



**THE CITY OF SAN DIEGO  
M E M O R A N D U M**

DATE: March 26, 2009

TO: Members of the Budget and Finance Committee  
Members of City Council

FROM: Mary Lewis, Chief Financial Officer

SUBJECT: FY 2009 Sales Tax Revenue Update

This memorandum presents the updated sales tax revenue using updated information through March 20<sup>th</sup>, 2009.

TABLE I  
**FY 2009 Sales Tax Revenue Year-End Projections**  
(in millions)

Major General Fund Revenues	FY 2009 Revised Budget	FY 2009 Mid-Year Projection	FY 2009 March Projection	Change FY 2009 Mid-Year / 2009 March Projection
Sales Tax	\$ 216.2	\$ 216.2	\$ 213.2	\$ (3.0)

**Table I** displays the FY 2009 Revised Budget, the FY 2009 mid-year projection, the FY 2009 updated projection, and the corresponding variance for sales tax revenue. The FY 2009 March projection annual rate of growth is -6.5% of FY 2008 unaudited actual receipts compared to the FY 2009 mid-year projection annual rate of growth of -5.2%. The projection is based on the review of actual revenues, County and State tax data and projections, and include updated information gathered from monitoring economic conditions in the local and regional economy. This is a projection, and as such may undergo future revision.

**Sales and Use Tax**

*General Information*

Retailers engaged in business in California must remit sales tax receipts to the State Board of Equalization (BOE) equal to the tax rate specified in the particular jurisdiction in which they operate. The use tax generally applies to the storage, use, or other consumption in California of goods purchased from retailers in transactions not subject to the sales tax. Use tax may also apply to purchases shipped to a California consumer from another state, including purchases made by mail order, telephone, or Internet. The California BOE collects all funds from retailers subject to the sales and use tax and advances payments to local municipalities on a monthly basis. The local jurisdiction sales tax rate is broken into three parts – revenue collected that is remitted to the State of California, revenue that will be Counties, and revenue to Cities. The breakout of the County of San Diego’s sales tax rate is as follows:

SALES TAX RATE	ENTITY PAID TO	REVENUE FOR
4.75%	State of California	General/Local Revenue Funds
0.50%	State of California	Local Revenue Fund
0.25%	State of California	General Fund Revenue
0.50%	State of California	Local Public Safety Fund
0.25%	City of San Diego	General Fund - Triple Flip
0.75%	City of San Diego	General Fund Revenue
0.50%	SANDAG	SANDAG
0.25%	County of San Diego	County Transportation
<b>7.75%</b>	<b>TOTAL SALES TAX RATE</b>	

Economic Drivers

Consumer spending is determined based upon numerous factors, of which growth in per capita income and percent of income spent on goods and services can be the most reliable predictors of sales tax trends. Personal income growth has slowed to less than 4% as of the end of 2008 due to rising unemployment<sup>1</sup>, reduced hiring by new and existing business, and reduced business profits. The State of California has experienced a major increase in unemployment over the last year, rising from 6.8% to 10.5% over the last year; while the City of San Diego’s unemployment level for the same time period has increased from 5.3% to 8.8%, or an additional 25,000 unemployed people, totaling 62,000 unemployed out of a work force of 706,000<sup>2</sup>.

With a rising unemployment rate and the general uncertainty in the economy, consumer confidence has dropped an unprecedented 67% in the last year<sup>3</sup>. With this uncertainty about the economy, consumer savings has risen to provide a hedge against unforeseen circumstances. The average consumer savings rate has risen to 5% of post-tax income (compared to 0.1% the year prior) due to greater uncertainty in the economy and greater need for savings<sup>4</sup>. Business spending is directly linked to consumer spending on goods and services. As consumer discretionary spending drops, the gross receipts of most business sectors have declined and consequentially reduced the amount that is spent by businesses on inventories, new technologies, and creating new jobs.

The City has lost a significant amount of sales tax receipts over the last two years from portions of the local economy most affected by the drop in consumer spending and decline in the housing market. As can be seen from the latest available data for the City’s economic category and segment breakout, there has been a decline in construction and all associated industries, such as materials and light industry. There was also a drop in vehicle sales as would be expected with the decline in consumer spending as well as in the general retail economic category. In reviewing recent economic information for 2009, it is expected that the general retail, construction, and business-to-business categories would be most at risk for continued declines in sales tax receipts due to the drop in consumer / business discretionary spending in addition to the continuing decline in construction and durable goods orders.

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<sup>1,4</sup> U.S. Bureau of Economic Analysis  
<sup>2</sup> CA Employee Development Department  
<sup>3</sup> Consumer Confidence Board

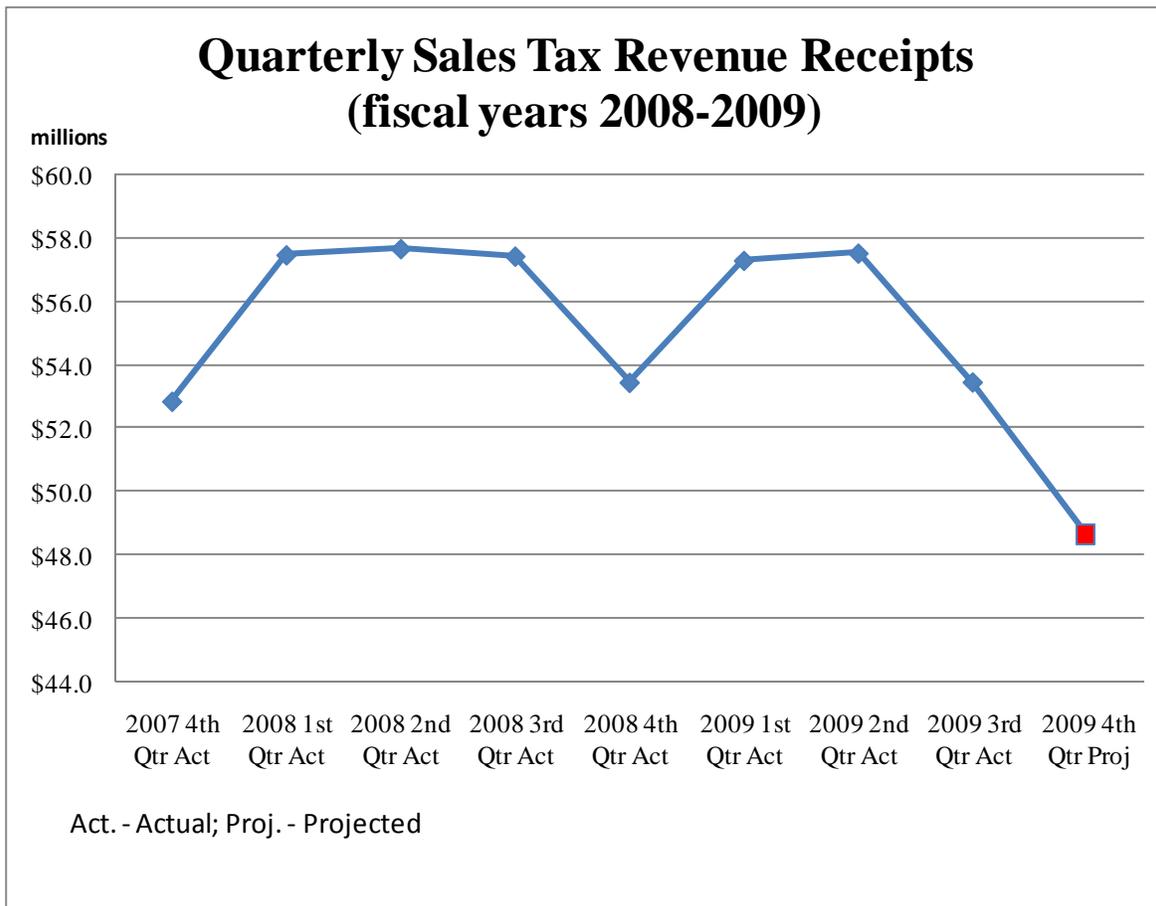
Payment Details

Monthly distributions to the City are based on State estimates which are reconciled on a quarterly basis. The BOE estimates City’s distributions based on the prior year audited receipts including a projected growth rate. On a monthly basis, the State distributes 90% of the amounts allocated in the same period in prior year. After the BOE audits the corrected amount of sales tax due to the City for the quarter, the State then distributes a true-up payment to reconcile payments made during the quarter with actual amounts owed. Payments are made in September, December, March, and June.)

**Sales Tax Forecast**

The BOE issues quarterly State-wide economic growth estimates in taxable sales used in preparing forecasts for estimated monthly distributions. The City reviews this information for possible inclusion in economic forecasting for sales tax revenue. The March quarterly payment for the holiday sales season of 2008 was \$1.4 million less than expected (estimated growth rate of -5% compared to actual -9%). Based on this information, an adjustment has been made to the growth rate for FY 2009 last quarter (from -5% to -9% resulting in additional decrease of \$1.6 million to the projected sales tax revenue.) This revised growth rate reflects a more pessimistic assumption about declining sales tax revenue for the upcoming months. Both of these factors have resulted in the projected sales tax revenue **shortfall of \$3.0 million compared to FY 2009 mid-year projections**.

The graph below illustrates the comparison of sales tax quarterly payments.



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The uncertain nature of sales tax due to the rapidly changing economic conditions leads to vulnerability in the sales tax revenue received by the City. The growth rates published by the State (which are used as guidance for sales tax revenue projections) and economic research the City monitors on an ongoing basis differ widely on expected consumer savings, consumer sentiment, personal income growth, and the housing market amongst other economic factors. There is a wide range of expected economic assumptions regarding revenue contraction in taxable sales. Staff continues to monitor the 2009 estimated sales tax revenue and its effects on FY 2009 year-end projections and on the FY 2010 Proposed Budget.

Mary Lewis  
Chief Financial Officer

cc: Honorable Mayor Jerry Sanders  
Jay M. Goldstone, Chief Operating Officer  
Andrea Tevlin, Independent Budget Analyst