**TOWN OF LOS GATOS**

**COUNCIL AGENDA REPORT**

MEETING DATE: 08/02/2022

ITEM NO: 18

DATE: July 29, 2022

TO: Mayor and Town Council

FROM: Laurel Prevetti, Town Manager

SUBJECT: Adopt a Resolution of the Council of the Town of Los Gatos for Model 3, Calling a Municipal Election for November 8, 2022, Requesting that the County Consolidate the Municipal Election with the General Election on November 8, 2022, and Submitting to the Qualified Electors of the Town at the November 8, 2022 Consolidated General Election a Measure to Amend Chapter 14 of the Los Gatos Town Code Relating to Business License Taxes

RECOMMENDATION:

Adopt a Resolution of the Council of the Town of Los Gatos for Model 3, calling a municipal election for November 8, 2022, requesting that the County consolidate the municipal election with the general election on November 8, 2022, and submitting to the qualified electors of the Town at the November 8, 2022 consolidated general election a measure to amend Chapter 14 – Licenses and Miscellaneous Business Regulations (Chapter 14) of the Los Gatos Town Code relating to business license taxes.

BACKGROUND:

On September 13, 2021, the Town Finance Commission reviewed the Town's Business License Tax Program and recommended that the Town Council authorize the Town Manager to issue a Request for Proposal (RFP) for consultant services to evaluate and recommend modernization options for the Town's Business License Tax Program. The Business License Tax supports all municipal services that are enjoyed by the businesses, including but not limited to streets, other infrastructure, and public safety.

On October 19, 2021, the Town Council received the Finance Commission recommendation and directed staff to engage a consultant to review the Town's 1991 Business Tax Ordinance and recommend options for modernizing the Ordinance.

PREPARED BY: Arn Andrews, Assistant Town Manager; Holly Young, Town Manager Administrative Analyst

Reviewed by: Town Manager, Town Attorney, and Interim Finance Director

BACKGROUND (continued):

On December 17, 2021, the Town issued an RFP for Business License Tax consulting services. Hinderliter, deLlamas & Associates (HdL) Companies was selected given their significant experience in business license review and analysis, including having performed dozens of tax study and modernization programs in California.

HdL submitted their Business License Analysis and Ordinance Review (Report) to the Town on June 8, 2022.

On June 13, 2022, the Finance Commission discussed the HdL Report and voted unanimously to move forward to continue research and public outreach on business license tax modernization.

On June 21, 2022, the Town Council unanimously directed staff to continue conducting research and public outreach and prepare options for proposed ballot measure language for Council consideration on August 2, 2022.

DISCUSSION:

Per Council direction, staff has been coordinating extensive business outreach and working with HdL to refine potential business license modernization models. Following are summaries of both efforts:

*Business Outreach*

The Town set up a dedicated webpage at www.LosGatosCA.gov/BLModernization with information regarding the current business license tax program, background on modernizing the tax, discussions to date, the options being considered, and the timeline for a ballot measure. The Town also set up a unique email address of BLModernization@losgatosca.gov for public comment and received several communications on this topic from a variety of businesses (see Attachment 1).

The Town hosted a community workshop on July 25, 2022 at 7:00 p.m. via teleconference. The Town publicized the potential business license modernization ballot measure and the July 25 informational workshop via the Town website homepage, weekly Newsletter, multiple posts on the Town's official social media accounts (Nextdoor, Facebook, Instagram, Twitter, and LinkedIn), and a postcard mailing. The postcard went out to every business the Town has on file and was mailed to a total of 5,167 valid business addresses with receipt occurring between July 15 and 21.

The community meeting provided an opportunity for Town residents and businesses to learn more about the potential business license modernization, discuss each of the proposed options

DISCUSSION (continued):

under consideration, ask questions, and provide feedback. The materials from the webinar are available at www.LosGatosCA.gov/BLModernization. Though lightly attended, the community answered a series of Zoom poll questions following the initial staff presentation:

- 75% felt the Town should update the business license tax.
- 100% felt the Town business license program should be equitable.
- 100% preferred the proposed Model 3.

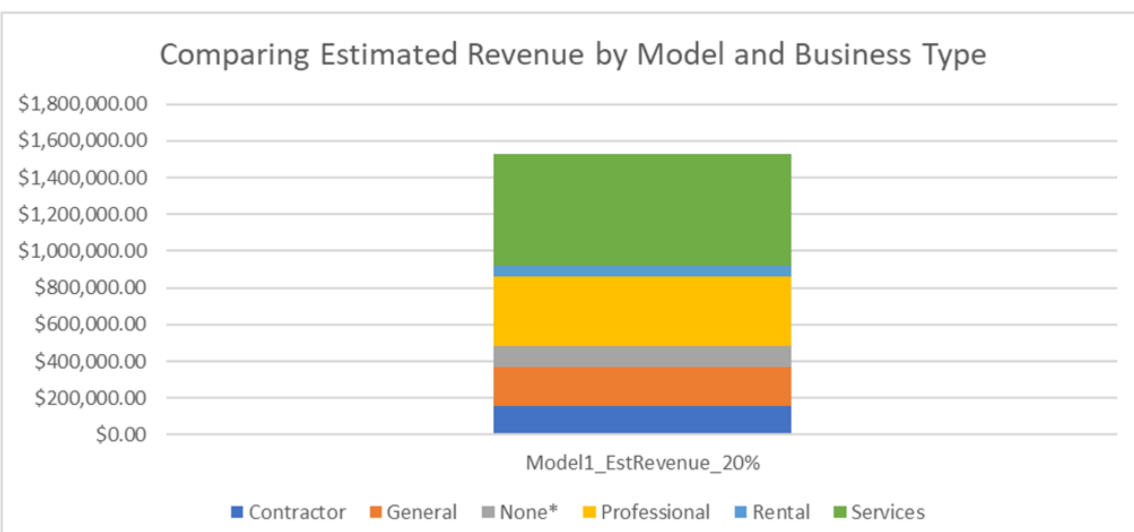
After further discussion and a question and answer session, the poll was launched again with an additional participant and the following results:

- 60% felt the Town should update the business license tax.
- 100% felt the Town business license program should be equitable.
- 20% preferred the proposed Model 1 and 80% preferred the proposed Model 3.

In addition to the community meeting and other outreach efforts, staff sent emails directly to the five largest businesses discussed within Model 3 and also had separate discussions with community stakeholders including the Los Gatos Chamber of Commerce and Netflix.

*Analysis of Potential Models*

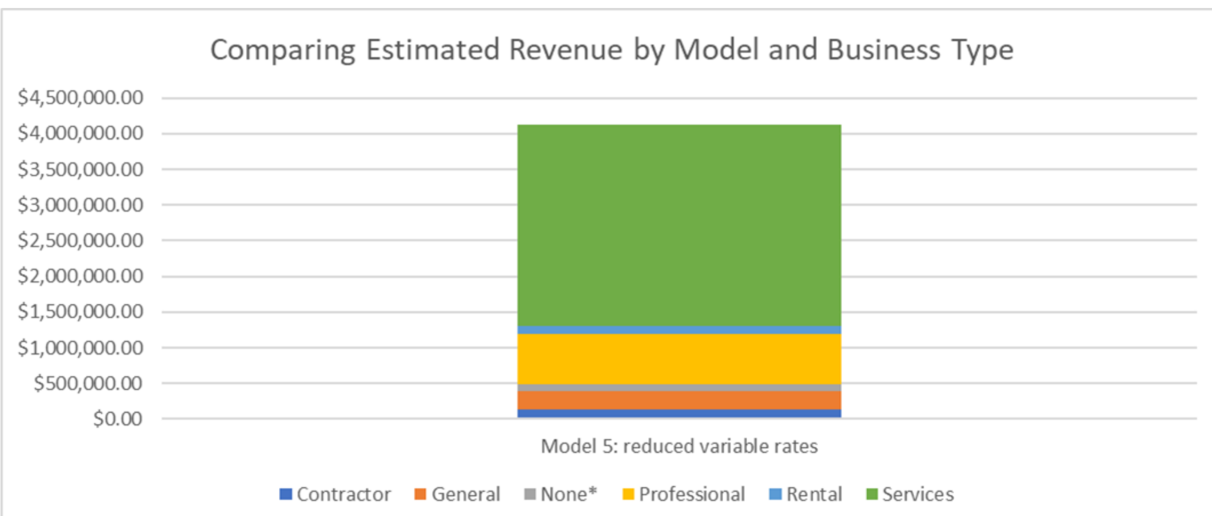
***Model 1*** – Would retain the existing structure while modifying the tax amounts for each category by 20%. The drawback of Model 1 is that the tax remains regressive. In fact, because it would increase the flat fees, it becomes more regressive. In addition, since 1991, inflation has risen approximately 117% or five times as much as the recommended increase. The advantage of this model is that the increases for each business type are minimal. This Model would increase revenues approximately $255,000 annually primarily from the Services category ($101,000).



DISCUSSION (continued):

***Model 2*** – Introduces the concept of converting the Town tax to a gross-receipts model for all businesses. This means that every business would pay based on their gross receipts, utilizing different single rates for five different business classifications. This Model also lowered the annual base rate to a uniform $25 flat rate for the first $25,000 to provide some additional tax relief for smaller businesses. This model affords the most flexibility for increasing revenues while accommodating certain business categories with differing rates. This Model would increase revenues approximately $2,861,000 annually primarily from the Services category ($2,321,000).

| Categories | Base Rate | Gross Receipts Tax Rate |
|---|---|---|
| General Commerce/Retail | $25 Flat Rate per Business (first $25,000 in Gross) | 0.0005 X Gross |
| Services | | 0.001 X Gross |
| Contractor | | 0.001 X Gross |
| Professional | | 0.002 X Gross |
| Rental Commercial/Residential | | 0.002 X Gross |

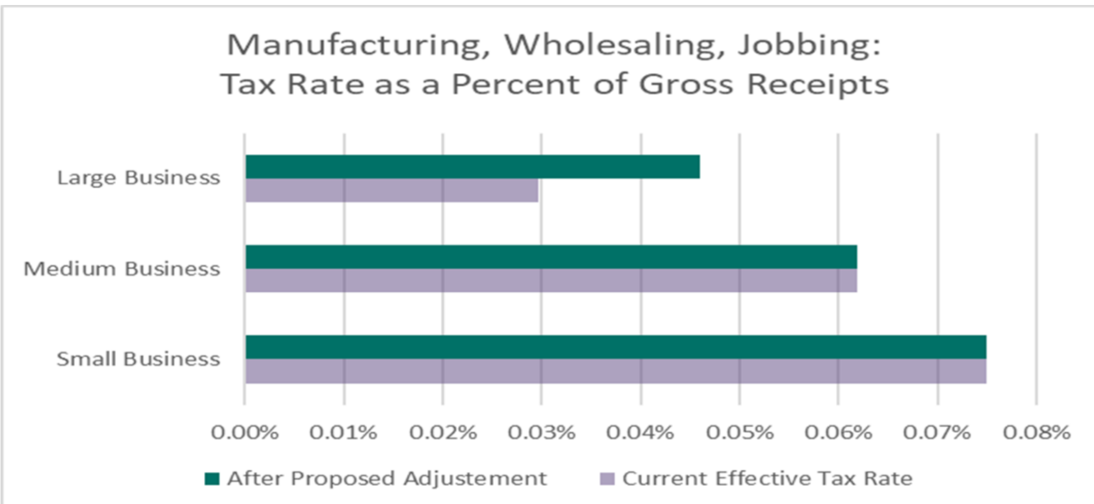



***Model 3*** - Maintains the existing gross-receipts structure for Manufacturing, Wholesaling, and Jobbing except for updating the rate of $75.00 for each $550,000 more than $12,000,000 to $300 for each $550,000 more than $12,000,000. For purposes of this schedule, Manufacturing refers to any manufacturing or processing of goods, wares, merchandise, articles, or commodities. Wholesaling refers to the sale of goods, wares, or merchandise for the purpose of resale. Jobbing is the business of selling goods, wares, or merchandise to wholesale

DISCUSSION (continued):

merchants for resale at wholesale. This model also includes the E-commerce category which includes commercial transactions conducted electronically on the internet.

This model would have the least change to the existing structure, only impacting businesses with gross receipts above $12,000,000, while helping to offset some of the inequities associated with the lower effective tax rates of larger businesses presented earlier. This Model would increase revenues approximately $1,100,000 annually.




*Finance Commission Alternative Model*

On July 28, 2022, the Finance Commission held a Special Meeting to discuss the results of community outreach and business feedback and the three models under consideration. At the conclusion of their discussion, the three resident Commission members present voted to provide the Town Council with an alternative Model. The proposed Model is an enhanced version of Model 1. The Commission Model would increase all flat fees and the gross receipts tax schedules for E-Commerce, Manufacturing, Wholesaling, and Jobbing and Retailing 100% to account for inflation. In addition, the Commission expanded the Retailing gross receipts table to include two additional payment levels above the current $2,000,000 (and above) threshold. The following table illustrates the additional payment levels.

DISCUSSION (continued):

| At Least | But Less Than | Tax |
|---|---|---|
| $1,900,000 | $4,000,000 | $1,950 |
| $4,000,000 | $8,000,000 | $3,900 |
| $8,000,000 | $16,000,000 (and above) | $7,800 |

Like Model 1, the drawback of this Model is that the tax remains regressive. This model would make up most of the inflation since 1991. This Model would increase revenues approximately $1,600,000.

*Ballot Initiative Process*

A ballot measure to modernize the Business License Tax requires a 4/5 vote of the Town Council to place it on the ballot. A General Tax can be expended on any program, service, or capital need at the discretion of the local government's governing body. A simple majority vote (50 percent of voters plus one additional voter) is required for approval of a general tax.

A resolution with corresponding ballot language and its draft ordinance have been prepared for each of the three models. For Model 1, see Attachment 2; for Model 2, see Attachment 3; and for Model 3, see Attachment 4. If the Council decides to move forward with one of the models, then the Council should adopt the resolution it would like, which would submit the Council's ballot measure to voters at the November 8, 2022 regular municipal election. Provided below is the ballot language for the three models.

**Model 1**

| | |
|---|---|
| Shall the measure to fund critical Town needs such as public safety by imposing a 20% increase to all flat fees and the gross receipts tax schedules for E-Commerce, Manufacturing, Wholesaling, and Jobbing and Retailing , raising about $255,000 yearly for general fund purposes until ended by voters, and which have not been increased since 1991, be adopted? | YES<br>NO |

DISCUSSION (continued):

**Model 2**

| | |
|---|---|
| Shall the measure to fund critical Town needs such as public safety by incorporating gross receipts reporting for all businesses at rates between \$0.50 and \$2.00 per \$1,000 after a \$25.00 flat fee for the first \$25,000 in gross receipts, replacing the existing regressive taxing system of flat fees and gross receipts, raising \$2.3 million yearly for general fund purposes until ended by voters, and increasing equity among small, medium and larger businesses, be adopted? | YES<br>NO |

**Model 3**

| | |
|---|---|
| Shall the measure to fund critical Town needs such as public safety by amending the gross receipts tax schedule for E-Commerce, Manufacturing, Wholesaling, and Jobbing for businesses with gross receipts above \$12,000,000 from \$75 per each \$550,000 in excess of \$12.0 million to \$300 per each \$550,000 in excess of \$12.0 million, raising about \$1.0 million yearly for general fund purposes until ended by voters, and increasing equity , be adopted? | YES<br>NO |

Should the Town Council choose to pursue a ballot measure, final approval including the ballot measure language will need to be submitted to the Santa Clara County Registrar of Voters by August 12, 2022. Provided below are ballot measure milestone dates:

- August 12, 2022: Last day for Resolutions calling a measure
- August 12, 2022: Deadline for submitting primary arguments in favor of or against a measure
- August 17, 2022: Last day to amend or withdraw a measure
- August 19, 2022: Town Attorney submits impartial analysis to the Town Clerk
- August 19, 2022: Deadline for submitting rebuttal arguments to primary arguments in favor of and against a measure.

The proposed resolutions authorize the Mayor, or his designee(s), to prepare a written argument in favor of the proposed measure on behalf of the Town Council. At the Mayor's discretion, the Argument may also be signed by bona fide associations or by individual voters eligible to vote in Los Gatos.

CONCLUSION:

Based on business and community feedback to date staff recommends that the Town Council adopt the resolution for Model 3 and call a municipal election for November 8, 2022, requesting that the County consolidate the municipal election with the general election on November 8, 2022 and submitting to the qualified electors of the Town at the November 8, 2022 consolidated general election a measure to amend Chapter 14 of the Los Gatos Town Code.

COORDINATION:

This staff report was coordinated with the Town Manager, Town Attorney, and Finance Director.

FISCAL IMPACT:

If approved by voters in November, the estimated additional revenue generated by the three models is between approximately $255,000 and $2,800,000 annually. These funds would be locally generated and therefore be safe from seizure by the State. In addition, they would enable the Town to invest in services and infrastructure that the community values. The cost of the ballot measure is approximately $59,000 and incorporated in the FY 2022/23 adopted budget.

ENVIRONMENTAL ASSESSMENT:

In accordance with CEQA Guidelines Section 15378(b)(4), placement of a ballot measure on the ballot to amend the Town's business license tax is not a project subject to CEQA, because it is a government fiscal activity.

Attachments:
1. Public Comment
2. Model 1 Resolution with corresponding Ordinance as Attachment A
3. Model 2 Resolution with corresponding Ordinance as Attachment A
4. Model 3 Resolution with corresponding Ordinance as Attachment A