



Proposition J: Del Mar TOT for Short-Term Rentals

March 2010

Board Recommendation:

OPPOSE

Rationale:

The City of Del Mar has not made adequate steps to reduce expenditures before pursuing a revenue enhancement proposal. Instead of making cuts and pursuing reform, the City is moving forward with a proposal to extend the current transient occupancy tax (TOT) rate to short-term renters.

The City argues that it will need this additional revenue as there is a similar pressure placed on city services by users of short-term rentals as those of hotel users. Although there is an increased pressure placed on city services by usage of short-term rentals, the City should pursue a regulatory mechanism to deal with this.

Consistent with our rationale in 2008, SDCTA opposed a measure that allowed the City of Encinitas to charge short-term rental users a TOT rate for the following reason:

“This is poor public policy that penalizes those property owners that have law-abiding tenants. It is also uncertain that the tax increase will address the problem the City is attempting to address. The City Council currently has the ability to adopt fines and levies, and should utilize their legislative authority to adopt ordinances, which would better address the problem.”

Background

Pursuant to Article XIII (c) of the California Constitution, local governments are only able to impose, extend, and increase general or special taxes by a vote of the people. General taxes are those that are imposed for general governmental purposes. These “general” taxes require a simple majority vote. Special taxes, however, are those that are imposed for specific purposes, even if they are directed into the General Fund. These taxes require a 2/3 majority vote.

Cities throughout the State charge visitors a surcharge on their stay, which is known as transient occupancy taxes (TOT). Some cities limit these charges to hotel visitors, while others include short-term renters, such as users of vacation rentals. The City of Del Mar’s TOT is considered a general tax as the funds go directly into the General Fund without a specified purpose.

The City of Del Mar’s Municipal Code (Chapter 3.12) allows the City the ability to increase the Transient Occupancy Tax up to a maximum of 13%.

“For the privilege of occupancy in any hotel, each transient shall pay a tax in an amount up to thirteen percent (13%) of the rent charged by the operator. The exact rate shall be as set by resolution of the City Council. The transient satisfies this tax obligation by paying the tax to the operator.”¹

¹ Chapter 3.12, Section 010.

The Municipal Code further defines a hotel as the following:

“Any structure or any portion of any structure **which has three or more units** occupied or intended or designed for occupancy by transients for dwelling, lodging or sleeping purposes, including any hotel, inn, tourist home or house, motel, studio hotel, bachelor hotel, lodginghouse, rooming house, apartment house, dormitory, public or private club, mobile home or house trailer at a fixed location or other similar structure or portion thereof.”² (emphasis added)

The Municipal Code further defines a transient as the following:

“Any person who exercises occupancy or is entitled to occupancy by reason of concession, permit, right of access, license or other agreement for a period of **thirty consecutive calendar days or less**, counting portions of calendar days as full days. Any such person so occupying space in a hotel shall be deemed to be a transient until the period of thirty days has expired unless there is an agreement in writing between the operator and the occupant providing for a longer period of occupancy; provided, that any person who actually occupies the same premises for a period of thirty-one or more consecutive days shall be deemed exempt from the tax imposed by this Chapter on that specific occupancy. In determining whether a person is a transient, uninterrupted periods of time extending both prior and subsequent to the effective date of this Chapter may be considered.”³ (emphasis added)

In the last decade, the City of Del Mar has twice sought to increase their Transient Occupancy Tax.

- In 2002, the City’s TOT rate increased from 10% to 10.5%. Voters supported the measure (Prop G) with 82% of the vote. If the measure wouldn’t have passed, the TOT rate would have dropped to 8%.
- In 2008, voters supported Prop H, which allowed the City’s TOT rate to reach 13%. The measure passed with 62% of the vote.⁴

On June 8, 2009, the City increased the TOT rate by 1% (from 10.5% to 11.5%). It was anticipated that the City would receive an additional \$123,743 for fiscal year (FY) 2010 and an additional \$126,218 for FY 2011 in TOT revenue.

The City of Del Mar has the following hotels:⁵

- Del Mar Inn/Clarion
- Hilton Del Mar
- Les Artistes Inn of Del Mar
- The Stratford Inn
- Del Mar Motel on the Beach
- L’Auberge
- Secret Garden Inn
- Wave Crest

Recently, the city’s hotels have begun consideration of a Tourism Business Improvement District (TBID) that would assess an additional 1% rate to each stay. This item will be brought before the Council for a hearing in early April.

Proposal

On February 8, 2010, the City Council of Del Mar voted to introduce an ordinance amending the Municipal Code’s definition of “hotel” to require payment of TOT on short-term rentals. The City argues that there is an increased demand on the City

² Chapter 3.12, Section 030.

³ Chapter 3.12, Section 030.

⁴ Voting ratios obtained from League of Women Voters, *SmartVoter.org*.

⁵ Collected from Del Mar Village Association and Del Mar Regional Chamber of Commerce.

for services when short-term rentals occupy a unit over its traditional residential use. The City also argues that the service demand on the City due to tenants of short-term rentals is similar to that of hotel users.

The question voters will be asked is as follows:

Shall the ordinance amending the definition of Hotel and thereby the payment of Transient Occupancy Taxes by guests of Short Term Rentals (for 30 days or less) be adopted?

The City anticipates that this extension of TOT into short-term rentals would garner an additional \$181,125 annually. The City estimates that there are 70 residential units that would be classified as short-term rentals. These rentals, on average, are used for nine weeks per year with an average rental rate of \$2,500 per week. The revenue generation is determined based upon the following: $\$2,500 \times 9 \text{ (weeks)} \times 70 \text{ (units)} \times 11.5\% \text{ (TOT rate)} = \$181,125$. This relies on the assumption that demand would remain the same following an increased tax.

The City is proposing the following definition to the term hotel: (emphasis added)

“Any structure or any portion of any structure ~~which has three or more units~~ occupied or intended or designed for occupancy by transients for dwelling, lodging or sleeping purposes, including any hotel, inn, tourist home or house, motel, studio hotel, **short-term rental**, bachelor hotel, lodginghouse, rooming house, apartment house, dormitory, public or private club, mobile home or house trailer at a fixed location or other similar structure or portion thereof.”⁶

The person renting the unit is responsible for paying the TOT; however, the property owner and/or management company is responsible for the administration, collection, and submittal of payment to the City.

Concurrently, the City is proposing an ordinance that would accommodate and regulate short-term rentals. This ordinance has not yet been adopted.⁷ The City plans to set up an application process for short-term rental permits combined with a fee to process those permits. Currently, the operation of short-term rentals is a violation of the City’s zoning code; however, the City has had a long history of using these types of rentals. If adopted by the Council, Chapter 9.39 would be added to the municipal code to state the following:

- Short-term rentals may be operated in any zone that allows residential units.⁸
- Short-term rental operations require an annually-issued permit and accompanying fee.⁹
- Occupancy for short-term rentals shall not exceed 12 persons.¹⁰
- There will be assigned penalties for violations; starting at \$250.

The proposed ordinance sets forth operational requirements for short-term rentals (such as ensuring that tenants will not create a disturbance to others) and relies on citizen complaints as a means to enforce these. If approved, the ordinance would go into effect 10 days after certification.

The City of Del Mar cites that Del Mar is the only coastal city in the County of San Diego that does not charge short-term renters a TOT.

⁶ Chapter 3.12, Section 030.

⁷ Through a staff interview with the Planning Manager, Adam Birnbaum, this ordinance will likely be reviewed for adoption in April. Zoning clarification is currently being crafted so that short-term rentals are an allowable use. March 3, 2010.

⁸ Chapter 9.39.050.

⁹ Chapter 9.39.060. The rate for such permits will be determined by resolution of Council.

¹⁰ Chapter 9.39.130.

City of Del Mar Municipal Analysis

Key Findings

- The City made significant reductions in expenditures between FY 2008 and FY 2009 (nearly 14% when accounting for transfers).
- The City's largest revenue loss between FY 1999 and FY 2011 came in FY 2008 where the City experienced a 10.15% decline in revenues over FY 2007.
- The City's reserves were 36.6% less in FY 2009 than in FY 1999 (when adjusting for inflation).
- The City's second highest source of revenue comes from TOT, which made up nearly 14% of the City's General Fund revenues in FY 2009.
- The City has lost much of its anticipated TOT revenue for FY 2010.
- The City's pension costs have increased 128% from FY 1999 – FY 2009.
- The City does not pick up any of its employees' pension costs for nonsafety workers; the City does, however, pick up an additional 4% for safety members.

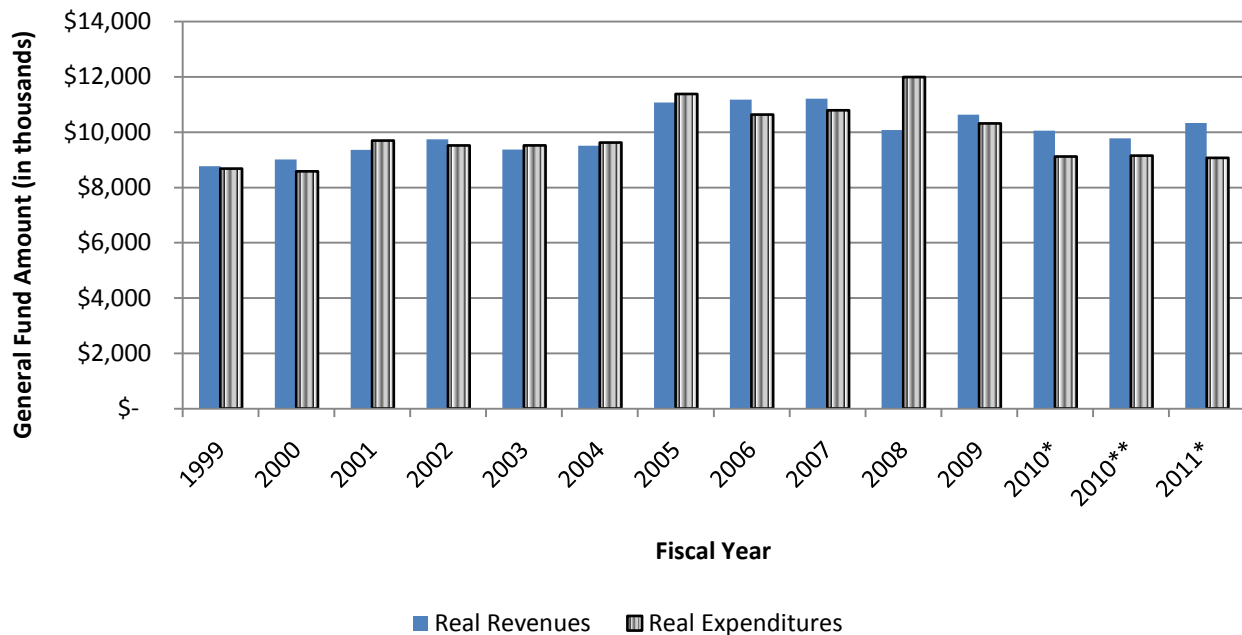
Revenues vs. Expenditures

The following graph outlines revenues and expenditures within the City of Del Mar (City) over the last decade. Between Fiscal Year (FY) 1999 and FY 2009, average annual total General Fund revenues increased 2.15%, while total General Fund expenditures experienced average annual increases of 2.14% during the same period. When accounting for transfers, the City has experienced four (4) deficits between FY 1999 and FY 2009. When adjusting for inflation, the City experienced its largest revenue growth in FY 2005 (over 16%), and its largest revenue decline in FY 2008 (10.15%). The City also experienced its largest expenditure growth in FY 2005 (over 18%), but its largest decline in expenditures came in FY 2009 (nearly 14%).

City of Del Mar General Fund Revenues and Expenditures FY 1999 - FY 2009, Projected Through FY 2011

(in 2008 dollars, adjusted for inflation)

Source: FY 1999 - FY 2009 CAFRs, FY 10 and FY 11 budgets, 2nd Quarter Financial Projections



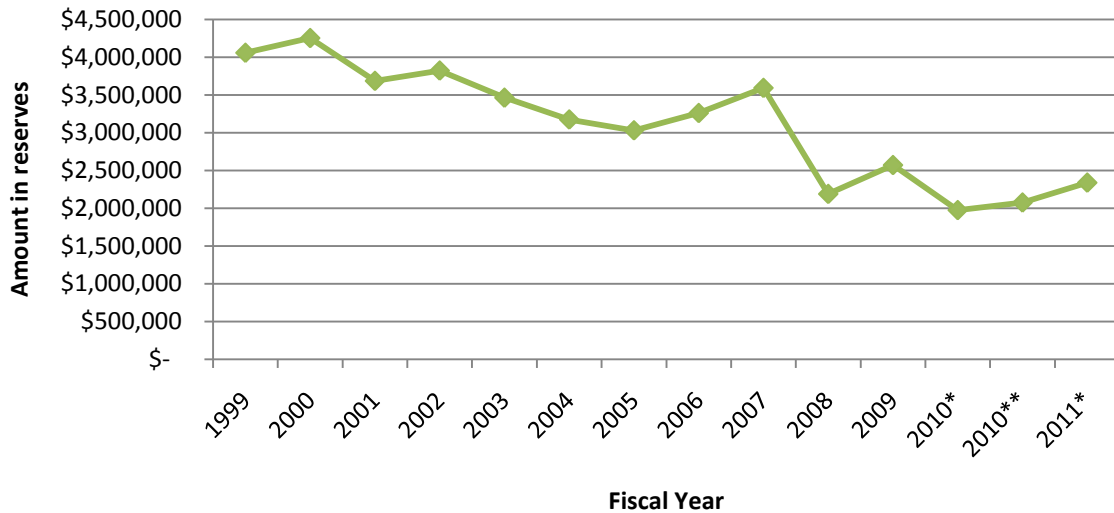
Note: * Denotes that the numbers were obtained from budgets and ** denotes that the numbers were obtained from the last quarter financial projections.

The City’s reserves were 36.6% less at the end of FY 2009 than they were in FY 1999 (when controlling for inflation). The City anticipates dipping into reserves in FY 2010 before partially replenishing them in FY 2011. Second quarter financial projections, however, show that the City would dip into reserves less than they expected to in the adoption of their FY 2010 and FY 2011 budget.

City of Del Mar Reserve Levels FY 1999 - FY 2011*

(in 2008 Dollars, adjusted for inflation)

Source: City of Del Mar Financial Statements and Budgets



Note: * denotes that the numbers were obtained from budgets and ** denotes that the numbers were obtained from the last quarter financial projections.

Tax Revenues

The largest source of General Fund revenue for the City of Del Mar comes from property taxes. In FY 2009, property taxes accounted for over 41% of the City’s General Fund revenues (not including transfers). The City’s property tax revenue grew 4.55% from FY 2008 to FY 2009. Within the City’s approved FY 2010 and FY 2011 budget, the City anticipated that this revenue source would account for 38.02% and 38.49% of General Fund revenues, respectively. However, FY 2010 second quarter financial projections showed that the City’s original projections for FY 2010 were 3.31% lower than they should have been.

The second largest source of revenue for the City has been its Transient Occupancy Tax (TOT). In FY 2009, TOT accounted for 13.92% of the City’s General Fund revenues. The City’s TOT revenue grew by 13.74% from FY 2008 to FY 2009. The City anticipated (within its approved budget) that in FY 2010 and FY 2011, this number would increase to 15.78% and 15.67%, respectively. According to the City’s second quarter financial projections, however, the City expects to receive 15.13% less in FY 2010 than anticipated within its approved budget.

Just behind TOT is sales and use tax revenue. In FY 2009, sales and use taxes accounted for 13.37% of the City’s General Fund revenue. The City’s sales and use tax revenue decreased by 3.28% from FY 2008 to FY 2009. In the City’s FY 2010 and FY 2011 budget, the city anticipated that this number would increase to 13.85% in FY 2010 and 13.93% in FY 2011. The second quarter financial projections indicate that the City will receive 3.59% less than it anticipated in FY 2010.

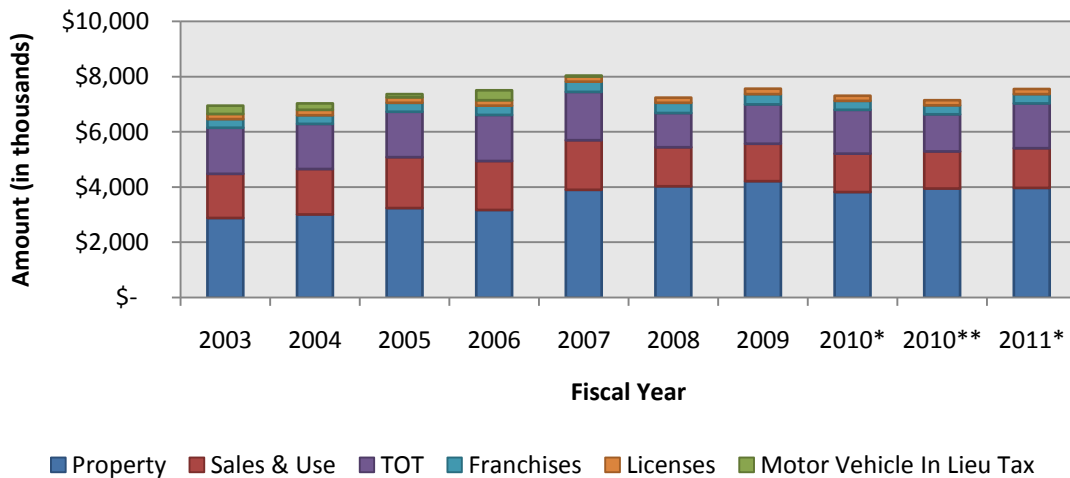
The City also receives revenue from franchises and business licenses.

When adjusting for inflation, the City’s total General Fund tax revenues have increased nearly 9% between FY 2003 and FY 2009. The City’s total tax revenue from FY 2008 to FY 2009 increased 4.47%. However, the from FY 2007 to FY 2008, the City’s total tax revenue decreased 9.86%.

General Fund Tax Revenue Sources From FY 2003 - FY 2011*

(in 2008 dollars, adjusted for inflation)

Source: City Financial Statements, Budgets, and 2nd quarter financial projections
(only actual amounts used through FY 2009)



Note: * denotes that the numbers were obtained from budgets and ** denotes that the numbers were obtained from the last quarter financial projections.

Expenditure Detail

The City of Del Mar contracts with the County of San Diego for law enforcement services. Due in large part to this contract, public safety represents the City of Del Mar’s largest General Fund expenditure. Between FY 2003 and FY 2009, public safety expenditures have grown nearly 21% (adjusted for inflation). From FY 2003 – FY 2009, general government expenditures increased nearly 17% (adjusted for inflation).

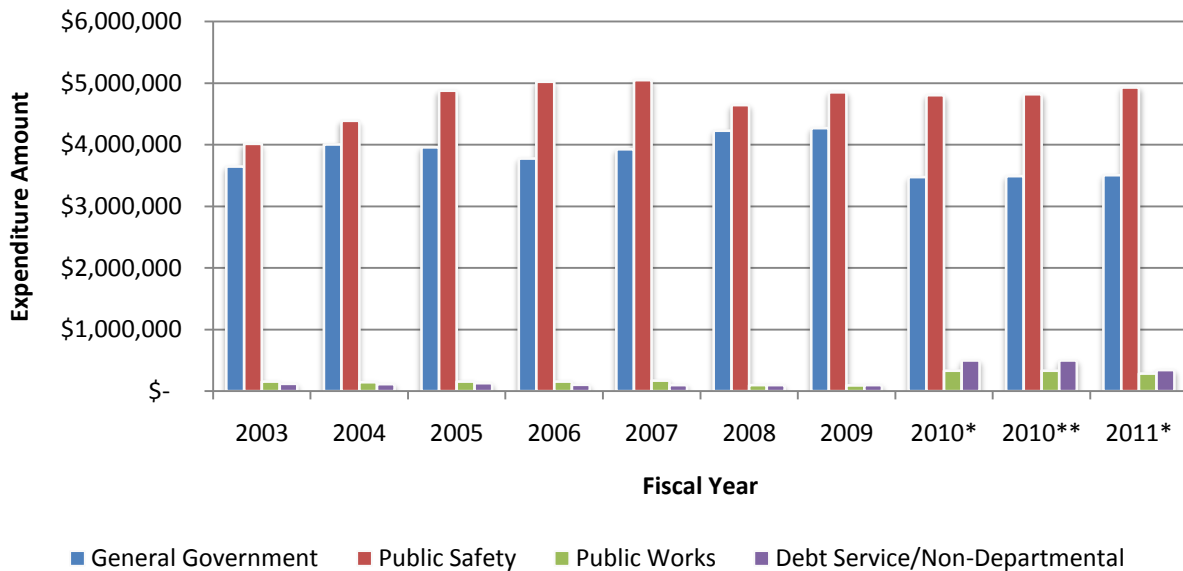
When adjusting for inflation, total General Fund expenditures have grown 17.25% between FY 2003 and FY 2011. Between FY 2008 and FY 2009, the City increased expenditures 2.64%. Within the adopted budget, the City decreased expenditures by 2.13% in FY 2010 and an additional .53% in FY 2011. However, FY 2010 second quarter financial projections show that the City anticipates decreasing expenditures from FY 2009 to FY 2010 by 1.78%.

Note: The City of Del Mar’s financial statements have different categories than the City’s budget documents; for this reason, some of the City’s “non-departmental” expenditures may also be considered general government expenditures.

City of Del Mar General Fund Expenditures by Department FY 2003 - FY 2011*

(In 2008 Dollars, adjusted for inflation)

Source: City Financial Statements, Budgets, and 2nd quarter financial projections (only actual amounts used through FY 2009)



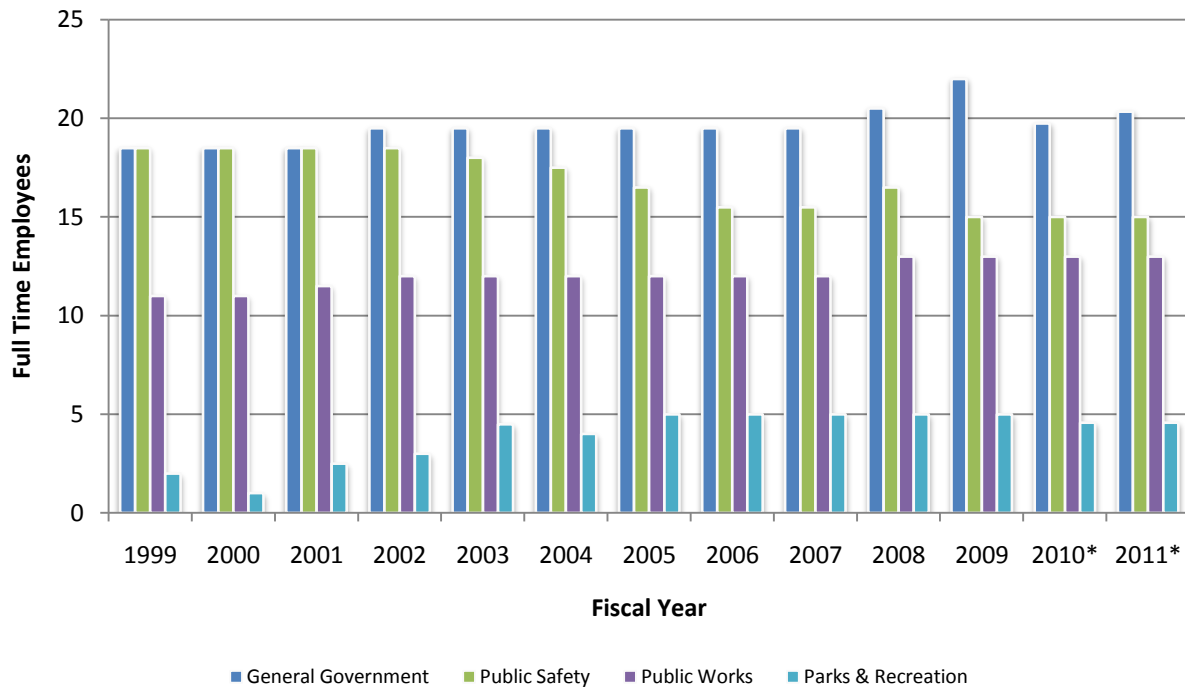
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Staffing Levels

The City of Del Mar currently contracts for City Attorney services, therefore there are no full time employees within that expenditure category. The same is true for engineering services. Between FY 1999 and FY 2011*, the City experienced the largest decline in employees within the public safety category; general government and parks and recreation experienced the largest increases.

City Staffing By Service Between FY 1999 and FY 2011

Source: City Financial Statements and FY 2010 and 2011 Budget

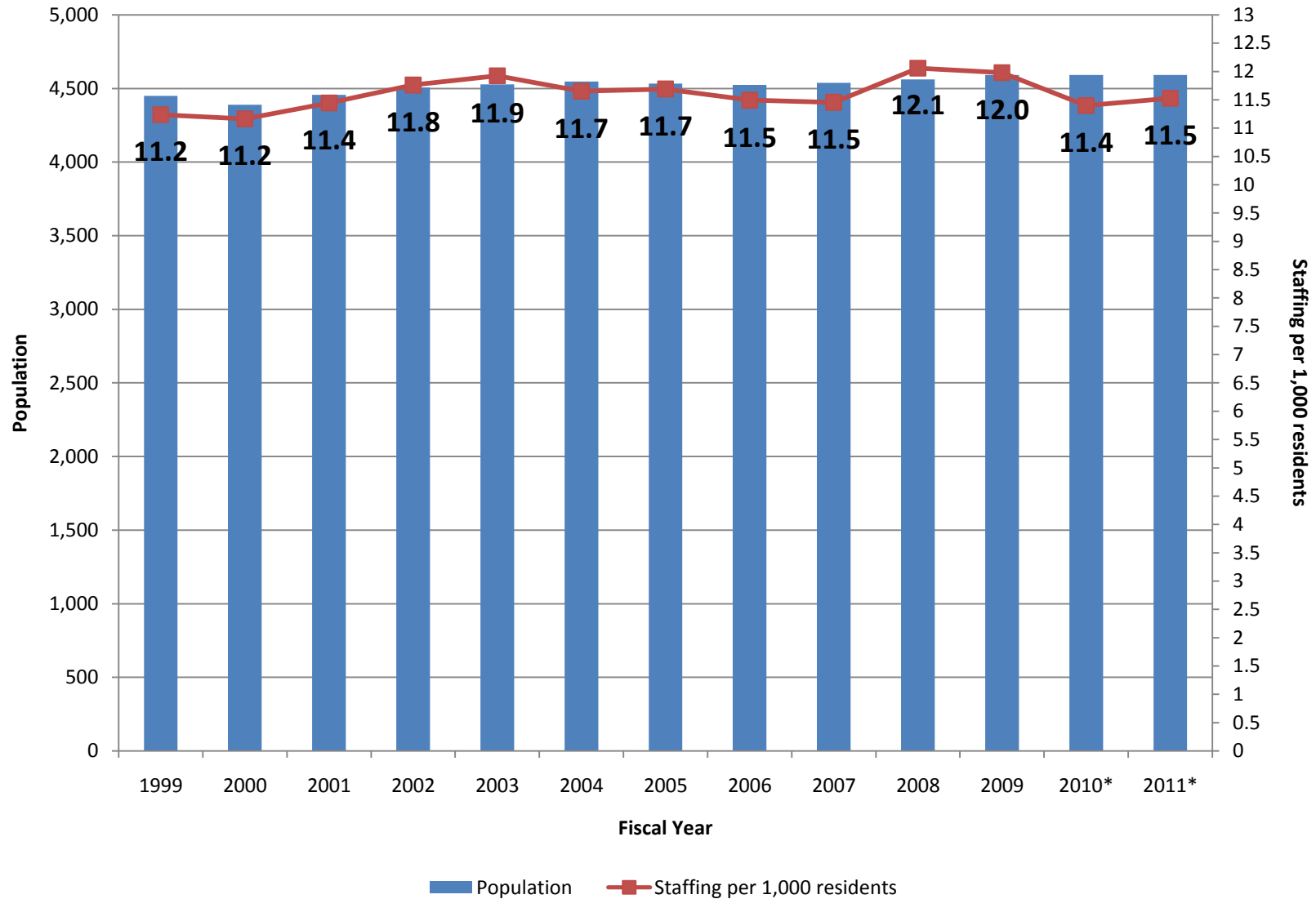


Note: * denotes that the numbers were obtained from budgets.

The City of Del Mar is the least populated city in the County of San Diego. In FY 2009, the California Department of Finance notes that the City had a population of 4,591. Despite how many services it contracts out, the City has one of the highest staffing ratios in the region.

Staffing Levels vs. Population

Source: City financial statements and FY 2010 and FY 2011 budgets; population data from the California Department of Finance. Note: Assumes no increase in population for FY 2010 and FY 2011, does not include any contracted po



Pension Costs

The city currently has two Memorandums of Understanding (MOU) with its labor groups. These MOUs outline all of the benefits that each group of city employees receives, including salary increases and pension benefits.

Labor Unit	Benefit Formula	Compensation Method Used	Employees pay	City picks up
Del Mar Firefighters Association	3% @ 50	Highest average 36 months	5%	4%
Del Mar City Employees Association	3% @ 60	Highest average 36 months	8%	0%
Del Mar Lifeguards (no contract)	2% @ 50	Highest average 36 months	5%	4%

The City contributes to the California Public Employees’ Retirement System (CalPERS), an agent multiple-employer public employee defined benefit pension plan. PERS provides retirement and personal disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. PERS acts as a common investment and administrative agent for participating public entities within the State of California.

Del Mar active plan members are “required” by State statute to contribute 8% for miscellaneous and 9% for safety employees of their annual covered salary. The City of Del Mar does not pick up any of the employee contribution—i.e. nonsafety employees pay their full 8% toward their pensions. The City employer does, however, pick up 4% of the contribution required of safety employees (this is known as Employer Paid Member Contributions, or EPMC). This means miscellaneous employees are responsible for 8% of their annual pension contributions and safety members are responsible for 5% of their pension costs.

Fire Safety Employee Example	
Highest Average 36 Months of Salary	\$100,000
Service Years	30
Benefit Factor	3%
Total Pension Benefit	\$90,000

Miscellaneous Employee Example	
Highest Average 36 Months of Salary	\$85,000
Service Years	30
Benefit Factor	3%
Total Pension Benefit	\$76,500

City of Del Mar Employee Retirement Benefits
CalPERS Formula: 3% @ 60 for miscellaneous employees, 3% @ 50 for fire safety employees, and 2% @ 50 for lifeguard employees.
Employee Contribution: City pays 4% of the employee contribution for safety members and 0% for miscellaneous.
Average highest 36 months benefit for final compensation

A summary of pension costs since FY 1999 is presented in the following table:

City of Del Mar Annual Pension Costs					
(not adjusted for inflation)					
<i>Source: City of Del Mar FY 1999 – 2009 CAFRs, PRAs</i>					
Fiscal Year	City Annual Required Contribution (ARC)	EPMC	Defined Contribution Plan	Total Pension Costs	Ratio of Total Pension Costs to General Fund
1999	see total	see total	\$ -	\$ 288,758	5.58%
2000	see total	see total	\$ 8,000	\$ 243,314	4.50%
2001	\$ 14,952	\$ 226,730	\$ 8,000	\$ 249,682	3.79%
2002	\$ 83,191	\$ 303,062	\$ 8,000	\$ 394,253	5.91%
2003	\$ 89,085	\$ 180,046	\$ 8,000	\$ 277,131	3.97%
2004	\$ 195,928	\$ 178,470	\$ 8,000	\$ 382,398	5.27%
2005	\$ 427,752	\$ 185,900	\$ -	\$ 613,652	6.77%
2006	\$ 507,497	\$ 176,227	\$ -	\$ 683,724	7.85%
2007	\$ 775,639	\$ 51,215	\$ -	\$ 826,854	9.39%
2008	\$ 820,409	\$ 48,138	\$ -	\$ 868,547	8.36%
2009	\$ 872,868	\$ 49,200	\$ -	\$ 922,068	10.68%

*Note: Contract costs for the County of San Diego law enforcement have been excluded from the General Fund amounts for purposes of this ratio.

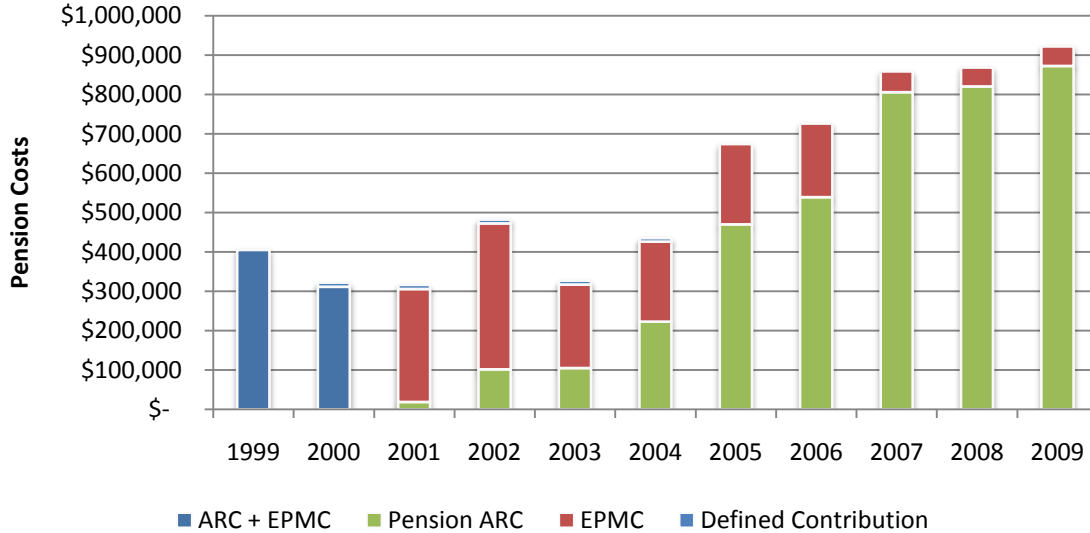
When adjusting for inflation, the city’s total pension costs have increased 128% between FY 1999 and FY 2009. During much of this time, the city’s pension fund was super-funded (where assets far exceeded liabilities), which meant that the city had a very low payment on its required contribution to CalPERS. During this time, however, payment toward EPMC did not stop.

Payment toward pensions will continue to consume greater portions of the City’s General Fund. This past fiscal year, CalPERS lost nearly 1/3 of its portfolio. These rates, in return, get pushed back onto cities in the coming years through higher rates.

City of Del Mar Pension Costs FY 1999 - FY 2009

(in 2008 Dollars, adjusted for inflation)

Sources: FY 1999 - FY 2009 CAFRs, Public Records Act Requests



For a more comprehensive look at public pensions in the region, please review SDCTA’s Phase I report issued in October of 2009.

SDCTA recognizes that while pension costs consume increasing portions of a City’s General Fund, total compensation needs to be taken into account as well. SDCTA has reviewed three “typical” positions in city government: firefighter/paramedics, executive assistants, and assistant planners and each of their corresponding monthly salaries.

City	Position	Monthly Salary	Position	Monthly Salary	Position	Monthly Salary
Carlsbad	Firefighter/ Paramedic	\$6,415	Executive Assistant	\$6,050	Assistant Planner	\$5,504
Coronado	Firefighter/ Paramedic	\$6,022	Executive Assistant	\$5,713	Assistant Planner	\$5,587
Del Mar	Firefighter/ Paramedic	\$5,846	Executive Assistant	\$4,623	Assistant Planner	\$5,309
Encinitas	Firefighter/ Paramedic	\$6,582	Executive Assistant	\$5,561	Assistant Planner	\$5,561
Poway	Firefighter/ Paramedic	\$6,088	Executive Assistant	\$4,499 - \$5,468	Assistant Planner	\$5,632
Solana Beach	Firefighter/ Paramedic	\$6,183	Executive Assistant	\$5,021	Assistant Planner	\$5,124
San Marcos	Firefighter/ Paramedic	\$6,104	Executive Assistant	\$6,060	Assistant Planner	\$5,361

Source for Firefighter/Paramedic Data: Del Mar Compensation Survey Data (dated thru October 2009).

Source for Executive Assistant Data: Coronado Compensation Survey Data (dated thru April 2009). City of Poway’s Salary Schedule for FY 2008/2009.

Source for Assistant Planner Data: Coronado Compensation Survey Data (dated thru April 2009).

As can be seen in the compensation table, Del Mar pays the least for Firefighters/Paramedics and Executive Assistants out of the selected neighboring cities and pays the second lowest for Assistant Planners.

Policy Implications & Analysis

The argument that this measure is needed to reimburse the City for services that short-term renters use is inadequate. Much of the “services” used by short-term renters are those likely displaced from the property owner. Therefore, the City’s claim that hotel users and short-term renters place the same demand on City services and thus deserve to pay the same rate is not justified. It is recognized, however, that there is *increased* demand placed on city services as a result of short-term rental usage.

No serious method of enforcement exists within the proposed ordinance. The only enforcement mechanism is the reliance on neighbor complaints. Also, the City does not currently allow the use of short-term rentals through zoning restrictions and thus did not have a process in place prior to consideration of this measure on how the City would regulate this type of use. This clarification of zoning will come forward through City Council in the next few months, but short-term rentals was not considered an allowable use at the time this measure was voted for placement on the June ballot. Finally, the City may not realize the revenue it hopes to collect from this measure once collection and enforcement costs are factored in.

The cost to place the measure on the ballot would be between \$8,000 and \$9,000.