

SRI International



REPORT SUPPORTING APPLICATION
FOR INCORPORATION ELECTION
IN EAST PALO ALTO

March 17, 1981

EPACCI
P.O. Box 50624
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Prepared for:

Institute for the Study of
Community Economic Development
East Palo Alto, California

SRI Project No. HSH-2079

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INTRODUCTION

The following report represents a justification for the application to San Mateo County Local Agency Formation Commission (LAFCo) for permission to hold an incorporation election in the unincorporated area of San Mateo County known as East Palo Alto.

The report consists of two parts: the first part is a description of the East Palo Alto area and some of the relevant trends in recent years; the second part is a fiscal analysis relative to projected revenues, proposed services, and service costs on a "best cost" basis after incorporation. This section includes a summary analysis of the different conclusions in reports prepared by Angus McDonald and Associates and by Kenneth G. Goode. Two appendices are attached: a recent letter from Angus McDonald and Associates, and a copy of the SRI International analysis of the LAFCo's draft environmental report.

This report is based on our analysis of the following documents:

- "Framework for Planning and Population and Housing;" chapters of the preliminary East Palo Alto Community Plan prepared by the San Mateo County Planning Staff, September 1980.
- "Draft Environmental Impact Report for Menlo Park/East Palo Alto Sphere of Influence Study" by San Mateo Local Agency Formation Commission staff, August 1980.
- "East Palo Alto Fiscal Analysis" prepared by Angus McDonald and Associates, October 1979.
- "East Palo Alto Municipal Council Staff Analysis, January 1980.
- Analysis by SRI International of LAFCo staff's "Draft Environmental Impact Report," November 1980 (See Appendix B).
- Other relevant reports and documents.

Under the Knox-Nisbet Act (Government Code, Section 54774), there are eight factors that are to be taken into account by LAFCo agencies when studying spheres of influence changes. These factors are:

- a. The maximum possible service area of the agency and possible service capabilities of the agency.
- b. The range of services the agency is providing or could provide.
- c. The projected future population growth of the area.
- d. The type of development occurring or planned for the area, including, but not limited to, residential, commercial, and industrial development.
- e. The present and probable service needs of the area.
- f. Local governmental agencies presently providing services to such areas and the present level, range, and adequacy of services provided by such existing local governmental agencies.
- g. The existence of social and economic interdependence and interaction between the area within the boundaries of a local governmental agency and the area which surrounds it and which could be considered within the agency's sphere of influence.
- h. The existence of agricultural preserves in the area which could be considered within an agency's sphere of influence and the effect on maintaining the physical and economic integrity of such preserves in the event that such preserves are within a sphere of influence of a local governmental agency.

This report speaks to three of those factors (a, b, and e). Four additional factors have been or are in the process of being answered by the County Planning Department (c and d) the LAFCo staff (f and g) and the SRI response to the LAFCo draft report (g). The remaining factor (h) does not appear applicable at this time because of the small amount of agricultural activity within the area.

Part I
DESCRIPTION OF AREA

East Palo Alto is an unincorporated area in the Southeast part of San Mateo County. Its area is approximately 2½ square miles and its boundaries are equivalent to County Service Area 5. Census tracts 6118, 6119, and 6120 represent the area east of Bayshore Freeway (U.S. Highway 101), and census tract 6121 represents the area west of the Freeway.

Population

Although the final population figures of the 1980 Census will not be available for at least a year, the preliminary census indicates that the 1980 population will be approximately 18,000, about the same as the 1970 Census of 17,837.

The 1970 Census ethnic breakdown for the four census tracts was: 61% Black, 27% Caucasian, 7% Hispanic, and 5% Other. The 1980 figures on ethnic breakdown are not yet available; however, a recent study* indicates that the ethnic nature of the area has gone through a substantial change since 1970. The study indicates there has been a 10% increase in the white and Hispanics population and a 14% decrease in the black population during that period.

Although there are some differences between the four census tracts, they all share the same shopping areas and the same problems of an unincorporated area that is without direct representative control.

Housing

There were approximately 6,400 housing units in 1970 in East Palo Alto. There is some conflict in estimates of the number of new housing units added during the 1970s, ranging from plus-200 to plus-600.

*Menkin-Lucero & Associates.

Based on 1970 Census information, there are differences in housing between the census tracts. Census tracts 6118, 6119 and 6120 had 81% single-family dwellings and of those, 53% were owner-occupied. The Census tract 6121 was 84% multi-family dwellings and 92% renter-occupied. The owner-occupied picture will probably increase west of the freeway through condominium conversions.

Although the median home values have increased during the 1970s (\$18,000 to \$46,000*), this still represents a significantly lower cost than other areas within the mid-Peninsula. However, the San Mateo County Assessor's Office indicates there has been a spectacular growth in the market value of properties being sold in East Palo Alto in the past two years--about 50% per year. This is about twice the rapid inflation rate for most of the surrounding mid-Peninsula area. Another significant trend has been the rapid increase in the use of housing rehabilitation loans within the area. There have been 130 such loans since 1975, and 45 of those were taken out in 1979 alone.

The Angus McDonald report indicated that a major reason for this tremendous increase in comparison with other neighboring areas is the discontinuance of the "redlining" practice as of around 1977. Thus, private mortgage finance money is much more available in East Palo Alto than in the past years. In addition, it is one of the few places in the mid-Peninsula where many homes are still available for under \$100,000. Many families are now considering buying in East Palo Alto who may not have looked for housing there in past years.

*This median figure is the 1979 estimate made by the San Mateo County Planning Department.

Part II

THE MUNICIPAL PLAN FOR THE CITY OF EAST PALO ALTO

The following municipal plan for the proposed City of East Palo Alto is based on three source documents:

- (1) "The East Palo Alto Fiscal Analysis" prepared by Angus McDonald and Associates, Inc., October 1979.
- (2) "The Staff Analysis" of the East Palo Alto Fiscal Analysis prepared by Kenneth G. Goode, January 1980.
- (3) "Analysis of San Mateo County LAFCo Draft Environmental Impact Report to Menlo Park/East Palo Alto and Districts Sphere of Influence Study" prepared by SRI International, November 1980.

Assumptions

This proposed plan is based on the following assumptions and findings:

- (1) Present service levels are maintained or are improved.
- (2) Voters have approved the proposed business license and utility franchise taxes.
- (3) All figures are in constant 1979 dollars.
- (4) There is a negotiated payment by the County of San Mateo to the new city of \$1,263,000, based on revenue collection after successful election and the beginning of first year of operation, and that start-up costs for the new city after election will not exceed \$500,000.
- (5) Sales tax revenue estimates by the Angus McDonald report were overestimated by \$120,800 for the period 1982/83 through 1984/85. Plus, the consultants left out a \$50,000 revenue under A.B. 90 for Fiscal Year 1982/83.
- (6) All employees would not be hired at the top step, which reduces the consultants' salary projections by 3.9%.

- (7) The new city will contract for: legal services, engineering, grounds maintenance, animal control, civil defense, garbage collection, street lighting, traffic signal maintenance, water purchase, and sewage treatment and disposal.
- (8) The new city will be incorporated under the general laws of the State of California and will be a council-manager form of government.
- (9) Water purchase could be reduced by \$60,000 because of new wells; however, only a \$30,000 reduction has been budgeted in order to accumulate a capital outlay reserve.
- (10) Employee benefits (other than Public Safety) have been estimated at 25% of salary, based on prevailing San Francisco-Oakland Bay Area costs as of 1979 for cities of the size and type as East Palo Alto. The Public Safety Department employee benefits are at 30% because of higher prevailing costs.
- (11) Services and supplies are estimated at 30% of total employee costs for all departments except Community Services (40%) because of estimates of current practices and costs within the Bay Area as of 1979 for cities of the size and type as East Palo Alto.
- (12) The initial equipment purchases for police and public works vehicles plus other operating equipment required are included in the estimated \$500,000 startup costs (see page 19).

Budget

The following pages represent the estimated revenues and expenditures for the operation of the City of East Palo Alto. The salaries shown are at top step. However, a reduction of 3.9% has been taken to reflect probable costs for the first 3 years of operation based on staff turnover and usual hiring of new employees at step B of a 5-step salary plan. The total estimated expenditures listed on the next page include all contractual costs. The details of contract expenditures are listed under the separate budgets for each department.

TOTAL ESTIMATED EXPENDITURES

General Government		\$ 318,890
Public Safety Services		1,177,466
Community Development		166,314
Community Services		179,405
Public Works		
Administration	\$158,057	
Streets	102,136	
Water	328,834	
Sanitation	<u>236,219</u>	
Subtotal		\$ 825,246
Contract Services		
Animal Control	9,400	
Civil Defense	3,500	
Garbage Collection	220,000	
Street Lighting	<u>120,000</u>	
Subtotal		\$ 352,900
Total Estimated Expenditures		\$3,020,221

It has been assumed that these estimated expenditures will be constant for the 3-year period 1982/83 through 1984/85, because they are based on constant 1979 dollars.

General Government

Function

The principal function of general government is to provide the city with legislation through its city council and general administration through its city manager. Additional functions are: city clerk, finance administration, personnel administration, management controls, general accounting, purchasing, water accounting, garbage accounting, and legal services by contract.

Budget

<u>Staff</u>	<u>Position</u>	<u>Salary</u>	<u>Total</u>
1	City Manager/City Clerk	\$ 35,000	\$ 35,000
1	Deputy Clerk/Secretary	15,000	15,000
1	Assistant to City Manager	25,000	25,000
1	Accountant	21,000	21,000
2	Administrative Assistant	22,000	44,000
1	Account Clerk	12,500	12,500
2	Staff Clerk	12,500	<u>25,000</u>
	Total Salaries		\$ 177,500
	Less 3.9%		<u>-6,922</u>
	Net Total Salary		\$ 170,578
	Employee Benefits @ 25%		42,645
	City Council @ \$1,800 ea		<u>9,000</u>
	Total Employee Cost		\$ 222,223
	Services & Supplies @ 30%		66,667
	Contract (Attorney)		<u>30,000</u>
	Total Service Cost		\$ 318,890

Public Safety Services

Function

The function of the Public Safety Service Department is to provide for crime prevention, law enforcement, investigation, traffic enforcement, community services, and coordination with the Menlo Park Fire Protection District. The staffing plan would include an investigation team of one sergeant and two patrolmen plus four patrol teams of one sergeant and five police officers on rotating shifts.

Budget

<u>Staff</u>	<u>Position</u>	<u>Salary</u>	<u>Total</u>
1	Director of Public Safety	\$ 30,000	\$ 30,000
1	Lieutenant	26,500	26,500
5	Sergeant	23,500	117,500
22	Police Officer	20,000	440,000
6	Clerk/Dispatcher	13,500	81,000
2	Community Service Officer	15,000	<u>30,000</u>
	Total Salaries		\$ 725,000
	Less 3.9%		<u>-28,275</u>
	Net Total Salary		\$ 696,725
	Employee Benefits @ 30%		<u>209,018</u>
	Total Employee Cost		\$ 905,743
	Services & Supplies @ 30%		<u>271,723</u>
	Total Service Cost		\$1,177,466

Community Development

Function

The function of Community Development is to provide for planning, zoning, and code development and enforcement.

Budget

<u>Staff</u>	<u>Position</u>	<u>Salary</u>	<u>Total</u>
1	Director of Community Development	\$ 28,000	\$ 28,000
1	Associate Planner	22,000	22,000
1	Associate Planner	22,000	22,000
1	Inspector	22,000	22,000
1	Staff Clerk	12,500	<u>12,500</u>
	Total Salary		\$106,500
	Less 3.9%		<u>-4,153</u>
	Net Total Salary		\$102,347
	Employee Benefits @ 25%		<u>25,587</u>
	Total Employee Cost		\$127,934
	Services & Supplies @ 30%		<u>38,380</u>
	Total Service Cost		\$166,314

Community Services

Function

The function of Community Services is to provide for recreation, cultural and age group activities, plus park maintenance (by contract). The following budget is for a core staff only. There are many community services that are available from various state and federal grant programs. The staffing for such programs would come from those fundings.

Budget

<u>Staff</u>	<u>Position</u>	<u>Salary</u>	<u>Total</u>
1	Director of Community Services	\$ 24,000	\$ 24,000
1	Director of Leisure & Cultural Activities	18,500	18,500
1	Recreation Supervisor	16,000	16,000
1	Staff Clerk	12,500	<u>12,500</u>
	Total Salaries		\$ 71,000
	Less 3.9%		<u>-2,769</u>
	Net Total Salaries		\$ 68,231
	Employee Benefits @ 25%		<u>17,058</u>
	Total Employee Costs		\$ 85,289
	Services & Supplies @ 40%		<u>34,116</u>
	Contract (Instructors)		\$ 20,000
	Contract (Gardening)		<u>40,000</u>
	Total Service Cost		\$179,405

Public Works

Function

The function of Public Works is to provide street maintenance, purchase and deliver water, collect sewage and deliver it to treatment plant, and maintain all pipes and facilities for delivering and collections. Street sweeping is not included but could be under contract at a cost of approximately \$40,000 per year.

Total Public Works Budget

Administration (detail on page 13)	\$ 158,057
Streets (detail on page 14)	102,136
Water (detail on page 15)	328,834
Sanitation (detail on page 16)	236,219
Vehicle Maintenance (detail on page 17)	<u>29,671</u>
Subtotal	\$ 854,917
Less Vehicle Maintenance (charged to using departments)	<u>-29,671</u>
Total Service Cost	\$ 825,246

Public Works--Administration

<u>Staff</u>	<u>Position</u>	<u>Salary</u>	<u>Total</u>
1	Director of Public Services	\$ 28,000	\$ 28,000
1	Maintenance Supervisor	24,500	24,500
1	Maintenance Worker II	17,000	17,000
1	Staff Clerk	12,500	<u>12,500</u>
	Total Salaries		\$ 82,000
	Less 3.9%		<u>-3,196</u>
	Net Total Salaries		\$ 78,804
	Employee Benefits @ 25%		<u>19,701</u>
	Total Employee Cost		\$ 98,505
	Services & Supplies @ 30%		29,552
	Contract (Engineering)		<u>30,000</u>
	Total Service Cost		\$158,057

Public Works--Administration

<u>Staff</u>	<u>Position</u>	<u>Salary</u>	<u>Total</u>
1	Maintenance Worker IV	\$ 21,000	\$ 21,000
2	Maintenance Worker III	19,000	<u>38,000</u>
	Total		\$ 59,000
	Less 3.9%		<u>-2,301</u>
	Net Total Salaries		\$ 56,699
	Employee Benefits @ 25%		<u>14,175</u>
	Total Employment Costs		\$ 70,874
	Services & Supplies @ 30%		21,622
	Contract (Signals)		<u>10,000</u>
	Total Service Cost		\$102,136

Public Works--Water

<u>Staff</u>	<u>Position</u>	<u>Salary</u>	<u>Total</u>
1	Maintenance Worker III	\$ 19,000	\$ 19,000
3	Maintenance Worker II	17,000	51,000
1	Account Clerk	12,500	<u>12,500</u>
	Total Salaries		\$ 82,500
	Less 3.9%		<u>-3,218</u>
	Net Total Salaries		\$ 79,282
	Employee Benefits @ 25%		<u>19,821</u>
	Total Employee Cost		\$ 99,103
	Services & Supplies @ 30%		29,731
	Contract (Water Purchase)*		170,000
	Debt Service (Loan)**		<u>30,000</u>
	Total Service Cost		\$328,834

* This represents a \$60,000 reduction in water purchases because of the use of new wells plus the retention of \$30,000 for future capital outlay.

** Annual payment on 5½% 30 year loan from the State of California.

Public Works--Sanitation

<u>Staff</u>	<u>Position</u>	<u>Salary</u>	<u>Total</u>
1	Maintenance Worker III	\$ 19,000	\$ 19,000
1	Maintenance Worker II	17,000	<u>17,000</u>
	Total Salary		\$ 36,000
	Less 3.9%		<u>-1,404</u>
	Total Net Salary		\$ 34,596
	Employee Benefits @ 25%		<u>8,649</u>
	Total Employee Cost		\$ 43,245
	Services & Supplies @ 30%		12,974
	Contract (Treatment Service)		120,000
	Debt Service (Palo Alto)*		<u>60,000</u>
	Total Service Cost		\$236,219

* Annual contract payment to City of Palo Alto for share of capital costs.

Public Works--Vehicle Maintenance *

<u>Staff</u>	<u>Position</u>	<u>Salary</u>	<u>Total</u>
1	Vehicle Mechanic	\$ 19,000	\$ 19,000
	Less 3.9%		<u>- 741</u>
	Net Total Salary		\$ 18,259
	Employee Benefit @ 25%		<u>4,565</u>
	Total Employee Costs		\$ 22,824
	Services & Supplies @ 30%		<u>6,847</u>
	Total Service Cost		\$ 29,671

* These costs are charged back to the using department and are included in the services and supplies budget for those departments..

ESTIMATED REVENUE
(in Thousands)

The following revenue is based on both the McDonald and Goode studies.

<u>Revenue by Source</u>	<u>1982-83</u>	<u>1983-84</u>	<u>1984-85</u>
Property Tax	\$ 536.0	\$ 542.0	\$ 550.0
Sales Tax	216.0	241.9	270.9
Business License Tax *	47.0	52.9	58.9
Utility Franchise Tax *	327.1	374.7	429.9
Licenses and Permits	40.0	40.0	40.0
Fines and Penalties	41.1	41.1	41.1
Use of Money and Property	89.3	93.5	96.6
Property Transfer Tax	16.1	16.4	17.0
Cigarette Tax	48.7	50.7	52.8
Alcoholic Beverage Fees	4.4	4.4	4.4
Vehicle In-lieu Fees	236.2	236.2	236.2
Gas Tax	98.4	67.2	41.7
General Revenue Sharing	162.0	288.0	308.0
A.B. 90 **	50.0	0.0	0.0
Public Works Charges & Fees ***	<u>1,087.0</u>	<u>1,087.0</u>	<u>1,087.0</u>
Total Revenue	\$3,098.3	\$3,135.7	\$3,234.5

* Requires 2/3 voter approval.

These two taxes would be applied to the East Palo Alto area if it were annexed to Menlo Park but would not require an election since Menlo Park currently collects these taxes.

** Grant for police community relations

*** Includes garbage, water, sewer and miscellaneous charges and fees.

THREE-YEAR COMPARISONS OF
REVENUES AND EXPENDITURES
(in constant 1979 Dollars)

	<u>1982/83</u>	<u>1983/84</u>	<u>1984/85</u>
Revenue	\$3,098,300	\$3,135,700	\$3,234,500
Expenditures	<u>3,020,221</u>	<u>3,020,221</u>	<u>3,020,221</u>
	\$ 78,079	\$ 115,479	\$ 214,279

When the one-time payment from San Mateo County estimated at \$1,263,000 is added and the estimated \$500,000 start-up cost is deducted, the City will have a surplus of \$763,000 at the beginning of fiscal year 1982/83. Based on this beginning balance, the accumulated surplus for the 3 years would be as follows:

	<u>1982/82</u>	<u>1983/84</u>	<u>1984/85</u>
Surplus	\$841,079	\$956,558	\$1,170,837

It is suggested that this surplus be budgeted as follows:

	<u>1982/83</u>	<u>1983/84</u>	<u>1984/85</u>
Contingency revolving fund (10% of operating budget)	\$302,022	\$302,022	\$302,022
Capital outlay and equipment replacement *	\$539,057	\$115,479	\$214,279

* This reserve could be used for the estimated \$40,000 cost for street sweeping.

ANALYSIS OF DIFFERENCE BETWEEN
McDONALD AND GOODE REPORTS

The analysis by Angus McDonald and Associates indicated that the incorporation of East Palo Alto was financially infeasible because the estimated revenue projected would not match the estimated expenditures until fiscal year 1984/85.

The Goode staff report indicates that it is financially feasible. The difference between these two opinions is summarized as follows. A more complete discussion of differences appears in Appendix B.

Revenue

The sum of the three years (fiscal 1982/83, 1983/84, and 1984/85) revenue projection by McDonald was \$9,539,300. The same period projection by Goode was \$9,468,500. The \$70,800 difference between these two projections is made up of a reduction of \$120,800 in estimated sales tax revenue and a \$50,000 addition for the remainder of the A.B. 90 grant to the police department.

Expenditures

The McDonald report estimated a per annum expenditure of \$3,259,700 per year. The Goode estimate is \$3,020,221 per year.

The \$239,479 difference is made up of the following estimated expenditure reductions:

	<u>Savings</u>
1. By assuming lower staff salaries at entrance and turnover	\$ 67,500
2. By reduction of two staff positions	62,000
3. Services and supplies (30%) reduced by lower salaries and reduced staff	23,979
4. \$30,000 reduction in payment to water supplier because of new wells	30,000
5. Charging cost of vehicle maintenance to using departments	27,000
6. Elimination of undocumented costs in Public Works budget	<u>29,000</u>
TOTAL	\$239,479

Of course, the principal difference between the two reports was the failure of the McDonald report to take into account the one-time start-up payment from the County of San Mateo. With this one-time payment, the new City of East Palo Alto will be financially feasible, with an accumulated surplus of over \$1 million by the end of fiscal year 1984/85.

Appendix A is a January 13, 1981 letter from Mr. Walter Kiesner representing Angus McDonald & Associates. Mr. Kiesner indicated that the Municipal Council's staff analysis "...is an accurate and professionally sound document. This means that if the assumption made in the staff analysis proves correct, that a City of East Palo Alto could be fiscally feasible."

APPENDICES

Angus McDonald & Associates

2150 Shattuck Avenue Berkeley, California 94704
Telephone (415) 548-5831

January 13, 1981

Thomas W. Fletcher, Director
Center for Public Policy Analysis
SRI International
333 Ravenswood Avenue
Menlo Park, California 94025

Dear Mr. Fletcher:

Thank you for the opportunity to comment on your recently published report, Analysis of Draft Environmental Impact Report to the Menlo Park/East Palo Alto and Districts Sphere of Influence Study (EIR). I have also reviewed the East Palo Alto Municipal Council's staff analysis, which was the quantitative basis for your report.

Our East Palo Alto Fiscal Analysis is well summarized by the following conclusion it contained:

"The fiscal analysis of East Palo Alto indicates that incorporation at the present time, given the assumptions we have made concerning municipal service costs and revenues, is infeasible. The analysis does provide a basis for further study and also makes explicit the key obstacles facing East Palo Alto.

Different conclusions about the costs of municipal services can be debated endlessly. We feel that the cost estimates provided, while not beyond reproach, are generally representative of the effort required to maintain existing service standards and to make necessary, generally minor improvements. However, lower levels of service or costs below our estimates would result in an improved fiscal balance. On the revenue side, we feel our estimates to be representative of a best case assumption concerning East Palo Alto. Achieving these revenues would require a concerted effort on the part of the community to improve property value and, most importantly, recover sales tax revenues which currently finance public services in Menlo Park, Palo Alto, other nearby areas."

January 13, 1981
Mr. Thomas W. Fletcher
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While our fiscal analysis produced a negative conclusion, it opened the door to more detailed analysis of problem areas. Our fiscal analysis was subjected to extremely close scrutiny by the East Palo Alto Municipal Council staff, who subsequently revised the fiscal analysis. This effort applied the same methodology as applied during the initial fiscal analysis, applying different assumptions and making significant corrections to our analysis of sewer plant capital improvements and water costs. My review of the staff analysis indicates that it is an accurate and professionally sound document. This means that if the assumptions made in the staff analysis prove correct, that a City of East Palo Alto could be fiscally feasible.

It must be noted that feasibility is dependent upon new special taxes and possibly increased service fees being approved in East Palo Alto. I recommend strongly that any decision to incorporate be contingent upon voter approval of special taxes, at the same time as the incorporation election. I suggest that approval be sought for a set of special taxes that, at maximum, would raise the amounts required under our assumptions. Our original estimate of the total additional revenue or special taxes required was approximately \$100 per household in 1979/80. If the collectively more optimistic assumptions of the staff analysis (with which you apparently concur) come to pass, the rate for the special tax levies can be lowered. If they do not, or if the adopted 1981/82 state budget reduces funding available to cities, the new city may still be financially feasible.

If you have further questions, please feel free to call.

Yours very truly,

ANGUS McDONALD & ASSOCIATES, INC.



Walter F. Kieser

cc: Kenneth Goode
B. Sherman Coffman
Gordon Shriver



Appendix B

ANALYSIS OF
DRAFT ENVIRONMENTAL IMPACT REPORT
TO THE MENLO PARK/EAST PALO ALTO AND DISTRICTS
SPHERE OF INFLUENCE STUDY

Prepared by: Phillip E. Vincent
Thomas W. Fletcher

For: Institute for the Study of
Community Economic Development

November 6, 1980

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ANALYSIS OF
DRAFT ENVIRONMENTAL IMPACT REPORT
TO THE MENLO PARK/EAST PALO ALTO AND DISTRICTS
SPHERE OF INFLUENCE STUDY

Introduction

In August of this year, the Institute for the Study of Community Economic Development, on behalf of the East Palo Alto Citizens' Committee on Incorporation, contracted with SRI International to: "Prepare a formal application to the San Mateo County's Local Agency Formation Commission for permission to hold a city incorporation election in the area known as East Palo Alto."

One of the major tasks in our scope of work involves a review and comment on LAFCO's Environmental Impact and Sphere of Influence Report. The attached material is in response to that task.

Assumptions

For the purpose of this review, it is assumed that the two viable alternatives are incorporation or annexation to Menlo Park. It is further assumed that for either annexation or incorporation the entire East Palo Alto area will be included rather than a division between the areas east and west of the Bayshore Freeway.

The reasons for these assumptions are (1) the East Palo Alto area needs some form of government structure offered to them for voter decision, (2) annexation to Palo Alto would involve a very complex County boundary alteration and the potential advantage of such an annexation does not appear worth the effort, and (3) the division of the East Palo Alto area would be detrimental to the remainder of the East Palo Alto area under either the annexation or incorporation alternatives.

Overview

The LAFCo is strongly opposed to incorporation and is apparently in favor of annexation to Menlo Park. Their position can best be summarized by looking at pages 166-168 under the heading "Unavoidable Adverse Impacts." This section lists 10 adverse impacts relative to incorporation and only 2 relative to annexation to Menlo Park.

The 10 adverse impacts can be summarized into 3 basic issues:

- (1) "...further isolation of the East Palo Alto community from neighboring communities..." (A)
- (2) Negative planning and environmental impacts:
 - "Decrease in quantity and quality of housing..." (B)
 - "...Dumbarton Bridge access would divide the community..." (C)
 - "...The disadvantage of long-term environmental goals..." (D)
- (3) Shortfall of revenues based on projected expenditures (B, D, E, F, G, H, I, J).

Our analysis of the negative impacts relative to incorporation listed by LAFCO are that they are either subjective with limited justification (isolation and negative planning capability) or they appear to be based on incomplete objective information (Finance).

The majority of negative impacts are based on the assumption that there would be: "A substantial revenue shortfall over the five-year projection period" (page 167). There is also the following statement in the executive summary: "The revenue shortfall shows incorporation to be infeasible at present" (page 13).

Our own financial analysis uses both the "East Palo Alto Fiscal Analysis" prepared by Angus McDonald and Associates and the staff analysis of the McDonald report prepared by Kenneth Goode and staff for the East Palo Alto Municipal Council.

The LAFCo report relies heavily on the McDonald report and incorporates large portions of it in their material. However, the LAFCo report does not appear to use any of the Kenneth Goode material even though it is referenced on page 177 of their report under the heading "List of Documents Consulted."

The following is our analysis of the potential fiscal consequences of incorporation vs. annexation to Menlo Park.

FISCAL ANALYSIS

In this section, we have assembled several elements of comparative fiscal data to evaluate the financial feasibility of incorporation of East Palo Alto into an independent city. The figures assembled in Tables 1 and 2 are taken from the generally high-quality reports by the consultant, Angus McDonald and Associates ("East Palo Alto Fiscal Analysis," October 1979), and the staff of the East Palo Alto Municipal Council under the direction of Administrative Officer, Kenneth G. Goode ("Staff Analysis: East Palo Alto Fiscal Analysis," January 15, 1980). Unfortunately, the Draft Environmental Impact Report of August 1980 did not include the important reanalysis by Goode and his staff of the basic McDonald and Associates' effort in presenting conclusions on the financial feasibility of a prospective new city.

In the Goode report, a careful evaluation of the expenditure and revenue analyses of McDonald and Associates was made. On the expenditure side in particular, the findings were that most of the government staff positions had been assumed to be at rather high starting salaries. Based on a careful review of real staffing needs and likely salaries that need to be paid in a competitive labor market, the Goode report finds that 1980-81 total operating expenditures (in 1979 dollars) for a new city with all the major functions should run \$3,040,600. This ("Scenario IV") estimate--used in the construction of Table 1 below--is \$134,500 (4.2%) below the estimates of McDonald and Associates, \$3,175,100 (labeled "Scenario I" in the Goode report).

On the revenue side, the Goode report generally accepts the estimates of McDonald and Associates. The former does add in A.B. 90 funds of \$50,000 in the projections through 1982-83. And Goode reduces the estimates for sales tax collections starting in 1983-84 since Goode did not believe that significant improvements in local shopping centers could be assumed as was done by McDonald and Associates. Thus, by the end of

Table 1

EAST PALO ALTO INCORPORATION
REVENUE AND EXPENDITURE ESTIMATES:
FISCAL YEARS 1982-83 THROUGH 1984-85

	<u>1982-83</u>	<u>1983-84</u>	<u>1984-85</u>
<u>Revenues by Sources</u>			
Property Tax	\$ 536.0	\$ 542.0	\$ 550.0
Sales Tax	216.0	241.9	270.9
Business License Tax	47.0	52.9	58.9
Utility Franchise Tax	327.1	374.7	429.9
Licenses and Permits	40.0	40.0	40.0
Fines and Penalties	41.1	41.1	41.1
Use of Money and Property	89.3	93.5	96.6
Property Transfer Tax	16.1	16.4	17.0
Cigarette Tax	48.7	50.7	52.8
Alcoholic Beverage Fees	4.4	4.4	4.4
Vehicle In-lieu Fees	236.2	236.2	236.2
Gas Tax	98.4	67.2	41.7
General Revenue Sharing	261.0	288.0	308.0
A.B. 90	50.0	0.0	0.0
Service Charges and Fees	<u>1,087.0</u>	<u>1,087.0</u>	<u>1,087.0</u>
Subtotal: Annual Revenues	\$3,098.3	\$3,135.7	\$3,234.5
One-time Transfer of Funds for City Start-up by San Mateo County (estimate for 1980-81)	<u>1,263.0</u>	--	--
Total Revenues	\$4,361.3	\$3,135.7	\$3,234.5
<u>Expenditures by Department/Function</u>			
General Government	\$ 321.5	\$ 321.5	\$ 321.5
Police	1,188.5	1,188.5	1,188.5
Community Development	167.9	167.9	167.9
Community Services	180.8	180.8	180.8
Public Works	<u>769.0</u>	<u>769.0</u>	<u>769.0</u>
Subtotal	\$2,627.7	\$2,627.7	\$2,627.7
Animal Control	9.4	9.4	9.4
Civil Defense	3.5	3.5	3.5
Garbage Collection	220.0	220.0	220.0
Street Lighting	<u>120.0</u>	<u>120.0</u>	<u>120.0</u>
Subtotal: Annual Operating Expenditures	\$2,980.6	\$2,980.6	\$2,980.6
One-time City Start-Up Expenses	<u>500.0</u>	--	--
Total Expenditures	\$3,480.6	\$2,980.6	\$2,980.6
<u>Net: Revenues Less Expenditures</u>	\$ 820.7	\$ 155.1	\$ 253.9
<u>Accumulated Funds at End of Fiscal Year</u>			
<u>Contingencies and Capital Improvements</u>	\$ 820.7	\$ 975.8	\$1,229.7

Source: Based on tables and analyses in Kenneth G. Goode, Staff Analysis: East Palo Alto Fiscal Analysis, January 15, 1980. "Scenario IV" expenditure estimates and revenues estimates are assumed. All figures are in thousands of 1979 dollars.

the five-year projection period, the Goode report estimates revenues of \$3,234,500 in 1984-85--\$63,800 (1.9%) below the projection in the McDonald and Associates' report.

Table 1 shows the revised projections in the Goode report for both revenues and expenditures as well as a netting of revenues less expenditures and an estimate of accumulated funds and capital improvements for contingencies at the end of the fiscal year. This table has collected the results of several tables in the Goode report starting with Fiscal Year 1982-83 and added two important elements noted in both the McDonald and Associates and Goode reports but perhaps not made completely clear even in the latter document.

First, Goode's projections indicate that an incorporated East Palo Alto would have regular annual revenues in excess of regular operating expenditures in 1982-83 (\$3,098,300 less \$2,980,600). This year is the first really important one in the analysis since the best timing of an incorporation election (assumed to be successful) would be July 1981 with the new city taking full responsibility for its new functions in July 1982. The new city would then be on a path of increasing positive annual net revenues, according to the projections.

Second, the county is required to build up a contingency fund for a new city before the latter takes full responsibility for its own operations. And there are one-time start-up ("front end") costs that will have to be paid while the city hires and trains new staff members /and establishes its operating practices. In Table 1, a one-time transfer of funds from San Mateo County of \$1,263,000 is shown in the first column (1982-83) under Revenues while a start-up cost estimate of \$500,000 is shown in the same column under Expenditures. In actuality, both the one-time transfer of funds and the start-up expenses might take place in the previous year, but they are shown here for convenience as taking place in 1982-83 to suggest that the new city would end its first fiscal year of independent operations with a substantial amount of funds for contingencies and capital improvements (in the range of the \$820,700 shown at the bottom of the 1982-83 column). The estimate of funds available for a one-time transfer is actually for 1980-81 and is likely to be understated.

On the other hand, the \$500,000 start-up cost is only a guess made in the Goode report with no analytical support. Thus, the city is likely not only to be financially viable starting in 1982-83 but also will start off with a rather healthy contingency and capital improvements fund to supplement the projects likely to be completed by San Mateo County and other government agencies. The Goode report shows contingency funds balances of \$736,700 at the end of 1982-83 after certain set-asides for water and sanitary capital improvements.

Table 2 addresses an alternative for East Palo Alto that received encouragement in the "Draft Environmental Impact Report" fiscal analysis summaries: annexation of East Palo Alto to the City of Menlo Park. The McDonald and Associates report devotes a few pages in an appendix to indicating how there might be major economies in annexation to Menlo Park. However, the treatment is highly incomplete. Thus, Table 2 was derived by the present authors from partial estimates by McDonald and Associates of revenues and expenditures for East Palo Alto for 1978-79. The bracketed amounts in Table 2 are drawn from various tables in the McDonald and Associates report that appeared to be consistent with the estimates of the impact of annexation on Menlo Park finances and estimates for the status quo (i.e., East Palo Alto continuing as an unincorporated section of San Mateo County).

Both the McDonald and Associates and Goode reports indicate that there was a net subsidy from the rest of San Mateo County to East Palo Alto in 1978-79 of \$885,700 (\$2,908,100 in revenues less \$3,793,800 in expenditures). Unfortunately, the revenue side derivation for this amount was not laid out clearly in the reports. Thus, it is difficult to reconstruct how this estimated amount of subsidy was determined. The first column of Table 2 (San Mateo County) presents our attempt to indicate revenue flows from and expenditures in East Palo Alto as consistently as possible with the revenue and expenditure categories in Table 1 above. On the expenditure side, the total of \$3,296,900 differs from the above McDonald total expenditures figure by the exclusion of expenditures for fire protection and libraries, government functions that would not be taken over by either a new city in East Palo Alto or by Menlo Park in case of annexation to the latter. The bracketed amounts

Table 2

COMPARISONS OF REVENUES AND COSTS FOR EAST PALO ALTO
FOR PRESENT CASE OF SAN MATEO COUNTY AND SPECIAL DISTRICTS SERVICE
PROVISION VERSUS ANNEXATION TO THE CITY OF MENLO PARK (1978-79 DATA)

<u>Revenues by Source</u>	<u>San Mateo County</u>	<u>City of Menlo Park</u>
Property Tax	\$ 350.0	\$ 350.0
Sales Tax	151.0	151.0
Business License Tax	n.c.	23.5
Utility Franchise Tax	n.c.	9.8
Licenses and Permits	40.0	40.0
Fines and Penalties	41.0	41.0
Use of Money and Property	50.0	50.0
Property Transfer Tax	15.8	31.0
Cigarette Tax	45.0	45.0
Alcoholic Beverage Fees	3.7	3.7
Vehicle In-lieu Fees	191.0	191.0
Gas Tax	160.0	160.0
General Revenue Sharing	<u>233.0</u>	<u>233.0</u>
Subtotal	\$1,280.5	\$1,329.0
A.B. 90	[50.0]	[50.0]
Service Charges and Fees	<u>[1,087.0]</u>	<u>[1,087.0]</u>
Total Revenue	[\$2,417.5]	[\$2,466.0]
 <u>Expenditures by Department/Function</u>		
General Government	\$ 231.2	\$ 280.0
Police	1,472.1	850.0
Community Development	36.2	80.0
Parks and Recreation	169.7	[169.7]
Public Works (excluding Sanitation)	814.5	[814.5]
Sanitation	<u>280.8</u>	<u>[280.8]</u>
Subtotal	\$3,004.5	[\$2,475.0]
Animal Control	8.4	[8.4]
Civil Defense	[3.5]	[3.5]
Refuse Disposal	160.5	[160.5]
Street Lighting	<u>[120.0]</u>	<u>[120.0]</u>
Total Expenditures	[\$3,296.9]	[\$2,767.4]
 <u>Net: Revenues Less Expenditures</u>	 [(-\$ 879.4)]	 [(-\$ 301.4)]

n.c. - Not collected by San Mateo County

[] - Items estimated by the present authors; see text.

Source: Angus McDonald and Associates, East Palo Alto Fiscal Analysis, October 1979. In particular, see Tables I-1, IV-1, B-5, B-6, and B-7 and associated analysis. When small differences in estimates for revenues existed, revenue estimates for Menlo Park were used. All figures are in thousands of current dollars.

for civil defense and street lighting are our additions that were not in the McDonald and Associates totals yet are budget items included in the Goode fiscal analyses presented in Table 1 above. On the revenue side, A.B. 90 funds and service charges and fees consistent with the data on Table 1 have been added to the revenue data in the McDonald and Associates report. The deviation of the \$2,908,100 revenue estimate by the latter could not be documented by us. Our Net Revenues Less Expenditures estimates, i.e., the effective subsidy from San Mateo County given our reconstruction of the figures, is \$879,400, which is close to the subsidy estimate of \$885,700 indicated in the McDonald and Associates report.

The second column of Table 2 is our attempt to complete the analysis of what annexation to Menlo Park would mean to that city from a fiscal viewpoint. Expenditure increase estimates for annexation to Menlo Park were shown for only three functions by McDonald and Associates--General Government (\$280,000), Police (\$850,000), and Community Development (\$80,000). We have added in the expenditures for the other functions at the level estimated for San Mateo County (first column) for lack of a better procedure. Furthermore, on the revenue side, we added in A.B. 90 funds and Service Charges and Fees for consistency with the estimates for San Mateo County on this table and with the Table 1 array. The striking thing about the McDonald and Associates conclusions about annexation to Menlo Park, accepted and repeated nearly verbatim in the "Draft Environmental Impact Report," is that revenues of \$1,329,000 (page 138) are compared with the total for only three expenditure categories--of \$1,210,000 for annexation and \$1,714,000 for incorporation (page 140)--to support the conclusion that annexation is highly efficient. The major function where such economies are supposed to occur (compared with service provision by San Mateo County) is in police services. There is no discussion of why Menlo Park is either very much more efficient than the (much larger) San Mateo County Sheriff's Department or will have much less demand from East Palo Alto placed on its police department after annexation compared with the present situation for the county. Police service costs are estimated to drop by \$622,100 (42.3%) with annexation. Other service costs are projected not to rise sufficiently to outweigh the savings in the police area, it appears.

In the other service areas, comparative per capita expenditure estimates presented by McDonald and Associates suggest that the additional expenditures of Menlo Park necessitated by annexation of East Palo Alto would be about the same as those presently made by San Mateo County. Thus, the bracketed items for expenditures in the second column are the same as the expenditure estimates by function in the first column. The end result for our completion of the analysis for annexation is that the Net Revenues Less Expenditures would be a subsidy by (loss to) Menlo Park of \$301,400 per year for 1978-79. However, this estimate should be reconsidered both from a more complete assembly of the appropriate data by McDonald and Associates and/or Goode and Staff and in comparison with the revenue and expenditure projections for the later years. As Table 1 indicates, revenues are projected to be much higher in later years and expenditures significantly lower than the data used for constructing Table 2 suggest.

To summarize, it is quite likely that East Palo Alto is financially viable as an incorporated city and that annexation to Menlo Park does not yield the level of financial savings projected by McDonald and Associates or LAFCo, although some cost savings could well occur. The annexation issue requires a much more complete investigation, comparable to that done for incorporation.

Based on this financial analysis, it would appear that a majority of the negative impacts listed by LAFCo are either not correct or would require extensive additional study or justification before they could be acceptable.

PLANNING ANALYSIS

Job/Housing Imbalance

There are a number of references in the LAFCo Report that indicate that the so-called jobs/housing imbalance in the Mid-Penninsula area would be adversely affected if the East Palo Alto area were to incorporate rather than annex to Menlo Park. This assumption is apparently based on the so-called revenue shortfall projected for incorporation.

There are a number of difficulties in trying to reconcile this LAFCo conclusion. The first problem is that our analysis indicates that a revenue shortfall is more likely under annexation than under incorporation. The second problem is that San Mateo County currently has under preparation a comprehensive plan for the East Palo Alto area. This plan would include housing, commercial, and industrial elements. In reference to this plan, the LAFCo report, beginning at the bottom of page 4, states: "Staff further recognizes that the East Palo Alto Community Plan, when complete, will provide the basis for future planning decisions for the area under any of the alternatives considered in the Sphere of Influence Study. The East Palo Alto area is mostly urbanized and, as such, equivalent levels of service would be required under each alternative. Land use policies will vary little from those set forth in the Community Plan, whichever sphere of influence is adopted by LAFCo. The Plan, after review and acceptance by the local community, should guide the physical development of East Palo Alto, regardless of the governmental structure that is eventually decided upon by LAFCo and the community." This would seem to indicate that LAFCo itself does not believe that incorporation would have that severe an impact.

The third problem is that it is difficult to see how an area that has only 250 undeveloped acres left could have an impact one way or another on a job/housing imbalance for the entire Mid-Penninsula area.

A fourth problem is that LAFCo apparently believes that the East Palo Alto community is not concerned about the preservation and improvement of their own housing stock. Indications are that this area is already involved in a major local effort to revitalize and protect this housing area. There are also strong indications that the neighborhoods in East Palo Alto will not tolerate adverse industries and commercial intrusion within their area.

A fifth problem is the apparent contradiction in the LAFCo report relating to housing. On page 85, they state: "East Palo Alto is one of the few areas in San Mateo County where persons of low and moderate income can afford to live. The impact on affordable housing, therefore, could be significant if enhancement of the tax base is a prerequisite to incorporation." However, on page 86, two of the suggested mitigation measures state: "D. Give extensive consideration to applications to convert apartments to condominiums

so as to lessen the displacement effect on persons of low and moderate income. E. Encourage higher income housing to balance the East Palo Alto community and generate new income." Also on page 132, Menlo Park is encouraged to: "E. Menlo Park should develop policies to encourage the construction of higher income housing in East Palo Alto." These statements would seem to indicate that LAFCo is desirous of reducing the available low and moderate income housing in the East Palo Alto area in order to achieve this job/housing imbalance.

Dumbarton Bridge Access

One of the unavoidable negative impacts (6.2.c-page 167) listed for incorporation is the problem of access roads to the new Dumbarton Bridge. This is not listed as an unavoidable negative impact relative to annexation (6.3-page 168). However, the referenced mitigation solutions for both incorporation and annexation are basically the same (pages 89 and 133).

Isolation

The remaining unavoidable negative impact listed relative to incorporation is (6.2.a-page 167): "The further isolation of the East Palo Alto community from neighboring communities." This comment has been made a number of times throughout the report, but there appears to be no justification for this conclusion. At present, the East Palo Alto community has a directly elected municipal council that has been in existence since 1967. Although they have only advisory authority, they nevertheless represent an opportunity for political involvement within San Mateo County and the so-called neighboring communities. Incorporation would assure a continuing representative participation within the southern San Mateo County area. Annexation, on the other hand, does not appear to offer a similar assurance of representation. There is a recommendation on page 135 which seems to indicate that Menlo Park would have to amend its charter to provide for additional council members and go to district elections in order to prevent so-called isolation. This was not done when the Belle Haven area was annexed in 1948, and is there any reason to expect the Menlo Park residents would be willing to change their government structure in

order to accommodate the East Palo Alto area? It should also be pointed out that if this solution were to be recommended it would then require an affirmative vote by both East Palo Alto for annexation and by Menlo Park for charter change. The risk would be run that the area could be annexed without charter ammendment. Based on this, it would appear that potential isolation would more likely be an unavoidable negative impact relative to annexation rather than incorporation.

Conclusion

Based on the above analysis, it would appear that almost all of the "unavoidable negative impacts" listed in the LAFCo report relative to incorporation (page 167) are either incorrect, unsubstantiated, or purely subjective. On the other hand, it would appear that there should be a substantial increase in the so-called unavoidable negative impacts listed under Menlo Park annexation. This is particularly true, based on our financial and planning analysis. It is our opinion that incorporation is, in fact, feasible and justifiable for the East Palo Alto area.