

Capitola City Council

Agenda Report



Meeting: November 13, 2025

From: City Manager Department

Subject: Annexation Feasibility Study Analysis Report

Recommended Action: Receive a presentation from RSG, Inc. on the results of the annexation feasibility study and authorize the City Manager to submit the analysis to the Santa Cruz Local Agency Formation Commission for analysis and revision of the City's sphere of influence.

Background: The City of Capitola's current sphere of influence (SOI), as defined by the Santa Cruz Local Agency Formation Commission (LAFCO), includes approximately 2,200 parcels totaling 622 acres located outside the existing city limits. For reference, the City of Capitola's incorporated area includes about 4,489 parcels and approximately 1,600 acres (two square miles).

In 2022, LAFCO completed a service and sphere review for the City, reaffirming Capitola's existing SOI and recommending the City develop a plan to assess the potential future annexation of these parcels. LAFCO also set a May 2027 deadline for the City to submit this analysis.

As part of the Fiscal Year 2024–25 Goals and Priorities, and in alignment with LAFCO's recommendation, the City Council identified the need to evaluate the fiscal, operational, and service impacts of potentially annexing portions of unincorporated Santa Cruz County into the City. This evaluation is intended to help determine if, when, and how annexation could occur.

To fund the study, the City Council allocated \$30,000 in the FY 2024–25 budget. LAFCO provided an additional \$15,000; the total project budget was \$45,000.

Discussion: On August 14, 2024, City staff issued a Request for Proposals (RFP) for consultant services to perform an annexation feasibility study. The City received two proposals, both from highly qualified firms but each initially exceeding the City's available budget. Staff worked with both firms to refine their scopes of work and reduce costs.

Following evaluation of the amended proposals and consultation with LAFCO staff, the City selected RSG, Inc. based on their detailed understanding of the project scope and LAFCO processes and strong experience with similar annexation feasibility studies.

On September 26, 2024, the City Council authorized a contract with RSG, Inc. The agreement's scope of work included data collection and stakeholder interviews and analysis of fiscal, service, and other impacts of possible annexation. Due to the size of the City's current SOI, City staff and RSG spent time and consideration on how to effectively study the area, ultimately determining to split the SOI into two sections: the North (around Capitola Mall and the 'keyhole' area, and including Opal Cliffs) and the South (Pleasure Point). A map indicating these two areas is included as Attachment 1. The study is therefore divided into three possibilities: the annexation of the North, the South, or both areas.

RSG, Inc. gathered data from City and Santa Cruz County staff to analyze the financial impacts of potential annexation. One important revenue source challenging to research due to confidentiality requirements was the Transient Occupancy Tax (TOT) revenue within the County. Staff ultimately relied on the number of short-term rentals in the SOI, and their exact locations, and evaluated them against comparable short-term rentals within the City of Capitola's to estimate revenue.

At the November 13 meeting, RSG staff will provide a presentation summarizing their findings and recommendations regarding the feasibility, potential impacts, and strategic considerations of annexation.

Because current analysis does not point to annexation being financially feasible or advantageous, City staff asked that RSG pause their work to present their initial findings before conducting time-consuming

interviews with City Departments to begin estimating projected new City costs, though this was initially part of their scope of work.

Staff suggest the study be submitted to LAFCO and the City's sphere of influence be adjusted by LAFCO. Before approving a revised Capitola SOI, the LAFCO Board will receive options from LAFCO staff, who have offered to partner with Capitola City staff on this endeavor. The City of Capitola's LAFCO representative will also have the opportunity to make comments and vote on the revised SOI before it is approved.

Fiscal Impact: None.

Attachments:

1. Study Area Map
2. RSG Preliminary Findings Presentation

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