In fiscal year 2015–16, San Jose’s adopted budget of \$3.2 billion was made up of more than 100 individual funds that fell into three categories: general, special and capital improvement.<sup>4</sup> Summarized in Figures 1 and 2 below, the General Fund of \$1.2 billion paid for most of the core city services, like public safety, parks, libraries and general city management. Special funds totaled roughly \$1.6 billion and included large fee-based programs such as waste management and sewage treatment, as well as housing and city planning activities services that relied on federal community block grants. Capital improvement funds totaled nearly \$1 billion in 2015–16 and were dedicated to large, one-time construction needs including streets, buildings and storm water and sewer systems.<sup>5</sup> The sum of general, special and capital improvement funds was larger than the total budget by \$625 million due to some double counting in transfers and loans between funds.



**FIGURE 1:**  
**What Are the Main Funds of the San Jose Budget?**  
 San Jose’s budget categories, in millions  
 San Jose’s General Fund is about one-third of the city’s overall \$3.2 billion budget.

Source: San Jose’s 2015–16 Adopted Budget in Brief, <http://www.sanjoseculture.org/DocumentCenter/View/48001>

Throughout the budget process, the General Fund gets a great deal of attention, as it’s the large, flexible pool of money that can be adjusted to meet core service needs. Breaking down just the General Fund, Figure 2 shows that the largest sources of revenue are the property tax, sales tax and utility tax, which together provide over half of the General Fund revenues. In turn, roughly half of the General Fund is used for public safety, which includes police and fire services. It’s worth noting that the entirety of the city’s property tax revenue only covers roughly half the cost of delivering public safety services. This is typical of other large urban cities in California as well.

<sup>3</sup> Population figures for 2015 are available from the California Department of Finance at: <http://www.dof.ca.gov/research/demographic/reports/estimates/e-1/view.php>. According to the San Jose City Auditor, citing the 2013 American Community Survey, San Jose’s residents are 33% Asian, 33% Hispanic, 28% Non-Hispanic White, 3% African American, and 3% Other. Job statistics for 2013 are available from the Center for Continuing Study of the California Economy: <http://www.sanjoseca.gov/DocumentCenter/View/47999>

<sup>4</sup> See: Office of the City Manager, Adopted 2015–2016 Operating Budget, <https://www.sanjoseca.gov/DocumentCenter/View/47377>

<sup>5</sup> Some city services, like transportation, are funded from a combination of funds.

General Fund Sources		
	Source	\$ (in millions)
Revenue	Property tax	\$255
	Sales tax	\$190
	Utility tax	\$115
	Licenses and permits	\$49
	Franchise fees	\$48
	Other revenue	\$45
	Business tax	\$44
	Local, state and federal aid	\$44
	Charges for services	\$41
	Hotel tax	\$15
	Fund balance	\$293
Other	Transfers	\$76
	<b>TOTAL</b>	<b>\$1,215</b>

General Fund Uses	
Use	\$ (in millions)
Public safety	\$525
Reserves	\$186
Community services	\$139
City-wide expenses	\$123
General government	\$90
Capital maintenance	\$69
Capital contributions	\$56
Transfers	\$27
<b>TOTAL</b>	<b>\$1,215</b>

**FIGURE 2:**  
**Sources and Uses in San Jose's General Fund, 2015-16**

Property tax is the largest General Fund revenue source, but it covers only about half of public safety costs.

Source: San Jose's 2015-16 Adopted Operating Budget, pp. III-35 to III-38, <https://www.sanjoseca.gov/DocumentCenter/View/47401> and <https://www.sanjoseca.gov/DocumentCenter/View/47402>

## What Is the Budget Process in San Jose?

The annual budget process stretches from October through June and begins with a review of the previous year's financial and service-level performance. In the fall, a preliminary base budget is developed for the upcoming fiscal year by comparing the projected cost of delivering existing services with projected revenues for that year. In February, the city manager's budget office releases five-year cost and revenue projections that include expected revenue growth and the cost of current services adjusted for inflation. At the direction of the city manager, each city department proposes services and expenditure strategies that correspond to the city's fiscal outlook. Throughout late winter and early spring, the City Council and mayor set budget priorities based on community, staff and council input, which culminates in the City Council-approved Mayor's March Budget Message. With guidance from this message, the proposed budget is released in May for review in public workshops and budget study sessions. Incorporating feedback from these meetings, the mayor issues a June Budget Message, and the City Council adopts a final budget by June 30.<sup>6</sup>

June 30 also marks the close of the fiscal year. At this time, the city's finance department compiles receipts of all prior-year revenues and expenditures, along with the value of what the city owns (assets) and what it owes (debt), and publishes these numbers in the San Jose Comprehensive Annual Financial Report. These reports are used to track how well the budgeted projections of revenues and costs performed and to assess the fiscal health of the city.<sup>7</sup>

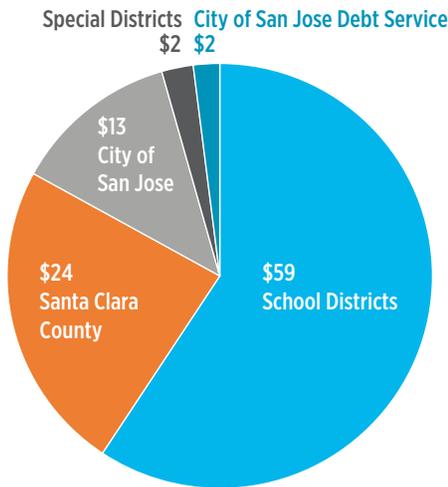
Across California, there are two broad categories of property tax. The main category, general property tax, is assessed on the value of property, pooled at the county level and redistributed to counties, schools, cities and special districts, as well as to pay off some kinds of debt. The other category is made up of special property taxes that require voter approval and are assessed with a specific purpose in mind, such as improving the sidewalks in a particular neighborhood. Figure 3 shows that most of the total property tax (general and special) that San Jose residents and businesses pay goes to schools and the county. This is common across all cities in California.

Property tax is levied on both residential and business owners. In the late 1970s, businesses and residents paid an equal share of the total property tax. After the landmark voter initiative Proposition 13 changed property tax rules in California, residents began paying a much greater share. In fiscal year 2015-16, residential owners paid more than 65 percent of Santa Clara County's property tax.<sup>8</sup> (Proposition 13 and its effect on property tax revenues is discussed more in Chapters 3 and 4.)

<sup>6</sup> For a full schedule of the budget process, see: <http://www.sanjoseculture.org/index.aspx?NID=489>

<sup>7</sup> San Jose also makes audited financial data available through this portal: <http://www.sanjoseculture.org/DocumentCenter/View/48227>

<sup>8</sup> See: 2015-2016 Assessor's Annual Report, p.16, <https://www.sccassessor.org/DocLib/Annual%20Report15.pdf>



**FIGURE 3:**  
**Where Do San Jose's Property Taxes Go?**

For every \$100 of property tax paid by San Jose residents and businesses in 2014–15, the city only kept \$13, with most of the remainder going to schools and the county.

Source: Statistical section of San Jose's 2014–15 Comprehensive Annual Financial Report, p. 225, [http://sanjose.granicus.com/MetaViewer.php?meta\\_id=546403](http://sanjose.granicus.com/MetaViewer.php?meta_id=546403)

San Jose owns numerous assets, including infrastructure, buildings, land, vehicles, equipment and furniture. As these assets age, they depreciate or lose value, much like a personal car. Figure 4 shows that after accounting for depreciation, San Jose's infrastructure is its largest asset. In turn, the cost of maintaining this infrastructure is also very large. Net capital assets fall into two categories: governmental functions and enterprise functions. "Governmental" refers to core city functions; these assets include all roads, bridges and buildings such as libraries and City Hall. "Enterprise" functions raise and use revenue as if they were a separate business; these assets include San Jose's airport and its municipal water, wastewater treatment and parking systems.

	Governmental net capital assets	Enterprise net capital assets
Infrastructure	\$ 3,946	\$ -
Buildings	\$ 1,080	\$ 1,140
Land	\$ 389	\$ 135
Improvements other than buildings	\$ 206	\$ 623
Construction in progress	\$ 50	\$ 29
Vehicles, equipment, furniture and fixtures	\$ 27	\$ 92
Intangible assets	\$ -	\$ 13
Property under capital leases	\$ -	\$ 1

**FIGURE 4:**  
**What Assets Does San Jose Own?**

Capital asset value minus depreciation, as of June 2015 (in millions)

Citywide infrastructure is San Jose's largest asset. Enterprise assets include San Jose's airport and its municipal water, wastewater treatment and parking systems. Every other asset in San Jose falls under the first column.

Source: Notes to Basic Financial Statements, San Jose Comprehensive Annual Financial Report 2014–15, p. 71: [http://sanjose.granicus.com/MetaViewer.php?meta\\_id=546403](http://sanjose.granicus.com/MetaViewer.php?meta_id=546403)

Like most cities, San Jose has used debt to finance capital investment. Debt that must be paid over the next year totaled \$278 million as of June 2015. San Jose's long-term obligations, or those due beyond the next year for capital purposes, include long-term governmental debt, long-term enterprise debt and redevelopment debt.

San Jose's long-term debt issued for governmental purposes totaled \$1.2 billion in fiscal year 2014–15, or roughly \$1,200 per resident. This included things like general obligation bonds and special assessment bonds. Long-term enterprise debt totaled \$1.4 billion in fiscal year 2014–15 and will be paid back by user fees. Also, the city financed developments and improvements in redevelopment areas over the last 30 years by dedicating a stream of the incremental property tax revenues generated from these projects to pay back the debt. Redevelopment debt totaled \$2

billion in fiscal year 2014–15, and San Jose is currently sending \$38 million per year in property tax revenue to pay it down.<sup>9</sup>

San Jose's other large long-term obligation is for pension and post-retirement benefits, which totaled \$3.4 billion in unfunded liability as of June 2014. However, the actual amount paid by the City of San Jose over time is likely to differ from this figure, as investment funds cover a portion of the cost. The total bill also varies according to health care costs, the performance of retirement investment funds, and any changes to retirement plans and policies the city makes, and more.<sup>10</sup>

## How Should a City Decide Where to Spend Its Money?

During the budget process, cities and constituents face many trade-offs as they consider how to use the revenue they've raised. A city must weigh many factors to decide how to deploy a limited amount of resources to meet all of its needs.

### **Risk trade-offs:**

Should the city grow reserves to protect existing services in future downturns, or should it use any excess revenues to expand services now?

### **Timing trade-offs:**

Should the city attract the best employees through paying higher wages in the near term or by promising better retirement benefits in the future?

Should the city prioritize infrastructure maintenance now or push it off to pay for more immediate services and pay a bigger maintenance bill later?

### **Capital-vs.-services trade-offs:**

Should the city pursue revenues that allow for the building of capital, or should it pursue the development of revenue streams to fund ongoing services?

### **Land use trade-offs:**

Should the city make land use decisions based primarily on fiscal needs (such as approving more big-box stores that generate sales tax revenue) or pure city planning goals that improve the city (such as retrofitting shopping centers to become more walkable and neighborhood-focused)?

San Jose has adopted 13 guiding budget principles to help in weighing these and other trade-offs. By employing these principles, the city aims to: structurally balance ongoing costs and revenues, use one-time revenues for one-time costs, prioritize all new service requests together, maintain adequate reserves and fund balances, not issue long-term debt for ongoing service needs, limit capital improvement projects that require high maintenance and operations costs from the General Fund, and use performance data to evaluate new service funding requests.<sup>11</sup> How well the city adheres to these principles and what tradeoffs San Jose makes with its resources together determine the services and amenities that are offered to citizens and businesses in San Jose.

<sup>9</sup> Redevelopment figures were gathered through interviews with accountants at the Santa Clara Controller-Treasurer's Department in March 2016.

<sup>10</sup> See: San Jose City Auditor, Measuring San Jose's Financial Condition (2016), p. 7, <https://www.sanjoseca.gov/DocumentCenter/View/53977>

<sup>11</sup> Budget guiding principles can be found in Appendix A of San Jose's Five Year Economic Forecast and Revenue Projections, 2016–2020, <http://www.sanjoseca.gov/DocumentCenter/View/40704>

# What Is San Jose’s Fiscal Challenge?

To characterize San Jose’s fiscal challenge and inform our recommendations, we first evaluated San Jose’s fiscal performance against seven objective and commonly used measures of fiscal health.

Fiscal health is a city’s ability to pay for the services that citizens have come to expect with the resources they provide, year after year.<sup>12</sup> Fiscal health means a city can pay for expected services in three time frames:

1. It can pay quickly approaching bills on time.
2. It can balance costs and revenues over a fiscal year.
3. It can pay bills it’s obligated to pay well into the future.

The analysis of fiscal health reveals two key findings. First, San Jose experienced an acute fiscal strain when rising personnel costs coincided with the dot-com recession in the early 2000s and the Great Recession, which stretched from late 2007 through mid-2009. Second, even after the recovery from these recessions, which led to deep cuts in personnel costs and the elimination of service delivery citywide, San Jose continues to struggle with inadequate resources to meet growing deferred maintenance needs or to fully plan for its future.

	Indicator	What it tells us
Ability to pay bills on time	Low liquidity	A city is having trouble paying its upcoming bills on time due to limited available funds.
Aligning revenues and costs	Operating deficits	At the end of the fiscal year, the city’s revenues have not been enough to cover operating costs.
	Fixed costs rising more quickly than revenues	The costs that a city has little flexibility to change in the short run are growing more quickly than revenues to cover them.
	Declining service delivery	A city has had to cut services to balance the budget.
Ability to pay bills in the future	Growing deferred maintenance bills	The city has not sufficiently invested in maintaining its infrastructure, leading to a growing overall deferred maintenance bill and higher annual maintenance costs in the future.
	Declining governmental unrestricted net position	A city’s net position is its assets minus liabilities. Assets include cash, property, land and equipment. Liabilities are all the upcoming bills the city is legally required to pay. If a city’s net position is negative, the city owes more than it could liquidate to pay for governmental services.

**FIGURE 5:**  
**Seven Indicators of a City’s Fiscal Strain**

Together these indicators offer a full picture of a city’s fiscal health.

Sources: SPUR adaptation of League of California Cities’ *The California Municipal Financial Health Diagnostic* (2014), <http://www.californiacityfinance.com/Diagnostic1411.pdf>; and *Governing* magazine’s 10-Point Test of Governmental Financial Health, [http://www.governing.com/papers/A-Guide-to-Managing-Your-Jurisdiction-s-Financial-Health-1500.html?promo\\_code=gov\\_papers\\_web\\_instituteslider](http://www.governing.com/papers/A-Guide-to-Managing-Your-Jurisdiction-s-Financial-Health-1500.html?promo_code=gov_papers_web_instituteslider)

<sup>12</sup> Justin Marlowe, *Governing Guide to Financial Literacy*, vol. 2 (2015).

## Can San Jose Pay Its Bills on Time?

### Indicator 1: San Jose's liquidity declined between 2008 and 2013.

There were several years when San Jose had relatively fewer available resources to pay upcoming bills. Current net assets are defined as all the investments, inventory and receivables expected to be converted to cash in the very near term, minus payables, accrued liabilities and the current portion of debt also expected to be paid in the very near term. While there is some natural fluctuation in current net assets from year to year, a multiyear decline demonstrates a period of fiscal strain.

San Jose experienced multiple years of current net asset decline starting in 2007-08 and was the most strained in 2010-11, its third straight year of decline, the lowest point on Figure 6. In addition, for the following two fiscal years, the city had no funds available in its Budget Stabilization Reserve.<sup>13</sup>



**FIGURE 6:**  
**San Jose's Liquidity Dropped Sharply After the Great Recession**

Current net assets in millions, not inflation adjusted

Current net assets — which are all assets expected to be converted to cash in the very near term, minus all debt expected to be paid in the very near term — dropped after the Great Recession. This indicates a low liquidity roughly from 2008-09 to 2012-13.

Source: SPUR analysis of "Balance Sheet, Government Funds," City of San Jose Comprehensive Annual Financial Reports, Fiscal Years 2003-04 through 2014-15. Latest year available on p. 24, [http://sanjose.granicus.com/MetaViewer.php?meta\\_id=546403](http://sanjose.granicus.com/MetaViewer.php?meta_id=546403)

## Are San Jose's Revenues in Line With Its Costs?

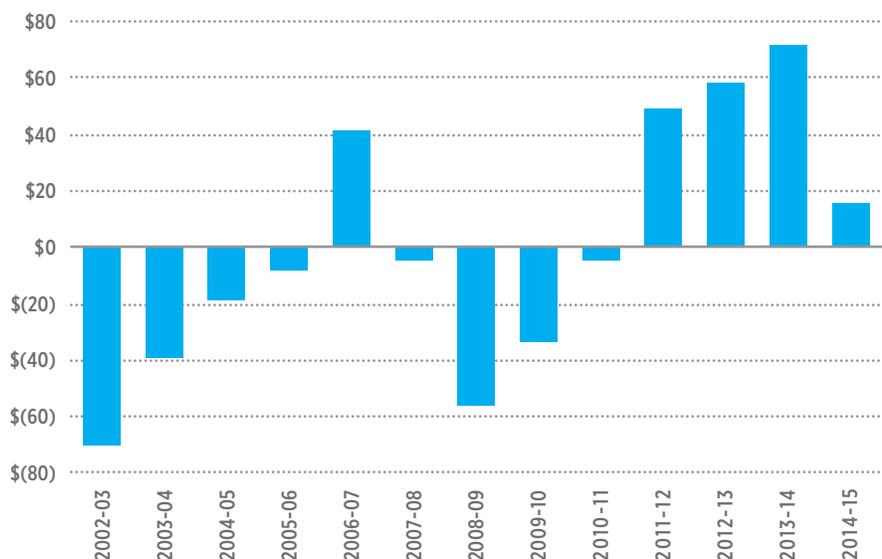
### Indicator 2: The City of San Jose's General Fund revenues were not enough to cover operating costs in almost every year from 2003 to 2011.

Figure 7 shows the difference between San Jose's total General Fund revenues and expenditures at the close of each fiscal year. In a year with a negative number (i.e., an operating deficit), San Jose's total service costs were higher than the revenues to pay for them.

A deficit in any one year may simply be the result of a short-term or cyclical trend and can be addressed in a number of ways: by drawing down the General Fund balance, moving funds between accounts, using reserves, or even borrowing or making service cuts. However, operating deficits that persist for multiple consecutive years may be a symptom of a larger structural problem. We see evidence of this in San Jose. Operating deficits were the norm from 2002-03 through 2010-11, with the exception of 2006-07, mirroring a pattern of recessions and recovery. While San Jose's operating deficits turned to surpluses starting in 2011-12, San Jose is still recovering from drawing down its reserves to cover expenses.

<sup>13</sup> The Budget Stabilization Reserve is designed to help the city maintain services in years when revenue or cash is suddenly less than expected. Data on reserve levels are taken from Exhibit 4, p. 13, <https://www.sanjoseca.gov/DocumentCenter/View/41113>

In addition, the latest budget forecast projects mostly small budget deficits for the next five fiscal years.<sup>14</sup> The only surplus, of \$5.7 million, is expected in 2016–17. The following four years of deficits range between \$4.2 and \$15.8 million. This indicates that the actual surpluses of 2011–12 through 2014–15 may not continue.



**FIGURE 7:**  
**Operating Deficits Were the Norm in San Jose From 2002-03 to 2010-11**

**General Fund operating deficits in millions, not inflation adjusted**

The difference between San Jose’s total General Fund revenues and expenditures is shown here. In a year with a negative number (i.e., an operating deficit), San Jose’s total service costs were higher than the revenues to pay for them.

Source: SPUR analysis of “Excess (Deficiency) of Revenues Over Expenditures,” San Jose City Comprehensive Annual Financial Reports, Fiscal Years 2002-03 through 2014-15. Latest year available on p. 151, [http://sanjose.granicus.com/MetaViewer.php?meta\\_id=546403](http://sanjose.granicus.com/MetaViewer.php?meta_id=546403)

**Indicator 3: The largest fixed cost to the General Fund — labor costs — grew faster than revenues during the 2000s.**

Personnel costs — including salaries, benefits, pensions and post-retirement costs — are the largest General Fund expenditure. These costs are relatively fixed and cannot be altered without changes to city policy.

Over the last decade and a half, three trends have emerged in San Jose’s personnel costs. First, between 2000–01 and 2008–09, personnel costs rose faster than revenues. Second, pension and post-retirement health-care payments made from the General Fund rose continually over the same time period, starting at roughly 4 percent and ending up at around 21 percent of General Fund expenditures. Third, overall personnel costs came down through a reduction in labor force and cuts in salaries and benefits to current employees starting in 2008–09.

While the increase in personnel costs as a percentage of the General Fund was partly caused by shrinking revenues, it was mostly due to accelerating pension and post-retirement costs (see Figure 8). In a 2010 review of San Jose’s pension cost structure, the city auditor found that the rising costs were due to five factors: 1) the growing number of retirees compared to the number of employees, 2) increased benefit policies that San Jose enacted in the late 1990s, 3) unfunded and rising health-care costs for retirees, 4) an error in the actuarial estimates that predict retiree costs, and 5) a decline in the value of retirement fund investments due to the Great Recession.<sup>15</sup> Except for San Jose’s benefit policies, these pressures apply to all cities and public-sector entities and are driving up the cost of providing pension payments and post-employment benefits everywhere.

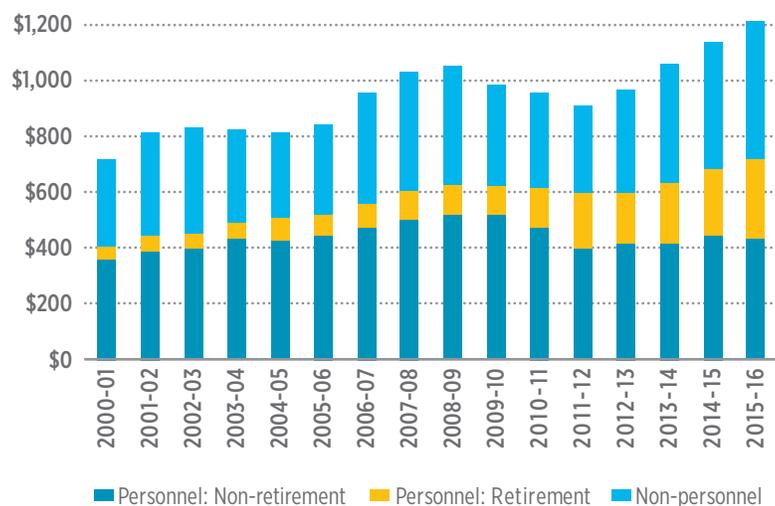
The City of San Jose recognized that its retirement costs weren’t sustainable and took action to modify pension policies and benefits by placing Measure B on the June 2012 ballot. Voters passed

<sup>14</sup> See: 2016–2017 City Manager’s Budget Request & 2017–2021 Five-Year Forecast and Revenue Projections for the General Fund and Capital Improvement Program, <https://www.sanjoseca.gov/DocumentCenter/View/54731>

<sup>15</sup> See: Office of the City Auditor, Pension Sustainability: Rising Pension Costs Threaten the City’s Ability to Maintain Service Levels — Alternatives for a Sustainable Future (2010), <https://www.sjretirement.com/uploads/fed/Item17FedOct2010.pdf>

the measure, but unions contested it and the Santa Clara County Superior Court overturned it.<sup>16</sup> Eventually a settlement was reached, and the city eliminated one-time annual bonus checks for retirees, established lower pension benefits for new civilian employees and required that all new employees pay into the health-care plans they'll have in retirement. San Jose should save nearly \$3 billion over the next 30 years from these changes, with \$2 billion coming from the shift of new employees to the new pension program.<sup>17</sup> While substantial, these savings will take multiple decades to take effect.

In the meantime, to bring personnel costs in line with revenues, the city froze wages, laid off staff, reduced benefits and restructured departments for an estimated savings of nearly \$40 million every year these policies are in effect.<sup>18</sup>



**FIGURE 8:**  
**Retirement and Other Fixed Costs in San Jose's General Fund**  
 While staffing costs declined after 2008, retirement costs continued to grow to over \$200 million per year.

Sources: San Jose Adopted Budgets 2000-01 through 2015-16, latest year available at <http://www.sanjoseculture.org/DocumentCenter/View/47403>; and "General Fund Structural Budget Deficit History & Service Restoration Priorities and Strategies," slide 8, [http://www.avca-sj.org/1-20-15\\_Study\\_Session\\_Presentation.pdf](http://www.avca-sj.org/1-20-15_Study_Session_Presentation.pdf)

**Indicator 4: Services across the city were continually cut year after year between 2001-02 and 2011-12.**

Recognizing that its fiscal strength was in trouble, the city adopted a three-pronged strategy: 1) reduce costs, 2) increase revenues and 3) reduce and eliminate services.<sup>19</sup> While eliminating services was a last resort, from 2001-02 to 2011-12 the city cut increasing numbers of staff and services. These cuts were made strategically, with nonessential services like street paving making up the first cuts and public safety reductions coming last. The duration of continued cuts indicates that minor reductions were not enough.

With personnel as its single largest cost, the city removed more than 1,600 positions from its budget. San Jose's adopted operating budgets from 2008-09 through 2012-13 show that, of the 1,600 cut positions, roughly 50 percent resulted from the reshuffling of employees and consolidating of departments, roughly 32 percent represented unfilled positions that were removed from the budget, roughly 17 percent came from layoffs or resignations, and less than 1 percent stemmed from removing benefits from part-time employees. Much of the reshuffling resulted in "bumping," which means that workers with more seniority lost their jobs and took positions usually filled by workers with less seniority, leading to job loss for those with the least

16 See: "Measure B Settlement Discussions," <http://www.sanjoseca.gov/index.aspx?nid=4657>

17 See: "Alternative Pension Reform Settlement Frameworks," <http://www.sanjoseca.gov/DocumentCenter/View/48248>

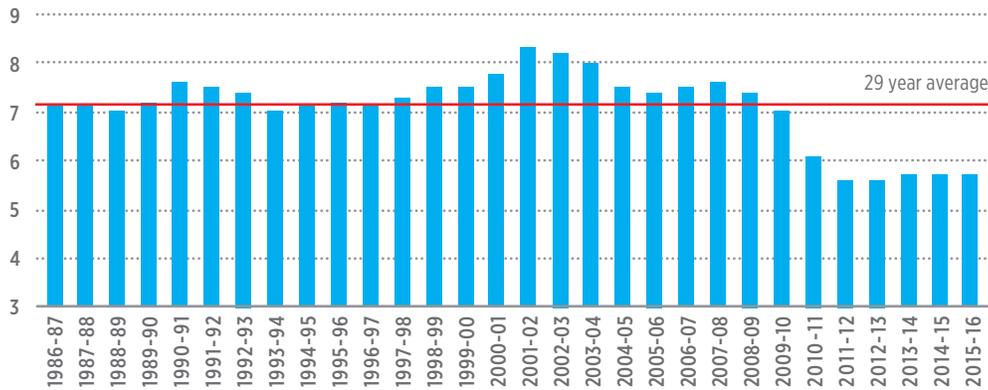
18 Slide 17 shows personnel cuts as an annual figure: [http://www.avca-sj.org/1-20-15\\_Study\\_Session\\_Presentation.pdf](http://www.avca-sj.org/1-20-15_Study_Session_Presentation.pdf)

19 The three-pronged approach is detailed in San Jose's General Fund Structural Deficit Elimination Plan (2008), <https://www.sanjoseca.gov/DocumentCenter/View/4627>

seniority. While this bumping took into account the long tenure of individual workers, it was highly disruptive during San Jose's cuts.

Rearrangement of personnel at this order of magnitude can evoke a sense of loss for many; residents and workers may be affected when the quality of their parks decline, police take longer to respond to calls and other aspects of their everyday lives are disrupted. City employees may also find themselves working for less compensation in an organization that is losing colleagues, productivity and morale.

In contrast to other financial indicators, the staffing reductions translate most directly into a palpable and clear loss for people across San Jose.



**FIGURE 9:**  
**San Jose Cut Many Positions From Its Budget in Recent Years**

San Jose's city staff per 1,000 residents, 1986-2015  
San Jose's budgeted staffing levels are at record lows.

Source: Office of the City Auditor, "Measuring San Jose's Financial Condition," (February 2016), <https://www.sanjoseca.gov/DocumentCenter/View/53977>

Figure 10 gives an overview of staffing cuts. The Parks, Recreation and Neighborhood Services Department experienced the most dramatic cuts, followed by strategic support staffing services (information technology, human resources and finance). Transportation and general government staff saw the next highest reductions, followed by public safety (police and fire) and library staff.

Some cuts were due to cost-savings innovations as opposed to reductions in services. For example, San Jose took advantage of partnerships with nonprofits to help staff and run community centers and to patrol some areas for public safety. Cities have also found that some services can be staffed through contractors at a lower cost, which may not affect the delivery of these services in the eyes of residents and businesses.

While Figure 10 shows deep staffing reductions, the full depth of cuts may not be represented here. In the most recent budget year, San Jose has been able to reinstate positions in some departments, and this year's staff count may not be a department's lowest in recent memory. Although the service cuts have been disruptive and difficult, not every service necessarily needs to be restored to its prior level. The city can now strategically decide which services to restore and which ones to modify in order to best meet its current and long-term needs.

Figure 10:

## San Jose Cut Staff Across Departments to Reconcile Rising Costs and Declining Revenues

### Reductions in budgeted positions across San Jose from 2001-02 to 2014-15

To cope with budget shortfalls, San Jose slashed key city services, including more than 40 percent of all budgeted staff in the parks and recreation department and nearly a third in the transportation department.

Service Area	Peak Staffing (Fiscal Year)	Current Staffing (2014-15)	Change From Peak	Change in Service Experience for Residents
Sworn Police Positions	1,395 (2008-09)	1,109	(21%)	It takes police nearly twice as long to respond to Priority 2 calls <sup>20</sup> compared to peak staffing years.
Sworn Fire Positions	758 (2007-08)	679	(10%)	In 2014-15, only 27 percent of trucks responded to the most urgent calls within their 8-minute target.
Parks, Recreation and Neighborhood Services	887 (2002-03)	551	(42%)	Cuts mean fewer rangers, less maintenance of open spaces and diminished community programs. Since 2006-07, the Safe Schools Campus Initiative has responded to 50% fewer incidents.
Libraries	367 (2005-06)	315	(15%)	Forty-four library staff were added in the last budget year, but average weekly library hours are still 33% lower than in 2007-08.
Transportation	536 (2001-02)	391	(27%)	The pavement condition index across the city is "fair" but slipping, a result of lack of funding and staffing.
General Government	219 (2005-06)	161	(26%)	Cuts to the administrative backbone of the city created a slower and less organized support system for direct city services.
Strategic Support (IT, HR, Finance)	206 (2002-03)	136	(34%)	Technology investments and training programs for city staff were largely curtailed, limiting efficiencies and opportunities to advance citywide skills.

Sources: San Jose's Adopted Budgets (2004-05 through 2014-15), annual San Jose City Auditor reports on service delivery from Jan 2011 through December 2015, and "General Fund Structural Budget Deficit History & Service Restoration Priorities and Strategies" (January 2015), [http://www.avca-sj.org/1-20-15\\_Study\\_Session\\_Presentation.pdf](http://www.avca-sj.org/1-20-15_Study_Session_Presentation.pdf)

## Can San Jose Pay Its Bills in the Future?

### Indicator 5: The city's annual unfunded maintenance need is growing every year, mostly from deteriorating roads.

The value of San Jose's land, buildings, vehicles and infrastructure is declining because depreciation and wear are happening faster than the city can invest in and maintain these assets.<sup>21</sup>

The city's largest capital asset is its roads. San Jose paved or resurfaced nearly 300 miles of its roads in 2002-03 but in 2014-15 resurfaced only 98 miles,<sup>22</sup> a drop of two-thirds. Much of this reduction is due to a decline in federal and state gas tax revenues, which provide roughly 60 percent of San Jose's road maintenance funding. Whatever the federal, state and county governments cannot fund becomes the responsibility of the city.

<sup>20</sup> According to the City Auditor's 2014-15 Annual Report on City Services, Priority 2 calls include those for recent or impending injury or property damage or for an incident where the property damage suspect is still in the area, as well as reports of missing children under 12 years old and missing persons with mental illness or disability.

<sup>21</sup> See: Office of the City Auditor, Measuring San Jose's Fiscal Condition (Feb. 2016), p. 21, <https://www.sanjoseca.gov/DocumentCenter/View/53977>

<sup>22</sup> "General Fund Structural Budget Deficit History & Service Restoration Priorities and Strategies" (Jan. 2015), [http://www.avca-sj.org/1-20-15\\_Study\\_Session\\_Presentation.pdf](http://www.avca-sj.org/1-20-15_Study_Session_Presentation.pdf)

In Figure 11, the two columns illustrate San Jose’s unfunded one-time needs and annual needs. One-time needs are singular repairs or installments of updated infrastructure. Of San Jose’s \$992 million in one-time needs in 2015, transportation made up roughly \$650 million, while parks, pools and open space accounted for another \$120 million.<sup>23</sup> Ongoing maintenance typically includes the regular repaving or sealing of roads, the repair of sidewalks and other needs that arise perennially. Every year that general maintenance is deferred, the annual cost of these needs compounds. The cost to restore all infrastructure to good condition has grown nearly four-fold since 2007, to its latest total of \$175 million. Of this, transportation’s share (which is mostly roads) was \$100 million as of 2015.

If the city does not address its rising deferred maintenance cost, this bill will only grow, a troubling sign that the status quo may make it very difficult for San Jose to maintain its current infrastructure into the future.

Year	One-time need (in millions)	Annual unfunded need (in millions)
2007	\$915	\$45
2009	\$873	\$49
2013	\$909	\$148
2015	\$992	\$175

Source: City of San Jose’s “Status Report on Deferred Maintenance and Infrastructure Backlog,” various years.<sup>24</sup>

**FIGURE 11:**  
**San Jose’s Annual Deferred Maintenance Bill Is Rising Quickly**

One time and annual unfunded infrastructure needs, not inflation adjusted

San Jose’s unfunded infrastructure maintenance bill is growing over time.

**Indicator 6: The city’s unrestricted governmental net position has declined by roughly 175 percent between 2002–03 and 2013–14.**

Year after year the City of San Jose has seen a decline in its governmental unrestricted net position, which is a measure of assets (cash, investments) minus liabilities (debt, interest and other obligations) that belong to governmental activities and that are not already earmarked or restricted for specific purposes. This figure does not include the capital assets discussed in Chapter 1, and it includes net pension liabilities only as of the 2014–15 fiscal year.<sup>25</sup> In total, governmental unrestricted net position reflects the resources the San Jose City Council could authorize to spend on services. When net position is negative, it means a city’s assets are worth less than the debt it owes for all future governmental unrestricted activities.

The trend in this indicator is troubling. As show in Figure 12, San Jose’s governmental unrestricted net position has declined fairly steadily, by roughly 175 percent, from 2002–03 to 2013–14. What’s worse, the net position has been negative for the last six fiscal years. Given that the City of San Jose sets aside reserves for general purposes (the Budget Stabilization Reserve and the Contingency Reserve), unrestricted governmental net position should at least equal the dollar amount kept in these reserves. In fact, San Jose has a policy that the Contingency Reserve retain a balance of roughly 3 percent of operating expenditures,<sup>26</sup> which would equate to between \$16 million and \$24 million across the fiscal years shown in Figure 12.

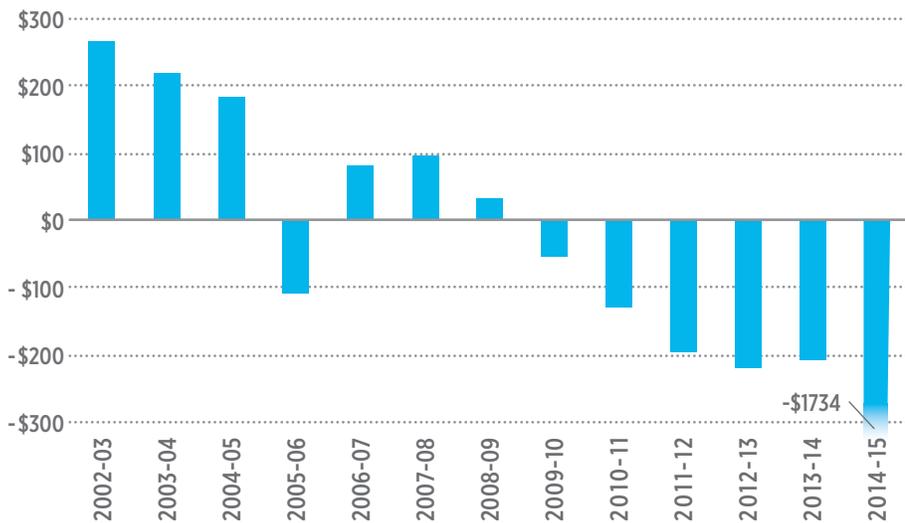
This suggests that San Jose’s deep cuts and recovery from the Great Recession have not been enough to push the city’s governmental unrestricted net position back into the black. San Jose will need to correct this in addition to restoring and adding services.

23 Other state and federal sources of revenue for transportation infrastructure are also in decline, putting more stress on local governments to pay these bills.

24 The latest “Status Report on Deferred Maintenance and Infrastructure Backlog” can be found here: <http://sanjoseca.gov/DocumentCenter/View/42827>

25 This change is due to a new requirement made by Governmental Accounting Standards Board Statement No. 68, which requires that cities now report net pension liability as part of the Statement of Net Position.

26 See: Office of the City Auditor, *Fund Balance and Reserves: San Jose Should Aim to Have Higher Safety Net Reserves Within the General Fund* (March 2015), <https://www.sanjoseca.gov/DocumentCenter/View/41113>



**FIGURE 12:**  
**San Jose's Net Position Has Declined Steadily**

**Governmental unrestricted net position in each year, not inflation adjusted**

San Jose's governmental unrestricted net position has been in a troubling, steady decline. Due to a change in the Governmental Accounting Standards Board, cities were required to start adding net pension liability to net position figures starting in 2014-15. For San Jose, this figure was roughly \$1.5 billion in liabilities that year, which pushes the bar down and off the chart.

Source: "Statement of Net Position," San Jose Comprehensive Annual Financial Reports for Fiscal Years 2002-03 through 2014-15. Latest year available on p. 22, [http://sanjose.granicus.com/MetaViewer.php?meta\\_id=546403](http://sanjose.granicus.com/MetaViewer.php?meta_id=546403)

## In short, San Jose has corrected many worrying fiscal trends, but its financial future is fragile.

It's clear that San Jose has gone through difficult times. The indicators above show a confluence of trends: rising personnel costs, declining revenues as a result of the Great Recession, and a correction to align costs and revenues that eliminated thousands of city staff positions and reduced services across the city. In more recent years, revenues have come into line with costs, but the city finds itself at a lower level of service than before. As we look forward, an unmet growing deferred maintenance bill and a lower net position mean that San Jose will have to dig itself out of a hole before it can invest in or grow services. In the next chapters, we'll explore how the city got into this position and what it can do to build a brighter future.

# What Long-Term Factors Shaped San Jose's Fiscal Situation?

While recent recessions and the rising costs of retirement benefits help explain San Jose's fiscal strain since 2000, this is not the full story. In fact, San Jose's fiscal options have long been constrained by a combination of state laws, economic cycles, competition with other South Bay cities and policy decisions made by previous city councils.

What factors have detracted from San Jose's long-term ability to raise and capture revenues, keep costs in line with revenues and weather economic downturns? To answer this question, in this chapter we analyze the external and internal factors, as well as constraints that have affected San Jose's ability to control costs or to manage its long-term fiscal health in other important ways. Six long-term factors have shaped San Jose's fiscal health over time.

The external factors, which are largely beyond San Jose's control, include:

1. The California system of public finance that cities operate under
2. Business cycles and macroeconomic conditions
3. Regional competition and the spatial growth of Silicon Valley

The internal factors, which are mostly within San Jose's control, include:

4. San Jose's economic development and land use decisions
5. San Jose's expenditure decisions
6. San Jose's revenue and taxation decisions

In summary, San Jose's current fiscal picture is affected by state laws that restrict all cities in their ability to adjust local tax rates or pursue additional revenues. San Jose also competes for jobs and investments with its neighbors in Santa Clara County yet, as the South Bay's largest city, faces greater demands for services. San Jose's widespread use of redevelopment (discussed on pages 27 through 29), in combination with the small share of land area devoted to employment uses, has limited current revenues. Lastly, San Jose has pursued a narrow set of new revenues since the 1990s and has kept many large costs low compared to other large cities.

## External Factors That Shape San Jose's Fiscal Strength

### **California's system of public finance restricts all cities in how they can raise and use important local revenues.**

While cities retain discretion in how they spend revenues, since the 1970s California voters and the state legislature have adopted numerous laws and policies that restrict how each city can raise revenue or adjust the rates of taxes. For example, state law regulates how much property owners pay in general property tax, how much of the property tax a city gets, the definition of city "fees," and what level of voter approval cities must seek before raising revenue for local purposes. Figure 13 outlines when these laws were approved and how each has affected cities in California.

In particular, state law has imposed important restrictions on property and sales tax revenues, which supply the two largest sources of general revenue to cities across California. For example, Proposition 13 limited the property tax rate, limited annual increases for property owners and gave the state the authority to redistribute all property tax revenues. Additionally, any attempt to expand what is covered by the sales tax (such as including services) requires a two-thirds vote of

the state legislature.<sup>27</sup> These constraints matter because while city service costs increase with the economy, or with competition in the local labor market, the revenue from the sales and property taxes may not. This leads to an imbalance between a city’s costs and its major sources of revenue.

**FIGURE 13:**  
**Key State Actions Affecting Local Finance**

State policies have shaped and limited cities’ ability to adopt or adjust local revenues.

Year	Policy
1955	Bradley-Burns Uniform Local Sales and Use Tax: Created a uniform 1% local sales tax that would be collected by the state and flow to the General Fund of the jurisdiction where the sale occurred. <sup>28</sup> Also identified that the sales tax would apply to “tangible personal property.” <sup>29</sup>
1972	SB 90: Created minimum funding levels for schools that the state must meet, which prompted the state to look at covering education costs with local property taxes.
1978	Proposition 13: Limited property taxes to 1% of assessed value, with maximum annual growth of 2% per year, gave the state the ability to allocate all property tax revenue, and required that local special taxes be passed by a 2/3 vote.
1979	AB 8: Established the current system of allocating property tax revenue back to local jurisdictions based on pre-Proposition 13 shares of revenue and created a method for allocating the growth in property tax revenue over time.
1984	Proposition 62: Required that cities only levy general-purpose taxes after a majority of local voters approve them.
1992	First ERAF* change: Permanently reallocated some property tax revenue to K-14 education districts from local cities, counties and special districts.
1993	Second ERAF* change: Permanently allocated more property tax revenue to K-14 education.
1996	Proposition 218: Mandated that new general-purpose taxes must be approved by a majority vote and that new taxes dedicated to a specific purpose must be approved by a two-thirds vote. Also required that property-related fees be approved by ratepayers and that there’s a nexus between development fees and how fees are used.
2004	Triple Flip: Authorized the use of local sales tax to finance state deficit bonds and arranged to pay back cities and counties with property tax revenue taken through ERAF. As of the 2014–15 fiscal year, the deficit bonds were paid off and cities now receive their 1% levy of the sales tax. VLF* swap: Permanently moved a portion of property tax revenue from ERAF and K-14 education to cities and counties to compensate for taking their VLF funds. Temporary ERAF* allocation: Moved a portion of property tax revenue from cities and counties to K-14 education for two years. Proposition 1A: Limited the state’s ability to move property tax revenue away from cities, counties and special districts.
2006	Proposition 26: Limited cities to charging fees only based on cost recovery (such as for licenses and inspections). As a result, many local “fees” had to go back to voters for approval as taxes.
2009	Borrowing under Proposition 1A: Authorized the state to borrow \$1.9 billion in property tax revenues from local governments.
2010	Proposition 22: Removed the state’s ability to borrow property tax revenue and to reallocate revenue from redevelopment agency property taxes.
2012	Dissolution of redevelopment agencies: Eliminated redevelopment agencies, shifting their property tax revenue to local jurisdictions over time

\*ERAF stands for Educational Revenue Augmentation Fund, and VLF stands for Vehicle License Fee.

Sources: Legislative Analyst’s Office, *Understanding California’s Property Taxes* (Nov. 2012), Figure A-1, <http://www.lao.ca.gov/reports/2012/tax/property-tax-primer-112912.pdf>; and League of California Cities, *Proposition 26 Implementation Guide* (April 2011), <http://www.cacities.org/Resources-Documents/Policy-Advocacy-Section/Hot-Issues/Proposition-26-Implementation-Guide>

27 See: Legislative Analyst’s Office, *Understanding California’s Sales Tax* (May 2015), p. 13, <http://www.lao.ca.gov/reports/2015/finance/sales-tax/understanding-sales-tax-050615.pdf>

28 See: Paul Lewis and Elisa Barbour, *California Cities and the Local Sales Tax* (1999), [http://www.ppic.org/content/pubs/report/R\\_799PLR.pdf](http://www.ppic.org/content/pubs/report/R_799PLR.pdf)

29 See: “Bradley-Burns Uniform Local Sales and Use Tax,” [https://www.boe.ca.gov/info/fact\\_sheets/bradley-burns.htm](https://www.boe.ca.gov/info/fact_sheets/bradley-burns.htm)

**The property tax rate is set in the California constitution. State statute controls the distribution of the property tax and the amount the city receives.**

Proposition 13, adopted by voters in 1978, reshaped local finance in California by making the following changes to the local property tax<sup>30</sup>:

- First, it limited the tax rate property owners would be charged to 1 percent of assessed value (which includes the market price plus the value of improvements to the property). Prior to Proposition 13, each local government (including cities, counties, school districts and special districts) set their own property tax rates, with the average combined property tax rate being 2.7 percent.<sup>31</sup> These tax rates were set under a variety of statutory tax-rate limits.
- Second, it changed the method for determining the property's assessed value and restricted the increase in the growth of assessed value to 2 percent per year (or inflation, whichever is lower) plus new assessed value for any improvements to the property. This 2 percent restriction means that cities' major revenue stream grows more slowly than both inflation and labor costs (except during a period of major new construction or when there is significant turnover of property ownership).
- Third, it established the state's authority to reroute property tax revenues across cities, schools and counties. Before Proposition 13, property tax simply stayed with the entity that had levied it.
- Fourth, it requires local taxes designated for a specific purpose to be approved by two-thirds of the voters.

The adoption of Proposition 13 immediately decreased the property tax revenue available to cities across the state. San Jose, for example, lost 55 percent of its annual property tax revenue the year Proposition 13 first took effect. It would slowly regain its pre-Proposition 13 per capita property tax revenues, but that process would take seven more years.<sup>32</sup>

A lesser-known byproduct of Proposition 13 was a state law that legislators passed the following year — AB 8. This measure froze the share of the property tax that an individual city would receive. Today, the share of property tax revenues that a city keeps is based on the share of the countywide property tax that they received in the mid-1970s. For example, if a city generated \$1,000 in property tax in 1977, and the county it was in generated \$10,000, the city still gets 10 percent of today's countywide property tax revenue, even if the value of property in the city has grown faster than property values in the rest of the county.

In addition, this policy does not distribute property tax revenue according to the services each city provides. Some cities had very low property tax rates in 1977 but nonetheless provide city services to large populations today. These are called "no and low" cities, and some adjustments have been made to give them a fair allocation of property tax revenue. Since San Jose was largely a suburban, residential city with a limited industrial or commercial sector in 1977, some have argued that its AB 8 allocation is unfairly low and has contributed to San Jose's relatively low property tax base. However, San Jose does not qualify as a "no and low" city, and it takes 5.3 percent of the county share of the 1% property tax. This is within midrange of comparable large cities and the highest of all Santa Clara cities.<sup>33</sup>

30 See: Legislative Analyst's Office, Understanding California's Property Taxes (Nov. 2012), <http://www.lao.ca.gov/reports/2012/tax/property-tax-primer-112912.pdf>

31 Ibid., p. 19; and Carolyn Chu, "Why the Mid-1970s Play a Large Role in Property Taxes Today," Jan. 27, 2016, <http://lao.ca.gov/LAOEconTax/Article/Detail/166>

32 SPUR analysis of Lincoln Institute of Land Policy's Fiscally Standardized Cities database.

33 Based on interviews with tax allocation experts at various county controller-auditors throughout California.

The impact of the state's authority to reallocate property tax revenue has affected cities most dramatically since the early 1990s, when the state shifted revenues away from cities and counties to the K-14 schools through the Education Resources Augmentation Fund (ERAF). ERAF cost San Jose approximately \$40 million a year for two consecutive years — significant losses at a time when the General Fund was less than \$600 million and the city was struggling with recession-induced reductions in tax revenues.<sup>34</sup> Since the 1990s, San Jose has received some reimbursement from the state to compensate for ERAF losses. A further constitutional amendment, Proposition 1A, was adopted in 2004 to prohibit large transfers of property tax revenues away from cities by the state.

Ultimately, the main impacts of Proposition 13 were that it changed the fundamental rules around local government finance and that it shifted the power over the property tax away from local governments to the state. The state's ability to change the allocation of property tax revenues from year to year created uncertainty for cities. In addition, Proposition 13 and subsequent legislation created complicated ways to redistribute all property tax revenue, which has led to a lack of transparency and has made it difficult to connect property tax raised in a city to property tax revenue received by a city.<sup>35</sup>

**Sales taxes are increasingly disconnected from the growth of the economy and are distributed based on where sales take place, not where services are delivered to shoppers or retail employees.**

Sales taxes are a major revenue source for San Jose and all California cities. However, under state law, sales taxes in California are only levied on tangible products, not on services and intangible goods. This disconnects this important revenue from the growth of the economy for several reasons. First, every year consumers spend less of their income on taxable products. Historically, consumers spent half their income on taxable products, but in the 1980s, consumers began to spend more on services, which are not taxed. Second, many products that used to be tangible and taxable (video games, movies, music, software, books) are no longer taxed by the state, as they are now distributed digitally via the web. Third, prices have increased in the service sector much more rapidly than they have for tangible products, partially because products are more vulnerable to global competition and the public is willing to pay more for services.

Over time, the total value of taxable sales has grown more slowly than the economy. In part, this is why local and state governments have had to raise sales tax rates in order to generate the revenue they need.

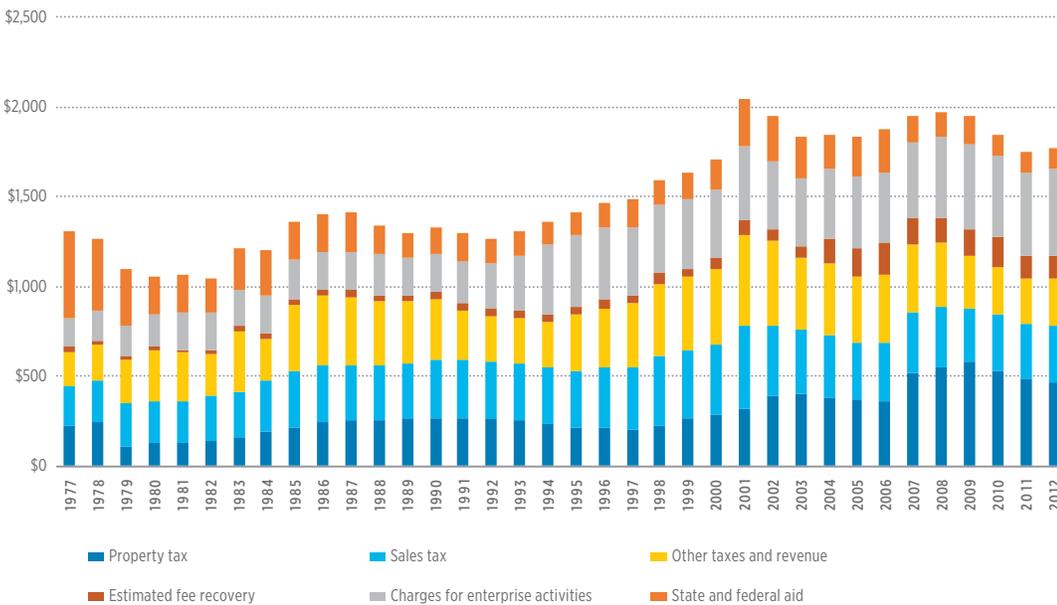
In addition, the share of sales taxes allocated to local government is based on where the sale took place, not on where the purchaser resides. Such an arrangement often creates a disconnect between jurisdictions that receive sales tax revenues (through shopping centers or corporate sales offices) and jurisdictions that provide basic services to shoppers or retail employees. However, cities do have some control over the local portion of the sales tax rate. Local governments (including cities, counties and special districts) are collectively authorized to raise their district's sales tax rate by as much as 2 percent above the state base, assuming the voters approve. Any one of those entities could raise their rates and subsequently prevent other entities from further raising theirs. For example, if there were only 0.75 percent left underneath the 2 percent cap and San Jose were to increase its district sales tax more than 0.25 percent, Santa Clara County would not be able to raise its sales tax by 0.5 percent.

<sup>34</sup> See: City of San Jose, 1999–2000 Operating Budget, <http://www.sanjoseculture.org/ArchiveCenter/ViewFile/Item/2104>. (Note: General Fund was \$620 million in 1998. Data for prior years are not available online.)

<sup>35</sup> See: Legislative Analyst's Office, Reconsidering AB 8: Exploring Alternative Ways to Allocate Property Taxes (Feb. 3, 2000), [http://www.lao.ca.gov/2000/020300\\_ab8/020300\\_ab8.html](http://www.lao.ca.gov/2000/020300_ab8/020300_ab8.html)

**State laws require higher levels of voter approval to raise local revenues and have made it more difficult for cities to use fees.**

Two additional constitutional amendments have significantly reduced the ability of California cities to raise revenues. Proposition 218 (1996) mandated that all local taxes require voter authorization. It also made the use of citywide benefit assessment districts much more difficult. In addition, Proposition 218 prevented cities from using revenues from sewer system rates or other property-based fees for general city services.



**FIGURE 14:**  
**How Have San Jose's Revenues Changed With State Law?**

San Jose's total revenues per capita (1977-2012), in 2012 dollars.

Proposition 13 (1978) led to an immediate reduction in property tax revenues per capita, but these have grown substantially over time. Per capita sales tax revenues, on the other hand, have been in a slow decline. San Jose has also started charging higher fees to cover the cost of services, as seen in the small but growing "estimated fee recovery" segment in this chart.

Source: SPUR analysis of Lincoln Institute of Land Policy's Fiscally Standardized Cities database, <https://www.lincolinst.edu/subcenters/fiscally-standardized-cities/search-database>. Note: Data in this chart might not match other data in this chapter. Data from the Lincoln Institute rely on U.S. Census figures, which are accounted differently than the California State Controller data used in all other graphs of this chapter.

Proposition 26 (2006) recharacterized a number of fees as taxes, making them subject to voter approval. For example, previously cities could assess a fee for any damages that a business may have caused, such as soil contamination. After Proposition 26, this fee became a tax and had to be authorized by voters. As a result, now cities can only charge fees to recover the cost of providing a service, such as fees to pay the cost to have city staff inspect old water heaters in homes and fees to pay the staff and material costs associated with issuing licenses. In addition, cities can only spend fees on the activity that the fees pertain to. In other words, local governments cannot charge higher fees on building inspections to pay for police officers or other general government services.

California's municipal finance laws constrain all cities, which means that these alone do not explain San Jose's fiscal strain — they simply make clear the conditions under which the city must operate. Overall, these laws strongly restrict each city's flexibility to raise new revenues when costs escalate or recessions hit. In addition, while service costs rise with the economy, inflation and labor markets, each city's two most important revenue streams — sales and property taxes — do not.

**Economic and business cycles, including recessions and economic downturns, directly impact every city's revenues.**

Markets swings and business cycles greatly affect city revenues. In a sluggish economy, there are fewer sales of taxable goods, fewer turnovers of residences (at lower sale prices), fewer

construction projects and fewer hotel taxes collected. Recessions are painful for public-sector finances at all levels.

In recent decades, California's cities have been impacted by multiple downturns: the slowdown caused by the pullback of defense spending in the early 1990s, the dot-com bust from 1999 to 2001 and the Great Recession from late 2007 to mid-2009. The National League of Cities argues that cities recovered from the Great Recession — perhaps the most serious of all these economic downturns — more slowly than from previous downturns in the 1990s and early 2000s.<sup>36</sup>

This begs the question of how typical San Jose's recent fiscal strain was. Compared to cities in the Bay Area, San Jose's general revenue recovered from the Great Recession both more slowly and with a lower rate of growth. Figure 15 shows each city's change in general revenue from the previous year. Figures in red represent a decline in revenue, while those in black represent growth.<sup>37</sup>

From Figure 15, we also see that cities in the Bay Area tended to rebound more quickly than other cities in California. The general revenue in most Santa Clara County cities and in San Francisco started growing again in 2011, while the revenue in most other California cities started growing in 2012. In the Bay Area, the cities of San Jose, Fremont, Oakland, Morgan Hill and Mountain View were notable exceptions, as their return to growth began in 2012, with the rest of the state. San Jose, Gilroy and Sunnyvale have lower post-recession growth rates than other Bay Area cities. For example, San Jose's post-2011 growth rate for general revenue has not surpassed 3 percent, while other cities have seen growth rates from 5 percent up to 27 percent.<sup>38</sup>

Both San Jose's slow pace toward recovery and its modest growth during recovery suggest that it isn't capturing as much general revenue during the Bay Area's current boom. This is somewhat due to the spatial structure of Silicon Valley, which we explore next.

<sup>36</sup> See: Christiana McFarland and Michael A. Pagano, National League of Cities, *City Fiscal Conditions*, 2015, <http://www.nlc.org/Documents/Find%20City%20Solutions/Research%20Innovation/Finance/CSAR%20City%20Fiscal%20Conditions%202015%20FINAL.pdf>

<sup>37</sup> For more on how SPUR conducted city comparison analyses, see the appendix.

<sup>38</sup> As discussed in Chapter 1, a city's ability to weather downturns depends on a number of factors. For example, even though Cupertino lost 15 percent of its general revenue in 2010, this doesn't mean it was financially unstable as a result. Ultimately, evaluating the balancing of costs and revenues over time and through downturns is the only way to explore whether or not a city is experiencing fiscal strain.

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	
Large California Cities	Anaheim	-4%	12%	5%	6%	-4%	-7%	-8%	-1%	2%	8%	4%
	Bakersfield	-6%	11%	6%	6%	-9%	-7%	-15%	2%	6%	2%	21%
	Fremont	-1%	10%	1%	4%	-3%	-3%	-8%	-1%	1%	5%	2%
	Fresno	-3%	9%	7%	6%	-5%	0%	-16%	-1%	2%	3%	7%
	Long Beach	-1%	6%	2%	9%	2%	-3%	-9%	5%	-7%	15%	-7%
	Los Angeles	3%	5%	5%	3%	-3%	0%	-7%	-1%	-1%	6%	1%
	Oakland	0%	-1%	9%	-2%	-6%	-3%	-5%	-3%	5%	2%	1%
	Riverside	-1%	11%	13%	10%	5%	-24%	-10%	-4%	0%	5%	-1%
	Sacramento	-1%	6%	1%	10%	-3%	-7%	-8%	-12%	0%	9%	6%
	San Diego	26%	2%	2%	2%	-7%	-2%	-6%	-6%	18%	-6%	1%
	San Francisco	4%	4%	9%	2%	1%	-4%	0%	5%	3%	3%	6%
	Santa Ana	2%	9%	5%	1%	-1%	-1%	-7%	-8%	21%	-14%	2%
	Stockton	-1%	27%	24%	-6%	-10%	-18%	-9%	-4%	-3%	-1%	0%
Santa Clara County Cities	San Jose	-7%	8%	6%	7%	-1%	-8%	-10%	-1%	3%	1%	-1%
	Campbell	1%	2%	-3%	9%	1%	-3%	-7%	3%	3%	5%	3%
	Cupertino	-8%	11%	10%	9%	-5%	-1%	-15%	13%	5%	11%	23%
	Gilroy	8%	-3%	9%	-1%	-5%	-14%	0%	-5%	1%	-9%	1%
	Milpitas	-15%	17%	9%	1%	-5%	-3%	-9%	0%	5%	9%	6%
	Morgan Hill	-4%	7%	6%	3%	2%	-12%	-6%	-3%	6%	24%	-3%
	Mountain View	-18%	22%	-1%	8%	-1%	-7%	-6%	-9%	17%	5%	4%
	Palo Alto	-19%	2%	6%	5%	0%	0%	-7%	3%	27%	-14%	2%
	Santa Clara	-17%	5%	-4%	10%	-20%	11%	-12%	5%	2%	2%	13%
	Sunnyvale	-11%	5%	2%	11%	0%	-12%	-1%	9%	-4%	1%	1%

**FIGURE 15:**  
**How Have Recessions Affected General Revenue for Cities?**

Change in general revenue from previous year, in 2014 dollars

San Jose recovered from the Great Recession that stretched from late 2007 through mid-2009 more slowly than other Bay Area cities and at a more modest rate. For example, most Bay Area cities saw general revenues begin to grow again in 2011 (see sections outlined in blue), but San Jose started to grow one year later. And while many Bay Area cities saw post-recession general revenue growth rates between 5 and 24 percent, San Jose's peaked at only 3 percent.

Source: SPUR analysis of California State Controller's Office, Cities Raw Data for Fiscal Years 2003-14: <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>.

**San Jose faces strong economic competition from surrounding cities because the spatial pattern of the region's innovation economy is centered to the north of San Jose.**

The innovation and tech industries are the economic engines of the Peninsula and South Bay, where the percentage of employment in these industries is more than twice the national average.<sup>39</sup> Although San Jose has more tech jobs than any other South Bay city, the actual number of jobs is low relative to San Jose's large population. It has long been one of the only metropolitan areas in the U.S. with more employed residents than jobs,<sup>40</sup> which means that it has the capacity to add more jobs.

The high-tech cluster now referred to as "Silicon Valley" began in northern Santa Clara County around Stanford University, an institution that fostered applied research and innovation. The South Bay's technology cluster initially grew in concentric circles south, generating industrial development first in Stanford's home town of Palo Alto, then Mountain View, then Sunnyvale, then Santa Clara. Eventually, in the 1990s, San Jose became home to the corporate headquarters for Cisco, Adobe and eBay.<sup>41</sup>

In choosing where to locate, new arrivals in Silicon Valley have wanted to stay close to the cluster's core, to take advantage of proximity to Stanford and venture capital firms with expertise in the legal and financial elements of startups and deal-making. New companies in this industry have generally chosen locations as close to Palo Alto as they can afford. San Jose's tech jobs have

39 See: Bay Area Council Economic Institute, *A Regional Economic Assessment of the San Francisco Bay Area* (2012), Table 1, <http://bayarearegionalcollaborative.org/abag/events/agendas/J111612a-Item%2008,%20Regional%20Economic%20Assessment.pdf>

40 See: Wendell Cox, "U.S. Suburbs Approaching Jobs-Housing Balance," *NewGeography.com*, April 12, 2013, <http://www.newgeography.com/content/003637-us-suburbs-approaching-jobs-housing-balance>

41 IBM established their first West Coast laboratory in San Jose in 1956. But much of the subsequent tech job growth took place in other cities. Additionally, Apple's location in Cupertino is somewhat of an outlier in this pattern.

grown mainly at the end of economic cycles, when available space decreases and real estate costs increase in cities to the north. The city has had little power to alter the organic pace and direction of this trend.

In the more recent boom, the cluster has grown to the north, through Menlo Park (Facebook), Redwood City (Oracle), San Bruno (YouTube) and into San Francisco (Salesforce, Uber and Twitter). Apple and Samsung have also made more recent investments in North San Jose, but this has not been enough — yet — to change the historic trend that leaves San Jose outside the center of the innovation economy.

Ultimately, the pattern of tech innovation growth took a long time to reach San Jose, leaving it more vulnerable to economic cycles than surrounding cities, which pose strong competition. The fiscal impact is that San Jose has had less new commercial and industrial development, limited tools to expand it, and lower associated tax revenues as a result.

## Internal Factors That Contribute to San Jose’s Fiscal Challenges

San Jose responded to the external forces described above with the tools it had available. It made decisions about land use, economic development and redevelopment, as well as taxes and expenditures, to maximize its revenues under these constraints and provide services to its constituents.

### **San Jose’s historic annexation and auto-oriented housing strategies have yielded less property tax revenue in the post-Proposition 13 era and less land for employment uses.**

Between the end of World War II and the 1970s, San Jose encouraged sprawling residential development, partly by annexing neighboring towns (such as Alviso and Willow Glen) and unincorporated land at the city’s edges.<sup>42</sup> Once incorporated, much of the land was quickly developed with low-density tract housing. Between 1950 and 1969, San Jose grew from fewer than 100,000 residents and 17 square miles to more than 450,000 residents and 137 square miles. Over this same time period, the city’s gross density declined by 40 percent, from nearly 5,600 residents per square mile to less than 3,400.<sup>43</sup> Commercial and industrial development expanded much more slowly: Major companies downtown included IBM, Del Monte Packing, Mariani Packing, and Food and Manufacturing Corporation (FMC), but little else. The city’s downtown lost shoppers and business to suburban-style shopping malls and office parks. Many new office parks and employment centers were built in surrounding cities, not San Jose.

Sprawling residential development led to a larger volume of roadways, which led to high costs for street maintenance. Today, the city’s 2,400 miles of roads are its largest infrastructure asset and its largest infrastructure liability.<sup>44</sup>

Perhaps most importantly, much of San Jose was built out as a bedroom community, leaving the city with a low overall ratio of jobs to housing. This strategy, pursued in the decades after 1950, made a certain amount of sense during a period when cities could adjust their property tax rates to meet service needs. But after the passage of Proposition 13, San Jose confronted a growing population’s demand for city services spread out over a very large geographic area, with less flexibility to adjust property tax rates and less available land to diversify its revenue stream.

Planning for residential growth post-Proposition 13 presented San Jose with conflicting pressures. On the one hand, adding new houses would generate new property tax revenue, but perhaps not enough to offset the additional service costs they would incur. On the other hand,

42 See: *San Jose Modernism Historic Context Statement*, PAST Consultants, LLC (June 2001), <http://www.sjredevelopment.org/PublicationsPlans/SanJoseModernismJune2001.pdf>

43 SPUR analysis.

44 SPUR analysis of annual unfunded deferred maintenance needs (see Indicator 5 in Chapter 1). See also: “General Fund Structural Budget Deficit History & Service Restoration Priorities and Strategies,” slide 44, [http://www.avca-sj.org/1-20-15\\_Study\\_Session\\_Presentation.pdf](http://www.avca-sj.org/1-20-15_Study_Session_Presentation.pdf)

restricting housing production could lead to slower job growth within the region's technology sector, which San Jose wanted to capture.

Essentially, San Jose weighed its options and allowed housing production to continue, albeit at a slower pace. While the total population grew by 255,000 in the 1960s, net new growth declined to 170,000 in the 1970s, 150,000 in the 1980s, 112,000 in the 1990s and only 50,000 from 2000 to 2010. Beginning in the 1970s, San Jose blocked additional sprawl, embraced infill development, adopted a greenbelt and encouraged the development of multifamily projects.

The shift toward denser development is important from a fiscal perspective. In 2015, consultants to San Jose estimated that new residential development over a certain density level (e.g., 45 units per acre) and price point (e.g., greater than \$415,000 per unit) would generate more in property and sales taxes than they would be required in average, per capita service costs.<sup>45</sup> In addition, dense developments can save on infrastructure costs because they require fewer miles of roads and sewers and can make greater use of existing facilities, such as parks and libraries.<sup>46</sup> Another fiscal benefit of density is its effect on consumer behavior — and therefore on sales tax revenue. Pedestrians often buy more goods locally than do automobile drivers, who can easily access retail stores outside city boundaries. Lastly, some research shows that both the millennial generation and older households are now looking for housing in dense, walkable developments.<sup>47</sup> San Jose can aspire to capture this growing segment of the market.

As it pursued its residential growth strategy, San Jose converted thousands of acres of commercial and industrial land to residential uses. Between 1980 and 2015, the city converted 2,298 acres of employment lands to other uses, resulting in a 16 percent decline in employment lands, from 15,912 acres to 13,614. The converted lands could have accommodated between 50,000 and 100,000 jobs.<sup>48</sup> While San Jose still has more land available for employment uses than surrounding cities, maintaining this capacity into the future is key to giving the city an important comparative advantage (or balancing out the disadvantage San Jose faces from being south of the employment centers in Silicon Valley).

Maintaining significant employment lands is also important for fiscal reasons. While employment lands take up only 15 percent of San Jose's total land area (compared with 57 percent for residential lands), they contribute a net \$124 million to the city's budget.<sup>49</sup> In contrast, all residential lands have a net negative impact of \$110 million on the city's budget. Largely, the negative impact stems from the large stock of older single-family homes some whose properties have not been reassessed in many years.

Hanging onto its remaining employment lands will ensure that San Jose can continue to attract major industrial and commercial tenants. In 2015, Apple selected an 86-acre site in North San Jose for an expansion that can accommodate up to 20,000 workers.<sup>50</sup>

### **San Jose's extensive use of redevelopment reduced its current property tax base without adding significant new revenue streams.**

From 1952 to 2012, California's statewide redevelopment program enabled San Jose and other cities to finance development by borrowing against future property tax revenues. While

45 See: Memo from Applied Development Economics, April 10, 2015 (rev. Nov. 24, 2015), Table 9, [www.sanjoseca.gov/DocumentCenter/View/47763](http://www.sanjoseca.gov/DocumentCenter/View/47763)

46 See: Chris Schildt, *Strategies for Fiscally Sustainable Infill Housing*, Center for Community Innovation (Sept. 2011), <http://communityinnovation.berkeley.edu/reports/Fiscally-Sustainable-Infill.pdf>

47 See: M. Leanne Lachman and Deborah L. Brett, *Gen Y and Housing: What They Want and Where They Want It*, Urban Land Institute (2015), <http://uli.org/wp-content/uploads/ULI-Documents/Gen-Y-and-Housing.pdf>

48 See: "History of Employment Land Conversions in San José and the Fiscal Impact of Land Use," City Council Study Session, April 14, 2015, Item 11.3, <http://www.sanjoseca.gov/DocumentCenter/View/42306>

49 See: Kim Welsh, "Strategies to Enhance San Jose's Fiscal Health," Envision San Jose 2040 4-Year Review, Task Force Meeting #3, Jan. 28, 2016, [www.sanjoseca.gov/DocumentCenter/View/53650](http://www.sanjoseca.gov/DocumentCenter/View/53650)

50 See: Ramona Givargis, "San Jose Council Approves Agreement for Apple Campus in North San Jose," *San Jose Mercury News*, Jan. 26, 2016, [http://www.mercurynews.com/bay-area-news/ci\\_29436388/san-jose-council-approves-agreement-apple-campus-north](http://www.mercurynews.com/bay-area-news/ci_29436388/san-jose-council-approves-agreement-apple-campus-north)

redevelopment provided a way to pay for many worthwhile economic development, affordable housing and infrastructure projects in San Jose, it also borrowed against future property taxes that could have been spent on services today. It is impossible to know what might have happened without redevelopment, and weighing the benefits, costs and fiscal impacts of the program is tricky. Nonetheless, it is worth considering its history, the tradeoffs made through property tax finance, and the potential effects of its underlying economic development strategy.

Beginning shortly after WWII, cities in California could establish redevelopment agencies as a tool to fight “blight” and promote economic development. In 1952, state law established tax increment financing (also known as TIF), which enabled redevelopment agencies to finance infrastructure and development by selling bonds backed by future property tax revenues that would accrue within the designated redevelopment area.<sup>51</sup> This form of financing also allowed the local redevelopment agency to capture the growth in property taxes rather than sharing such revenues with other local taxing entities, such as schools and counties.

San Jose first formed its redevelopment agency in 1956 as a legal entity separate from the City of San Jose. Much of its extensive work began in the late 1970s and continued until 2012 state legislation dissolved all California’s redevelopment agencies.

There is no question that redevelopment provided San Jose with a source of financing to make many iconic investments in San Jose, such as the Dr. Martin Luther King, Jr. library (a combined public and San Jose State University library), the arena where the San Jose Sharks hockey team plays, the convention center, and many community and cultural facilities. Redevelopment also helped finance 11,000 units of affordable housing and numerous public-private partnerships for hotels, offices, street improvements and other public amenities.<sup>52</sup> In addition, it helped pay for ongoing city services such as the City Council and the economic development office. Redevelopment paid for these local investments by borrowing against the entire future property tax growth, including not only the city’s share of property tax revenues but also the much larger share that otherwise would have gone to the county, schools and special districts.

On the other hand, the use of redevelopment left a significant amount of debt that will take decades to pay down. As of 2015, San Jose’s former redevelopment agency was responsible for roughly \$1.9 billion in debt.<sup>53</sup> Debt service will remain above \$150 million per year until 2028 and will only drop well below \$50 million per year in fiscal year 2035–36, near the end of the term of the outstanding redevelopment debt.<sup>54</sup> San Jose forgoes \$38 million in today’s dollars to pay down its portion of redevelopment debt.<sup>55</sup>

In addition, redevelopment investments did not generate as many economic benefits as hoped, failing to create promised jobs and investment in the private sector or to boost sales tax and other tax revenues.

One reason for the shortfall might have to do with how and where the city chose to focus its redevelopment efforts. From 1977 until 2012, the redevelopment agency financed projects totaling around \$1.9 billion. Of this, \$1.8 billion was spent in the downtown. This was only possible because San Jose was the first city in California to merge its redevelopment areas together, which enabled it to borrow future tax increment in one part of the city and invest it in another.<sup>56</sup> San Jose persistently shifted redevelopment tax increment out of North San Jose, its district with the

51 See: Casey Blount et al, *Redevelopment Agencies in California: History, Benefits, Excesses and Closure*, U.S. Dept. of Housing and Urban Development (Jan. 2014), [https://www.huduser.gov/portal/publications/Redevelopment\\_WhitePaper.pdf](https://www.huduser.gov/portal/publications/Redevelopment_WhitePaper.pdf)

52 See: San Jose Redevelopment Agency, “Housing,” <http://www.sjredevelopment.org/housing.htm>

53 See: City of San Jose, *Comprehensive Annual Debt Report, 2015*, <http://www.sanjoseca.gov/documentcenter/view/48226>

54 San Jose’s 2015 *Comprehensive Annual Financial Report* shows the last RDA debt payment in 2036; see p. 140, [http://sanjose.granicus.com/Viewer.php?meta\\_id=546403](http://sanjose.granicus.com/Viewer.php?meta_id=546403)

55 San Jose’s property tax increment going to redevelopment debt was supplied by the office of the Santa Clara County Controller-Treasurer in March 2016.

56 See: Egon Terplan, “Shaping Downtown San Jose,” *The Urbanist* (April 2013), <http://www.spur.org/publications/article/2013-04-04/shaping-downtown-san-jose>

greatest potential for industrial expansion, into downtown.<sup>57</sup> While the downtown turnaround has provided the city with a new cultural and recreational core, these types of activities don't generate significant revenues from new sales and other taxes. The downtown's small job base (currently at around 40,000 jobs) and small retail base also contribute to this low tax revenue potential.

Meanwhile, San Jose only spent \$300 million on industrial projects in North San Jose and Edenvale.<sup>58</sup> This meant that San Jose had limited funding to invest in the amenities in North San Jose, which may have made the district less attractive to potential new businesses. The redevelopment agency also deliberately restricted the development of hotels in North San Jose in order to encourage growth in downtown. While some hotels located downtown, many others located in adjacent cities just outside North San Jose. Also, the strategy in North San Jose initially placed less emphasis on overall placemaking and on housing, retail, restaurant and entertainment development. As a result, the area today is relatively light on such amenities.

In sum, redevelopment left the city with a dramatically improved downtown, as well as an industrial district in North San Jose. It also left San Jose with significant debt for several additional decades, and it may have limited the incremental property tax revenue growth to schools, the county and other jurisdictions in the process. While it's difficult to imagine San Jose without the benefits of redevelopment, it has also been challenging for the city to forego some portion of property tax revenue that could fund services today.

### **San Jose adapted its revenue strategy over time but did not raise significant new revenues.**

Over time, San Jose has adapted its revenue model, collecting fees for services where it could and updating and increasing taxes where appropriate and with the political will it had.

As discussed above, state laws increasingly limited how cities in California could raise local taxes and fees. For example, after Proposition 218 passed in 1996, new general-purpose taxes required a majority vote, and new taxes dedicated to a specific purpose required a two-thirds vote. Property-related fees had to be approved by ratepayers, and development fees could only be used to mitigate the effects of the development.

However, San Jose did monitor and increase fee levels where it could. Today, fees support inspections and other work by the building, planning and fire departments. The city has also imposed development fees on specific projects, traffic mitigation fees in certain planning areas, and citywide park and housing impact fees. These are all deliberate strategies to gather revenues for needed public services or investments. San Jose also regularly conducts impact fee studies to assess whether or not existing fees cover service delivery costs and if they should be adjusted.

San Jose chose to raise few taxes from the mid-1990s to today, partially because raising taxes is never easily politically and because Proposition 218 made it even more difficult. In 1995, the city did establish a 10-year citywide benefit assessment district for library services that yielded approximately \$6 million. When Proposition 218 curtailed that strategy, parcel taxes in 2004 and 2014 successfully replaced the assessment district. Nevertheless, other local governments — most notably, Santa Clara County and the City of Campbell — have pursued more new taxes since the late 1990s. (Figure 32 in the appendix shows the taxes the county or local cities pursued and passed.)

Although the San Jose City Council retained the right to raise taxes until the late 1990s, it only attempted to raise them once, as part of a legislative effort dubbed "New Realities." The plan included increasing the business license tax by 3 percent and linking future increase to inflation, and expanding the utility tax to include out-of-state phone calls. It was expected to generate about \$11 million per year, but voters defeated the revenue measures in November 1998.

57 San Jose also spent \$355 million in neighborhood initiatives citywide, many of which did not generate any tax increment, meaning that the future tax increment from the other areas subsidized them.

58 See: San Jose Redevelopment Agency Fact Sheet, [http://www.sjredevelopment.org/ProjectGallery/SJRA\\_fact\\_sheet\\_0807.ai.pdf](http://www.sjredevelopment.org/ProjectGallery/SJRA_fact_sheet_0807.ai.pdf)

After 1998, the city pursued a few noteworthy tax updates and increases with mixed success. In 2008, the city asked voters to replace a 911 fee with a slightly smaller tax, and in 2009, the city proposed expanding the number of calls subject to the telephone tax coupled with a reduction in its overall rate. Both measures passed but did not raise additional revenue. In 2010, the city proposed increased taxes on card rooms and new taxes on marijuana dispensaries under the business tax. Both passed, raising roughly \$7 million per year.<sup>59</sup> The city also began pursuing a sales tax increase to pay for basic municipal services starting in 2010. Polling indicates growing support for a higher sales tax, from 54.4 percent in favor in 2010 to 60 percent in 2011, 65 percent in 2012 and 67 percent in 2014. In 2012, city staff proposed raising the sales tax, but the City Council blocked it. During the 2014 debate over the sales tax, the City Council deadlocked, with some members urging a general-purpose tax and others insisting on a special tax for public safety. For the first time, the City Council has voted to put a 0.25 percent general-purpose sales tax increase on the June 2016 ballot. If approved, this quarter-cent city sales tax, combined with a half-cent countywide Santa Clara County Valley Transportation Authority sales tax (proposed for November 2016), would reach the maximum amount of sales tax that state law allows and would prevent San Jose from being able to increase the sales tax again.

Lastly, in early 2016, a signature-gathering campaign attempted to establish a gross receipts tax for San Jose that would have replaced the existing business tax and greatly increased the amount businesses pay. Opponents argued that the tax was developed without sufficient input from the business community and would significantly harm the city's economic competitiveness. The initiative's proponents subsequently agreed to forgo putting it before voters in exchange for an agreement from the mayor and other leaders that San Jose would pursue a more modest increase in its business tax.<sup>60</sup>

### **While pension and post-retirement payments have increased overall costs, major cuts after 2009 reduced overall spending.**

Expenditures don't seem to be at the root of San Jose's fiscal challenges. Historically, the compensation for city staff has not been excessive compared with salaries in surrounding cities, and overall staffing levels have remained relatively low.<sup>61</sup> Over several decades, San Jose maintained an average of 7.1 budgeted employees per 1,000 residents. That figure dropped to 5.7 budgeted employees per 1,000 residents from 2001 to 2015, mostly from reshuffling employees (as part of San Jose's 1,600 job cuts, discussed in Chapter 2). Many large cities in California have a significantly higher number of budgeted city staff per capita. Oakland has 9.8 workers per 1,000 residents; Los Angeles, 9.2; Sacramento, 8.9 and San Diego, 7.7.<sup>62</sup>

Public safety staffing accounts for more than half of San Jose's General Fund costs, but San Jose has far fewer public safety staff per capita than other large cities. While understaffed, the city has been fortunate to maintain relatively low crime rates. According to the FBI's Uniform Crime Reporting, San Jose is one of the safest big cities in California; among the 14 cities listed in Figure 16, it is third-safest in violent crime and sixth-safest in property crimes. This suggests that the city is using its limited resources effectively.<sup>63</sup>

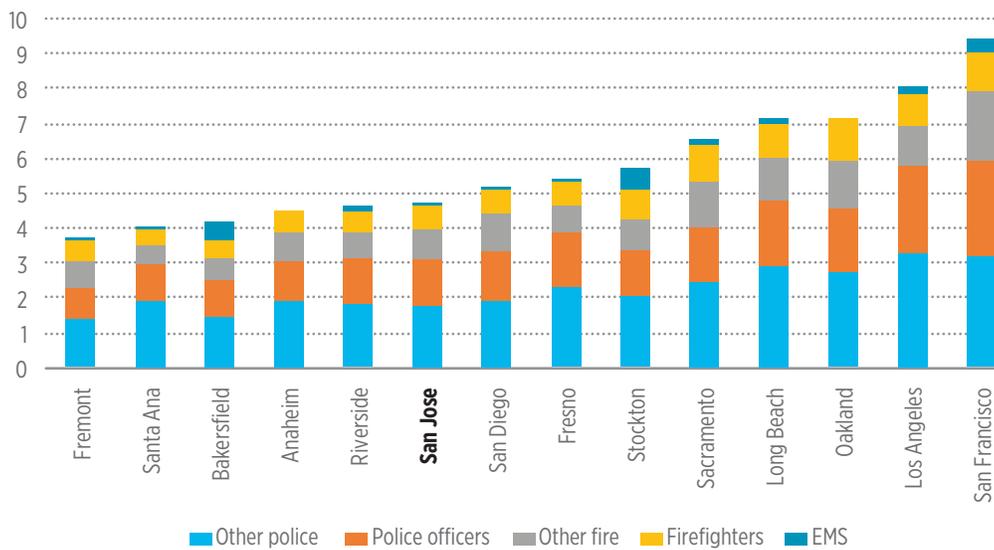
<sup>59</sup> *Supra* note 22, slide 19.

<sup>60</sup> The modified business tax is slated to go before voters in November 2016.

<sup>61</sup> Source: Interviews for this report.

<sup>62</sup> SPUR analysis of city budget and population figures.

<sup>63</sup> It is beyond the scope of this report to assess the quality of service delivery. San Jose does release reports on the effectiveness of expenditures and services, including the City Auditor's annual report on city services and the Budget Office's service descriptions in its annual report.



**FIGURE 16:**  
**How Does Public Safety Staffing Compare Across California's Large Cities?**

Public safety personnel per 1,000 residents, annual average for 2003-2014

San Jose has fewer public safety staff for its population size compare to most other large cities in California.

Source: SPUR analysis of California State Controller's Office, Cities Raw Data for Fiscal Years 2003-14, <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>

However, in one area San Jose has overextended itself to compensate personnel: retirement benefits (including pensions and retiree health care). San Jose has two pension plans — one for police and fire personnel and one for other staff. The plans were in strong fiscal condition at the turn of the millennium; in fact, the police and fire plan was substantially overfunded.

But in the late 1990s, San Jose enacted several policies that weakened the plans. The city took partial “pension holidays” for several years (failing to pay the normal cost of the pensions), it paid bonuses to retirees from pension plan surpluses, and it negotiated increased pension benefits for employees, which were applied retroactively. We don't know what the effects of these actions might have been if the American economy had remained stable and growing. However, there is no question that, when combined with the Great Recession, the growing cost of health care and the growing number of retirees, these actions generated large unfunded pension liabilities and costly financial losses to the city. (Because many of these factors are not unique to San Jose, the rising cost of providing pension and retiree benefits is a challenge for many public-sector employers.)

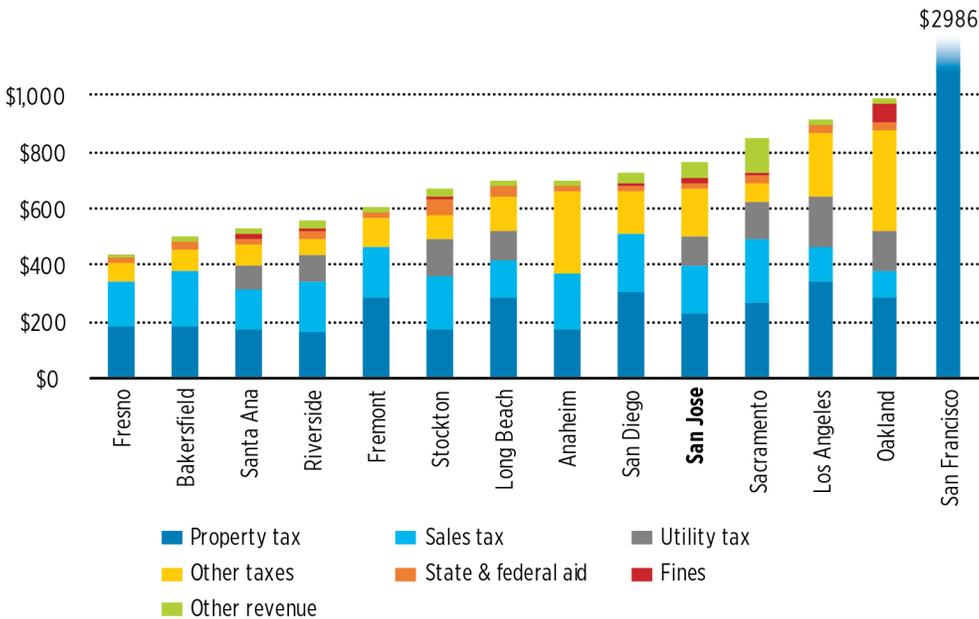
As stated earlier in Chapter 2, San Jose recognized that it could not sustain such high retirement costs, and subsequently pursued Measure B in 2012. After legal challenges to Measure B, San Jose eventually came to agreement with unions on an updated retirement structure, which is estimated to save the city nearly \$3 billion over the next 30 years.<sup>64</sup>

<sup>64</sup> *Supra* note 17.

# Putting San Jose’s Major Sources of Revenue in Context

Comparing revenues in cities across California builds a picture of what is typical statewide. Compared to its large urban peers, San Jose has a relatively low per capita property tax base and a moderate per capita sales tax base. But compared to the neighboring cities in Santa Clara County that it competes with for retail sales, San Jose has the lowest per capita sales tax revenues. The combination of low property and sales tax revenues in San Jose means that it has had less flexible funding to pay for core government services.

Figure 17 shows how San Jose stacks up against other large California cities in total per capita general revenue,<sup>65</sup> or the overall level of flexible spending power each urban city has for core government services. By charting each city’s mix of general revenue sources, it also illustrates that San Jose has relatively low property and sales tax revenues, but somewhat higher revenues from other taxes,<sup>66</sup> such as hotel tax, franchise tax, business tax,<sup>67</sup> real estate transfer tax and other non-property tax revenues. Because property tax and sales tax revenues are the largest general revenue sources for cities across California,<sup>68</sup> low revenues in these categories leave a city pursuing multiple other revenues to cover service costs.



**FIGURE 17:**  
Each Large City in California Has a Slightly Different Mix of General Revenues

Annual average per capita general revenues by source (2003-2014), in 2014 dollars

While San Jose’s combined general sales and property tax revenue per capita is well below many of its peers, San Jose has pursued other kinds of taxes to make up the shortfall.

Source: SPUR analysis of California State Controller’s Office, Cities Raw Data for Fiscal Years 2003-14: <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>

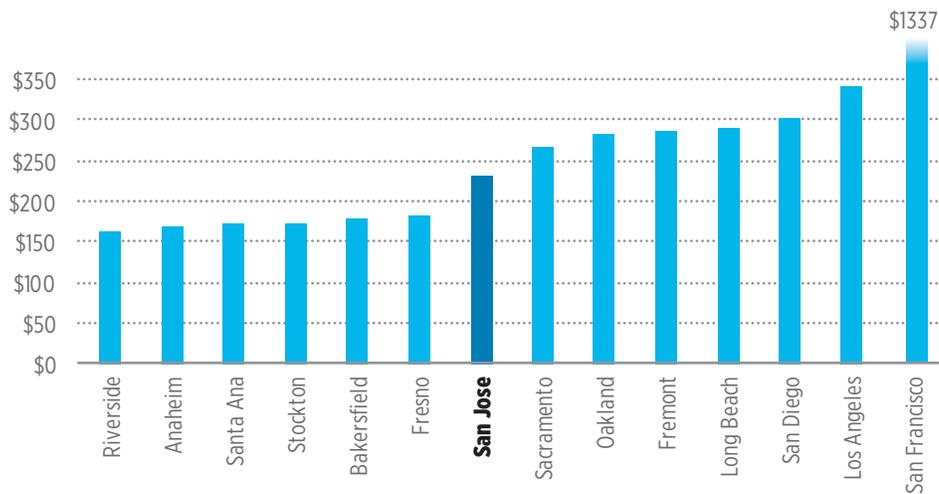
65 To compare San Jose’s financial picture, we benchmarked it against the largest cities in California and Santa Clara County. Within each grouping, we compared more than 30 general revenue and expenditure categories, using data that cities report to the State Controller. We looked at the period between 2003 and 2014, and figures are deflated to 2014 dollars, divided by population, and averaged over our time horizon. (See the appendix for more on data, methods, and supporting graphics.)

66 For a breakdown of these revenues as a percentage of each city’s total general revenues, see Figure 27 in the appendix. For a similar illustration of the general revenue portfolio of cities across Santa Clara County, see Figure 28 in the appendix. Figure 29 in the appendix breaks down these exact percentages for Santa Clara Cities.

67 San Jose’s relatively new taxes on card rooms and marijuana have increased the level of business tax revenues it receives compared to its peers.

68 Michael Coleman, *A Primer on California City Finance*, League of California Cities, p. 3, <http://www.californiacityfinance.com/FinancePrimer05.pdf>

Because San Jose’s property tax revenues are lower than other large California cities, they deserve a closer look.<sup>69</sup> As seen in Figure 18, San Jose’s per capita property tax revenues rank ninth among the 14 largest cities in the state. The per capita property tax revenues line up mostly in two groups, with cities with high property values at the high end and cities with lower property values on the lower end, as we would expect. But San Jose breaks this pattern, falling below cities with lower-average property values. This raises the question of why San Jose’s property tax base is so low compared to what might be expected for a city of its size, desirability and location.



**FIGURE 18:**  
**How Property Tax Revenues Vary Across California’s Largest Cities**  
 Annual average per capita property tax revenue (2003-2014), in 2014 dollars  
 San Jose’s general property tax revenue per capita is well below most of its large urban peers and is not aligned with its relatively high property values.

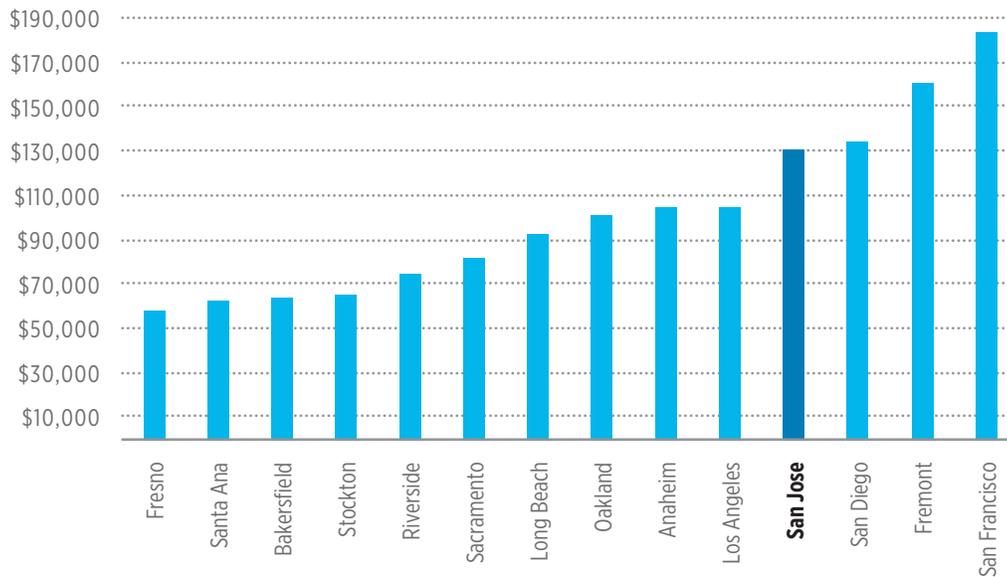
Source: SPUR analysis of California State Controller’s Office, Cities Raw Data for Fiscal Years 2003-14, <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>

## What Are Some of the Causes of a Low Property Tax Base?

In general, the property tax base of a city is shaped by three main factors: property values, the distribution of the tax at the county level and the lingering effects of redevelopment or other debt. To the extent possible, we have compared San Jose along these dimensions with its large urban peers in California.

**1. Low assessed values.** The lower a city’s assessed values, the more likely it is that the city will have lower property tax revenue. Since general property tax is levied on the assessed value of residential and commercial property, cities with dense, high-end properties and significant new construction tend to have higher property tax revenues. In addition, the assessed value of property grows fairly slowly under Proposition 13 (at roughly 2 percent per year plus the value of any improvements) unless a property is sold. When it’s sold, its value is reassessed to the market value, which usually exceeds its previously assessed value. Therefore, areas with higher property turnover rates tend to have higher assessed values and property tax revenues. San Jose has relatively high assessed property values, as seen in Figure 19. Its turnover rate for residences (the majority of the market in San Jose) falls in the middle of the range for comparable cities.<sup>70</sup> Since San Jose’s assessed values aren’t below average on a per capita basis, low assessed values aren’t driving San Jose’s low property tax revenues.

<sup>70</sup> Based on SPUR analysis of the percentage of a city’s housing stock to turn over each year from 2008 through 2015. Data are from Zillow, <http://www.zillow.com/research/data/>



**FIGURE 19:**  
**How Assessed Property Values Vary Across California's Largest Cities**

Annual average per capita assessed property values (2003-2014), in 2014 dollars

San Jose's assessed property values suggest the city should have higher property tax revenues per capita.

Source: SPUR analysis of California State Controller's Office, Cities Raw Data for Fiscal Years 2003-14, <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>

**2. Low share of property tax allocation.** Cities in California receive varying shares of the general property tax that is collected within their boundaries. As mentioned in Chapter 3, the state law AB 8 mandates how all property tax collected on behalf of overlapping taxing entities (cities, schools, counties and special districts) flows back to them, and it uses a formula that's based on the proportion of the countywide property tax revenue that each entity collected in the mid-1970s, before Proposition 13. Cities that collected a smaller share of countywide property taxes in the 1970s receive a lower share of property tax revenues today.<sup>71</sup> San Jose's past history means that it gets 48 percent of the property tax revenue that goes to cities in Santa Clara County, but it provides services for 54 percent of countywide residents. In contrast, Oakland gets roughly 28 percent of the property tax revenue that Alameda County sends back to cities, but just 26 percent of the county's residents live in Oakland.<sup>72</sup> This system is not equitable and is likely a contributing factor in San Jose's relatively low property tax base.

**3. High debt resulting from redevelopment.** As discussed in Chapter 3, California cities used redevelopment to finance capital and other improvements until 2012, when state law dissolved redevelopment agencies. Cities like San Jose, which relied heavily on redevelopment financing, must use today's property tax revenue to pay down their redevelopment debt. The impact of redevelopment in San Jose is likely a contributing cause of its relatively lower property tax base. But it's also important to note that without the large investment made by redevelopment, San Jose's assessed property values might be lower, which would have compromised its property tax revenues in a different way.

<sup>71</sup> Supra note 30.

<sup>72</sup> Population figures are from the U.S. Census Bureau's Quick Facts portal, <https://www.census.gov/en.html>. AB 8 factors for cities in Santa Clara County and San Jose were obtained from interviews with the Santa Clara Treasurer-Controller in March 2016, and the AB 8 factors for Alameda County and Oakland were obtained through interviews with the Tax Analysis Unit of Alameda County's Auditor-Controller in March 2016.

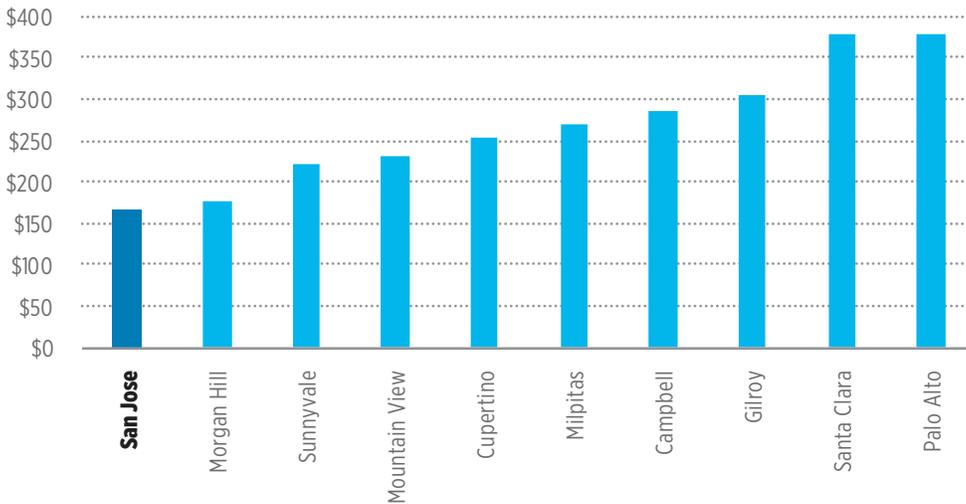
## How Well Does San Jose Capture Sales Tax Revenue?

Sales tax receipts are best compared at the regional level because San Jose competes for retail shoppers and business sales with its neighbors. As seen in Figure 20, San Jose falls well below its neighbors in per capita sales tax revenue.<sup>73</sup>

Several factors could explain this. First, some San Jose residents may do much of their shopping in neighboring cities. When a large number of residents take their dollars to shop elsewhere, this is referred to as “sales tax leakage.” Second, San Jose’s surrounding cities may have stronger manufacturing industries than San Jose. Since manufactured goods sell for much more than consumer retail goods, the resulting difference in sales tax revenue can be substantial. Third, San Jose’s residents may have less purchasing power (i.e., lower incomes) and may simply spend less than residents in neighboring cities.

Among these factors, sales tax leakage appears to be the most problematic. In 2004, consultants estimated that, after accounting for differences in income, San Jose was losing roughly 24 percent of potential sales to neighboring jurisdictions every year, mostly in the form of general merchandise, restaurant meals, home furnishings, building materials and some specialty retail goods.<sup>74</sup> In 2008, San Jose got an updated estimate that sales tax leakage had fallen to 19 percent.<sup>75</sup>

A lack of competitive retail stores in San Jose could cause sales tax leakage. The phenomenon could also be fueled by the fact that many who live in San Jose commute to other cities for work, giving them plenty of opportunities to shop outside the city’s borders.



**FIGURE 20:**  
**Sales Tax Revenue in Santa Clara County Cities**  
 Annual average per capita sales tax revenue across cities in Santa Clara County (2003 - 2014), in 2014 dollars  
 San Jose has the lowest per capita sales tax revenue among large Santa Clara County cities.

Source: SPUR analysis of California Controller’s Office, Cities Financial Reports 2003-14, <https://bythenumbers.sco.ca.gov/finance-explorer/view-by-city>

73 For a complementary illustration of how San Jose compares with the largest cities in California in per capita sales tax revenues, see Figure 31 in the Appendix.

74 See: San Jose Office of Economic Development, *San Jose Neighborhood Retail Model: Summary Report* (Jan. 2004), p. 17, [http://media.wix.com/ugd/7796e8\\_2648e308987544b0af1527f8cc68afbc.pdf](http://media.wix.com/ugd/7796e8_2648e308987544b0af1527f8cc68afbc.pdf)

75 See: Memorandum re: Prevention Measures to Avoid Sales Tax Leakage, August 7, 2008, [http://www3.sanjoseca.gov/clerk/CommitteeAgenda/CED/20080825/CEDC20080825\\_i.pdf](http://www3.sanjoseca.gov/clerk/CommitteeAgenda/CED/20080825/CEDC20080825_i.pdf)

## Recommendations: Strengthening San Jose's Fiscal Health

San Jose experienced many years of fiscal strain, with major cuts in services and staffing. It's time now for the city to shift toward reinvestment. Going forward, San Jose should strive to be an amenity-rich city with high-quality services that will attract residents, businesses, employees and visitors. This will require restoring some services and staffing that were cut during the downturn, as well as identifying new areas to grow services and make investments, such as infrastructure.

Delivering quality public services requires good fiscal health. That means capturing revenues that exceed or are equal to ongoing costs and managing assets and debt well. Based on the findings in this report, San Jose needs additional resources, at least in the short run, both to invest in services and to build up its reserves. These resources will also provide the city greater fiscal security in the event of future economic downturns.

Over time, new taxes could expire when the city General Fund receives an infusion of property tax revenue once redevelopment debt is paid off. But that property tax growth isn't expected for roughly three decades. In the meantime, San Jose needs to consider how it will raise revenues if it wants to avoid slipping even further behind.

Before pursuing new revenues, wise fiscal management calls for cutting costs in areas where there is inefficient spending. Our recommendations do not include this, however, because San Jose has already taken this step. The city underwent a thorough review of its costs in 2008 and, as described in Chapter 2, pursued numerous strategies to reduce costs, including reducing salaries, staff and services. As a result, there are few opportunities left for additional cuts.<sup>76</sup>

Another way to free up resources is to deliver services differently. Again, San Jose has taken steps in this direction. It changed many of its service delivery models, outsourced positions and required departments to recover costs where possible. Additional modifications, such as investing more in technology so staff can work more productively with improved outcomes, are being explored.<sup>77</sup>

The city made significant advances to create efficiencies in the years after the dot-com bust. It should continue to seek improvements and cost-savings opportunities, especially as city departments regain stable teams and there is capacity to explore such innovations.

A prudent overall fiscal strategy for San Jose must focus on growing the city's tax base while identifying sensible ways to expand revenues. It remains important to look for ways to innovate and save costs. But the bigger need moving forward is to raise sufficient revenue to meet the city's needs. This section proposes four strategies for strengthening San Jose's fiscal position:

- 1. Expand San Jose's tax base through strategically attracting investment and supporting economic growth.**
- 2. Increase local resources through well-designed revenue measures for *specific* purposes.**
- 3. Increase local resources through well-designed revenue measures for *general* purposes.**
- 4. Reform the public finance system to provide more flexibility and to support the regionalization of revenues and services.**

<sup>76</sup> Pensions and post-retirement health care are major cost areas for all cities. San Jose has spent considerable time renegotiating its pensions and post-retirement health care and is expected to save several billion over decades.

<sup>77</sup> See: Office of the Mayor, "Smart City Vision: Making San José America's Most Innovative City by 2020," <http://www.sanjoseca.gov/DocumentCenter/View/55021>

## **Strategy 1: Expand the city’s tax base through strategically attracting investment and supporting economic growth.**

For the last three decades, the City of San Jose has actively pursued strategies to attract and grow jobs, private investment and a stronger revenue base. The city’s economic strategy makes strengthening the economy a citywide business and focuses on actions that improve the city’s fiscal position.<sup>78</sup> In its General Plan, San Jose outlines strategies to become a fiscally strong city and a center of innovation and employment for the region through increasing jobs and implementing the city’s General Plan and its concept of developing densely along commercial corridors near transit.<sup>79</sup>

### **1. Support dense, mixed-use development in walkable, transit-supported areas.**

*Implementers: Office of Economic Development, Department of Planning, Building and Code Enforcement*

City planning and economic development staff should prioritize growing the city’s jobs and housing in places that can best capture the benefits of increased density. In particular, as large a share as possible of the city’s projected 120,000 new housing units (by 2040) should be developed at densities greater than 45 housing units per acre and in walkable communities. An analysis of five new multifamily developments in San Jose showed that all were greater than 43 units per acre and were likely to contribute between \$8,000 and \$180,000 in net revenue to the city.<sup>80</sup>

Adding more residents in denser development makes an area more attractive to retailers. This in turn generates greater local revenue from sales tax receipts. Simultaneously, employers want to locate in areas where they can find talented workers. Due to shifts in housing preferences, many highly skilled workers now live, or wish to live, in urban settings. If San Jose can encourage more well-designed multifamily housing at greater than 45 units per acre in walkable areas, the city is likely to capture both more residents and more jobs.<sup>81</sup> This could result in a fiscally positive cycle for San Jose.

New office developments should also be built at higher densities (i.e., more workers per acre), both to use limited employment lands more efficiently and to reap the fiscal and environmental benefits of shifting to a more compact urban form. San Jose should continuously strive to increase the job density in many of its employment areas, particularly in downtown and large parts of North San Jose. The only exception should be certain industrial uses that require significant land area for a small number of workers and that don’t need to increase their employment density to remain viable and competitive. Maintaining industrial lands is an important part of the city’s economic and fiscal strategy and should not be undermined.

### **2. Maintain restrictions on the conversion of key employment lands to residential uses.**

*Implementers: City Council, Office of Economic Development, Department of Planning, Building and Code Enforcement*

Between 1980 and 2015, San Jose converted nearly 2,300 acres of employment lands to other uses. Today, 57 percent of San Jose’s land is devoted to residential use, with only 15 percent focused on employment.<sup>82</sup> This is in contrast with surrounding cities such as Sunnyvale, Santa

78 See: City of San Jose, San Jose Economic Strategy 2010: Full Report, <http://www.sanjoseca.gov/DocumentCenter/View/6824>

79 See: Envision San José 2040 General Plan, adopted November 1, 2011, <https://www.sanjoseca.gov/DocumentCenter/Home/View/474>

80 See: “Net Fiscal Impact: New Higher-Density Residential Projects,” <http://www.sanjoseca.gov/DocumentCenter/View/42306>

81 This strategy presumes that San Jose will also continue to invest in and encourage greater construction of affordable housing throughout the city.

82 See: “History of Employment Land Conversions in San José and the Fiscal Impact of Land Use,” City Council Study Session, April 14, 2015, <http://www.sanjoseca.gov/DocumentCenter/View/43609>. Also see: Kim Walesh, “Strategies to Enhance San Jose’s Fiscal Health,” Jan. 28, 2016, <https://www.sanjoseca.gov/DocumentCenter/View/53650>

Clara and Mountain View, where 24 percent to 28 percent of the land area is used for employment. Some of those cities also have higher-density uses within their employment lands, which yields more workers and higher revenue per acre. Even with land conversions, San Jose maintains significantly more total acres of employment land compared with its neighbors. This asset will increase in value as land for economic development becomes increasingly scarce in the region.

Looking forward, the city should continue to grow its residential base. However, it should also retain most of its current restrictions on the conversion of key employment lands. There are some circumstances where key employment lands could be converted to residential properties — for example, where an employment parcel is surrounded by housing on three sides. Other possible candidates for conversions include land that is close to transit, land that can be used for other employment purposes, proposed sites of dense residential development, areas where there are contiguous acres of land available and parcels where nearby industries are compatible with residential use.

Any conversions — or modifications of policies to allow for more conversions — should be monitored carefully and regularly. For example, if affordable housing becomes an allowable use for the conversion of some employment lands, it is important that affordable housing is actually built on the sites that were converted.

### **3. Provide additional resources to the economic development and planning departments to facilitate private investment and economic growth.**

*Implementers: City Council, Office of Economic Development, Department of Planning, Building and Code Enforcement*

Placemaking has become a key component in economic development. San Jose's 2040 General Plan is an ambitious vision for reshaping the city in a way that moves beyond the automobile and creates walkable places throughout the city. Implementing the plan's long-range goals will require resources. Additionally, an effective economic development strategy means responding quickly to businesses interested in expanding or relocating to San Jose and encouraging property owners to lease or redevelop their properties.

The property tax base grows when residents and businesses build new buildings or make improvements or additions to existing property. For example, one key way to grow the tax base is by expanding the number of secondary units, also known as in-law apartments or accessory dwelling units (ADUs). Because there are so many residential parcels in San Jose, the city should develop specific policies to facilitate secondary units and work proactively to encourage residents to build these units or make other improvements that will increase their quality of life, or their ability to age in place, while also growing San Jose's property tax revenues. Since much of the opposition to secondary units comes from surrounding neighbors, the city could circumvent this obstacle by making a new unit within an existing property "as of right." This means that a neighbor could not restrict a property owner from creating a secondary unit as long as it complies with the building code and other planning regulations.

The property tax base also grows when commercial property owners reinvest in their property or businesses lease new space. For example, signing a new lease can result in remodeling and tenant improvements or the introduction of business equipment, all of which leads to a growth in the property tax base (as business equipment is also taxed as personal property in California). While the leasing, building and development of land is typically done by property owners and real estate brokers, city staff play a key role in helping facilitate this process.

As noted earlier, some of San Jose's departments are thinly staffed compared to other large cities. The planning department is largely funded by fees and has little support from the General Fund. As a result, there are few long-range planners or extra staff to plan for long-range projects or to respond to major development opportunities. In the Office of Economic Development, there are also few people (approximately five citywide) who are available to work directly with

companies, investors and developers on relocations, expansions, improvements, major leases or other economic development activities that lead directly to increased city revenue.

Accomplishing the vision outlined in this report will require adding staff, particularly to the economic development and planning departments. The following are some of the key staff needs and functions:

- Planning staff focused on long-range planning and permit approvals.
- Business outreach staff in the economic development department.
- Staff focused on promoting business improvement districts and other neighborhood economic development needs, particularly in areas of the city with limited current investment or development activity.
- Staff focused on promoting specific uses, such as retail or hotel development, citywide.
- Staff with a general focus on encouraging commercial property owners to make investments and enhancements to their properties. This includes remodels that increase overall values and bring in additional property tax revenues.

While adding to the city's workforce requires additional resources for salaries and benefits, investing in these two departments has the potential to increase the city's underlying tax base. Hiring and retaining high-quality long-range planning and economic development staff can generate significant new city revenue. Maintaining well-funded and well-staffed departments, even during downturns, is essential to ensuring that San Jose is able to effectively plan for development and manage business expansions.

#### **4. Implement a citywide retail strategy.**

*Implementer: Office of Economic Development*

Retail activity can generate significant tax revenue for a city through the local portion of the sales tax. According to estimates from the City of San Jose, big box retail generates nearly \$96,000 annually in city revenue per acre and auto dealerships produce more than \$80,000 per acre. These two retail types yield more in local revenue per acre than other uses (office space is \$60,000 to \$78,000 per acre; condominiums and apartments are about \$50,000 per acre).<sup>83</sup>

Yet over numerous years, San Jose has attracted less retail development and overall retail sales than surrounding communities. The City of San Jose estimates that about 19 percent of retail purchases by San Jose residents happen in neighboring cities.

In a traditional retail strategy, a city might focus on providing big-box stores with sufficient land or might designate an area as an auto dealership row. While such approaches have yielded significant revenue for some jurisdictions, they might not be the best strategy for the long term, given that younger generations are not buying as many cars and that people across the economy are spending less on tangible taxable goods and more on non-taxed services.<sup>84</sup> Increasing numbers of consumers are using their disposable income on online shopping, eating out and retail that is entertainment or is experiential (i.e., where the purchaser is a co-creator and not simply a consumer).<sup>85</sup> Given these changes, the future of retail will look different than its past.

In devising its retail strategy, San Jose should:

- Make sure that the city's policies and codes are consistent with current trends and do not lock the city into older retail patterns (such as suburban malls).

<sup>83</sup> See: "History of Employment Land Conversions in San José and the Fiscal Impact of Land Use," City Council Study Session, April 14, 2015, slide 42, <http://www.sanjoseca.gov/DocumentCenter/View/43609>

<sup>84</sup> See: Joe Cortwright, "On the Road Again," April 25, 2016, <http://cityobservatory.org/on-the-road-again-2>. Also see: "Young People Are Buying Fewer Cars," April 22, 2015, <http://cityobservatory.org/young-people-are-buying-fewer-cars>

<sup>85</sup> See: Shifting From Consumption to Experience: Winning in the Omnichannel Retailing, Ernst & Young (2014), [http://www.ey.com/Publication/vwLUAssets/EY-Shifting-from-consumer-to-experience/\\$FILE/EY-Shifting-from-consumer-to-experience.pdf](http://www.ey.com/Publication/vwLUAssets/EY-Shifting-from-consumer-to-experience/$FILE/EY-Shifting-from-consumer-to-experience.pdf)

- Continue to support and allow retail that serves neighborhoods. Plan for retail as part of larger communities, and make sure stores can be easily reached on transit or on foot from nearby residential developments. Once residents get in their cars, it may be just as easy for them to drive to a nearby city for shopping.
- Make it easy to add or expand food and drink establishments that can generate significant sales taxes. This aligns with the growing trend toward eating out.
- Identify and promote preferred sites for “urban-format” retail development (i.e., smaller stores with multiple levels and less parking). As SPUR has argued previously, San Jose should proactively develop policies about the location of such urban-format retail, as well as specifications about parking, setbacks and other urban design features. Having a clear policy approach will strengthen the city’s ability to negotiate effectively with retailers that may otherwise propose more traditional, auto-oriented retail developments.<sup>86</sup>
- Support continuous reinvestment in older retail areas (such as Eastridge Center) that will have to adjust over time to stay relevant, and ensure that the zoning allows for such changes.
- Make it easy for existing retail establishments to use the adjacent sidewalk and street space for expansion and activity, such as sidewalk cafés.
- Reduce parking requirements for new retailers in areas that are becoming more walkable. Cities often require additional parking beyond what the retailer needs. For example, San Jose required the CVS store on The Alameda to add additional parking. In order to acquire enough space, CVS bought two single-family homes and demolished them to create a surface parking lot. Today, most of those parking spots are not occupied.
- Provide more up-front support to inexperienced and first-time restaurateurs, particularly around drafting a business plan, understanding city permit or zoning regulations, and negotiating a lease. Many restaurants fail in their first year of operation, often because they are unaware of the challenges of opening a business and of city requirements and regulations.

The approach outlined here is often called the “fiscalization of land use,” and it has its downsides. Critics argue that California’s tax structure encourages communities to avoid land uses that generate less revenue (like housing) and instead prioritize uses like retail, particularly auto dealerships and big-box stores, due to the potential boost in local sales tax revenue.

In addition to the actions outlined above, another strategy to increase retail spending within a city is to increase consumers’ purchasing power, particularly for lower-wage and middle-wage workers, who spend a greater portion of their income on taxable goods. Cities can do this by promoting the growth of industries or firms that provide middle-income jobs, as well as by making policy or passing legislation that increases the wages of lower-wage workers.

<sup>86</sup> See: Benjamin Grant, *Getting to Great Places* (Dec. 2013), [https://www.spur.org/sites/default/files/publications\\_pdfs/SPUR\\_Getting\\_to\\_Great\\_Places\\_spreads.pdf](https://www.spur.org/sites/default/files/publications_pdfs/SPUR_Getting_to_Great_Places_spreads.pdf)

## Strategy 2: Increase local resources through well-designed revenue measures for *specific* purposes.

Evidence in this report points to the need for San Jose to pursue targeted revenues for specific purposes where appropriate. Below are three such options San Jose should consider.

### **5. Identify opportunities to raise local fees to the levels recommended in San Jose’s user fee study.**

*Implementer: City Manager’s Office*

San Jose charges a range of fees for services. The fees charged must be limited to what it actually costs the city to deliver the service. As a result, all fees must be supported by a user fee study.<sup>87</sup>

While San Jose has aggressively pursued increases in its fees, nonetheless it should continually update all appropriate fee studies to ensure that it knows the full cost to deliver services. In particular, San Jose should aspire to an accounting system that tracks fully allocated costs and expenses down to the level of each individual service. While San Jose may not always want to charge residents the full fee equal to the precise cost of delivering a service, it is essential for the city to be aware of the full cost so that it is selecting fee reductions with complete information.

Statewide, cities typically charge less in fees than costs demand. As a result, they may leave millions of dollars on the table by not fully charging fees that they are legally entitled to, often by failing to include cost of living adjustments in the fee structure. The public will better understand moderate annual fee increases than dramatic jumps in fees that align with publicly identified budget deficits.

### **6. Pass new general obligation bonds to pay for deferred maintenance, particularly roads.**

*Implementers: Department of Transportation, Public Works Department, City Council*

General obligation (GO) bonds are debt instruments issued by a state or local governments to raise funds for public projects. These entities sell GO bonds to investors and promise to pay the investor back, plus interest, over time. GO bonds require the approval of two-thirds of voters. In San Jose, they could be used to fund the most significant deferred maintenance, housing or other capital infrastructure needs.

Once voters pass a GO bond, they have formally given the city the authority to sell bonds as needed up to the authorized amount and to levy a tax on property sufficient to pay the upcoming debt service on the bonds. Generally, the bonds are sold over a period of time, as necessary, to fund specific projects (such as building a new public facility). This way, the city and its taxpayers are not paying interest on bonds before they actually need the capital.

San Jose’s one-time deferred maintenance bill is nearly \$1 billion, and its annual need is currently at \$175 million and growing. A major portion of the deferred maintenance is street paving. San Jose’s road network is both its biggest infrastructure asset and liability.<sup>88</sup> The city should pursue a major GO bond to fund its deferred road and other transportation needs. Depending on political support, such a bond could generate at least several hundred million dollars.

Annual road maintenance is paid for through a variety of ongoing revenues such as state and federal gas tax revenues, county vehicle registration fees and San Jose’s real estate development tax.<sup>89</sup> San Jose does not typically spend any General Fund revenue on servicing streets. However,

<sup>87</sup> See: City of San Jose, Final Report on the Fee Analysis and Study for the Department of Public Works, Development Services Division (April 29, 2009), <http://www.sanjoseca.gov/documentcenter/view/33699>

<sup>88</sup> Supra note 22.

<sup>89</sup> Supra note 22, slide 46.

because gas tax revenues have been in a steady decline, San Jose's deferred maintenance backlog has grown, and since costs increase annually due to deterioration, it is appropriate to consider debt financing. Also, using a GO bond for roads would facilitate capital investment in expanding sidewalks and adding bike lanes. This strategy would reinforce the city's overall goal to reduce driving from 80 percent of trips to 40 percent while increasing biking, walking and transit.

The city's Department of Transportation, in partnership with the Department of Public Works, should identify key capital projects that could be financed through GO bonds and then work with the City Council to place the bonds on the ballot.

GO bonds carry a relatively low interest rate, which reduces both the city's overall cost of borrowing and the burden to taxpayers. These bonds are repaid from the property tax paid by property owners who will benefit from improved city infrastructure, and the additional tax is levied only until all of the debt has been repaid. On the downside, GO bonds must be approved by two-thirds of voters, so they're often difficult to pass.

### **7. Expand the use of economic development and investment tools such as community facilities districts, enhanced infrastructure financing districts and business improvement districts.**

*Implementers: Office of Economic Development, Public Works, Planning Building and Code Enforcement, existing business improvement districts*

There are several policy tools in California to raise new revenues to pay for infrastructure or added services in a specific area without increasing citywide taxes. These economic development tools are increasingly relevant in the post-redevelopment era in California and include the following:

- Community facilities district (CFD): increases to the property tax rate for a select group of properties
- Business improvement district (BID): specific tax assessments on property owners and businesses in an area
- Enhanced infrastructure financing district (EIFD): a smaller version of redevelopment in which a district captures a portion of the tax increment to finance a wide variety of public projects

CFDs are typically referred to as "Mello-Roos districts" (named after the senator and assemblyman who authored the original legislation). They allow property owners in a certain area to agree to a special tax increase in exchange for additional investments that benefit all property owners in the area. In most cases, to approve a Mello-Roos district, at least 12 property owners must be involved and two-thirds of them must agree to the tax increase. A Mello-Roos district can be used to finance both facilities and services such as park maintenance, fire and police protection, storm drainage maintenance and environmental cleanup and remediation services.<sup>90</sup>

BIDs or property business improvement districts (PBIDs) are formed when a majority of property owners in an area approve the additional assessment to pay for the district. These districts can fund everything from additional street cleaning to community ambassadors and local events to infrastructure investments such as improved parks. San Jose has several BIDs but has not used the tool nearly as much as other cities in the Bay Area, most notably San Francisco and Oakland.

Another tool to capture investment is the EIFD. Similar to a redevelopment area, an EIFD sells bonds that it pays back with tax increment from the growth in property taxes in that area. Unlike redevelopment, the EIFD does not use the schools' tax increment. EIFDs should be applied more often throughout the city, though particularly in North San Jose.

<sup>90</sup> See: Daniel Bort, An Introduction to California Mello-Roos Community Facilities Districts (2006), <https://www.orrick.com/Events-and-Publications/Documents/1180.pdf>

San Jose should also focus on expanding Mello-Roos districts, business improvement districts (BIDs) and EIFDs in parts of the city, particularly in some of the areas targeted for growth in the General Plan. Other possible areas for BIDs include the area around the airport, Edenvale and North First Street.

To get established, these tax assessment districts, particularly Mello-Roos districts, require hundreds of thousands of dollars in start-up costs, which cover everything from legal counsel and financial consultants. In order to support the expansion of these tools, San Jose might consider funding some or all of the up-front costs.

There are some downsides and important considerations regarding these tools. For example, it raises equity concerns when some areas of the city receive more services because the residents/voters are more willing and financially able to tax themselves than poorer, less affluent areas of the city.

### **Strategy 3: Increase local resources through well-designed revenue measures for *general* purposes.**

The evidence in this report suggests that San Jose needs more funding to invest broadly in core services. While this report lists eight taxes, we are not recommending that the city pursue all of them. Instead we offer them as a menu of potential revenues that are appropriate to consider.

The city's portfolio of tax revenues should be designed to grow with the economy over time. It should also be predictable enough for the city to make reliable budget projections. Ultimately, it is important to have a set of criteria to evaluate upcoming tax measures and weigh the merits of the overall set of tax revenues that the city relies on to deliver services.

San Jose already levies a number of city-generated taxes and fees, including a utility tax, hotel tax, marijuana tax, card room tax, real estate transfer tax and disposal facility tax.<sup>91</sup> Some of these taxes were set decades ago and have not had their rates adjusted.

The revenue measures on the following pages are options for San Jose to investigate and consider. The sales tax increase will appear on the June 2016 ballot, and the business tax modernization is slated for future modification. All measures have different benefits and drawbacks, each of which is discussed in more detail below. In determining which of these tax measures to pursue, and in evaluating the specific details of a particular tax proposal, it is important to apply the "Principles and Framework of Good Tax Policy" outlined on page 44.

91 See: Five-Year Economic Forecast and Revenue Projections: 2017–2021, "Appendix B: General Fund Revenue Descriptions," <https://www.sanjoseca.gov/documentcenter/view/54739>

# Principles and Framework of Good Tax Policy

An effective revenue system allows a local government to have a diversified and balanced portfolio of taxes and fees. For example, while some revenues will fluctuate, others will be more stable. For a city to function successfully, not only must it have stable and growing revenues, but it must also seek to capture new revenues in the least disruptive way. No revenue measure is likely to satisfy all the criteria listed below. Instead, these criteria offer a way to evaluate the effects of various revenue strategies and to compare different options.<sup>92</sup> Any city will have to carefully weigh the trade-offs in their revenue-raising — and spending — strategy. (Common trade-offs are listed in Chapter 1.)

## Criteria for Good Tax Policy

- 1) **The tax raises a sufficient amount of money.**
  - a) The money raised is substantial enough to offset the political costs of passing the tax and the administrative costs of creating, collecting and enforcing it.
- 2) **The tax is efficient.**
  - a) It is not overly difficult to administer and collect and doesn't add complexity to the existing administrative structure.
- 3) **The tax has low transaction costs.**
  - a) It is relatively easy to understand and comply with.
- 4) **The tax revenue is not volatile.**
  - a) It is not overly sensitive to political or economic swings and does not create an undue risk for the jurisdiction that will rely on it or the services it will support.
- 5) **The tax is equitable and fair.**
  - a) Taxpayers with similar economic circumstances have a similar tax burden.<sup>93</sup>
  - b) The tax does not unnecessarily favor one type of industry or business over another.
  - c) The tax levied is proportionate to the ability to pay the tax.
  - d) The tax does not disproportionately affect certain groups unless it's for an important public purpose.<sup>94</sup>
  - e) The tax does not exacerbate negative conditions for low-income people.
- 6) **The tax sends an appropriate signal to achieve socially desired behavior.**
  - a) If possible, it taxes what is detrimental to society — for example, smoking.
  - b) If possible, it tries to avoid creating perverse incentives or negative unintended consequences (i.e. a sweetened beverage tax that increases demand for diet sodas or other untaxed alternatives).
- 7) **The tax policy does not cause economic flight or reduce economic competitiveness.**
  - a) The tax has minimal impact on where households or businesses choose to locate.
  - b) The tax does not result in negative shifts in economic activity, such as businesses or investors leaving the jurisdiction.
- 8) **The tax was developed through a broad and effective process.**
  - a) The process to develop the tax was transparent and open.
  - b) The tax proposal was developed with input from a wide range of impacted parties.
  - c) The process to develop the tax included an evaluation of various options and alternatives before selecting one specific proposal.

<sup>92</sup> References for this framework include: Annette Nellen, Policy Approach to Analyzing Tax Systems; and Tax Foundation, Ten Principles of Sound Tax Policy; and the Legislative Analyst's Office.

<sup>93</sup> For example, two shopping center owners should have similar tax burdens.

<sup>94</sup> For example, a soda or tobacco tax will affect those who use such substances. But reducing the consumption of a harmful substance is an important public purpose. In contrast, a tax that unduly overburdens low-income households compared to high-income households should be avoided.

Revenue Measure	Estimated revenue generation
Update the existing business tax	\$12 million or more per year, depending on how it is designed
Raise the existing sales tax <sup>95</sup>	A 0.25% tax increase could raise roughly \$40 million per year
Raise the existing utility tax	A 1% increase could raise about \$20 million per year; a 2% increase could raise almost \$40 million
Create a parking tax	More than \$9 million per year
Create a sugar-sweetened beverage tax	A penny-per-ounce tax could raise \$30 million per year
Raise the existing conveyance tax (real estate transfer tax)	An increase from \$3.30 to to \$4.95 per \$1,000 of assessed value would generate an additional \$19 million per year
Create new parcel taxes	A \$50 annual tax on all parcels would raise roughly \$13.2 million per year
Increase disposal tax on solid waste	An additional \$4.50-per-ton tax, plus including recycling transfer facilities and eliminating other exemptions, could bring in \$5 million per year

FIGURE 21:

### Potential Revenue-Raising Measures for San Jose to Consider

There are at least eight different measures San Jose could pursue to increase revenue.

Source: SPUR analysis of City of San Jose estimates.

*Note: All the taxes discussed in this section have the same set of implementers; they could be developed by city staff and elected officials in partnership with business and civic leaders and adopted by the voters.*

## 8. Update, restructure and modernize the business tax.

San Jose has an employment-based business tax, which was adopted in 1964 and updated in the mid-1980s. Businesses with up to eight employees pay a flat rate of \$150 annually. For each employee over eight, the business pays \$18 annually, up to a maximum of \$25,000.

Currently, San Jose's business tax per firm is in the mid-range in Santa Clara County, but it's below Oakland's and San Francisco's. Among South Bay cities, there is great variation in the average business tax per firm. For example, firms in Milpitas pay \$24 on average annually, while those in Fremont pay \$453 and those in Santa Clara, Sunnyvale and San Jose pay \$80, \$192 and \$171, respectively.<sup>96</sup> San Jose gathers more total business tax revenue than any other city in Santa Clara County simply because it is a much larger city and has many more firms. Yet compared to big cities like Oakland and San Francisco, San Jose makes only a fraction on business tax revenue.

In its Fiscal Reform Plan of 2011,<sup>97</sup> San Jose considered modernizing the business tax as part of a short list of revenue-raising ideas, culled from more than 320 revenue-raising, cost-savings and service-elimination options generated in the effort to solve San Jose's General Fund structural deficit.<sup>98</sup>

The city has previously discussed six ways it could alter the business tax:

- Charge more than \$150 as the basic rate.
- Grow the increment to make it more progressive, such as charging more than \$18 per employee or establishing multiple tiers at higher rates.
- Increase or remove the maximum tax amount, which is currently \$25,000 annually.
- Add an administrative fee.
- Tie the tax to inflation so that it grows with the economy.
- Modify the definition of what constitutes an "employee" to capture more workers whom a firm might otherwise identify as contractors.

95 This sales tax increase is scheduled for the June 2016 ballot.

96 See: City of San Jose, "San Jose's Business Tax: Preliminary Analysis of Gross Receipts Tax Ballot Measure, Options for Updating Current Business Tax," Feb. 26, 2016, slides 7-8, <http://media.bizj.us/view/img/8733142/city-staff-grt-report-2-26-16.pdf>

97 See: City Manager's Memo, "Fiscal Reform Plan: Budget Addendum #1," May 2, 2001, <https://www.sanjoseca.gov/DocumentCenter/View/4628>

98 See: City Manager's Memo, "General Fund Structural Deficit Task Force Report," Jan. 7, 2008, <https://www.sanjoseca.gov/DocumentCenter/View/4626>

The city has made clear that it only wants to enact changes that will not encourage firms to leave San Jose; that will not create administrative burden; that will distribute equal tax responsibility across employees, residents and businesses; and that will enable San Jose's revenues to grow with the economy, as service costs do.<sup>99</sup>

Depending on its design, San Jose's business tax could be a source of revenue that grows with the economy over time. This could tie the city's revenue to the dynamism of the broader economy, something not every revenue stream can do. If done well, with engagement and input from the business community, changing the business tax could also raise a decent portion of tax revenue for vital services.

Modernizing the business tax in San Jose might also have downsides. The city already has a hard enough time keeping and attracting jobs. Increasing costs to businesses might spur companies to leave or avoid coming to San Jose. Because many cities near San Jose offer similar amenities and lower business tax rates, San Jose should closely evaluate how any business tax adjustments would affect the city's competitiveness, and for which types of industries.

Ultimately, the best way to change a business tax is through a very broad and inclusive process that engages affected businesses. San Francisco underwent an extensive process in modernizing its business tax, which involved traditional and social media outreach, nearly 30 industry working group meetings and a five-year phased implementation.<sup>100</sup>

<sup>99</sup> Supra note 96, slides 58-59.

<sup>100</sup> See: Corey Marshall, "Business Tax Reform Heads to November Ballot," May 21, 2012, <http://www.spur.org/news/2012-05-21/business-tax-reform-heads-november-ballot>

FIGURE 22:

**Business Tax Rates for Various Cities Across California**

Business taxes in California can be assessed as a fee per employee or per unit of property or as a percentage of the gross receipts of the business.

	City	Type of Business	Annual Tax/Fee	Additional Tax Increments
<b>Large Cities in Santa Clara County</b>	San Jose	Businesses	\$150 up to 8 employees	\$18 per employee over 8
		Residential landlords	\$150 up to 30 units	\$5 per unit over 30
		Commercial landlords	\$150 up to 15,000 sq. ft.	\$0.01 per sq. ft. over 15,000
		Mobile home parks	\$150 up to 30 lots	
	Campbell	Most businesses	\$119 for 1-5 employees \$189 for 6-15 employees \$271 for 16-50 employees \$541 for 51+ employees	
	Cupertino	Most businesses	\$133	
	Gilroy	Most businesses	\$40 under \$40,000 of gross receipts	Additional \$20-\$40 per \$100,000-\$200,000 of gross receipts
	Milpitas	Most businesses	\$35	\$5 per employee up to 10 \$1 per employee thereafter
	Mountain View	Most businesses	\$30	
		Larger businesses	\$50 for 5-50 employees \$75 for 51-100 employees \$100 for 100+ employees	
	Mobile home parks	\$12 plus \$2 per space		
Palo Alto	Businesses	\$51		
Santa Clara	Most businesses	\$15-\$500 based on number of employees		
	Rental units	\$3 per unit		
Sunnyvale	Businesses and rental units	\$35 for first employee \$58 for 2 to 5 employees or rental units	\$58 for each additional group of 5 employees or rental units	
<b>Large Cities in California</b>	Anaheim	Businesses	\$0.095 for each \$1,000 of gross receipts	
	Bakersfield	Most businesses	\$0.30 for each \$1,000 of gross receipts	
		Professional businesses	\$0.65 for each \$1,000 of gross receipts	
	Fremont	Services, rentals	\$1 for each \$1,000 of gross receipts	
		Professional	\$1.30 for each \$1,000 of gross receipts	
	Fresno	Most businesses	\$34 for up to \$3,000 in gross receipts	Additional fees per \$3,000-\$5,000 in gross receipts
	Long Beach	Most businesses	\$345.55	\$9-\$27 per employee
	Los Angeles	Most businesses	\$1.01-\$4.75 for each \$1,000 of gross receipts	
	Oakland	Most businesses	\$0.60-\$4.50 for each \$1,000 of gross receipts	
		Commercial and residential rentals	\$13.95 for each \$1,000 of gross receipts	
	Riverside	Retail businesses	\$118.50 for gross receipts up to \$25,000	\$0.83 for each \$1,000 of gross receipts above \$25,000
	Sacramento	Most businesses	\$30 for gross receipts up to \$10,000	\$30 plus \$0.40 per \$1,000 of gross receipts above \$10,000
	San Diego	Businesses	\$34 up to 12 employees	\$125 plus \$5 per employee for 13 employees and up
	San Francisco	Businesses	\$0.1875-\$1.40 for each \$1,000 of gross receipts	
		Rental and leasing	\$0.7125-\$0.75 for each \$1,000 of gross receipts	
Santa Ana	Businesses	\$60 plus \$0.10-\$0.50 per \$1,000 of gross receipts		
Stockton	Most businesses	\$0.90 for each \$1,000 of gross receipts		

Source: Working Partnerships USA analysis.

### 9. Increase the local sales tax by one-quarter cent (0.25 percent).

The local sales tax in San Jose is currently 8.75 percent. Raising San Jose’s sales tax by a quarter-cent, to 9 percent, would raise approximately \$40 million annually in city revenue.<sup>101</sup> As a general tax, it would require a simple majority to pass, which polls indicate is possible.<sup>102</sup>

Raising the sales tax offers a number of benefits. It’s a simple adjustment that would be easy for San Jose to administer and easy for consumers to comply with. In addition, all of the revenue would go to the City of San Jose and not be split among overlapping jurisdictions (as with property taxes). It has the potential to generate significant revenue fairly quickly and can just as easily sunset (i.e., expire), if appropriate in the future. Small increases in the sales tax rate would likely have a negligible impact on consumer spending patterns. So San Jose would not expect to see residents leaving the city to make purchases as a result of the tax.

Raising the sales tax also has its downside. Sales taxes are regressive — lower-income residents pay a higher share of their income on taxable retail goods like clothing and housewares. However, the regressive impact of sales tax can be mitigated if resulting revenues are spent on services that disproportionately benefit low-income populations.

In the longer term, it might make sense to apply the sales tax more broadly, extending it to intangible goods and services, such as haircuts. Such a change would require state policy, as it is beyond any one city’s control. (This point is discussed in more detail in Strategy 3.)

	City	Rate
<b>Large cities in Santa Clara County</b>	San Jose	8.75%
	Campbell	9.00%
	Mountain View	8.75%
	Palo Alto	8.75%
	Santa Clara	8.75%
	Sunnyvale	8.75%
<b>Large cities in California</b>	Anaheim	8.75%
	Fremont	8.75%
	Long Beach	8.75%
	Los Angeles	9.50%
	Oakland	8.00%
	Sacramento	9.00%
	San Diego	9.00%
	San Francisco	9.50%
	Santa Ana	8.50%

**FIGURE 23:**  
**Sales Tax Rates for Various Cities Across California**  
 Many California cities have increased their local sales tax beyond the state rate and any county increases. Within Santa Clara County, Campbell is the only city so far with an additional local sales tax.

Source: California State Board of Equalization, “California City & County Sales & Use Tax Rates”: <http://www.boe.ca.gov/cgi-bin/rates.cgi>

### 10. Increase the Utility User Tax.

Many cities in California tax the use of various utilities. This Utility User Tax (UUT) can be assessed on a range of services, such as gas, electricity, telecommunications, water and prepaid mobile phone or wireless service. Cities can choose whether to charge the same rate across all the utility types, as well as whether to charge the same rate to businesses or utilities.

San Jose’s UUT is currently 5 percent on gas, electricity and water, and 4.5 percent on telecommunications and prepaid wireless. Most large cities in Santa Clara County — and in California as a whole — have a similar tax, and about a third charge a higher rate than San Jose does. Notably, Santa Clara, which is right on San Jose’s border, operates its own utility and therefore does not charge a UUT. Since San Jose takes in close to \$100 million annually with its UUT, if the city were to raise its UUT on gas, electricity, water and telecom/prepaid wireless to 6

101 See: Mayor Sam Liccardo’s Memo, “March 2015 Budget Message for Fiscal Year 2015–2016,” <https://www.sanjoseca.gov/ArchiveCenter/ViewFile/Item/2559>

102 See: City Manager’s Memo, “Potential General Purpose Sales and Use Ballot Measure,” Feb. 26, 2016, [http://sanjose.granicus.com/Viewer.php?view\\_id=&event\\_id=2126&meta\\_id=559688](http://sanjose.granicus.com/Viewer.php?view_id=&event_id=2126&meta_id=559688)

percent, it would generate an additional \$20 million per year. An increase to 7 percent would bring in close to \$40 million.

	City	Rate
<b>Large cities in Santa Clara County</b>	San Jose	5% on gas, electricity, water; 4.5% on telecom, prepaid wireless
	Campbell	None
	Cupertino	2.4% on telecom, electricity, gas
	Gilroy	5% on electricity, gas; 4.5% on telecom, prepaid wireless
	Milpitas	None
	Mountain View <sup>103</sup>	3%
	Palo Alto	5%
	Santa Clara	None
Sunnyvale	2%	
<b>Large cities in California</b>	Anaheim	None
	Bakersfield	None
	Fremont	None
	Fresno	None
	Long Beach	5%
	Los Angeles	10% on energy; 9% on telecom
	Oakland	7.5%
	Riverside	6.5%
	Sacramento	7.5% on energy, cable TV; 7% on telecom
	San Diego	None
	San Francisco <sup>104</sup>	7.5%
	Santa Ana	5.5%
	Stockton	6% on gas, electricity, water, telecom; 5.5% on prepaid wireless

**FIGURE 24:**  
**Utility Tax Rates for Various Cities Across California**

Utility taxes vary widely in California; many cities do not have one at all. San Jose's rates of 4.5 percent and 5 percent are well below some of the state's highest utility taxes.

Source: California State Controller, Muni Services and Management Partners, Inc. (2008)<sup>105</sup>: <http://www.uutinfo.org>

Increasing the utility tax promises several benefits. The consumption of gas and electricity powered by fossil fuel contributes to climate change and degrades air quality and public health. While determining the mix of fuels that generate San Jose's electricity is outside the scope of this report, typically taxes that raise the cost of energy produced by fossil fuel can reduce the use of this energy, which carries social and environmental benefits.

Also in the positive column, increasing an existing tax is simple for cities to administer and for consumers to comply with. No new systems for tracking and collecting the tax would be necessary.

On the other hand, raising the utility tax has drawbacks, too. For energy-intensive industries, particularly advanced manufacturing, energy is a large cost. Because utility tax rates are patchwork across the Bay Area, energy-intensive companies may find it worthwhile to leave San Jose if its utility taxes get too high. In addition, charging more for energy results in a regressive tax, as low-income households use a larger share of their income to run household appliances and control the temperature of their homes.

103 See: City of Mountain View, "Utility Users Tax," <http://www.mountainview.gov/depts/fasd/tax/uut.asp>

104 San Francisco's UUT is assessed on residential electricity and gas.

105 See: California State Controller's Office Fact Sheet, [http://www.sco.ca.gov/Files-ARD-Local/LocRep/adhoc\\_city\\_9899utilityuserstax.pdf](http://www.sco.ca.gov/Files-ARD-Local/LocRep/adhoc_city_9899utilityuserstax.pdf). Also see: City of San Jose and Management Partners, Inc., Development of Strategies to Address the City's General Fund Structural Budget Deficit (Jan. 2008), <https://www.sanjoseca.gov/DocumentCenter/View/4626>

## 11. Adopt a parking tax.

San Jose currently has no parking tax, but this is not uncommon. In 2014, only 23 cities in California reported parking tax revenues to the California State Controller, most notably Oakland, Berkeley, San Francisco and Los Angeles.<sup>106</sup> San Francisco places a 25 percent parking tax on each space operated by a private parking operator, which typically generates over \$80 million for the city's General Fund each year.<sup>107</sup> In 2008, San Jose was considering this tax and estimated that a 10 percent tax on all public and private lots would generate roughly \$9 million per year.<sup>108</sup> The City of San Jose owns 7,480 parking spaces (in both lots and garages), and there are many more spaces in privately owned garages and lots citywide.<sup>109</sup>

Taxing parking can have social benefits. For example, limiting parking and/or charging for it are effective ways to minimize car trips. With less driving comes a reduction in tail-pipe emissions and negative climate and health impacts, such as asthma, other respiratory issues and heart disease.<sup>110</sup> In addition, a tax on parking could make operating a parking structure less profitable and create an incentive for some owners to redevelop their surface parking lots into more productive uses, such as buildings for jobs, housing or commercial uses or spaces for recreation.

On the downside, a parking tax might generate a lot of political opposition for a relatively small return, revenue-wise. And developing the administrative, legal and enforcement systems to design and carry out the new tax might take considerable effort and expense. Further, given that San Jose's neighbors do not have such a tax, and that the South Bay's sprawl and relative lack of transit have made driving the convenient choice for many, increasing the cost to drive in San Jose could put the city at a slight competitive disadvantage.

## 12. Pass a "soda tax" on sugar-sweetened beverages.

Commonly referred to as "soda taxes," taxes on sugar-sweetened beverages also cover fruit drinks, presweetened teas, flavored water and energy drinks. The City of Berkeley passed a 1-cent-per-ounce tax on sweetened beverages in 2014, the only California city with such a tax on its books. Both San Francisco and Oakland have a 1-cent-per-ounce tax on their November ballots.

In general, taxing something with harmful health effects offers social benefits. In the case of taxing soda and other sugar-sweetened beverages, the benefits are twofold. First, if the tax is passed on to consumers, the increased cost of these beverages could reduce how much sugar people consume. A widely cited meta-analysis found that drinking more sugar-sweetened beverages raised the risk of metabolic syndrome and Type 2 diabetes.<sup>111</sup> Reducing the risk of these diseases through a tax may be an effective public health move. Second, others have posited that simply placing a "sin tax" on sugar-sweetened beverages sends the signal that they are bad for you. This alone could discourage some consumers from buying sugar-sweetened beverages.<sup>112</sup>

These taxes can raise substantial revenue. According to several estimates, a penny-per-ounce tax in San Jose could generate approximately \$30 million based on the city's current consumption of more than 23.5 million gallons of such beverages a year.<sup>113</sup>

106 SPUR analysis of California State Controller's Cities Financial Reports, 2014, <https://bythenumbers.sco.ca.gov/finance-explorer/view-by-city>

107 See: Office of the Controller, City and County of San Francisco, "FY 2014-15 and FY 2015-16 Revenue Letter," June 10, 2014, <http://sfcontroller.org/Modules/ShowDocument.aspx?documentid=5417>, page 5

108 Supra note 19, p. 65.

109 See: City of San Jose, 2015-2016 Proposed Budget in Brief, <https://www.sanjoseca.gov/DocumentCenter/View/43265>

110 See: Union of Concerned Scientists, "Lower Tailpipe Emissions Will Lead to Cleaner Air, More Jobs," March 29, 2013, [http://www.ucsusa.org/news/press\\_release/lower-tailpipe-emissions-0371.html#.VwU31B1rLBI](http://www.ucsusa.org/news/press_release/lower-tailpipe-emissions-0371.html#.VwU31B1rLBI)

111 See: Vasanti Malik et al., "Sugar-Sweetened Beverages and Risk of Metabolic Syndrome and Type 2 Diabetes," *Diabetes Care*, vol. 33, no. 11 (Nov. 2010), <http://care.diabetesjournals.org/content/33/11/2477.full>

112 See: Allen D. Kanner, "The Hidden — and Not So Hidden — Benefits of a Soda Tax," [http://www.berkeleyvsbigssoda.com/benefits\\_of\\_a\\_soda\\_tax](http://www.berkeleyvsbigssoda.com/benefits_of_a_soda_tax)

113 See: Rudd Center for Food Policy and Obesity, "Revenue Calculator for Sugar-Sweetened Beverage Taxes," <http://www.uconnruddcenter.org/revenue-calculator-for-sugar-sweetened-beverage-taxes>. According to their analysis, San Jose consumed the following gallons of the following sugar-sweetened beverages annually: soft drinks (9,935,331), fruit drinks (4,060,826), sports drinks (3,195,480), ready-to-drink tea (2,205,799), energy drinks (3,413,386), flavored water (331,629), ready-to-drink coffee (366,283).

While distributors technically pay the tax, they pass some of it on to consumers. In Berkeley's case, roughly 22 percent of the tax was passed on to consumers,<sup>114</sup> and it raised an estimated \$1.5 million in its first fiscal year in Berkeley.<sup>115</sup>

Imposing a sugar-sweetened beverage tax has some negative consequences as well. Because it's a regressive tax, the cost of it is borne more by those with lower incomes. Additionally, passing such a tax requires a political fight with the large sugar and beverage distribution industries in the U.S.

### **13. Increase San Jose's real estate transfer tax and allow some of the incremental growth to support General Fund activities.**

San Jose's existing real estate transfer tax is set at \$3.30 for each \$1,000 of value and applies evenly to residential, commercial and industrial development. This rate has been in place for many years and is comparable to the level in nearby Mountain View and Palo Alto.

Since the tax is tied to property sales and construction activity, the revenue from the tax fluctuates based on economic activity. Between 2003 and 2014, the tax generated between \$15 million and \$64 million (in 2014 dollars). The low years were 2009 and 2010, and the high year was 2014.

San Jose should explore increasing the transfer tax to at least \$4.95 per \$1,000 of property value, a 50 percent increase. Assuming that the tax generates about \$38 million per year on average, a 50 percent increase would bring in about \$19 million in additional revenue.<sup>116</sup>

Under current rules, all proceeds from the transfer tax are dedicated to specific uses, such as parks and community facilities development, communications, the fire department, libraries and service yards (i.e. maintenance facilities). None of the transfer tax proceeds are allocated to general uses. San Jose should consider allowing a portion of the new revenue to be used for General Fund purposes.

While the current tax provides an important source of dedicated revenue for capital, one modification would be to allow a portion of the revenue to go to other uses, particularly maintenance. In 2008 the City of San Jose considered a 50 percent increase in the transfer tax and also amendments to allow 40 percent of the parks allocation to be used for parks operation and maintenance as well as 40 percent of the non-parks allocation to be used for operations and maintenance of the specific programs funded with the revenues of the tax.<sup>117</sup>

But the City Council ultimately did not put this measure on the ballot. This report does not argue for specifying where the incremental funds should be used. Instead, we recommend that new proceeds from an increase in the transfer tax be flexible to allow the city to invest them where they're most needed.

The real estate transfer tax is widely considered to be one of the most economically efficient taxes. It does not impact job creation or business attraction and retention. Other types of taxes, such as the business tax, can slow down the economy as a whole, so they're less ideal sources of revenues, especially in difficult economic times. In addition, because real estate purchases are so large, an additional charge at the time of sale is negligible and unlikely to have a significant dampening effect on real estate transactions.<sup>118</sup>

114 See: Ted Boscia, "Study: Berkeley Soda Tax Falls Flat," Cornell Chronicle, Aug. 17, 2015, <http://www.news.cornell.edu/stories/2015/08/study-berkeley-soda-tax-falls-flat>

115 See: Jessica Lynn, "City Council Votes to Allocate 'Soda Tax' Revenue to School District, City Organizations," The Daily Californian, Jan. 20, 2016, <http://www.dailycal.org/2016/01/20/city-council-votes-allocate-soda-tax-revenue-school-district-city-organizations/>

116 City of San Jose estimates.

117 See: Jim Zito, "Changes to the Conveyance Tax and the Construction and Conveyance Fund Proposed by the City Manager," [http://www3.sanjoseca.gov/clerk/Agenda/20080619/20080619\\_03b\\_att.pdf](http://www3.sanjoseca.gov/clerk/Agenda/20080619/20080619_03b_att.pdf)

118 See: "Proposition L — Real Property Transfer Tax," SPUR Voter Guide (Nov. 2002), <http://www.spur.org/publications/voter-guide/2002-11-01/proposition-l-real-property-transfer-tax>

On the other hand, some parts of the real estate industry have tended to oppose increasing transfer taxes, which may make it difficult to approve a rate increase. In addition, to the extent that real estate firms can pass the cost of the transfer tax on to consumers, they will. If they are able to do this, buying a home in San Jose will become even more expensive. To ease this burden for most homebuyers, the city could levy the real estate transfer tax only on homes above a certain price point.

Typically, the revenue from real estate transfer taxes is not stable, as it rises and falls based on the level of activity in the housing market or the total value of particular sales. Major land sales can swing the numbers from one year to the next. As a result, it's important to ensure that the revenue from real estate transfer taxes is spent primarily on one-time uses, not on ongoing programs.

	City	County Transfer Tax per \$1,000	City Transfer Tax per \$1,000
<b>Large Cities in Santa Clara County</b>	San Jose	Seller pays \$1.10	Buyer/seller split \$3.30
	Campbell	Seller pays \$1.10	
	Cupertino	Seller pays \$1.10	
	Gilroy	Seller pays \$1.10	
	Milpitas	Seller pays \$1.10	
	Mountain View	Seller pays \$1.10	Buyer/seller split \$3.30
	Palo Alto	Seller pays \$1.10	Buyer/seller Split \$3.30
	Santa Clara	Seller pays \$1.10	
	Sunnyvale	Seller pays \$1.10	
	<b>Large Cities in California</b>	Anaheim	Seller pays \$1.10
Bakersfield		Seller pays \$1.10	
Fremont		Seller pays \$1.10	
Fresno		Seller pays \$1.10	
Long Beach		Seller pays \$1.10	
Los Angeles		Seller pays \$1.10	Buyer/seller split \$4.50
Oakland		Seller pays \$1.10	Buyer/seller split \$15.00
Riverside		Seller pays \$1.10	Seller pays \$1.10
Sacramento		Seller pays \$1.10	
Santa Ana		Seller pays \$1.10	
San Diego		Seller pays \$1.10	
San Francisco		(see "City Transfer Tax" column)	Seller pays \$5.00 for less than \$250,000 \$6.80 from \$250,001 to \$999,999 \$7.50 from \$1,000,000 to \$4,999,999 \$20.00 from \$5,000,000 to \$9,999,999 \$25.00 from \$10,000,000+
Stockton		Seller pays \$1.10	

**FIGURE 25:**  
**Real Estate Transfer Taxes for Various Cities Across California**

While San Jose's \$3.30 transfer tax rate is higher than some cities, it is far below what Oakland and San Francisco charge.

Source: Working Partnerships USA analysis.

#### **14. Pass a parcel tax dedicated to General Fund activities.**

A parcel tax is a flat tax on each parcel of property. Parcel taxes have become more common since Proposition 13 limited increases to property taxes based on the property's assessed value. Parcel taxes are generally considered special taxes and require a two-thirds vote to pass even if they'll be used for general purposes.<sup>119</sup> There are about 240,000 taxable parcels in San Jose.<sup>120</sup> Adopting an annual \$50 parcel tax, for example, would generate nearly \$12 million in annual revenue to the city.

One of the only ways a local community can increase property taxes, parcel taxes generate a consistent amount of revenue and are therefore easy to plan for.

But on the downside, a parcel tax is not equitable, because parcels of all sizes pay the same flat rate. Careful policymaking, though, could mitigate this problem. The City of San Jose is allowed to categorize parcels under a parcel tax, so that a small condo could pay a different rate from a major corporation with a large campus on a single large lot. The only other drawback is that parcel taxes can be difficult to pass because two-thirds of voters must approve them.

#### **15. Increase the disposal tax on solid waste.**

San Jose currently assesses a \$13-per-ton Disposal Facility Tax on landfills located in the City of San Jose. This tax generates roughly \$11 million per year. To grow that revenue, the city could increase the dollar charged per ton, make more waste products subject to the tax and/or end the exemption for some disposal activities. Each of the proposed ideas has slightly different revenue potentials, benefits and drawbacks. These reform ideas and an analysis of them were included in San Jose's 2011 Fiscal Reform Plan.<sup>121</sup>

In all cases, the broad benefit is that taxing solid waste would not have any direct negative economic impacts and in some cases it might reduce the generation of solid waste. In addition, raising the per-ton rate would be simple for the city to administer and simple for consumers to comply with. The other two options might be slightly less simple but still fairly straightforward.

Combined, the reform options could raise \$5 million total. Imposing an additional \$4.50-per-ton tax would bring in an estimated \$2 million in added revenue annually. This number would fall over time as people began disposing waste at cheaper facilities in other locations. Including waste from recycling and transfer facilities under the tax would generate \$1.5 million per year. Similarly, including the waste that's used as cover for landfills, which is currently exempt from the tax, would raise \$1.5 million annually.

119 See: Legislative Analyst's Office, A Look at Voter-Approval Requirements for Local Taxes, March 20, 2014, <http://www.lao.ca.gov/reports/2014/finance/local-taxes/voter-approval-032014.aspx>

120 See: "Property Tax Exemption Data for U.S. Cities," Governing, <http://www.governing.com/gov-data/finance/tax-exempt-property-values-totals-for-cities.html>

121 Supra note 97.

## **Strategy 4: Reform the public finance system to provide more flexibility and to support the regionalization of revenues and services.**

As we've seen, there's only so much that a local community can do to improve its fiscal situation. Many of the rules and policies that affect city revenues are controlled by the state. Complicating the situation is the fact that cities have very different — and tremendously unequal — tax receipts and service needs, particularly within the same labor and housing markets (e.g., some cities collect more in taxes but don't have to provide as many services as others because their populations are smaller). There is also no incentive for a tax-rich community to share with its neighbors, even if a neighbor provides something of value, such as housing (especially affordable housing).

This strategy argues that San Jose and Silicon Valley should be leaders in reforming the state's tax system, particularly the property and sales tax, and should promote innovations such as tax sharing or service sharing throughout the region. While many cities will likely resist any suggestion to share revenue, it might be possible to combine changes to local housing production requirements with an agreement about revenue sharing that recognizes the regional benefit of both producing housing and paying for the local services consumed by new residents.

*Note: The measures discussed in this section include a broad set of implementers that range from the City of San Jose to civic and business leaders. Implementers also include elected leaders and staff from surrounding jurisdictions as well as the state legislature.*

### **16. Make adjustments to property taxes and Proposition 13.**

This recommendation is not a new idea. Residents and political leaders from the South Bay have long led reforms to state policies, particularly Proposition 13.

Silicon Valley can and should play a leadership role again, particularly in efforts to modernize Proposition 13. The fundamental structure of the measure has not changed in nearly 40 years and has two current inequities worth addressing. First, new and growing businesses that buy property at market prices today pay substantially higher taxes than older firms that have not changed their location for many years (unless the older business made significant improvements to its property that increased its taxable value).<sup>122</sup> This puts some innovative companies at a disadvantage, particularly those that need to buy and modify land and buildings and cannot simply rent existing spaces. Second, the share of total property taxes paid by residences has increased over time compared to the share paid by businesses, because there are significantly more residential parcels; they make up about 80 percent of all parcels in California.

Proponents of equalizing the share of property tax paid by businesses have often called for a split roll, which would require that all commercial properties be reassessed to their current market value. One of the most notable pushes for this reform was a state bill introduced by California Senators Loni Hancock (D-Oakland) and Holly Mitchell (D-Los Angeles) in 2015.<sup>123</sup> A less significant change would be to institute a split rate so that commercial properties pay a higher rate than residential properties (though the rate would be based on the existing property tax assessment).

In a similar vein, lawmakers could simplify the complicated formulas that exist under AB 8, which allocates the largest portion of property tax proceeds based on tax and service levels from the mid-1970s. The urban landscape of California has changed significantly since 1975. Reforming AB 8 could distribute property tax more equitably.

<sup>122</sup> Supra note 30.

<sup>123</sup> Their bill can be found here: [http://www.leginfo.ca.gov/pub/15-16/bill/sen/sb\\_0001-0050/sca\\_5\\_bill\\_20150326\\_introduced.html](http://www.leginfo.ca.gov/pub/15-16/bill/sen/sb_0001-0050/sca_5_bill_20150326_introduced.html)

San Jose should work with other cities' leaders on pursuing reforms to Proposition 13 and ensuring that future adjustments do not cause unintended consequences. For example, a split roll could reinforce the fiscal incentive for cities to pursue commercial development at the expense of new housing. But lawmakers could mitigate this to some degree by mandating that local governments spend a portion of the increased commercial property tax revenues on affordable housing. The state could also collect a portion of the growth in the commercial property tax and redistribute it to cities' general funds according to a formula.

#### **17. Broaden and revise the state and local sales tax.**

Silicon Valley leaders could also help reform the state sales tax base. Sales tax in California is assessed only on the purchase of tangible goods bought at retail stores or dealerships (clothes, appliances, furniture, housewares, vehicles, etc.). However, consumers are spending a growing share of their money on intangible goods (streaming services for music and movies) and services (ride sharing, haircuts, etc.). California should follow the lead of other states that do apply sales taxes to services, but should take a broad look at consumer spending patterns in order to design a new sales tax that better captures economic activity.<sup>124</sup>

The benefits of such a reform are multiple. If the base of the sales tax were broadened, the tax rate on tangible goods could be reduced. Revenues would stay the same or increase, depending on the reform. Over time, aligning government revenues with the dynamism of the economy could provide a predictable and growing revenue stream for governments. Having lower taxes with a broader base would also ease tax burdens for particular groups of consumers. In short, this reform could be a win-win for governments and consumers alike.

The drawback of this approach is that, like any state reform, it would be a politically heavy lift for any city or region to carry on its own without major support statewide.

#### **18. Reform the state and/or federal gas tax.**

State and federal gas tax revenues have declined for many years due to improvements in vehicle fuel efficiency mandated by the U.S. Corporate Average Fuel Economy (CAFE) standards. While the improvement in vehicle efficiency is a victory for climate change, for air pollution and for public health, it is a loss for annual road financing across the country. For example, state and federal gas tax revenues provide almost two-thirds of San Jose's annual road maintenance funding. A decline in a major revenue source is always problematic for cities that have few substitutes for state and federal funding streams.

To the extent possible, San Jose leaders should join any effort to align road maintenance revenue with the way people use the transportation system. One such idea is to replace the existing gas tax with a vehicle-miles-traveled fee, which would be based on how much drivers use public roads. An easier idea is simply to raise the gas tax under the current system. This could be done at the state level first, since that is likely easier.

Charging more for a good that directly causes pollution is a good use of a tax. However, low-income families in places without driving alternatives pay a disproportionate share of their income on gas. Coupling a hike in the gas tax with a reduction in a different tax (such as income tax) could mitigate this regressive effect.

#### **19. Lower voter thresholds for general obligation bonds, particularly for housing.**

GO bonds, paid for by increasing property taxes to cover debt service, are one of the least expensive ways to finance capital projects because they're come with a low interest rate as bonds

124 The states of Hawaii, New Mexico and South Dakota impose a sales tax (or comparable tax, such as a general excise tax) on all services provided. See: "Understanding Sales Tax in Service Industries," BizFilings, <http://www.bizfilings.com/toolkit/sbg/tax-info/sales-taxes/sales-tax-in-service-industries.aspx>

backed by a city's property tax base are considered low risks. Today, they require a two-thirds vote to pass.

San Jose and Silicon Valley should pursue modifications at the state level to reduce the voting threshold for GO bonds, particularly for housing, just as they led such reforms in the past.

Initially, Proposition 13 made it illegal for local governments to issue GO bonds to pay for capital projects and infrastructure. This changed in 1986, when California Assemblyman Dom Cortese (D-San Jose) spearheaded Proposition 46, which restored the constitutional authority for voters to adopt GO bonds.<sup>125</sup> More recently, Silicon Valley leaders were instrumental in passing 2000's Proposition 39, which allowed school districts to approve bonds by a 55 percent margin instead of 67 percent. Proposition 39 passed with 53.4 percent of the vote, in part because proponents spent \$38.6 million on their campaign (largely from Silicon Valley CEOs and venture capitalists) while their opponents spent only \$5.9 million.

Today, although a majority of voters in many communities may approve of increased revenues for affordable and low-income housing construction, such measures usually fail to gain a two-thirds majority except in a small number of jurisdictions or in unique political circumstances. By lowering the margin for adopting new GO bonds to 50 percent or 55 percent of voters (as was done in Proposition 39), GO bonds could become more feasible throughout the state.

## **20. Pursue revenue sharing across Santa Clara County and consider tying it to housing production.**

Revenue or tax sharing has long been promoted as a way to reduce the "fiscalization of land use" and tax competition between jurisdictions and to increase fiscal equity among jurisdictions within a metropolitan area. The most prominent national tax-sharing model in the United States is in the Twin Cities metropolitan area of Minnesota. In 1971, Minnesota's state legislature established a tax-sharing program in which 40 percent of the growth of the commercial and industrial tax base of each city in the seven-county region goes into a regional pool that is then redistributed back to cities based on property values and population growth.<sup>126</sup> This method allows cities with lower property values (hence poorer tax bases) to boost their total property tax receipts by receiving a larger share of the regional property-tax pie than wealthier cities. Were it not for the tax sharing, communities with low property values might have to raise their local tax rates to capture sufficient revenue to pay for local services, which would result in inequities (because poorer people would have to pay more than wealthier people in other cities) and might further dissuade investment in the community.

Certain areas of California (such as most of Santa Clara County) function as a single labor and housing market and arguably a single retail market. In other words, people work, live and shop without respect to jurisdictional boundaries. This makes Santa Clara County an appropriate environment to test out various models for revenue sharing.

While California's tax structure does not allow local communities to adjust property tax rates as they could in Minnesota, it's still possible for them to share resources. In one option, the cities within Santa Clara County could pursue a pilot to share the commercial and industrial property tax. This tax is appropriate for revenue sharing because the broader job growth in Santa Clara County has resulted from regional amenities (such as skilled labor, access to capital, the presence of existing industry clusters, or even weather), not from the service or tax levels of a specific city.

Applying a similar approach as Minneapolis, Santa Clara County could allocate 40 percent of the growth of the commercial and industrial property tax for sharing. From 2007 to 2015, the

<sup>125</sup> Previous efforts were strongly rejected by voters, as in the example of Proposition 4 in 1980.

<sup>126</sup> See: Metropolitan Council, "Fiscal Disparities: Tax-Base Sharing in the Metro Area," <http://www.metrocouncil.org/Communities/Planning/Local-Planning-Assistance/Fiscal-Disparities.aspx>

commercial-industrial base in Santa Clara County grew from \$57.4 billion to \$79.4 billion.<sup>127</sup> Forty percent of the \$22 billion increment is \$8.8 billion, which generates \$88 million in total property tax (based on the 1 percent rate). Assuming that about 11 percent of this property tax flows to the cities (as opposed to the schools and county and other taxing jurisdictions), this would leave about \$10 million in total increment that could be shared among cities.<sup>128</sup> While this is not a significant amount of revenue, it would grow over time. For example, although the Twin Cities program also began small, by the early 2000s (40 years after the program began), the region was sharing 32 percent of the total metro commercial and industrial tax base.

The question then is how to share these revenues among the cities. Given that there is an ongoing housing crisis that stems partly from a lack of supply, and given that many cities resist developing new housing, it would make sense to base the tax-sharing allocation on housing (since job growth helps fuel the growth of the commercial tax base, and new workers need new housing).<sup>129</sup> Because some communities have large existing housing stocks, an appropriate allocation formula might reflect both a city's share of the county's total housing units and its share of new housing production over a particular time period.

It's important to note that such a revenue-sharing model would not be a major solution to San Jose's — or any city's — fiscal problems. The broader goal of revenue sharing is to take a revenue stream that grows based on regional attributes (like the commercial property tax) and connect it with communities based on something they provide of regional value (like housing). Further, since communities would still keep the local portion of the residential property tax, this revenue-sharing scheme is an additional incentive to help cover the service costs for developing new housing.

A major drawback to such a program is that it invariably creates winners and losers. For example, cities that have provided a large share of regional housing in the past may not benefit from this policy unless they continue to provide additional housing. And because it creates winners and losers, it may face strong political opposition. In a final word of caution, a complex mechanism like this takes great care and administrative support to set up and operate.

## **21. Explore opportunities to regionalize services by providing key services to neighboring jurisdictions on a contract basis.**

Some California cities are exploring ways to regionalize key services by joining forces with a neighboring jurisdiction, either a nearby city or the county. This is already common practice among fire or police services in small communities.

San Jose might consider working with its neighboring jurisdictions to deliver certain services jointly. Since San Jose is the largest jurisdiction in its area, this might look more like San Jose negotiating a contract with its neighbors to deliver a service (like road repaving or labor standards enforcement).

For San Jose, this strategy would not generate new revenue. But it could offer potential cost savings by spreading the administrative cost of delivering a particular service over more people and achieving a greater economy of scale.

<sup>127</sup> For the purposes of our analysis, commercial and industrial property included the following categories of real property: office, other industrial/nonmanufacturing, R&D industrial, specialty retail and hotels, major shopping centers, electronic and machinery manufacturing, other industrial and manufacturing, and other urban uses.

<sup>128</sup> It is also worth noting that the period from 2007 to 2015 covered the Great Recession, resulting in a smaller-than-expected pool.

<sup>129</sup> See: Legislative Analyst's Office, California's High Housing Costs: Causes and Consequences, March 17, 2015, <http://www.lao.ca.gov/reports/2015/finance/housing-costs/housing-costs.aspx>

# Methodology and Additional Data

This appendix includes additional data and charts, as well as information on some of the analytic methods used throughout this report. In particular, it details the methods and data behind SPUR's original research to benchmark revenues and expenditures across California cities. Most of this analysis focused on comparing San Jose's general revenues to those of other large urban cities in California and of neighboring cities in Santa Clara County.

## Choosing Cities to Compare to San Jose

We compare San Jose to other cities in Figures 15 through 20 of this report. This section explains the methods and data on which those figures are based.

To compare San Jose to peer cities, we began our in-depth original research by identifying the largest cities in California and the largest cities in Santa Clara County based on population in 2015. Figure 26 on the following page lists population figures for the cities in our analysis. For the largest California cities, we chose cities with populations over 300,000. These cities are often the central city of their respective county or region and face larger demands for public services than surrounding smaller communities. Even though it has fewer than 300,000 residents, we also included the City of Fremont because it's a relevant regional comparison for San Jose. The fourth-largest city in Bay Area and the 16th-largest in California, Fremont is located just north of Milpitas and the Santa Clara County border. It's a large urban peer and nearly a neighbor in Santa Clara County.

To compare San Jose to appropriate peers in Santa Clara County, we chose the 10 cities with populations over 40,000. The cities and towns not included in our comparisons are Saratoga, Monte Sereno, Los Altos, Los Altos Hills and Los Gatos.

	City	Population
California cities over 300,000 (plus Fremont)	Los Angeles	3,957,022
	San Diego	1,368,061
	San Jose	1,016,479
	San Francisco	845,602
	Fresno	520,159
	Sacramento	480,105
	Long Beach	472,779
	Oakland	410,603
	Bakersfield	369,505
	Anaheim	351,433
	Santa Ana	335,264
	Riverside	317,307
	Stockton	306,999
	Chula Vista*	257,989
	Irvine*	250,384
Fremont	226,551	
Santa Clara cities over 40,000	San Jose	1,016,479
	Sunnyvale	148,028
	Santa Clara	120,973
	Mountain View	77,914
	Milpitas	72,606
	Palo Alto	66,932
	Cupertino	59,756
	Gilroy	53,000
Campbell	41,857	
Morgan Hill	41,779	

FIGURE 26:

**Largest Cities in California and Santa Clara County**

**City populations in 2015**

San Jose is the third-largest city in the state, and the largest in the Bay Area and Santa Clara County.

\*Chula Vista and Irvine are not included in our city comparisons.

Source: State of California, Department of Finance, E-1 Population Estimates for Cities, Counties and the State with Annual Percent Change — January 1, 2014 and 2015 (May 2015), <http://www.dof.ca.gov/research/demographic/reports/estimates/e-1/view.php>

## Data and Methods for City Comparisons

Data are from city transactions reports collected by the California State Controller’s Office and range from 2003 through 2014. It is important to note that these data aren’t audited and may differ from the financial numbers prepared in each city’s comprehensive annual financial report, which provides the most accurate picture of a city’s finances. The report did not use comprehensive annual financial report data because of the lack of standardized reporting across cities.

Our analysis deflates the State Controller’s data to 2014 dollars and divides by population in each city for each year to capture deflated, per capita revenues. The report then averages over the time frame to get an annual average of deflated, per capita revenues for each city. This method accomplishes three things: it adjusts for inflation, it makes cities more comparable by adjusting for population and it smoothes out the regular variation a city might experience in revenues from year to year.

In comparing San Jose to other cities, this analysis focused mostly on general revenues. Other revenues, such as capital and enterprise revenues, are less comparable and more often support special projects than core government functioning. In other words, by looking at just general revenues, we eliminate key differences between cities, such as the presence of an airport, seaport or other large enterprise that brings in and spends a closed loop of resources that could throw off the benchmarking.

While this report compared general *revenues* extensively, we did not feel it was appropriate to do the same level of comparison for general *expenditures*. General expenditures are defined in the data sets as just those expenditures paid for by general revenues like property taxes or sales taxes. But a city might choose to raise a number of dedicated taxes to boost expenditures (such as a parcel tax for parks or street repair). This means that comparing expenditures across cities might leave out some major sources of funding for city services. Nuances in expenditure strategies and accounting simply make it more difficult to compare expenditures across cities, and for this reason we have omitted them from this report.

## Additional City Comparison Figures

Figure 17 in Chapter 4 illustrates the mix of per capita general revenues across the largest cities in California. Figure 27 below supports this by listing the share of individual revenues in each city’s general revenue portfolio. Figure 28 offers a graphical representation of the cities’ mix of general revenues, but compares San Jose to its neighboring cities in Santa Clara County. Figure 29 complements this by listing the numerical shares of revenues in every Santa Clara County city’s general revenue portfolio.

Additionally, Figure 18 in Chapter 4 compares property tax revenues across California’s largest cities. Figure 30 does the same but for cities across Santa Clara County. Similarly, sales tax revenues across Santa Clara County were illustrated in Chapter 4, and the complementary illustration for large cities in California is graphed in Figure 31.

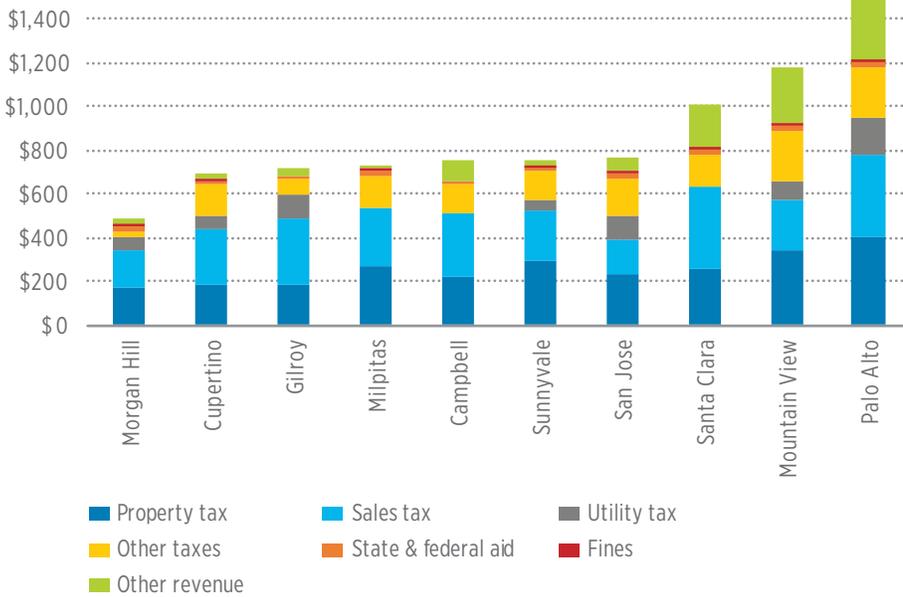
	Property tax	Sales tax	Utility tax	Other taxes	State and federal aid	Fines	Other revenue
Anaheim	24%	28%	0%	42%	3%	1%	3%
Bakersfield	36%	40%	0%	15%	6%	1%	3%
Fremont	48%	29%	0%	17%	4%	1%	2%
Fresno	42%	37%	0%	15%	5%	1%	0%
Long Beach	41%	18%	14%	18%	5%	0%	3%
Los Angeles	38%	13%	20%	25%	2%	0%	2%
Oakland	28%	10%	14%	36%	2%	7%	2%
Riverside	30%	32%	17%	11%	5%	1%	5%
Sacramento	32%	26%	16%	8%	3%	1%	14%
San Diego	42%	28%	0%	21%	3%	1%	5%
San Francisco	45%	7%	4%	34%	4%	1%	7%
San Jose	30%	22%	14%	22%	2%	2%	8%
Santa Ana	33%	26%	17%	15%	3%	2%	3%
Stockton	26%	29%	19%	13%	8%	1%	4%

**FIGURE 27:**  
**General Revenue Portfolios of California's Largest Cities**

Percent of total general tax revenue by source, based on per capita annual average over 2003–2014, in 2014 dollars

While most cities across California depend mainly on property and sales taxes, the degree to which they rely on these and other taxes varies considerably.

Source: SPUR analysis of California State Controller’s Office, Cities Raw Data for Fiscal Years 2003–2014, <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>



**FIGURE 28:**  
**How Do General Revenue Portfolios Compare Across Cities in Santa Clara County?**

Annual average per capita general revenue (2003-2014), in 2014 dollars

San Jose's combined per capita property and sales tax revenues are the smallest of all the cities in Santa Clara County.

Source: SPUR analysis of California State Controller's Office, Cities Raw Data for Fiscal Years 2003-2014, <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>

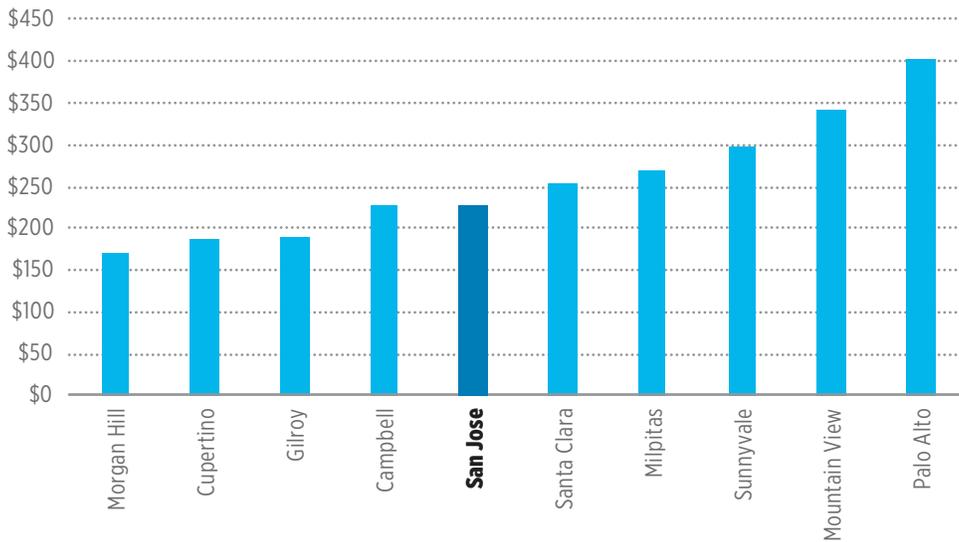
	Property Tax	Sales Tax	Utility Tax	Other Taxes	State and Federal Aid	Fines	Other Revenue
Campbell	30%	38%	0%	17%	2%	0%	12%
Cupertino	27%	37%	9%	21%	3%	1%	4%
Gilroy	27%	43%	14%	10%	3%	0%	4%
Milpitas	37%	37%	0%	20%	3%	1%	2%
Morgan Hill	35%	36%	11%	7%	4%	0%	7%
Mountain View	29%	20%	7%	20%	2%	1%	22%
Palo Alto	26%	25%	11%	15%	1%	0%	21%
San Jose	30%	22%	14%	22%	2%	2%	8%
Santa Clara	25%	37%	0%	15%	2%	1%	20%
Sunnyvale	40%	29%	7%	17%	3%	0%	4%

**FIGURE 29:**  
**General Revenue Portfolios of Santa Clara County's Largest Cities**

Percent of total general tax revenue by source, based on per capita annual average over 2003-2014, in 2014 dollars

While cities across Santa Clara County depend mainly on property and sales taxes, the degree to which they rely on these and other taxes varies.

Source: SPUR analysis of California State Controller's Office, Cities Raw Data for Fiscal Years 2003-2014, <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>

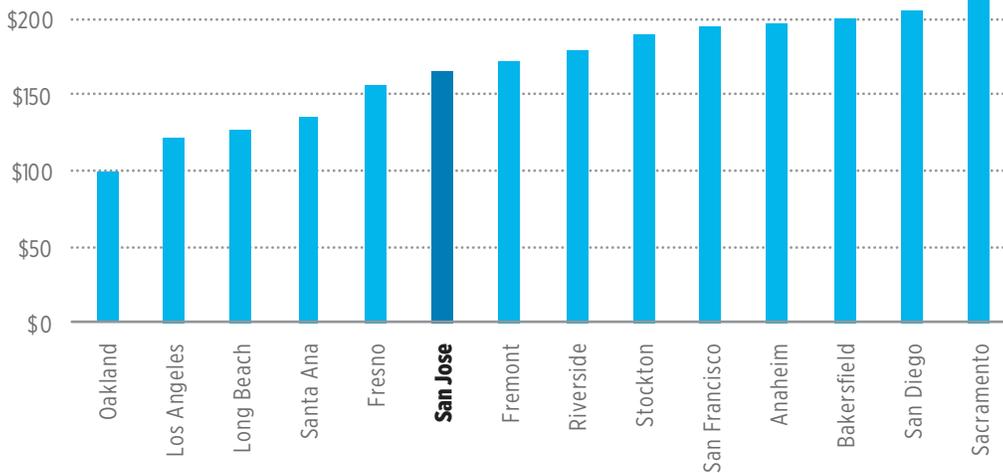


**FIGURE 30:**  
**San Jose Is Below Average in Property Tax Revenue in Santa Clara County**

Annual average per capita property tax revenue (2003-2014), in 2014 dollars

San Jose ranks sixth of nine in per capita property tax revenue among cities in Santa Clara County, another indication of its relatively low property tax base.

Source: SPUR analysis of California State Controller's Office, Cities Raw Data for Fiscal Years 2003-2014, <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>



**FIGURE 31:**  
**San Jose Is Below Average in Sales Tax Revenue Among Large Urban Peers**

Annual average per capita sales tax revenue (2003-2014), in 2014 dollars

San Jose ranks ninth out of 14 in per capita sales tax revenue among its large-city peers.

Source: SPUR analysis of California State Controller's Office, Cities Raw Data for Fiscal Years 2003-2014, <https://bythenumbers.sco.ca.gov/browse?category=Raw+Data&utf8=%E2%9C%93>

### Supporting Figure for Chapter 3

Chapter 3 discusses some of the revenue measures San Jose has pursued in recent years. Figure 32 lists key revenue measures in San Jose and Santa Clara County since 1995.

Year	Jurisdiction	Tax Measure	Votes
1995	City of San Jose	Library Benefit Assessment District: City Council established a 10-year citywide benefit assessment district for library services	Council vote: 11-0
1996	City of San Jose	Measure AA: Measure AA proposed the continuation of three existing taxes, known as the "New Realities Taxes": a 3% increase in, and future indexing of, the business license tax, an expansion of the 5% utility tax to include out-of-state calls, and an alternative business tax on fuel tank farms	Failed majority approval (Yes: 42.6%, No: 57.4%)
2000	Santa Clara County	Measure A: Half-cent sales tax increase for transportation projects, including BART	Passed 2/3 approval (Yes: 70.6%, No: 29.4%)
2004	City of San Jose	Measure S: A parcel tax to replace the city's expiring annual library assessment	Passed 2/3 approval (Yes: 67.2%, No: 32.8%)
2006	Santa Clara County	Measure A: Half-cent sales tax increase for general county purposes such as transportation improvements and health services	Failed majority approval (Yes: 42.9%, No: 57.1%)
2008	Santa Clara County	Measure B: One-eighth of a cent sales tax measure for BART operations	Passed 2/3 approval (Yes: 66.8%, No: 33.2%)
2008	City of San Jose	Measure K: A 10% reduction in the 911 fee, from \$1.75 per telephone line to \$1.57, coupled with an expansion to more telephone technologies, to support essential city services such.	Passed majority approval (Yes: 77.7%, No: 22.3%)
2008	City of San Jose	Measure J: Reduced the telecommunications users tax from 5% to 4.5% and made the tax apply equally regardless of the technology used	Passed majority approval (Yes: 79.6%, No: 20.5%)
2008	City of Campbell	Measure O: Quarter-cent sales tax to maintain city services and facilities	Passed majority approval (Yes: 70.5%, No: 29.5%)
2010	Santa Clara County	Measure A: \$29-per-year parcel tax to fund health insurance premiums to continue providing health care for otherwise uninsured, low-income children of working families	Failed 2/3 approval (Yes: 58.7%, No: 41.2%)
2010	City of San Jose	Measure K: Increased the card room tax on gross revenues from 13% to 15% and revised the municipal code to expand the number of tables allowed per card room	Passed majority approval (Yes: 76%, No: 24%)
2010	City of San Jose	Measure U: 10% gross receipts tax on marijuana businesses in San Jose to fund essential city services	Passed majority approval (Yes: 78.3%, No: 21.7%)
2012	Santa Clara County	Measure A: One-eighth of a cent sales tax for general county purposes such as public safety, health services and insurance, student programs and job creation	Passed majority approval (Yes: 56.6%, No: 43.4%)
2012	Santa Clara Valley Water District	Measure B: Renewed an existing special parcel tax	Passed 2/3 approval (Yes: 73.7%, No: 26.3%)
2013	Santa Clara County	Measure A: Continuation of tax rates levied by the Santa Clara County Library District Joint Powers Authority to maintain book collections, children's reading programs, library hours and staff, and bookmobile services	Passed 2/3 approval (Yes: 81.4%, No: 18.6%)
2014	Santa Clara County Open Space Authority	Measure Q: \$24-per-year special parcel tax to fund open space services and improvements	Passed 2/3 approval (Yes: 68%, No: 32%)
2014	City of San Jose	Measure B: Continuation of existing library parcel tax	Passed 2/3 approval (Yes: 81.5%, No: 18.5%)

FIGURE 32:

### Key Local Tax Measures in San Jose and Santa Clara County

While San Jose has raised some local taxes, it has not been as assertive as Santa Clara County in pursuing increases in local taxes.

Source: SPUR and Working Partnership USA analysis of Voter's Edge California, [www.votersedge.org/ca/page/smartvoter](http://www.votersedge.org/ca/page/smartvoter)