



Taxpayers watchdog since 1945

1855 First Avenue #201, San Diego, CA 92101 • (619) 234-6423 • info@sdcta.org • www.sdcta.org

22 May 2017

The Honorable Kevin L. Faulconer
Mayor
City of San Diego
202 C Street
San Diego, CA 92101

Dear Mayor Faulconer:

Please find enclosed the San Diego County Taxpayers Association's (SDCTA) recommendations for a potential transient occupancy tax increase ballot proposal to fund the expansion of the Convention Center, homeless services, and street repairs. SDCTA also states that these conditions are necessary, but may not be sufficient for any future support; other principles may need iteration as the proposal develops.

We look forward to working closely with your office and the City Council in the proposal's further development.

Yours respectfully,

A handwritten signature in black ink, appearing to be "Haney Hong", written in a cursive style.

Haney Hong
President and CEO

CC:

Council President Myrtle Cole
Council President Pro Tem Mark Kersey
Councilmember Barbara Bry
Councilmember Laurie Zapf
Councilmember Chris Ward
Councilmember Chris Cate
Councilmember Scott Sherman
Councilmember David Alvarez
Councilmember Georgette Gómez
Independent Budget Analyst Andrea Tevlin

Transient Occupancy Tax Increase for the Expansion of the San Diego Convention Center, Homeless Services, and Street Repairs Policy Recommendations

May 2017

Executive Summary

The San Diego County Taxpayers Association has historically supported the expansion of the San Diego Convention Center, as the facility is a driver of economic activity in the region. As such, the Association is not automatically against a funding mechanism for that expansion so long as there are protections to the taxpayers and that taxpayers earn more on the investment than spent. Because the proposal will also contain elements to fund efforts to fight homelessness and to fund infrastructure, there are serious questions of oversight and effectiveness that need to be addressed. The Association's mission is to uphold the notion that any request by city officials for more taxpayer dollars contains measures for accountability, transparency, and the most effective methods of addressing an issue. With these considerations in mind, SDCTA states the following principles are important and be taken into account as the proposal is developed. SDCTA also states that these conditions are necessary, but may not be sufficient for any future support; other principles may need iteration as the proposal develops.

- 1. Ensure Performance Audits and Oversight**
- 2. Require Cross-Governmental Coordination of Homeless Services**
- 3. Create Protections for Taxpayers in the Case of Economic Recession**
- 4. Prevent Waste in the Case of Larger Economic Growth than Anticipated**
- 5. Share Investment Costs with the Port of San Diego**
- 6. Include Language in the Initiative Requiring Legal Rights to Land**

Additionally, SDCTA recognizes that in order to potentially share costs, the City would need to engage in dialogue with the Port of San Diego. The Port of San Diego is in a complicated legal position with respect to their obligations to Fifth Avenue Landing, LLC, (FAL) on the exercise of "good faith" on FAL's hotel option, which FAL is legally allowed to propose. The City of San Diego defaulted on its payment for the leasehold interest on the land where the Convention Center expansion would be built, and as such, no longer has legal rights with respect to that land. The Port of San Diego, if it engages with the City of San Diego on use of land to which it has no rights, risks creating legal exposure for itself without a release from FAL. Therefore, the mayor needs to exercise leadership and persuade FAL to release the Port of San Diego of potential damages with respect to "good faith."

Discussion

On April 5, 2017, the Office of Mayor Kevin Faulconer presented his proposed ballot measure to increase the transient occupancy tax (TOT) to the City Council's Rules Committee. The measure, which has not yet been fully drafted, would be presented to the City Council in June and subject to a public vote in a special November 2017 election. The proposal seeks to raise revenue to fund a Phase III of the San Diego Convention Center Expansion, homeless services, and street repairs.

The measure would increase the TOT in the City of San Diego by up to one, two, or three percent based on the location of the lodging business in question. Lodging businesses located in Tax Boundary 1, which would be a citywide boundary, would be subject to a 1% TOT increase. Lodging businesses located in Tax Boundary 2—those north of Highway 54 and south of Highway 56—would be subject to an additional 1% TOT increase for a total of 2%. Finally, lodging businesses in Tax Boundary 3—located in the downtown area—would be subject to an additional 1% TOT increase from Boundary 2 for a total of 3%. These TOT increases would remain in place for up to 40 years after the issuance of revenue-backed bonds to finance the construction, maintenance, and operation of the contiguous expansion of the Convention Center.

Revenue raised from the TOT would be deposited into three separate funds with the individual purposes of financing the expansion, homeless services, or street repairs. Ballot language would avoid defining specific methods of repairing roads or aiding the homeless in order to account for potential changes in circumstance, technology, and research regarding the most effective approaches to address these issues.

If approved by voters, TOT increases would take effect in the second half of Fiscal Year 2018 and short-term notes would be issued in Fiscal Year 2019. Long-term bonds would be issued against these revenues in Fiscal Year 2020, with estimated 44-month construction for the Convention Center Expansion to begin in July 2019.

Historically, except in extraordinary circumstances, SDCTA has opposed special elections on the basis that they create an unnecessary added cost to taxpayers. The Mayor's proposal argues that the cost of delaying until 2018 would be greater than the \$5 million special election cost due to rapid increases in the cost of construction, a claim which SDCTA has not yet validated.

SDCTA supported the expansion of the Convention Center in 2012, on the condition that the financing mechanism was found legal, as anticipated additional TOT revenues generated were expected to cover the cost of the project as well as provide surplus revenue. As this proposal has not been fully drafted and involves the financing of other city assets and services, there are certain other considerations that must be made regarding the spending of these taxpayer funds.

With these considerations in mind, SDCTA states the following principles are important and should be taken into account as the proposal is developed. SDCTA also states that these conditions are necessary, but may not be sufficient for any future support; other principles may need iteration as the proposal develops.

1. Ensure Performance Audits and Oversight

The proposal's performance should be consistently monitored by City staff including the City Audit Committee and the Independent Budget Analyst. It is vital that the use of new revenues on the Convention Center Expansion in particular does not negatively affect service levels in other areas. The proposal should also require independent oversight of the three created funds, including annual audits to account for the value and effectiveness of funds spent.

2. Require Cross-Governmental Coordination of Homeless Services

Funds collected for addressing homelessness should be used in coordination with regional efforts to promote evidence-based practices and maximize the effectiveness of each tax dollar. Services provided without coordination with the County Health & Human Services Agency, for example, could be limited in effectiveness, as they would not leverage cross-governmental resources, policies, and funding and lack coordination. These funds should also be used, when appropriate, in coordination and partnership with private organizations seeking to address homelessness.

3. Create Protections for Taxpayers in the Case of Economic Recession

The proposal intends to create a stability reserve, but should also include other protections for city funds in the case of an unexpected economic downturn. This could involve, for example, implementing a limit on the City's contribution to the Convention Center expansion. In 2012, SDCTA stated that the City could cap its annual contribution at the amount of the estimated increase in TOT revenue from the proposal and require that the Tourism Marketing District cover all costs in excess of that amount.

4. Prevent Waste in the Case of Larger Economic Growth than Anticipated

With adequate stability reserves and protections from economic recession there ought also to be protections in the event economic growth occurs faster than anticipated. Excess revenue beyond the building of stability reserves and debt service should be placed into escrow so that earlier debt payments can be made and so taxpayers' interest liability can be lowered. The financial instruments that credit against this revenue should allow for earlier payoffs.

5. Share Investment Costs with the Port of San Diego

The San Diego Unified Port District (Port of San Diego) commissioned several studies regarding the original Phase III Convention Center Expansion proposal in 2012, each of which found that the Port of San Diego stood to gain anywhere from \$3 million to \$6.2 million in new annual revenue from the completion of the project. As such, the Port of San Diego agreed to contribute \$3 million annually for 20 years to fund the expansion. SDCTA believes that given the substantial economic benefit the project stands to provide the Port of San Diego, the District should again share in the investment costs for the new proposal.

Additionally, SDCTA recognizes that in order to potentially share costs, the City would need to engage in dialogue with the Port of San Diego. The Port of San Diego is in a complicated legal position with respect to their obligations to Fifth Avenue Landing, LLC, (FAL) on the exercise of “good faith” on FAL’s hotel option, which FAL is legally allowed to propose. The City of San Diego defaulted on its payment for the leasehold interest on the land where the Convention Center expansion would be built, and as such, no longer has legal rights with respect to that land. The Port of San Diego, if it engages with the City of San Diego on use of land to which it has no rights, risks creating legal exposure for itself without a release from FAL. Therefore, the mayor needs to exercise leadership and persuade FAL to release the Port of San Diego of potential damages with respect to “good faith.”

6. Include Language in the Initiative Requiring Legal Rights to Land

Given the above consideration, SDCTA believes that the Mayor’s final initiative must include language that ensures no new tax dollars will be collected as a result of the initiative until and unless the City has legal rights to the land necessary for the Convention Center Expansion.