



REPORT TO THE CITY COUNCIL

DATE: Regular Meeting of February 25, 2020

TO: Mayor Esquivias and Members of the City Council

SUBMITTED BY: J. Patrick Tang, City Attorney
David Biggs, City Manager

SUBJECT: Process for Becoming a Charter City for the Purpose of Increasing the Real Property Transfer Tax (RPTT)

RECOMMENDED ACTION:

Receive report, discuss, and provide direction, if any.

COMMISSION/SUBCOMMITTEE ACTION AND RECOMMENDATION:

There was no commission or subcommittee review of this item.

FISCAL IMPACT: There is no direct cost associated with the preparation of this report. Future steps of considering a ballot measure, including possible polling, preparing a proposed charter, undertaking the process to place the measure on the ballot, and conducting an election, would all incur costs. The exact amount of the impact would depend on what type of community engagement the Council would want. Any process would involve staff and city attorney time. If a ballot measure were approved by the voters, Hercules would see an increase in RPTT revenue. The amount of increase would depend upon the RPTT rate set by the City; various estimates are provided in the Revenue Rate Comparison Table, see page 4. However, it is uncertain whether voters would approve an increased RPTT.

BACKGROUND: At its January 14, 2020 regular meeting, the City Council directed the city attorney and staff to prepare a report for Council information regarding the process for becoming a charter city, for the limited purpose of setting real property transfer tax (RPTT) rates beyond the rate set by state law for general law cities.

DISCUSSION: Cities in California are organized as either general law cities or charter cities. The City of Hercules is a general law city. Cities are general law cities by default, but may go through a process to

become charter cities. A general law city has the authority to exercise its police powers to act locally, but its acts must be consistent with all general laws adopted by the State Legislature. This is why general law cities are “locked in” to receiving a real property transfer tax (RPTT) rate of \$0.55 per \$1,000 as set by the state. In contrast, a charter city may use its “home rule” authority to adopt local laws regarding “municipal affairs” that vary from state laws, so that a charter city has more control over local affairs than a general law city. A significant authority possessed by charter cities is the authority, with voter approval, to impose a higher RPTT rate. Charter law cities are not subject to state law regarding RPTT because the setting of RPTT rates is deemed a municipal affair. As a result, charter cities may impose RPTT at a rate higher than the maximum statutory rate otherwise received by general law cities. A list of all California general law and charter cities, along with their respective RPTT rates, is provided as Attachment 1.

There are other reasons why a general law city may seek to become a charter city other than to set RPTT rates, including but not limited to changing the number of elected officials, establishing district elections, and providing for a strong mayor form of government (see Attachment 2), but given Council’s direction to limit the discussion to becoming a charter city for the sole purpose of adjusting RPTT rates, other reasons for becoming a charter city are not discussed in this report. An example of the type of limiting language that can be included in a charter to restrict the scope of local authority to setting the RPTT rate is provided below:

“The City may exercise the powers of a charter city to generate revenue by imposing a tax on the conveyance of real property, based upon the price paid for the real property ("real property transfer tax"). Any real property transfer tax imposed by the City shall be in addition to any similar tax authorized by the general laws of the State of California. Except as provided in this Charter, the powers of the City shall otherwise be constrained by, subject to, and governed by the general laws of the State as now and hereafter existing relating to cities organized under such general laws.”

It should be noted that, while other governance changes may not be in consideration as part of the approval of an initial charter, charter city status does expand the possible universe of both council and voter-initiated changes to governance and other matters via the electoral process that may otherwise not be possible as a General Law City. However, once a charter is adopted by the voters, it can only be changed by an affirmative vote of a majority of the electorate. And, once a RPTT rate has been approved by the voters, as a general tax it cannot be changed without receiving the affirmative vote of a majority of the electorate. In other words, the Council could not change the charter without voter approval, nor could the Council change the RPTT rate without voter approval.

What is RPTT? The real property transfer tax (RPTT) applies to transactions involving the sale and purchase of all improved property with homes or commercial structures, and all unimproved land with no structures. The tax is paid when ownership transfers from the seller of the property to the purchaser of the property. Generally, the tax can be paid by either the seller or the purchaser, or the tax can be shared between the seller and the purchaser. It is a one-time expense related to the transfer of ownership, and is unrelated to the annual payment of property taxes. Currently under the California Revenue and Taxation Code, property in general law cities when it is sold is assessed a county transfer tax of \$1.10 for every \$1,000 of the real estate’s sales price. Counties then split that tax with the cities, so that the city where

the sale took place receives \$0.55 for every \$1,000 of sale price. Hercules thus currently receives an RPTT of the maximum allowed for general law cities of \$0.55 per \$1,000 of value.

Recently a number of general law cities have utilized the legal process to become charter cities for the limited purpose of setting RPTT rates beyond the baseline rate of \$0.55 per \$1,000 established for general law cities.¹ Under State law and the California Constitution, cities cannot impose, increase or extend any tax unless the tax is approved by the voters. Accordingly, a measure to become a charter city, and an increase to the RPTT, would require voter approval by a simple majority of the electorate.

How much does the property buyer pay? Property owners/sellers in general law cities in California pay a RPTT of \$1.10 per thousand dollars of sales price or \$275 on a \$250,000 property sale; by way of example, that means \$550 on a \$500,000 property sale; \$825 on a \$750,000 property sale, and; \$1,100 on a \$1,000,000 property sale. The RPTT amounts above are split between the county and the city, so that the city receives half. Should the City become a Charter City and enact a higher RPTT, the full \$1.10 per thousand provided for under State law would go to the County, and the City rate authorized under the Charter would be in addition to the base \$1.10 per thousand that the County would receive. The local increase to the RPTT is essentially a local tax measure; unlike the property tax where the City gets back less than 4 cents per dollar, all of the additional RPTT amount would flow to the City, with none of it going to the State and the County receiving only the statutory allocation of \$1.10 per \$1,000.

The table below shows the RPTT paid under the General Law city provisions now in effect, and four additional illustrations on what a possible Charter City rate would impose. As you can see, under the charter city examples, the amount that goes to the County remains the same, regardless of the RPTT rate set by the City:

TAX RATE COMPARISON TABLE

	Gen. Law RPTT \$1.10/1,000	Charter RPTT \$4/1,000	Charter RPTT \$8/1,000	Charter RPTT \$12/1,000	Charter RPTT \$16/1,000
Property Sale Price	City/County	City/County	City/County	City/County	City/County
\$250,000	137.50/137.50	1,000/275	2,000/275	3,000/275	4,000/275
\$500,000	275/275	2,000/550	4,000/550	6,000/550	8,000/550
\$750,000	412.50/412.50	3,000/825	6,000/825	9,000/825	12,000/825
\$1,000,000	550/550	4,000/1,100	8,000/1,100	12,000/1,100	16,000/1,100

¹ Six cities attempted to increase their RPTT rates at the 2018 general election. Voters in five of the six cities approved the RPTT increases. Two of the cities, El Cerrito and Union City, were general law cities that sought to become charter cities for that limited purpose; El Cerrito voters approved becoming a charter city and increasing their RPTT to \$12.00 per thousand, while Union City voters did not approve a similar measure. Emeryville became a charter city to increase RPTT rates in 2014.

By way of comparison, a Hercules resident who buys a \$25,000 automobile in Contra Costa County pays \$2,187.50 in sales tax, based on the current 8.75% tax rate, of which the City receives \$375.00. **How much additional revenue would the city receive if the city adopted an increase to the RPTT?** The amount of additional revenue would depend on what RPTT rate was selected. Below is a chart showing the annual revenue that would be received using the average annual RPTT amounts received by Hercules for Fiscal Years 2014-2019 (\$115,248), and based on a range of RPTT rates:

REVENUE RATE COMPARISON TABLE

\$0.55/1,000		\$4/1,000		\$8/1,000		\$12/1,000		\$16/1000	
City	County	City	County	City	County	City	County	City	County
\$115K	\$115K	\$838K	\$230K	\$1.6M	\$230K	\$2.5M	\$230K	\$3.3M	\$230K

What is the process for becoming a charter city?

Becoming a charter city requires approval by a simple majority of voters. Prior to approving submission of the charter to the voters, the City Council must hold at least two public hearings on the proposal of the charter and the content of the charter, and notice of those hearings must be published at least twenty one (21) calendar days before the date of each hearing. The second public hearing must be held at least thirty (30) days after the first hearing, and at least one of the hearings must be held outside of normal business hours. The City Council may not vote on submission of the charter to the voters until twenty one (21) days after the second public hearing. A charter proposal can only be voted on at a regular general election, absent a declaration of a fiscal emergency. In order for the City Council to place a charter measure on the ballot for November 3, 2020, the City would need to hold the first formal public hearing on a proposed charter at the first meeting in May 2020.

An increased RPTT is not itself established by the charter. Rather, the RPTT would be established by a separate ordinance submitted simultaneously to the voters. The ordinance would include the RPTT rate along with other administrative rules. Since the draft charter would prohibit the City from exercising any of the powers of a charter city except for the enactment of an increased RPTT, becoming a charter city and the transfer tax are inextricably linked.

It is common for cities looking to adopt a charter to launch a community engagement process to inform the public about what becoming a charter city would entail and receive feedback prior to placing a charter measure on the ballot. Because becoming a charter city is a complicated issue that can easily cause confusion, it is strongly recommended that if the Council decided to try and become a charter city that communications professionals be retained to help explain to the public what becoming a charter city entails.

If the Council wished to explore this further, it would want to make some preliminary decisions about the RPTT, such as the proposed rate, before beginning the community engagement process. In addition, the need to renew the expiring existing Utility Users base rate and override by no later than 2024 or 2025, should be considered. These and other factors could also be assessed by undertaking polling to determine

the voter's reactions to a number of possible options. This would normally be one of the first steps before deciding to place a matter on the ballot. The City last undertook polling in 2015 prior to opting to place a measure on the ballot to renew the sales tax override, and the measure was crafted based on the information garnered from professional polling.

Ultimately, the Council would have the ability to make changes and adjustments prior to submitting the measure to the voters, based on feedback received during the engagement process and upon further review.

Possible options for community engagement could include all or some of the following:

- Conduct polling to gauge community interest before placing the measure on the ballot. This could include both scientific and unscientific polling; or
- Appoint a community committee to make recommendations regarding the draft charter and RPTT;
- Conduct official town hall meetings to provide information about the charter and RPTT to the community, as well as allow an opportunity for the public to ask questions and the Council to receive feedback;
- Mail information including FAQs to residents about becoming a charter city.

The above list of community engagement options is non-exhaustive and is intended only as an example of possible types of outreach. The more extensive the outreach, the more community feedback can be expected, but there would be a greater increase in staff time and costs to implement.

SUMMARY CONCLUSION: Becoming a charter city is an option that a number of general law cities have pursued, for varying reasons. Most recently, cities that have placed charter city measures on the ballot have done so primarily to allow local control over the setting of RPTT rates, and have opted to expressly exclude additional powers that are otherwise available to charter cities.

ATTACHMENTS:

1. RPTT Rates Statewide
2. League of California Cities Summary