MEMORANDUM

To: Erick Serrano, City of Cupertino

From: Economic & Planning Systems, Inc.

Subject: Fiscal Analysis of the Canyon View GPA Application; EPS #191050

Date: October 16, 2019

The Economics of Land Use

The City of Cupertino retained Economic & Planning Systems, Inc. (EPS) to prepare this fiscal impact analysis of an application for a General Plan Amendment (GPA). The applicant is proposing a low-density residential development on an 86-acre site composed of three parcels. The proposed development envisions 25 residential lots, including 23 single-family residences (SFR) and two lots planned for up to 6 below-market-rate (BMR) townhomes, yielding a total of 29 dwelling units.

The EPS analysis assesses the effect of the proposed development on the City of Cupertino's General Fund. The objective of the analysis is to quantify whether the proposed GPA will generate adequate revenues to cover the costs of providing ongoing services to new residents. The analysis does not consider the impact of the proposal on potential capital facilities cost requirements or other one-time costs.

This fiscal analysis is intended as a planning-level document to inform land use policy. EPS does not employ specific assumptions about the real estate product formats or the composition of the households that will occupy the proposed housing. The analysis does reflect typical housing development in the Cupertino hills and household characteristics that reflect the anticipated real estate price points. The analysis is based on the City's 2018-19 Actual General Fund Revenues and Expenses and presents findings in constant 2019 dollars.

A summary of fiscal impact estimates attributable to proposed GPA is provided below. Actual fiscal impacts will depend on a number of factors that cannot be predicted with certainty, including the market performance of the project, future changes in City or State budgeting practices, and the efficiency of various City departments in providing services. Key analytical inputs and assumptions used in this analysis are from the GPA application, City documents, information from City staff, and EPS industry knowledge. EPS has not performed detailed market research as part of this study effort.

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Summary of Findings

1. ***The proposed Canyon View project will result in an annual net fiscal benefit to the City of Cupertino General Fund.***

   This analysis estimates that the net annual fiscal impact of the GPA proposal on the City's General Fund is approximately $71,000. **Table 1** presents the estimated fiscal impact, assuming market rate home prices averaging $4 million per unit and for-sale BMR home prices of $840,000 per unit. The market rate home price reflects recent home sale transactions, and the BMR home price is calculated based on income limits set by the California's Department of Housing and Community Development.

   Table 1 Annual Fiscal Impact Summary (2019$)

Revenue / Expense Category	Fiscal Impact at Project Buildout
General Fund Revenues	$114,000
General Fund Expenditures	$43,000
Net Impact on General Fund	**$71,000**

2. ***At project buildout, property tax will account for the largest revenue source to the City.***

   The City of Cupertino will receive 7.0 percent out of the 1.0 percent base property tax levied on property in the City. At $4 million per market rate unit and $840,000 per BMR unit, the total assessed value of the development is $97 million. Subtracting out the assessed value of the existing vacant land results in a net addition of $93.5 million to the City's assessment roll. The total amount of property tax collected is estimated at $935,000, and the City's General Fund receives $65,500.

   The property tax calculation relies on the home price assumptions for market rate and BMR homes. For market rate homes, there are several factors that could affect how the home price is set. As an example, the size and specific characteristics of the proposed home development, including choice of finishes and construction materials influences the resulting home price. For instance, the developer may choose to use materials of a higher cost, which would likely raise the market price for the home. Given this potential variation in market rate home prices, EPS evaluated two additional scenarios to illustrate the range of the General Fund fiscal impact that the development could have. If the market rate home price is set at $3 million instead of $4 million, the net impact of the GPA on the General Fund would be about $25,000 lower. On the other hand, if the market rate home price is set higher at $5 million, the net impact of the project on the General Fund would increase by roughly

$25,000.[1] This sensitivity test suggests that the annual net fiscal impact of the project on the City's General Fund could range from about $46,000 to $96,000 based on the specified spectrum of potential home pricing.

Fiscal Impact on the General Fund

This section describes the methodology and key assumptions used to estimate the fiscal impacts of the proposed GPA. The analysis is based on information from three key sources:

(1) the GPA application material submitted
(2) interviews with City planning and finance staff
(3) existing EPS industry knowledge

EPS has not conducted an independent audit of the City's budget, performed in-depth interviews with service-providing City departments, or conducted detailed market analysis.

Proposed General Plan Amendment

The applicant is proposing a residential project to be developed on an 86-acre site located next to Linda Vista Park. The proposed development envisions 23 single-family residences on 23 lots and 6 BMR townhomes. The market rate homes range from 3,000 to 5,000 square feet, and the BMR townhomes range from 1,000 to 1,200 square feet. **Table 2** below presents the proposed GPA program identified by the applicant. The table also presents EPS assumptions concerning the population that would be supported by the project at buildout. A variety of revenues and costs included in this fiscal analysis are based on the anticipated "service population" shown in **Table 2**.

Table 2 Development Program and Service Population

Item	Development Program	Resident Density Assumptions (1)	Population	Service Population
Residential For-Sale				
Market-Rate	23 DU	2.97 Residents / HH	68.3	68.3
Below-Market-Rate	6 DU	2.97 Residents / HH	17.8	17.8
Total	**29 DU**		**86.1**	**86.1**

(1) Household resident densities vary based on product type. EPS assumptions reflect citywide average (State of California Department of Finance). Assumes persons per household will be the city average of 2.97.

[1] This sensitivity analysis reflects potential variation in the market performance of the proposed housing. The City has limited ability to influence market positioning after project entitlement.

General Fund Revenues

New General Fund tax proceeds attributable to the proposed GPA will include sales tax, property tax, property tax in lieu of vehicle license fee (VLF), property transfer tax, TOT, utility user tax, and franchise fees. **Table 3** provides a summary of the Cupertino 2018-19 Actual General Fund Revenues and a description of the forecasting method relied upon for each relevant revenue source.

Table 3 FY2018 - 19 Revenue Budget Summary and Fiscal Impact Estimating Factors

Item	FY2018-2019 Total	Factors Applied to Estimate Project Revenue	
Sales Tax	$23,933,459		
Business to Business Sales Tax		-	not applicable
Other Sales Tax		1.0%	of estimated taxable sales
Property Tax			
Property Tax in Lieu of VLF	$8,219,090	0.4%	of Citywide Assessed Value
Other Property Tax	$25,229,390	7.0%	of base property tax rate (1%)
Transient Occupancy Tax	$8,066,178	-	not applicable
Utility Tax	$2,814,223	2.4%	of utility bills
Franchise Fees	$3,093,283	$38.75	per service population
Business License	$876,455		
Apartments	n/a	-	not applicable
Hotel	n/a	-	not applicable
Other Commercial	n/a	-	not applicable
Other Taxes	$2,038,087		
Construction Tax		-	not estimated
Property Transfer Tax	$481,722	$0.55	per $1,000 in value
Licenses & Permits	$4,097,723	-	not estimated
Fines & Forfeitures	$1,642,227	-	not estimated
Use of Money & Property	$473,942	-	not estimated
Intergovernmental	$10,651,160	-	not estimated
Charges for Services	$450,675	-	not estimated
Miscellaneous	$1,104,017	-	not estimated
Total Revenues	**$92,689,909**		

Retail Sales Tax Revenue

The proposed GPA is expected to generate retail sales tax revenue accruing to the City from project residents' household spending on retail in the City (**Table 4**). This fiscal analysis relies on data from the U.S. Bureau of Labor Statistic Consumer Expenditure Survey to establish the retail spending pattern of households. The spending patterns reflect household consumer behavior observed nationally for households with specified levels of annual income. This analysis uses anticipated residential price points to estimate household income. Then, to identify taxable retail expenditures made by project households, the analysis identifies and isolates taxable retail spending from total household spending. The analysis estimates that for market-rate units, households spend approximately 18 percent of gross household income on taxable retail purchases. For the below-market-rate housing units, this analysis estimates that 26 percent of gross household income is spent on taxable retail purchases. The analysis assumes that about 25 percent of the taxable retail spending of new residents will be captured within the City. Local taxable spending in Cupertino is multiplied by project households to determine average annual taxable sales.

Table 4 Sales Tax Estimate

Item	Assumptions		Factor/ Estimate
Project Households Retail Purchases in Cupertino			
Estimated Annual Household Income (1)			
Market Rate	35%	of income is Housing Costs	$487,509
Below Market Rate	35%	of income is Housing Costs	$130,100
Household Taxable Retail Spending (2)			
Market Rate	17.6%	percent of income	$85,822
Below Market Rate	26.2%	percent of income	$34,096
Weighted Average Household Spending			$75,120
Household Retail Spending in Cupertino (3)	25%	of retail expenditures	$18,780
Project Households			29
Net New Taxable Retail Sales Captured in Cupertino			**$544,623**
Total Sales Tax Revenue	1.0%	of taxable sales	**$5,446**

(1) Income estimate relies on typical mortgage financing and the assumption that housing costs represent 35 percent of gross household income.
(2) Based on Bureau of Labor Statistics Consumer Expenditure Survey for respective income groups.
(3) Assumes 25 percent of taxable retail spending by Cupertino residents is captured by the retailers within the City based on discussions with the City's Economic Development Manager.

Sources: State Board of Equalization, ICSC Research Survey, U.S. Bureau of Labor Statistics

Property Tax Revenue

Property tax revenue estimates are based on the estimated assessed value of the proposed project. Relying on the applicant's proposed development program, EPS estimates the project's assessed value at about $97 million at buildout, as shown in **Table 5**. The City levies a one percent property tax rate, with approximately 7.0 percent allocated to the General Fund.[2]

Table 5 Property Tax Revenue

Land Use	Assumption / Factor		Total at Buildout
Assessed Value Estimate			
Market Rate (For-Sale)	$4,000,000	per Unit	$92,000,000
Below Market Rate (For-Sale)	$840,000	per Unit	$5,040,000
Total Assessed Value			**$97,040,000**
(Less) Existing Raw Land AV (1)			**-$3,500,000**
Property Tax	1.0%	Base Property Tax Rate	$935,400
Cupertino General Fund Revenue (2)	7.0%	Allocation to Cupertino General Fund	**$65,478**
Property Tax In Lieu of VLF			
Existing Citywide Property Tax in Lieu of VLF			$8,219,090
Citywide Assessed Value (3)			$23,402,123,229
Project Net Assessed Value Increase (4)			0.41%
Property Tax In Lieu of VLF Revenue (5)			**$34,082**

(1) Santa Clara County Office of the Assessor (Property Information as of 6/30/2019)
(2) Legislation requires Counties to provide "no/low tax" cities with a Tax Equity Allocation equal to 7 percent of property tax share.
(3) FY2018-2019 value based on secured assessed value from Santa Clara County's Annual Assessor's Report.
(4) Calculated by dividing the new assessed value by citywide assessed value.
(5) Calculated by multiplying existing property tax in lieu of VLF by project net assessed value increase.

[2] Property tax rate anticipated at project delivery; City of Cupertino 2016-17 Adopted Budget, page 80.

Property Tax In Lieu of VLF

In 2004, the State of California adjusted the method for sharing VLF with local jurisdictions. Recent State budget changes replaced VLF with property tax, which grows proportionately with increases in assessed value of the City. The proposed project will add about 0.41 percent to the current assessed value in Cupertino (assuming no other assessed value growth for simplification purposes) and will generate the same increased percentage in in-lieu VLF revenues, as shown in **Table 5**.

Property Transfer Tax

The project will generate real estate transfer tax revenue associated with future turnover in ownership. This analysis assumes that ownership of market rate homes is likely to turnover approximately every 16 years, an annual turnover rate of 6.0 percent. The ownership of BMR homes is estimated to turnover every 25 years, an annual turnover rate of 4.0 percent. The property transfer tax rate accruing to the City General Fund is $0.55 per $1,000 of the property value, as shown in **Table 6**.

Table 6 Property Transfer Tax Revenue

Land Use	Assumption / Factor		Annual Total at Buildout
Property Value			
Market Rate (For-Sale)[1]	$4,000,000	per Unit	$92,000,000
Below Market Rate (For-Sale)[2]	$840,000	per Unit	$5,040,000
Total			**$97,040,000**
Average Annual Turnover			
Market Rate (For-Sale)	6.0%	per Unit	$5,520,000
Below Market Rate (For-Sale)	4.0%	per Unit	$201,600
Total			**$5,721,600**
Property Transfer Tax Revenue	$0.55	per $1,000 in value	**$3,147**

(1) EPS assumption based on comparable sales in neighborhood. In-depth market study not prepared.
(2) EPS assumption based on City of Cupertino and HUD income limits for affordable housing.

Utility Tax

The City of Cupertino collects tax revenue on utility charges for services provided in the City. New residents will expand the use of utilities in the City. This analysis estimates an average monthly utility expense of $95 per resident. The City of Cupertino collects 2.4 percent of utility charges. **Table 7** presents utility user tax revenue attributable to the proposed project at buildout.

Table 7 Utility User Tax Revenue

Item	Assumption		Annual Total at Buildout
Total Residential Population	86	Residents	
Monthly Utility Cost	$95	per resident per month	
Annual Total			$98,188
Utility User Tax Revenue	2.4%	of utility bill	**$2,357**

Revenues from Other Taxes and Fees

In addition to the key revenues described above, other taxes and fees are estimated to be generated by the project. Specifically, franchise fee revenue, which reflects an average derived from City budget documents (see **Table 4**), is calculated for the residential development. **Table 8** presents forecasting assumptions and the revenue estimate.

Table 8 Revenue from Other Taxes and Fees

Item	Allocation Factor		Project Characteristic		Annual Total at Buildout
Franchise Fees (1)	$38.75	per service population	86	service pop.	$3,338
Subtotal					**$3,338**

(1) Franchise Fees based on existing general fund revenue per capita.

General Fund Expenditures

This fiscal analysis estimates the costs attributable to population growth by characterizing how expenses will change for each City department. For some departments, population growth in the City will not dramatically alter operations. For example, administrative functions in the City are not likely to scale up significantly to accommodate new projects. Alternatively, departments that provide services directly to residents and businesses likely will increase their operations and costs to accommodate new populations.

It is important to note that a range of external factors may influence responses to growth and cost effects in the future. Examples of factors that are beyond the control of the City and its departments that may act to magnify or reduce department costs over time include:

- Regional growth;
- Technology;
- State and federal policies; and
- Environmental factors.

This study does not speculate regarding the potential effects of such exogenous influences on the general fund expense budget. It focuses only on those factors attributable directly to the population growth, employment growth, and land use changes generated by the proposed GPA.

The fiscal analysis model relies on categorization of the likely budgetary response to population and employment growth for each department. The anticipated response to growth is expressed for fiscal modeling purposes in terms of "fixed expenses" and "variable expenses" within the department budget.

The fixed expenses are the portion of a City department's budget which is not affected by population and employment growth. Even a department which is anticipated to grow largely in step with the City's service population likely would have some fixed cost. For example, in most cases each department has only one director position, which is a fixed expense for the department. While the department may increase staffing to accommodate growth, the department will not add another director.

The variable expenses of a department are those that do increase with growth. As the City grows, increased demand for services requires some departments to scale up operations to meet new demand. The portion of a department's budget that scales up is identified as the variable share of the budget.

EPS uses a per-capita cost approach to estimate department costs attributable to new residents and workers. The variable portion of each department budget is used to determine the per-capita cost, as shown in **Table 9**. Then, to determine the new General Fund expenditures generated by the proposed project, the per-capita factors are multiplied by the projected increase in service population or population, as appropriate. Innovation and Technology and Non-Departmental expenditures are not estimated because the project is not expected to generate new ongoing costs in to these service providers.

Table 9 FY2018-2019 Expenditure Budget Summary and Fiscal Impact Estimating Factors

Item	City General Fund Expenses (FY2018-2019)	Percent Variable (1)	Annual Variable Expenses	Estimating Factors		Per Capita General Fund Expense	Project Population/ Service Population	Annual Total at Buildout
General Government (2)	$10,480,557	10%	$1,048,056	79,822	Service Pop.	$13.13	86	$1,131
Police (3)	$13,108,731	90%	$11,797,858	79,822	Service Pop.	$147.80	86	$12,730
Innovation and Technology (4)	$3,026,189	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Recreation & Community Services	$8,998,222	75%	$6,748,667	59,897	Population	$112.67	86	$9,704
Planning & Community Development	$9,024,628	50%	$4,512,314	79,822	Service Pop.	$56.53	86	$4,869
Public Works (5)	$18,339,121	75%	$13,754,341	79,822	Service Pop.	$172.31	86	$14,841
Non-Departmental	$19,376,096	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Total Expenditures	**$82,353,544**							**$43,276**

(1) Percentage of costs that are population-dependent, as opposed to fixed costs or costs recovered through fees or charges.
(2) Includes Administration, Administrative Services, and Council and Commissions.
(3) Reflects the contract portion of the police department's budget. To the extent the cumulative effect of new growth triggers the contract terms exceeding the cap agreed upon in 2014, the cost impact may be above that estimated based on the average cost approach.
(4) Formerly known as Public Affairs and includes services such as videography, applications, IT and GIS.
(5) Includes administration, environmental programs, development services,service center, grounds, streets, trees and right of way, facilities and fleet, transportation, and other programs.

Sources: City of Cupertino FY2018/19 Actuals

Net Fiscal Impact of Proposed Project

Table 10 summarizes the fiscal impact of the residential development proposal on the City of Cupertino's General Fund, with forecasted revenues and expenditure estimates based on the methodology described above. The annual fiscal impact of the proposed GPA is estimated at about $71,000.

Table 10 Summary of Fiscal Impact Analysis – Residential Homes at Buildout (2019$)

Item	Annual Fiscal Impact
General Fund Revenues	
Sales Tax (excl. business-to-business sales)	$5,000
Property Tax	$65,000
Property Tax in Lieu of VLF	$34,000
Property Transfer Tax	$3,000
Utility Tax	$2,000
Franchise Fees	$3,000
Total Revenues	**$114,000**
General Fund Expenditures	
General Government	$1,000
Police	$13,000
Recreation & Community Services	$10,000
Planning & Community Development	$5,000
Public Works	$15,000
Total Expenditures	**$43,000**
Net Impact on General Fund	**$71,000**