

389



**SUBMITTAL TO THE BOARD OF SUPERVISORS
COUNTY OF RIVERSIDE, STATE OF CALIFORNIA**

FROM: County Executive Office

SUBMITTAL DATE:
September 22, 2009

SUBJECT: Eastvale Incorporation Revenue Neutrality Agreement

RECOMMENDED MOTION: That the Board of Supervisors approve, and direct the Executive Office to return October 6, 2009, with formalized mitigating terms and conditions based on, the tax sharing framework listed in Attachment A, deemed necessary to remediate the financial impact on the County that will result should LAFCO approve incorporation of community of Eastvale.

BACKGROUND: LAFCO is currently processing an application for incorporation of the community of Eastvale. State law prohibits LAFCO from approving incorporation if the base year net revenue impact on the county is negative, unless mitigating terms and conditions are negotiated with the county. The public review draft of the Eastvale Incorporation Study Comprehensive Fiscal Analysis dated July 8, 2009, (Eastvale CFA) calculates a net revenue loss to the County of \$997,528 in the FY2008 base year.

The CFA does not address the effect of inflation on that amount over time. The terms proposed in Attachment A are intended to offset erosion of the present value of that base amount in order to sustain county services by splitting annual revenue growth with the proposed city 60/40 for a period of 30 years.

Denise C. Harden
Denise C. Harden, Principal Management Analyst

Departmental Concurrence

FINANCIAL DATA	Current F.Y. Total Cost:	\$	In Current Year Budget:
	Current F.Y. Net County Cost:	\$	Budget Adjustment:
	Annual Net County Cost:	\$	For Fiscal Year:

SOURCE OF FUNDS: NA	Positions To Be Deleted Per A-30	<input type="checkbox"/>
	Requires 4/5 Vote	<input type="checkbox"/>

C.E.O. RECOMMENDATION: APPROVE

BY: *Jay E. Orr*
Jay E. Orr

County Executive Office Signature

- Policy
- Policy
- Consent
- Consent

Dept's Recomm.:
Per Exec. Ofc.:

Subject: Eastvale Incorporation Revenue Neutrality Agreement

September 22, 2009

Page 2

The Eastvale CFA calculates \$5,030,186 in transferrable FY2008 base year revenue for boundary scenario #1, and \$4,017,298 in transferrable net county cost for municipal-type services to be taken over by the new city. Of that \$5 million in revenue, \$2.44 million, nearly half, is from sales tax. This represents 6.2 percent of the \$39.53 million in total sales tax received by the County in FY2008.

The difference of \$997,528 between revenue and net cost transferred represents the balance of the county's non-transferrable net costs that remain the county's statutory responsibility in perpetuity. These include essential ongoing countywide responsibilities such as funding the district attorney, public defender, jails, court services, child and adult protective services, public and environmental health, and general government functions.

If revenue neutrality payments by the city to the county were to remain fixed over time at the net base year amount of \$997,528, the buying power of that payment will erode over time due to inflation. The consequence will be an undercutting of the county's financial ability to sustain countywide services to that community as it matures, ultimately resulting either in other areas of the county subsidizing Eastvale, or reduction in services countywide.

To offset inflation, during revenue neutrality negotiations the Executive Office proposed to the Eastvale team a formula based on the base year calculation that escalates the base year net cost by an inflation factor of 3.5% and splits the growth in the county's deficit over that base year amount for a term of thirty years. This offsets the effect of inflation over time, but in a way that shares the economic risk by allowing a portion of the calculation to float. The county also offered to defer the first two years of payments to be paid back, with interest, in installments over a period of years.

The counter offer made by the Eastvale team split net revenue growth 50/50 for the first three years following incorporation, then dropped that split to the City's benefit to 40/60 in years 4 & 5, 30/70 in years 6 & 7, 20/80 in years 8 & 9, 10/90 in year 10, and zero thereafter. They propose deducting their 10 percent contingency reserve from revenue before calculating of the amount owed the County. Finally, their proposal makes only partial payments of the annual total owed the county, reserving a portion to be paid out to the county over years 11-19 following incorporation.

This essentially creates a ten-year term of accumulation payable over nineteen years. The proponents forthrightly admit their intent is to achieve a roundabout cash loan from the county to improve their appearance of viability while they get established.

The Executive Office is sympathetic, and supportive generally of self-determination. However, it is our understanding from the guidance provided by LAFCO that revenue neutrality negotiations are not to enhance an incorporation's viability, but to mitigate an incorporation's impact on the county in order to protect funding of ongoing county services. That is the approach the Executive Office is taking and recommends to the Board. The Eastvale proponents have taken a distinctly different view.

The recommendations presented today are particularly crucial because we are also in concurrent negotiations with the Jurupa incorporation team, and it will be important to be fair and even-handed to both of these adjoining communities. According to the

Subject: Eastvale Incorporation Revenue Neutrality Agreement

September 22, 2009

Page 3

administrative draft of the Jurupa Comprehensive Fiscal Analysis dated August 29, 2009, (Jurupa CFA), the FY2008 base year amount of sales tax listed in the Jurupa CFA for Boundary Alternative #2 is \$6.65 million or 16.8 percent of the total received that year. Between these two incorporation proposals combined there is a total of \$9.09 million, or 23 percent of the County's sales tax revenue at issue. This proposal recovers only a portion of that, but more than if the county receives only the base year amount.

The County's long-term financial forecasts place great hope on the eventual rebound of sales as well as property taxes to dig the County out of its current budget deficit. The revenue neutrality proposal the Executive Office offered the Eastvale proponents, and recommend offering in similar form to the Jurupa proponents, is as generous as the Executive Office believes prudent to keep the county's tax base diversified and protect the County's ability to sustain mission critical services.

Most counties, including the County of Riverside, have not taken such an approach with incorporations in the past. However, the current economic crisis has given us new perspective, and the Executive Office believes this approach is justified in that it recognizes and provides financially for the division of statutory responsibilities between both the city and the county.

LAFCO will be hearing this matter at their October 23 meeting. The Executive Office recommends the Board approve the attached framework on which to base a formal document to be submitted to LAFCO in advance of the October 23 Commission hearing.

Eastvale Incorporation
County Revenue Neutrality Offer

1. Establish the base year County deficit amount as whatever amount is established by LAFCO in their approved CFA.
2. Assume Net County Cost would escalate from the base year amount established by LAFCO at approximately 3.5% annually.
3. Calculate the County's annual deficit as the difference between the adjusted Net County Cost and amount of actual revenue for that year as reported by the City Treasurer in the City's year-end financial statements, adjusted as necessary on reconciliation with the City's audited annual financial report.
4. Calculate the annual neutrality payment from the City to the County as the sum of the County's base year deficit plus 40 percent of the net growth in the deficit over that base year amount for any given year, as follows:

$$\text{Annual Neutrality Payment} = \text{Base Year Deficit} + ((\text{Year X Deficit} - \text{Base Year Deficit}) * 40\%)$$

5. Deferral of neutrality payments for FY2011, FY2012 & FY2013.
6. Repayment of amount deferred in ten equal annual installments beginning in FY2014.
7. Accrual of interest on amounts owed at a rate of 3% compounded quarterly.
8. Payment of the estimated total annual amount owed, with interest, within 60 days following the end of the City's fiscal year.
9. Payment of reconciling adjustments within 60 days following completion of the City's audited annual financial report.
10. Term of agreement to extend through the end of the 30th year from date of incorporation.