

**SPECIAL REORGANIZATION OF THE HARBOR AREA**

**EXECUTIVE OFFICER'S REPORT**

TO THE

LOCAL AGENCY FORMATION COMMISSION  
FOR LOS ANGELES COUNTY

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## TABLE OF CONTENTS

Introduction.....	1
Background.....	2
Procedural Requirements.....	2
Special Reorganization History.....	5
Fiscal Background.....	9
Comprehensive Fiscal Analysis.....	9
Removal of Tidelands from Geographic Boundaries.....	10
Applicant’s Revised Service Vision.....	11
Revenue Neutrality Finding.....	13
Current Harbor City Revenues and Expenditures.....	13
Revenue Neutrality Finding.....	13
Fiscal Viability Finding.....	15
Potential Harbor City Revenues.....	15
Potential Harbor City Expenditures.....	17
Fiscal Viability Finding.....	23
Appendix.....	25
Executive Officer Fiscal Allocations: Tables.....	25

## **INTRODUCTION**

### **Purpose**

Pursuant to the Cortese-Knox Local Government Reorganization Act of 1985 (the “Cortese-Knox Act”)<sup>1</sup> the executive officer of a local agency formation commission is required to review each application for a change of organization or reorganization filed with the commission and prepare a report to the commission, including his recommendations on the application.<sup>2</sup> The objective of this Executive Officer’s Report is to provide the Local Agency Formation Commission for Los Angeles County (the “Commission”) with its Executive Officer’s recommendations regarding the application and proposal for special reorganization of the Harbor area of the City of Los Angeles (“Harbor Special Reorganization”).<sup>3</sup>

### **Context**

The Executive Officer’s Report is based on studies, negotiations and proposals that have been conducted in this process. This input includes, but is not limited to, the Comprehensive Fiscal Analysis (“CFA”) and supplemental report prepared by the Commission’s consultant, the State Controller’s review of the CFA, comments at public hearings, the “terms and conditions” round of negotiations between the City of Los Angeles and the Harbor Special Reorganization applicant (the “Applicant”) held during the last quarter of 2001, the written proposals of those parties, and the recommendations of the Commission’s Subcommittee on Findings, Terms and Conditions (the “Subcommittee”), which held multiple hearings and adopted recommendations on findings, terms and conditions for consideration by the Commission. All of the above submissions, reports and proposals, and all other written submissions which have been provided by the parties and interested third parties, and all recordings, transcripts and minutes of all meetings and hearings are incorporated in this Report by reference for consideration by the Commission.

### **Caveats**

This Report includes analysis and recommendations for the Commission to consider as it makes its determinations with respect to the Harbor Special Reorganization. The decision whether or not to approve or disapprove the proposal, with or without amendment, wholly, partially or conditionally, rests entirely with the Commission. This Report is not a substitute for those discretionary decisions yet to be made by the Commission.

This Report and the recommendations herein are subject to revision and reconsideration as additional and updated data and information becomes available or as may otherwise be directed by the Commission during the course of its deliberations.

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<sup>1</sup> Former California Government Code section 56000, *et seq.* The Cortese-Knox Act was amended by the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (the “Hertzberg Act”), which became effective January 1, 2001. The proposal for special reorganization of the Harbor area of the City of Los Angeles was accepted for filing prior to the Hertzberg Act’s effective date, and therefore, pursuant to the provisions of the Hertzberg Act it is being processed under the prior law, and all references herein are to the former Government Code sections of the Cortese-Knox Act.

<sup>2</sup> Government Code section 56833.

<sup>3</sup> Pursuant to Government Code section 56075.5, a “special reorganization” means a reorganization that includes the detachment of territory from a city or city and county and the incorporation of that entire detached territory as a city. The Harbor Special Reorganization, therefore, consists of a detachment of the Harbor area territory from the City of Los Angeles and incorporation of that area as an independent city.

## ***BACKGROUND***

### **PROCEDURAL REQUIREMENTS**

The special reorganization process for the proposed Harbor Special Reorganization is set forth in the Cortese-Knox Local Government Reorganization Act of 1985 (the “Cortese-Knox Act”).<sup>4</sup> While certain provisions of the Cortese-Knox Act are specific to special reorganization, most of the provisions that relate to incorporations are also applicable because a special reorganization includes an incorporation.<sup>5</sup>

### **Significant Voter Interest**

In order to initiate proceedings for a special reorganization, an applicant is required to obtain the signatures of 25 percent of the registered voters in the territory seeking special reorganization.<sup>6</sup> The Applicant filed its petitions in June 1999. In July 1999, the Executive Officer certified the petitions to be sufficient after the Los Angeles County Registrar/Recorder verified the requisite number of valid signatures of registered voters residing in the Harbor area.<sup>7</sup>

### **Fiscal Viability**

The Commission cannot approve a proposal for special reorganization unless it finds that the proposed city is financially viable, i.e. expected to receive revenues sufficient to provide public services and facilities and a reasonable reserve during the three fiscal years following incorporation.<sup>8</sup> The Executive Officer is charged with causing the preparation of a comprehensive fiscal analysis, which reviews and documents each of the following:

- (a) The costs to the proposed city of providing public services and facilities during the three fiscal years following incorporation;
- (b) The revenues of the proposed city during the three fiscal years following incorporation;
- (c) The effects on the costs and revenues of any affected local agency during the three fiscal years of incorporation; and
- (d) Any other information and analysis needed to make the findings required by Section 56375.1.<sup>9</sup>

The Executive Officer submitted the Harbor Comprehensive Fiscal Analysis (“CFA”) to the Commission on January 9, 2002.<sup>10</sup> The CFA concluded that the proposed city’s revenues would be \$36 million less than its expenditures if it were to rely on the City of Los Angeles for contract

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<sup>4</sup> Former California Government Code section 56000, *et seq.* As stated earlier, the Cortese-Knox Act, is applicable to the Harbor Special Reorganization, and not the Hertzberg Act, which became effective January 1, 2001. All references herein are to the former Government Code sections of the Cortese-Knox Act.

<sup>5</sup> Government Code section 56075.5.

<sup>6</sup> Government Code sections 56750 and 56761.

<sup>7</sup> Government Code section 56706.

<sup>8</sup> Government Code section 56375.1.

<sup>9</sup> Government Code section 56833.1.

<sup>10</sup> Public Financial Management, Inc., *Harbor Proposal for Special Reorganization Comprehensive Fiscal Analysis*, January 9, 2002.

services through its first three years.<sup>11</sup> The City of Los Angeles requested that the State Controller review the CFA. The Controller's report was released on April 1, 2002.<sup>12</sup>

### **Mitigation of Negative Fiscal Effects (“Revenue Neutrality”)**

Government Code section 56845 prohibits the Commission from approving a proposal that includes an incorporation unless it finds that the following are substantially equal:

- (a) revenues currently received by the agency transferring the affected territory which would accrue to the local agency receiving the affected territory; and
- (b) expenditures currently made by the local agency transferring the affected territory for those services which will be assumed by the local agency receiving the affected territory.

If these amounts are not substantially equal, the Commission may only approve a proposal if it finds that: (1) the county and all other subject agencies agree, or (2) the negative fiscal effect of the special reorganization is adequately mitigated by tax sharing agreements, or other terms and conditions imposed by the Commission.<sup>13</sup>

The CFA contains an analysis of the “revenue neutrality” test set forth above, and concludes that the Harbor Special Reorganization would not meet the revenue neutrality test because the Harbor currently generates less in revenue than the City of Los Angeles currently expends in providing the services that would transfer to the proposed Harbor city. As such, current revenues and current expenditures are not substantially equal. However, since the City of Los Angeles currently expends more in providing services to the Harbor than it receives in revenue from the Harbor, a special reorganization of the Harbor area would not cause a negative fiscal effect on the City of Los Angeles. Instead, the City would receive a fiscal benefit, and therefore, no mitigation for the City should be required.

Legal counsel has previously advised the Commission that the Harbor would not be entitled to a reverse mitigation payment from the City of Los Angeles.<sup>14</sup> While Government Code sections 56844 and 56845 provide the Commission with discretion to impose terms and conditions and to mitigate negative fiscal effects, the Commission's discretion must be exercised in light of the legislative intent of the Cortese-Knox Act and in the furtherance of its stated policy considerations. The Cortese-Knox Act emphasizes the formation of local agencies that are fiscally self-sufficient and sustainable and requires that the Commission take into consideration the limited financial resources of a community and weigh that against the community's service needs. If the Harbor needed to rely on a continuing subsidy from the City of Los Angeles, its fiscal viability would be subject to serious doubt.

### **Mitigation of Negative Environmental Effects**

The California Environmental Quality Act of 1970 (“CEQA”)<sup>15</sup> requires that significant environmental impacts be taken into consideration by the Commission prior to the Commission's

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<sup>11</sup> Certain findings contained in the CFA have been modified in the supplemental report. Public Financial Management, Inc., *Harbor Proposal for Special Reorganization Supplemental Report*, February 21, 2002.

<sup>12</sup> California State Controller, *California State Controller's Review of the Proposed Harbor Area Special Reorganization Comprehensive Fiscal Analysis*, April 2002.

<sup>13</sup> Government Code section 56845.

<sup>14</sup> County of Los Angeles Office of the County Counsel, *Imposition of Mitigation Payment Favoring a Proposed New City*, May 25, 2001.

<sup>15</sup> California Public Resources Code section 22000, *et seq.*

discretionary approval of a proposal for a change in local government organization or reorganization. The Commission has retained a consultant to prepare an environmental impact report (“EIR”) for the proposed Harbor Special Reorganization. The draft EIR has been released and distributed for review. The final EIR should be released in May 2002, and must be taken into consideration by the Commission before making its determinations regarding the Harbor Special Reorganization.

### **Terms and Conditions**

The Commission must adopt a resolution making determinations—a document indicating whether or not the Commission approves or disapproves the proposal and listing any terms and conditions for approval.<sup>16</sup>

In making its decision, the Commission is charged with taking into consideration such factors as:

- the likelihood of significant growth in the area, and in adjacent incorporated and unincorporated areas, during the next 10 years,
- the present cost and adequacy of governmental services and controls in the area,
- the probable effect of the proposed incorporation... and of alternative courses of action on the cost and adequacy of services and controls in the area and adjacent areas, and
- the effect of the proposed action and of alternative actions, on adjacent areas, on mutual social and economic interests, and on the local governmental structure of the county.<sup>17</sup>

The Legislature has given the Commission broad discretion regarding the terms and conditions that may be included in the resolution. The discretionary terms and conditions may include provisions regarding continuation of service delivery, the establishment of an effective date for the special reorganization, allocation of City assets and outstanding debts, and public employee rights and benefits, among other issues.

A resolution making determinations typically includes the following components:

- reasons for the reorganization,
- boundaries of the territory involved,
- a distinctive short-term designation to the affected territory and a description of the territory,
- property tax revenue to be exchanged by the affected local agencies,
- provisional appropriations limit of the proposed city, and
- directions for the conducting authority to initiate protest proceedings.

After the Commission adopts its resolution, there is a 30-day period during which parties may request reconsideration of the Commission’s decision or propose amendments to the resolution.<sup>18</sup> If any such requests are received, the Commission must consider the request and may choose to wholly, partially or conditionally approve or disapprove the request, which may require amendment of the resolution.

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<sup>16</sup> Government Code section 56851.

<sup>17</sup> Government Code section 56841.

<sup>18</sup> Government Code section 56857.

## **Conducting Authority Proceedings**

The conducting authority designated by the Commission conducts protest proceedings, and if required, calls for an election on the question of special reorganization. The conducting authority in most California incorporations is the Board of Supervisors;<sup>19</sup> however, in the case of the proposed Harbor Special Reorganization, the Commission has the option of designating either the Board of Supervisors or the City Council of the City of Los Angeles as the conducting authority.<sup>20</sup> The Commission has designated the Board of Supervisors as the conducting authority.

The conducting authority holds a protest hearing too receive written protests against the proposed special reorganization. Special reorganization proceedings must be terminated if the conducting authority receives written protests from a majority of the registered voters residing in the area.<sup>21</sup> In the absence of a majority protest, the conducting authority is required to call an election on the question of special reorganization.<sup>22</sup> The conducting authority would have to adopt a resolution calling for the election by August 9, 2002 in order for the proposal to be considered in the November 2002 general election.<sup>23</sup>

## **Voter Approval**

The conducting authority is required to call the election for special reorganization in the territory ordered to be detached from the city and the entire territory of the city from which the detachment is ordered to occur.<sup>24</sup> A majority of the votes cast in both the City of Los Angeles and the proposed Harbor Special Reorganization area would be required for approval the proposal for special reorganization.

If the proposal proceeded to election, the election of city council members would be held concurrently with the election on the question of special reorganization.

## **SPECIAL REORGANIZATION HISTORY**

Only two cities have been created from existing cities in California's history. In 1890, the City of Coronado was formed from a part of San Diego, and in 1920, the City of Montebello was created from a part of Monterey Park. Both cases predate the Legislature's establishment of local agency formation commissions, and the current legal requirements for special reorganization.

Coronado seceded from the City of San Diego a few years after the first beach resort was built on the peninsula, and after a battle over boundaries was waged in both the Legislature and the courts. The San Diego City Council opposed the detachment, but was compelled by the California Supreme Court to let the voters decide. A few months later, Coronado's detachment and incorporation were approved at a special election by a majority of the voters, both in Coronado and citywide.

The detachment of Montebello from Monterey Park was amicable. Monterey Park had incorporated only four years prior to the break-up "as a defensive measure to prevent neighboring Alhambra,

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<sup>19</sup> Under the Hertzberg Act, the Commission now acts as the conducting authority. This legislation, however, was not yet effective when the Harbor special reorganization petition was accepted for filing.

<sup>20</sup> Government Code section 56029.

<sup>21</sup> Government Code sections 57077 and 57078.

<sup>22</sup> Government Code section 57077.

<sup>23</sup> Government Code section 57132.5.

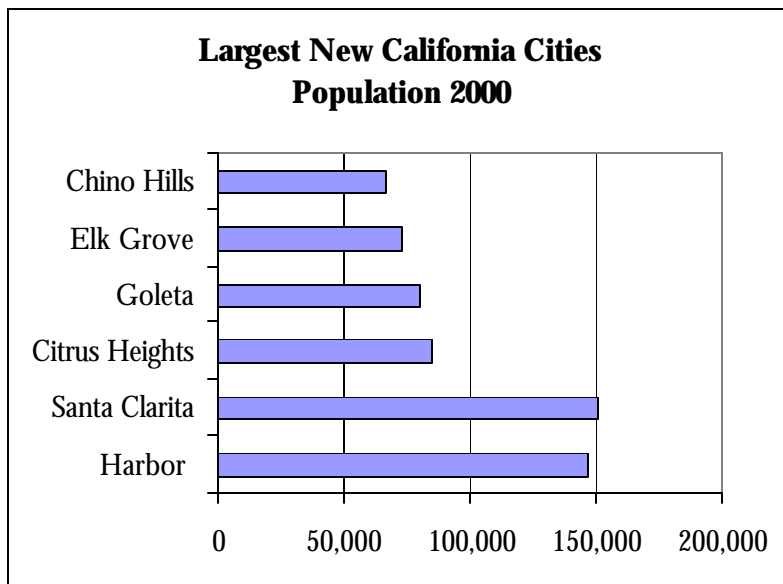
<sup>24</sup> Government Code section 57103.1.

Pasadena, and South Pasadena from converting the area into a sewer farm.”<sup>25</sup> Shortly after stopping the sewer farm project, the Monterey Park City Council approved a detachment proposal from residents of the territory that was to become Montebello.<sup>26</sup>

From 1977 until 1997, a city council could require the termination of any proceeding involving the detachment of territory from its jurisdiction. Legislation adopted in 1997 (AB 62) exempted special reorganizations from this provision, and the Legislature instituted the requirement of voter approval in both the area of special reorganization and the city as a whole.<sup>27</sup> AB 62 also provided for the preservation of existing collective bargaining agreements, existing retiree benefits, and recognition of exclusive employee representatives.

### The Harbor Area Proposal

Not long after the State Legislature’s 1997 reforms, the Applicant filed its application with LAFCO for special reorganization of the Harbor area of the City of Los Angeles. The area proposed for special reorganization is the portion of the Harbor area south of Lomita Boulevard. Most of this area voted to consolidate with the City of Los Angeles in 1909 after the City promised harbor improvements, a new highway, and stable terminal rents. At that time, the cities of San Pedro and Wilmington lacked the resources



needed to develop the harbor. Between 1919 and 1928, seven small areas neighboring the original City of San Pedro were annexed to the City.

The Harbor is relatively large compared with other recently incorporated California cities. Four percent of City of Los Angeles residents live in the Harbor area.<sup>28</sup> Seven percent of the current City of Los Angeles territory lies in the Harbor area.

The reasons cited for Harbor Special Reorganization are unresponsiveness and inadequacy of current services provided by the City of Los Angeles. The Applicant believes that Harbor Special Reorganization would provide:

- Greater local control over local neighborhoods and decisions affecting their quality of life,
- Improved basic municipal services,
- Lower taxes and fees,

<sup>25</sup> Leonard Pitt and Dale Pitt, *Los Angeles A to Z: An Encyclopedia of the City and County*, University of California Press, 1997.

<sup>26</sup> Commission on Local Governance for the 21st Century, *Financing The Fiscal Study For San Fernando Valley Secession*, June 11, 1999.

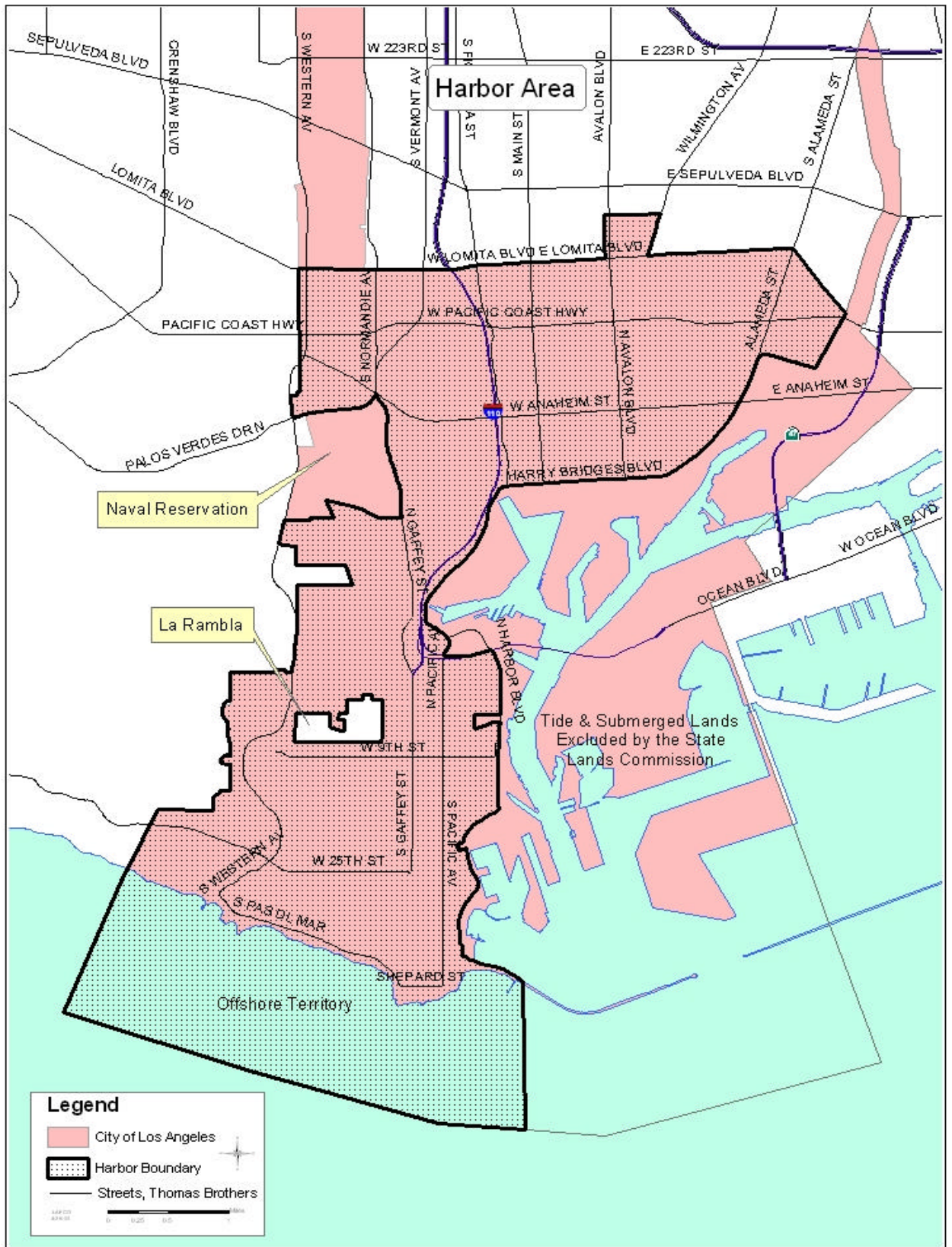
<sup>27</sup> Government Code sections 57079 and 57103.1.

<sup>28</sup> Population based on County of Los Angeles, Urban Research Division estimates from 2000 Census data.

- Safe and clean neighborhoods,
- Short, medium, and long term planning based on the public's priorities,
- A business environment that encourages new businesses, seeks to retain existing businesses, and seeks to create new quality jobs,
- Equal opportunity and fair representation for all residents,
- Equity in the distribution of services and representation, and,
- Government that is accessible, accountable, and responsive.<sup>29</sup>

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<sup>29</sup>Harbor Study Foundation, Inc., *Preliminary Applicant Vision: Proposed Services and Organization Structure*, April 28, 2000.



## ***FISCAL BACKGROUND***

### **COMPREHENSIVE FISCAL ANALYSIS**

The Commission's consultant Public Financial Management, Inc., has prepared a comprehensive fiscal analysis ("CFA") of the proposed reorganization.<sup>30</sup> The CFA must review and document each of the following:

- a) The costs to the proposed city of providing public services and facilities during the three fiscal years following incorporation.
- b) The revenues of the proposed city during the three fiscal years following incorporation.
- c) The effects on the costs and revenues of any affected local agency during the three fiscal years following incorporation.
- d) Any other information and analysis needed to make the findings required by Section 56375.1 (i.e., fiscal viability).<sup>31</sup>

Pursuant to Government Code section 56375.1, the Commission cannot approve a proposal for special reorganization unless it finds that the proposed city is financially viable, i.e. expected to receive revenues sufficient to provide public services and facilities and a reasonable reserve during the three fiscal years following incorporation. The CFA found that the City of Los Angeles currently spends \$34 million more in the proposed Harbor area than the amount of municipal revenues generated in the territory. Further, the CFA found that the new city would need to reduce its expenses by \$48 million after the transition period to achieve fiscal viability. The supplemental CFA indicated that a documentary transfer tax loss would leave the Harbor city with a budget deficit of \$39 million, and that the new city would need to borrow \$59 million and reduce costs by \$51 million by its third year in order to achieve fiscal viability.<sup>32</sup>

The City of Los Angeles requested that the State Controller review the comprehensive fiscal analysis with a focus on the City's concerns. For the most part, the State Controller's review of the comprehensive fiscal analysis validated that the fiscal analysis was both reasonable and accurate.<sup>33</sup> However, the Controller did raise several significant points that are addressed in this section of the Report.

This section also provides a review of fiscal issues that deviate from the assumptions used in the CFA. There are four types of deviations. First, there is a smaller geographic boundary for the proposed Harbor city which eliminates the tide and submerged lands subject to the jurisdiction of the California State Lands Commission.<sup>34</sup> Second, the Applicant's April 26, 2002 proposal to rely on the County for key municipal services alters the expected costs of services in the Harbor area. Next, there are recommended terms and conditions which were developed subsequent to the CFA's release and which deviate from the assumptions used in the CFA, such as the debt allocation factors.

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<sup>30</sup> Public Financial Management, Inc., *Harbor Proposal for Special Reorganization Comprehensive Fiscal Analysis*, January 9, 2002.

<sup>31</sup> Government Code section 56833.1.

<sup>32</sup> Public Financial Management, Inc., *Harbor Proposal for Special Reorganization Supplemental Report*, February 21, 2002.

<sup>33</sup> California State Controller, *California State Controller's Review of the Proposed Harbor Area Special Reorganization Comprehensive Fiscal Analysis*, April 2002.

<sup>34</sup> The recommended boundary changes would decrease the population of the proposed city by less than one percent, but would have more far-reaching effects on the proposed city's revenues.

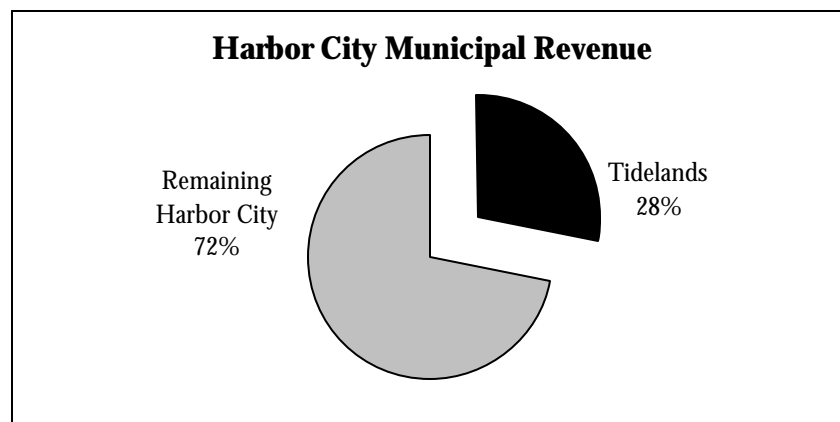
Finally, there is the issue of the documentary transfer tax revenue loss and certain minor discrepancies noted by the State Controller.

### **REMOVAL OF TIDELANDS FROM GEOGRAPHIC BOUNDARIES**

The comprehensive fiscal analysis and staff reports analyzed the Harbor Special Reorganization under the boundaries as originally proposed by the Applicant. The California State Lands Commission reviewed the boundaries of the proposed Harbor Special Reorganization area, and denied approval for the tide and submerged lands in the Harbor area to be included in the proposed special reorganization area on April 9, 2002.

The Lands Commission expressed four areas of concern over the tidelands inclusion in the proposed Harbor city. The first concern raised by the Lands Commission report is that the Port of Los Angeles would be adversely affected by the new Harbor city's need to raise taxes or significantly cut services to cover the revenue shortfalls and become fiscally viable.<sup>35</sup> The report expressed concern about whether the Port of Los Angeles would continue to receive its \$4.4 million annual revenue credit from the City of Los Angeles if the proposed Harbor city were responsible for providing municipal service to the Port. The report raised concerns about the proposed city's prospects for disrupting the administration of the Port and its maritime commerce, pointing to secession proponents' claim that the Port owes the local community \$100 million in environmental mitigation, and secession proponents' suggestion that the new city levy a tax on containers. Finally, the Commission report expressed concern as to whether the special Port Police operation would have the authority to operate, and expressed general concern about Port security if the proposed Harbor city were responsible for police and fire service.

The Lands Commission decision had the effect of removing approximately \$35.6 million in revenues from the proposed city's budget. The Port's tenants contribute on net about \$18 million in revenue to the City of Los Angeles primarily through the possessory interest (leased property) tax, use taxes, and electric utility users tax. Although the Port

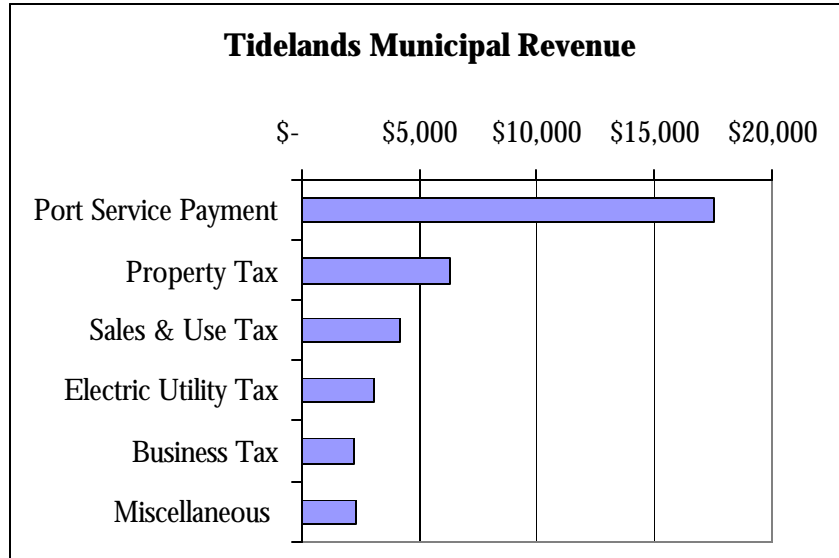


does pay \$23 million for fire and other services to the City of Los Angeles, the Port's service payment covered the City's cost of municipal service in the area in the special reorganization base year.<sup>36</sup> Of that \$23 million Port payment, the CFA had allocated the portion reflecting fire and park costs—which amounts to \$17.5 million—to the proposed city under its originally proposed boundaries.

<sup>35</sup> California State Lands Commission. *Consideration of a Request for Consent to Include Territory Involving Sovereign Tide and Submerged Lands in a Special Reorganization that Would Detach Those Sovereign Lands from the City of Los Angeles and Incorporate them into a new Proposed City Including the Areas of San Pedro, Wilmington, and Harbor City, Los Angeles County, April 9, 2002.*

<sup>36</sup> This assumption is accurate for the special reorganization base year. However, beginning in fiscal year 2001-02, the City of Los Angeles must cover one-quarter of the costs of providing fire service to the Port. This would reduce somewhat the actual net fiscal impact of the State Lands Commission decision.

The Port's payment for municipal service has been the subject of litigation between the State of California and the City, initiated in 1997. The State was concerned that the City of Los Angeles receives more revenue from the Port and its tenants than it is spending on providing service to the area. The State and the City reached a settlement agreement in January 2001 that allows the City only to recoup three-quarters of its cost of providing fire service to the area.



Further, the City must reimburse the Port for \$4.4 million annually over a fifteen-year period for having over-charged the Port in the past. This agreement did not become effective until the end of the special reorganization base year (fiscal year 2000-01). However, it has not had an appreciable effect on the Port's payment for service in nominal dollars.<sup>37</sup>

The Lands Commission recommended that LAFCO set a logical boundary separating Port lands managed by the City of Los Angeles from the proposed Harbor special reorganization area. The Executive Officer subsequently set a logical boundary separating Port lands from the proposed Harbor city (see map on page 8). Thus, the possessory interest, utility users, and use tax revenues generated in the Port of Los Angeles area would continue to accrue to the City of Los Angeles rather than the proposed Harbor city.

**APPLICANT'S REVISED SERVICE VISION**

The Applicant responded to the State Lands Commission decision by proposing a revised vision for the Harbor area involving a shorter transition period, a five-year loan for transition period services provided by the City of Los Angeles, reliance on the County of Los Angeles for key municipal services, and direct delivery of minor municipal services at costs incurred by comparable cities.<sup>38</sup>

Specifically, the Applicant has proposed that the City of Los Angeles provides services only during the first six months after incorporation and, subsequently, that the County of Los Angeles provide major services like police, fire and public works. The Applicant has proposed that refuse collection and park maintenance services be provided by private service providers. For other services, the Applicant has proposed to provide services directly after the six-month transition period at the costs of cities with populations comparable to the proposed Harbor area. In addition, the Applicant requested that LAFCO reduce or exclude a portion of the City of Los Angeles debt, liabilities and general fund contributions to special funds in the Harbor city budget. The Applicant argued that it

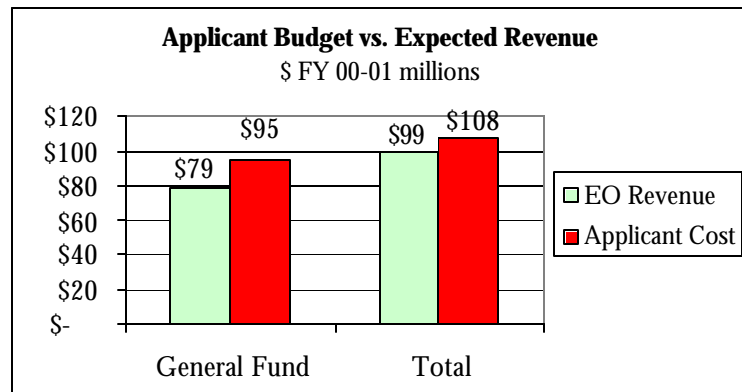
<sup>37</sup> The Port paid the City \$22.5 million in fiscal year 2000-01, \$17 million in fiscal year 2001-02, and is expected to pay \$18 million in fiscal year 2002-03. The Port payments subsequent to fiscal year 2000-01 include a \$4.4 million revenue credit for past over-charges.

<sup>38</sup> Harbor Study Foundation, Inc., *Revised Municipal Budget for the new Harbor Area City*, correspondence from Harbor Study Foundation Executive Director Andrew M. Mardesich to LAFCO Executive Officer Larry J. Calemine, April 26, 2002.

would be “unfair and unreasonable to expect the new city the [sic] fund costs that are currently not being funded.”<sup>39</sup> The Applicant refers to the finding in the CFA that the City of Los Angeles expends approximately \$36 million above local revenues in the Harbor area, and therefore, Harbor area revenues do not contribute to the City’s debt and liability payments or special fund contributions.

The Applicant’s consultant has submitted a budget consistent with the Applicant’s revised proposal.<sup>40</sup> In the Harbor Applicant’s budget, the new city would become a County contract city on the effective date of incorporation. Further, the new city would transform itself into a provider of public works, planning, building inspection, and general government functions upon the effective date at costs comparable to cities like Torrance, Garden Grove, Irvine, Carson and Chula Vista. The proposed budget provides for the proposed Harbor city to pay the City of Los Angeles for all of the Harbor city’s allocated share of lease obligation debt and judgment obligation bonded indebtedness, for one-half of its allocated share of workers’ compensation liability, and for none of the City of Los Angeles’ outstanding tort liability. Under the proposed budget, the new city would not make expenditures under the “General City Purposes” budget item for costs such as audited financial reports, official notices, LAFCO municipal cost-sharing, and the Los Angeles Bridges gang prevention proram. The proposed budget excludes general fund appropriations for the construction and renovation of municipal facilities, appropriations made by designated (“special purpose”) funds such as the gas tax fund for street repairs, and appropriations of funds that pass through the general fund and are transferred to designated funds such as the pass-through of hotel taxes for public arts and promotion of Los Angeles to potential tourists.

The Applicant’s budget projects that the new city’s ongoing general fund expenditures would be \$95.4 million.<sup>41</sup> By comparison, the Executive Officer estimates that the new city would have general fund revenues of \$78.6 million.<sup>42</sup> The Applicant’s budget exceeds by \$17 million the Executive Officer’s estimate of the proposed city’s potential general fund revenues.



<sup>39</sup> Harbor Study Foundation, Inc., *City of Los Angeles Allocated Costs to the Harbor City*, correspondence from Harbor Study Foundation Executive Director Andrew M. Mardesich to LAFCO Executive Officer Larry J. Calemine, May 6, 2002.

<sup>40</sup> Kieser, Walter. *Updated Municipal Budget Proposal, Harbor City*. Berkeley: Economic & Planning Systems, May 3, 2002.

<sup>41</sup> *Ibid.*, Table A-1.

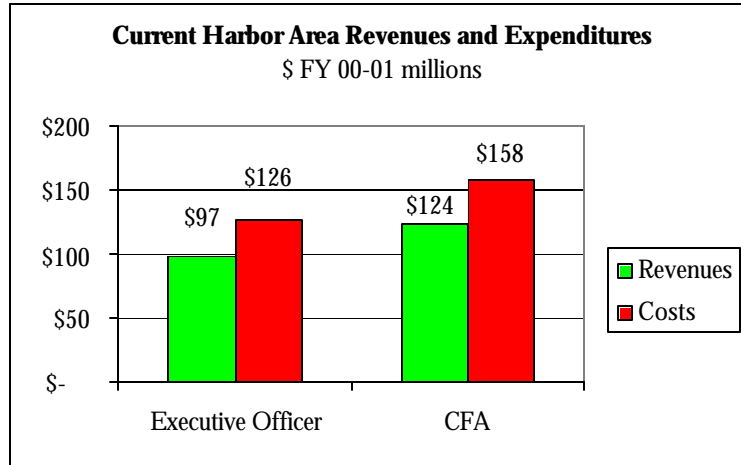
<sup>42</sup> Executive Officer estimate of the new city’s general fund revenues accounts for the reduction in the documentary transfer tax, the increase in the vehicle license fee allocation, and the imposition of electric, water and refuse collection franchise fees. See Appendix fiscal table entitled “Executive Officer Estimates of Potential Harbor City Revenue”.

## **REVENUE NEUTRALITY FINDING**

### **CURRENT HARBOR CITY REVENUES AND EXPENDITURES**

Subsequent to the State Lands Commission decision to exclude the tidelands from the Harbor Special Reorganization area, the Executive Officer has updated the estimates of the current revenues generated in the Harbor area as well as the City of Los Angeles current costs of servicing the area.

The Executive Officer estimates of current revenues and expenditures differ from the CFA in five key areas:



- 1) **Geography:** The Executive Officer estimates are based on the geographic area excluding the tidelands, whereas the CFA is based on the originally proposed special reorganization area including the tidelands.
- 2) **Port Payment:** The Executive Officer expenditure estimates reduce the new city's cost allocation factors to account for the municipal service costs associated with serving the Port of Los Angeles, whereas the CFA allocated the Port payment to the new city as revenue.<sup>43</sup>
- 3) **Financial Basis:** The Executive Officer estimates are calculated by applying revenue and cost allocation factors to the City of Los Angeles actual expenditures for fiscal year 2000-01, whereas the CFA estimates are based on the budgeted expenditures for fiscal year 2000-01.
- 4) **Debt Allocation:** The Executive Officer estimates allocate a share of the City of Los Angeles debt to the new city based upon the Harbor area's current contribution to the City of Los Angeles general fund, whereas the CFA allocated a share of debt to the Harbor area in proportion to the Harbor area's current service costs and staffing needs.
- 5) **Data Updates:** The Executive Officer estimates rely on more recent data on population, registered voters, and property tax allocations.

### **REVENUE NEUTRALITY FINDING**

Government Code section 56845 prohibits the Commission from approving a proposal that includes an incorporation unless it finds that the following are substantially equal:

- (c) revenues currently received by the agency transferring the affected territory which would accrue to the local agency receiving the affected territory; and
- (d) expenditures currently made by the local agency transferring the affected territory for those services which will be assumed by the local agency receiving the affected territory.

<sup>43</sup> The Executive Officer approach follows the recommendation of the State Controller's Review of the Proposed Harbor Area Special Reorganization Comprehensive Fiscal Analysis that the Port payment be treated as an offset to expenditures rather than revenue (page 13).

If these amounts are not substantially equal, the Commission may only approve a proposal if it finds that: (1) the county and all other subject agencies agree, or (2) the negative fiscal effect of the incorporation is adequately mitigated by tax sharing agreements, lump sum payments, payments over a fixed period of time, or other terms and conditions imposed by the Commission.<sup>44</sup>

The CFA contains an analysis of the “revenue neutrality” test set forth above, and concludes that the Harbor Special Reorganization would not meet the revenue neutrality test because the Harbor currently generates less in revenue than the City of Los Angeles currently expends in providing the services that would transfer to the proposed Harbor city. As such the Commission can only approve the proposed Harbor Special Reorganization with the agreement of the County and the City of Los Angeles, or if it finds that the negative fiscal effect of the proposal has been adequately mitigated.

The Executive Officer has reassessed the revenues and expenditures of the proposed city based on the boundaries developed subsequent to the State Lands Commission’s April 9 decision to exclude the tidelands from the proposed special reorganization area. The Harbor area currently generates \$30.6 million less in revenues than is spent on service delivery in the area. Thus, the proposed Harbor Special Reorganization would not be revenue neutral. Further, the Executive Officer finds that the City of Los Angeles would not owe any fiscal mitigation payment to the Harbor area as that would violate the policies and provisions of the Cortese-Knox Act .

It should be noted that the County of Los Angeles’ documentary transfer tax revenue would be reduced by \$176,000 pursuant to Revenue and Taxation Code section 11911, when the new city imposes its documentary transfer tax. This revenue reduction could be considered an annual negative fiscal effect on the County, however, since the County is required by statute to share these revenues with any city within its boundaries that imposes a documentary transfer tax pursuant to section 11911, the Executive Officer recommends against requiring mitigation for this loss. Because the City of Los Angeles’ documentary transfer tax was greater than that allowed pursuant to section 11911, the County has not had to share one-half of its tax with the City, and therefore, has received the benefit of collecting and retaining the full tax for a number of years.

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<sup>44</sup> Government Code section 56845(c).

## ***FISCAL VIABILITY FINDING***

### **POTENTIAL HARBOR CITY REVENUES**

The Executive Officer has estimated that the proposed Harbor city would have potential revenues of \$99.3 million following incorporation. The proposed city's potential revenues differ from the current City of Los Angeles revenues generated in the Harbor territory in several areas.

### **Documentary Transfer Tax**

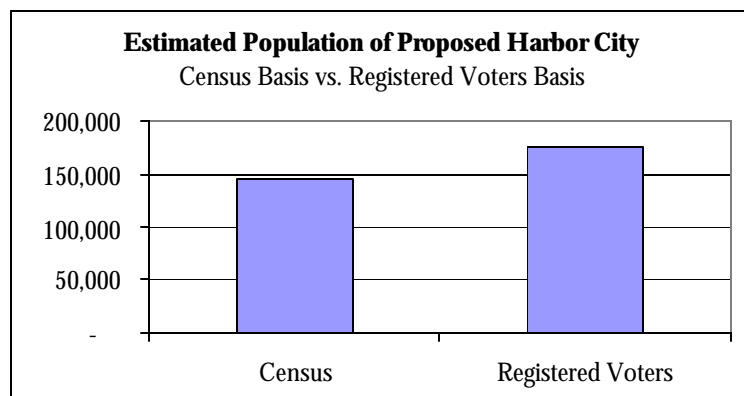
Previous staff reports to the Subcommittee and the supplemental CFA report have pointed out that the CFA overstated the proposed Harbor city's revenues due to the proposed city's inability to levy the documentary transfer tax at its current rate.<sup>45</sup> In its review of the San Fernando Valley CFA, the State Controller's office concurred that the new cities could not levy this tax after special reorganization.<sup>46</sup>

As a general law city, the proposed Harbor city cannot levy a documentary transfer tax in excess of the tax authorized by Revenue and Taxation Code section 11911. State law does not limit the City of Los Angeles' levying authority for a tax on the sale of property due to its status as a charter city.<sup>47</sup> The City currently charges \$4.50 per \$1000 in property value transferred. Revenue and Taxation Code section 11911 authorizes counties to impose a tax of \$1.10 per \$1000 in value of property on deeds transferring property. Section 11911 permits cities within counties that have imposed such a tax to capture half of that amount from the county. Property owners in the City of Los Angeles pay both the City-imposed tax of \$4.50 per \$1000 and the County-imposed tax of \$1.10 per \$1000 (a city not in compliance with section 11911 cannot take any portion of the county's documentary transfer tax revenue).

As a general law city, a new Harbor city would only be able to collect one-half of the County-imposed tax or \$0.55 per \$1000. This means that the City of Los Angeles would lose approximately \$1.4 million in documentary transfer tax revenue if the Harbor area detaches, and the Harbor area would only be able to collect \$0.2 million in documentary transfer tax, based on its statutory entitlement to one-half of the County-imposed tax if it complies with Revenue and Taxation Code section 11911.

### **State Subventions**

The State Controller allocates a share of vehicle license fees and gas tax revenues to California cities based upon the estimated population of each city. In the case of newly formed cities, the Controller estimates population as triple the number of registered voters in the territory. This



<sup>45</sup> *Special Reorganization of the Harbor Area Staff Report on Terms and Conditions*, March 18, 2002; Public Financial Management, Inc., *Harbor Proposal for Special Reorganization Supplemental Report*, February 21, 2002.

<sup>46</sup> California State Controller, *California State Controller's Review of the Proposed San Fernando Valley Special Reorganization Comprehensive Fiscal Analysis*, April 2002.

<sup>47</sup> *Fielder v. City of Los Angeles*, 14 Cal.App.4th 137 (1993).

allocation approach tends to favor newly formed cities if more than one-third of the population in the new city is registered to vote.

The Executive Officer's estimate of the actual population in the Harbor area is based on an analysis of 2000 Census data conducted by the Urban Research Division (URD) of the County of Los Angeles. By comparison, the URD analysts found that 58,783 voters were registered within the recommended boundaries of the proposed city in March 2001.

Due to the high voter registration rate in the Harbor area, the new city would receive an additional \$1.5 million in vehicle license fees and an additional \$0.9 million in gas taxes than it would receive if the state subvention allocation were based on the proposed city's actual population.

### **Franchise Fees**

In the terms and conditions previously recommended by LAFCO staff and approved by the Subcommittee, the new city's constituents would be obligated to receive electric and water utility service from the Los Angeles Department of Water and Power. This requirement would necessitate a franchise agreement between the proposed city and the City of Los Angeles. When such a franchise agreement is negotiated, it is common practice for the local government jurisdiction to impose a franchise fee on the gross receipts generated by the utility company in the boundaries of the city. Such a franchise fee may be imposed without the approval of the voters. California law limits the franchise fee on electric and water consumption to a rate of two percent.<sup>48</sup>

The Executive Officer estimates that the proposed city could raise \$2.0 million from an electric franchise fee and \$360,000 from a water franchise fee. These estimates assume that the new city would impose such a fee at the rate of two percent.<sup>49</sup>

The Applicant has proposed to privatize residential refuse collection service as a cost-saving measure. In the event that the new city hires a private refuse collection firm, the new city would negotiate a franchise agreement with that provider and could impose a franchise fee on the gross receipts of the private company. State law does not limit the rate at which the new city could levy such a franchise fee. The Executive Officer estimates that the new city could raise \$0.5 million by imposing a franchise fee at the rate of ten percent.<sup>50</sup>

### **Sanitation Equipment Charge Revenues**

The City of Los Angeles levies the sanitation equipment charge on the Department of Water and Power utility bill for purposes of recouping the refuse collection capital costs of garbage trucks and trash bins. Consistent with the Applicant's proposal to privatize refuse collection service, the Executive Officer estimates that the new city would lose approximately \$1.9 million in sanitation equipment charge revenues currently generated in the Harbor area.

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<sup>48</sup> Public Utilities Code section 6201, *et seq.*

<sup>49</sup> The Harbor share of potential franchise fee revenues is based on the Harbor share of electric utility users tax and wastewater service charges, as estimated by the City of Los Angeles and LAFCO staff. The utility gross receipts were estimated from the operating revenue reported on the City's FY 2000-01 water and power financial statements.

<sup>50</sup> Estimated gross receipts of the private sanitation company are based on the City of Los Angeles current fully allocated cost of providing refuse collection service.

## **POTENTIAL HARBOR CITY EXPENDITURES**

In response to the State Lands Commission decision, the Applicant notified the Executive Officer of a new municipal service concept for the Harbor area. “The decision and the related reduction in potential municipal revenue puts additional pressure upon us to assert that the new Harbor Area City can have a municipal budget that falls within the municipal revenue available and provides adequate levels of service to our residents.”<sup>51</sup>

The Applicant’s vision espouses the following five principles:

- 1) **County Contract Service:** The Applicant proposed that the new city receive key municipal services as a contract city of the County of Los Angeles. The key services were defined as police, fire, public works maintenance functions, library and animal control.
- 2) **Privatization:** The Applicant indicated that the proposed city would privatize refuse collection and park maintenance.
- 3) **Service Costs Based Upon Comparable Cities:** The Applicant indicated that the proposed city’s service costs would be similar to costs of other cities comparable in size to the proposed city, which the Applicant indicates are far below the costs of the City of Los Angeles.
- 4) **Transition Period Service Minimization:** The Applicant proposed that “due to the high cost of services provided by the City of Los Angeles,” the transition period be limited to a six-month period, that the scope of transition period service provided by the City of Los Angeles should be limited to essential services, and that the proposed city repay the cost of transition period services over a five-year period.
- 5) **Reduced Debt Payments to City of Los Angeles:** The Applicant proposed that the “allocated portions of the City of Los Angeles debt, liabilities, and general fund contributions to special funds should be reduced or not included at all in the Harbor City budget.”<sup>52</sup>

The Executive Officer analyzed the proposed city’s potential expenditures if all reasonable cost-saving approaches proposed by the Applicant were to be implemented.

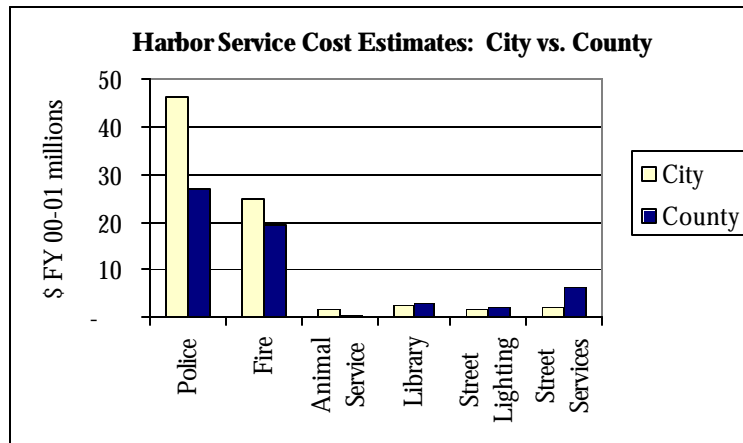
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<sup>51</sup> Harbor Study Foundation, Inc., *Revised Municipal Budget for the New Harbor Area City*, correspondence from Harbor Study Foundation Executive Director Andrew M. Mardesich to LAFCO Executive Officer Larry J. Calemine, April 26, 2002.

<sup>52</sup> Harbor Study Foundation, Inc., *City of Los Angeles Allocated Costs to the Harbor City*, correspondence from Harbor Study Foundation Executive Director Andrew M. Mardesich to LAFCO Executive Officer Larry J. Calemine, May 6, 2002.

## County Contract Service

The Executive Officer requested information from the County Sheriff, Fire Department, Public Works, Library and Animal Control departments to determine whether the County could service the Harbor area at a lower cost than the City of Los Angeles. The Sheriff and County Public Works departments provided estimates of the cost of serving the Harbor area. The other County departments provided data to assist in estimating their costs of serving the proposed Harbor city.



## Police Service

The Sheriff estimated that the cost of providing police service to the Harbor area would be \$27 million annually.<sup>53</sup> By comparison, the City of Los Angeles cost of policing the Harbor area is \$46 million.<sup>54</sup>

In addition to ongoing service costs, the Sheriff estimated that there would be an additional \$31.5 million cost of constructing a new police facility in the area, as well as an additional \$10 million cost to acquire an appropriate fleet of police vehicles, radios, mobile data communications, telecommunications and related systems equipment.<sup>55</sup> The Applicant's budget contemplates financing these start-up costs over a twenty-year period.

## Fire Service

The County Fire Department declined to provide a cost estimate of providing fire service to the proposed city at this stage due to the complexity of assessing fire service costs. In a letter to LAFCO dated Feb. 23, 2001, the County Fire Department indicated that it requires a city to issue a Request for Proposals, sign an agreement to pay for the County's costs of preparing the proposal and estimate, and to complete a 19-page questionnaire before providing a service cost estimate. Nevertheless, the County Fire Department provided data on its costs of servicing contract cities of similar size, and its billing rates for fire truck, fire engine, ambulance and fire inspection staffing.

The County fire cost estimate is based on applying County billing rates to the City's service configuration. Two of the three land-based fire stations located in the Port of Los Angeles primarily service the Harbor Special Reorganization area, whereas the four fire stations located within the proposed Harbor Special Reorganization area provide some service to the Port. The Executive Officer used Port of Los Angeles allocation factors relating to each squad at each fire

<sup>53</sup> County of Los Angeles Sheriff's Department. Correspondence from Sheriff Leroy D. Baca to LAFCO Executive Officer Larry Calemine, June 6, 2001.

<sup>54</sup> For comparability purposes, the City of Los Angeles service cost includes all overhead as defined in the City's budget under Related Costs.

<sup>55</sup> County of Los Angeles Sheriff's Department. Correspondence from Sheriff Leroy D. Baca to LAFCO Executive Officer Larry Calemine, October 1, 2001.

station in order to allocate the fire service costs to the proposed city and to the Port. These are the same allocation factors that the City of Los Angeles uses for purposes of billing the Port of Los Angeles for fire service.<sup>56</sup>

Using this approach, the Executive Officer estimates that it would cost approximately \$19.7 million for the County Fire Department to service the proposed city. This estimate appears to be fairly accurate, given that the City of Pomona pays approximately \$17.6 million for fire service to a comparably sized population.<sup>57</sup> For detailed calculations, see Appendix Table entitled: “Executive Officer Estimates of County Fire Cost in Proposed Harbor City” for detailed calculations.

In addition to the \$19.7 million in estimated ongoing costs for fire service, there would be start-up costs associated with constructing fire stations in the proposed Harbor city boundaries. The neighboring County fire stations do not appear to be situated in such a manner as to substitute for the City fire stations located in the Port of Los Angeles. Start-up costs are expected to be approximately \$7-11 million for constructing three to four new fire stations, which the new city might reasonably be expected to finance. The Applicant’s budget contemplates financing these facility construction costs over a twenty-year period.

### **Animal Control**

The County Animal Control Department provided data on its service costs in the City of Santa Clarita, which has a comparably sized population with less population density than the Harbor area. Based on the department’s cost of servicing Santa Clarita, the Executive Officer estimates that the County Animal Control Department’s cost of servicing the Harbor area would be approximately \$515,000 annually. As this figure is significantly lower than the Executive Officer’s estimate of the City of Los Angeles cost of serving the Harbor area, the Executive Officer assumed that the new city would contract for service with the County.

### **Library**

The County Library department provided information on its per capita costs covering its service areas throughout the county. By applying the per capita cost to the Harbor area population, the Executive Officer estimates that the County’s cost of providing library service to the proposed city would be greater than the City of Los Angeles cost. Thus, the Executive Officer assumes that the new city would contract for service with the City of Los Angeles.

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<sup>56</sup> *Memorandum of Understanding between the City of Los Angeles and the Harbor Department for City Service Reimbursement, Exhibit A: Emergency Fire Department Services Percent of Total Cost.* June 26, 1997.

<sup>57</sup> Certain factors that might reduce the cost of servicing the Harbor City area are:

- 1) The cost of the pump apparatus engineer used at three fire stations was allocated even though the County does not use a pump apparatus (or engineer). If the County does not require the pump apparatus engineer, there would be an additional \$1.4 million in cost savings.
- 2) The estimate did not make deductions in the Harbor city’s cost for the service provided by Fire Station 85 north of the proposed Harbor city’s boundaries. If 10% of this station’s service is provided north of the proposed Harbor city, there would be an additional \$0.5 million in cost savings.
- 3) The estimate did not make deductions in the Harbor city’s cost for the fire inspection service provided north of the proposed Harbor city’s boundaries. If 10% of fire inspection service is provided north of the proposed Harbor city, there would be an additional \$0.6 million in cost savings.

## **Public Works**

The County Public Works Department provided preliminary cost estimates for street maintenance and street lighting costs.<sup>58</sup> The department estimates that street maintenance costs in the proposed city would be at least \$6.2 million, which is higher than the estimate cost of City of Los Angeles street maintenance service. The Department estimated that street lighting costs would be \$2.25 million which is also more expensive than the City of Los Angeles' current costs of providing comparable services to the Harbor territory.

## **Privatization**

The Executive Officer analyzed the City of Los Angeles current financing of residential refuse collection service, and determined that the City currently subsidizes its residential refuse collection service with general fund monies. Although residents pay a sanitation equipment charge, that recoups only the capital costs associated with maintaining the garbage truck fleet and garbage bins and does not cover the labor costs associated with refuse collection. The Executive Officer estimates that the City of Los Angeles currently spends approximately \$5 million including overhead costs, and receives \$2 million in the form of sanitation equipment charges in the Harbor territory. Thus, the City general fund subsidizes approximately \$3 million in residential refuse collection services in the Harbor area. If the new city were to develop a franchise agreement with a private service provider, this \$3 million subsidy would not be borne by the proposed city. Instead, residents would pay the refuse collection company directly. The Executive Officer's fiscal estimates make the assumption that the new city would be able to privatize the refuse collection function by the end of its first year of operation.

The Executive Officer requested estimates of the cost of maintaining parks in the Harbor area from two private companies. Both companies independently estimated their costs at two cents per square foot for a total cost of approximately \$6.3 million. By comparison, the City of Los Angeles current cost of maintaining parks in the Harbor city is approximately \$5.9 million. Thus, the Executive Officer's expenditure estimates assume that the proposed city would contract with the City of Los Angeles for this service.

## **Comparable Cities**

The Executive Officer conducted an analysis of the budgets of comparable cities to determine their costs of general government functions.

In choosing the comparable cities, the Executive Officer used the following selection criteria:

- 1) **Comparable Population:** A comparable city must have a population that is roughly comparable to the estimated 145,000 population of the proposed city. Cities with a population within the range of 120,000 to 170,000 were considered.
- 2) **Geographic Proximity:** A comparable city must be located within the Los Angeles area to ensure that labor and real estate costs are roughly comparable. Cities within Los Angeles and Orange counties were considered.
- 3) **Comparable Revenues:** A comparable city must have revenues roughly comparable with the estimated potential revenues of the proposed city. The per capita revenues of the comparable cities range from \$547 to \$843, compared with \$684 in the propose city.

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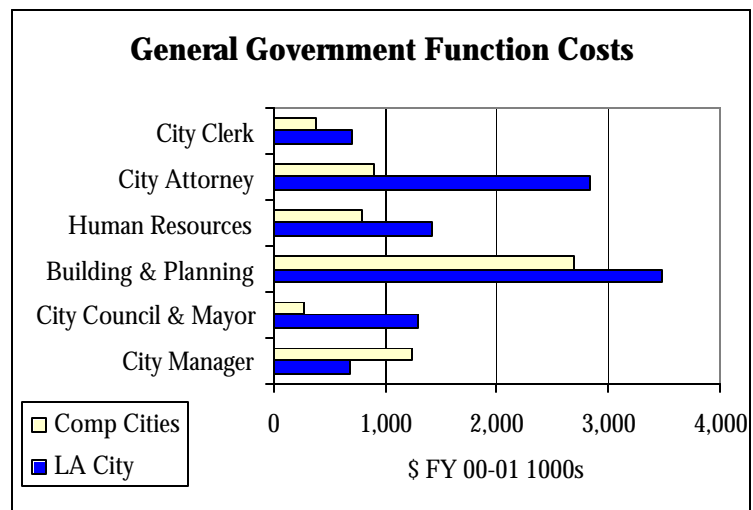
<sup>58</sup> County of Los Angeles Public Works Department. Letter to Larry J. Calemine, May 2, 2002.

Based on these criteria, the cities of Santa Clarita, Pomona, Orange, Garden Grove and Fullerton were selected as comparable cities. Of these cities, Santa Clarita is most comparable in terms of general government expenses because Santa Clarita relies on the County for police, fire and library services and is presumed to have overhead needs comparable to the proposed city. However, Santa Clarita has relatively more resources than the proposed city, with per capita revenues of \$843 compared with expected Harbor city per capita revenues of \$684.

In order to draw comparisons between the cities' costs, the Executive Officer combined certain related departments together. For example, the City of Los Angeles building and planning services are provided by separate departments, whereas several of the comparable cities budgeted these functions together.

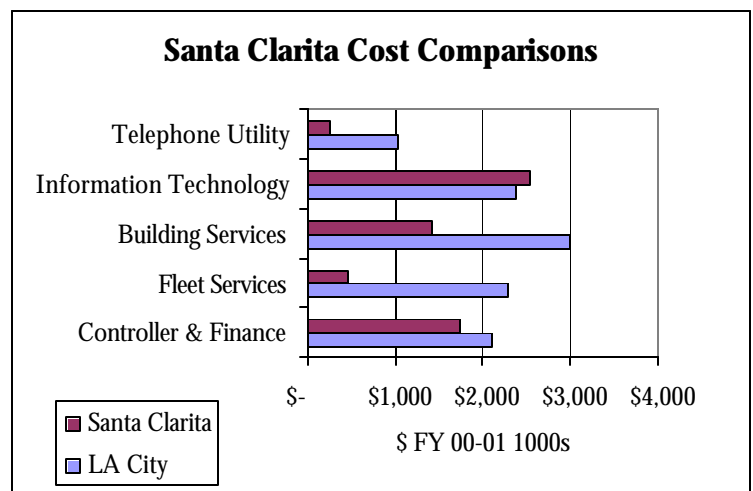
While the comparable cities had much lower costs for the City Council and Mayor, they also had much higher cost for City Manager compared with the City of Los Angeles. This would presumably be explained by the greater role played by a City Manager in a general law city with a legislative structure such as that proposed by the Applicant.

Several of the comparable cities use private law firms for City Attorney services, and those cities tended to have much lower legal costs after factoring in the expense associated with retaining a private firm.



As illustrated in the accompanying chart (and detailed in the Appendix table entitled “Municipal Government Expenses of Cities Comparable to the Proposed Harbor City”), the comparable cities tended to have lower costs associated with general government functions. The Executive Officer averaged the per capita costs associated with each of these functions, and thereby calculated the estimated cost that the proposed city would face if it were to provide for these functions in a manner comparable to the cities studied.

The City of Santa Clarita's budget is sufficiently detailed to provide comparable cost information for finance, fleet services, building maintenance services, information technology and communications services. In particular, the Santa Clarita Finance Division provides investment, revenue collection, accounting, financial reporting, purchasing, mail and graphics services. This division is comparable to the City of Los Angeles functions



performed by the City Controller, Finance Department and a portion of the responsibilities of the General Services Department. Further, Santa Clarita's building and fleet services are comparable to the remaining functions of the City of Los Angeles General Services Department. Additionally, the Santa Clarita budget provided information on its costs for services provided by the City of Los Angeles Information Technology Agency. As indicated in the chart, the telecommunications costs of Santa Clarita are significantly lower than the City of Los Angeles costs allocated to the proposed city.

### **Transition Period Service Minimization**

For purposes of estimating the proposed city's budget, the Executive Officer has made the assumption that the County Sheriff and Animal Control would be able to provide service beginning upon the effective date and that County Fire Service would begin in the second year. The budget makes the assumption that the proposed city would directly provide its own City Council, City Manager, City Attorney and City Clerk functions beginning upon the effective date through a combination of direct staffing and by retaining private firms such as a private law firm. The budget assumes that the City of Los Angeles would provide all other services during the transition period.

Given that the Applicant has separately proposed January 1, 2003 and July 1, 2003 as the effective date, the Executive Officer has presented budget calculations using either of these dates as the effective date.

### **Reduced Debt Payments to City of Los Angeles**

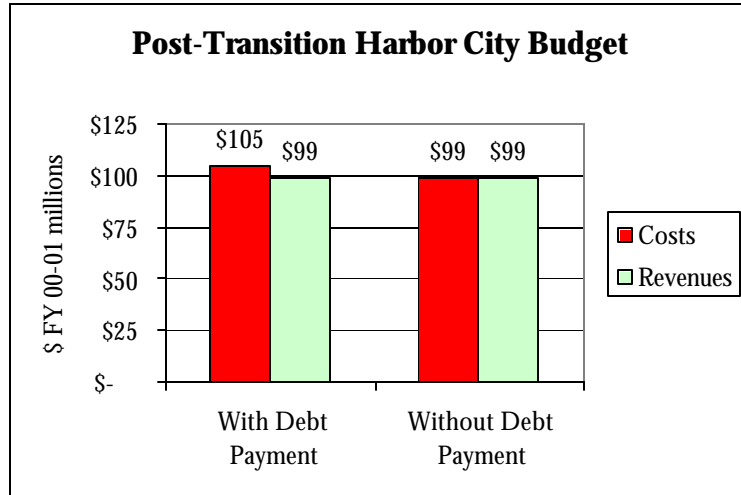
The Executive Officer has included all debt allocations with the exception of debt associated with the Convention Center in the budget calculations. With the exception of the transition year, the Executive Officer has excluded debt allocations associated with the sanitation equipment charge revenue debt. Otherwise, the proposed city's budget includes debt allocations for lease obligation debt, parking revenue bonds, judgment obligation bonds, workers compensation and outstanding tort liability in the new city's costs. In all cases, the debt allocated to the new city is based on the Harbor area's current rate of contribution to the City of Los Angeles general fund.

Given that it is within the Commission's discretion to determine whether or not the proposed city would be obligated to make debt payments to the City of Los Angeles, the budget for the proposed city is provided with and without debt payments. For the budget calculated without debt payments, the Executive Officer assumes that the new city would be required to pay lease obligation debt as that debt is associated with local service-related assets that would presumably transfer to the proposed city.

**FISCAL VIABILITY FINDING**

After taking into account the expected County contracting costs and the general government costs of comparable cities, the Executive Officer concludes that the ongoing expenses of the proposed city would be \$105 million, which is \$6 million greater than the potential revenues of the new city.

If the Commission were to relieve the Harbor city of the obligation to make payments to the City of Los Angeles for judgment obligation bonded indebtedness, outstanding workers compensation and tort liability, the proposed city would have ongoing expenditures of \$99.2 million. In this instance, the proposed city would have only \$157,000 in extra resources for purposes of accumulating reserves.



The proposed city would need a transition period of at least six months before it could achieve cost savings from contracting with the County Fire Department and establishing its own building regulation, planning and grant administration functions.

The Executive Officer has provided four scenarios which differ in the choice of effective date and in the allocation of debt payments to the proposed city. These calculations are presented in the Appendix Table entitled: “Executive Officer Harbor Area Fiscal Viability Computations.” All four scenarios assume that the new city would receive a pro rata share of the City of Los Angeles reserve fund, and that it would be allowed to finance transition period service costs over a five-year period as authorized by statute.

Under the best case scenario (Scenario A in the table) in which the proposed city has a six-month transition period and is not required to make debt payments to the City of Los Angeles, the proposed city would lack the resources to repay any loan extended by the City of Los Angeles in the form of transition period services. Because the new city cannot immediately achieve the cost savings envisioned in its budget and because the new city would owe transition costs, the proposed city is expected to operate at a \$7.5 million deficit during the six-month transition period. Even in the best-case scenario, the proposed city would lack the resources to repay the City of Los Angeles for a \$7.5 million loan of transition period services. Such a loan would require the new city to pay \$1.8 million for each of the next five years. That debt payment could not be made with the meager \$157,000 in annual budget surplus anticipated in the post-transition years. By the end of its second year of operation, the proposed city is expected to have depleted its share of the City of Los Angeles reserve fund. By the end of its third year, the proposed city is expected to have amassed \$4 million in debt for operating expenses. Thus, the proposed city is not expected to be able to accumulate any reserves during its first three fiscal years.

Even if the City of Los Angeles were to subsidize the \$7.5 million transition year deficit or implement cost savings to accommodate the proposed city’s resources, a Harbor city would not be able to accumulate reasonable reserves with its meager annual operating surplus of \$157,000.

The Executive Officer concludes that even under the best-case scenario, the proposed city would not receive revenues sufficient to provide public services and facilities and a reasonable reserve during the three fiscal years following incorporation.

The Executive Officer notes that the special reorganization base year of fiscal year 2000-01 was a particularly good year for the City of Los Angeles. The City actually spent less than anticipated and earned more revenue than anticipated in the base year, and ended up accumulating significant reserves during that year. If the proposed city is not expected to be viable when analyzed based upon a good year, its prospects of surviving average and recessionary years would appear to be bleak.

### **Executive Officer's Recommendation**

The Executive Officer recommends that the Commission find that the proposed city would not be fiscally viable, and that the Commission decline to approve the proposed Harbor Special Reorganization.

***APPENDIX***

**EXECUTIVE OFFICER FISCAL ALLOCATIONS: TABLES**

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