

*Proposition C: Mission Bay Lease Revenue Charter Amendment Proposal*

**Board Action:**

**OPPOSE**

**Rationale:**

The proposed charter amendment to adjust the formula that allocates Mission Bay Park lease revenues to maintenance needs within the park and eliminates the ability of City officials to suspend this funding in favor of other general fund priorities unnecessarily reduces budgetary flexibility.

The proponents of the measure point to recent suspensions of maintenance funding for Mission Bay Park and the accumulation of deferred maintenance throughout the Park as threatening this asset's unique ability to generate lease revenues for the City. While data shows that City officials have not lived up to the funding commitment of Park maintenance (in other words, the proponents' assertions regarding inadequate maintenance funding are valid), earmarking funds through a ballot measure ("Ballot Box Budgeting") has historically been frowned upon by SDCTA and represents poor public policy.

**Background:**

The proposed Charter Amendment to the Mission Bay Ordinance, which dictates the allocation of Lease Revenues from Mission Bay Park, requires the City of San Diego to allocate a more significant portion of the revenues generated from Mission Bay to the Mission Bay Park Improvement Fund (MBPIF). This proposal designates 75% of lease revenues generated from Mission Bay Park (above \$23 million until 2014, above \$20 million afterward) for Capital Improvements within the Mission Bay Park Improvement Zone, meaning that operating expenditures such as employee salaries may not be paid for with these earmarked funds. The proposal allocates the remaining 25% of revenue in excess of \$20 million generated from the Park to the Regional Park Improvement Fund (RPIF), which helps address capital improvements and deferred maintenance to other regional parks.

The proposal eliminates the annual \$5 million cap (\$2.5 million to each) on allocations to the MBPIF and RPIF, and disallows the reduction of operations and maintenance budget allocations to the park in greater proportion than any reduction to the overall Park & Recreation budget. In other words, the measure somewhat mitigates the potential for the additional allocation of funds for capital improvements to Mission Bay Park (MBP) to be negated by the reallocation of existing expenditures to operating costs or capital expenditures associated with the Park.

## Fiscal Impact

The proposed Charter Amendment caps the amount of annual revenue derived from MBP rents and concessions allocated to the General Fund at \$20 million. Additionally, the elimination of the cap on allocations to the MBPIF and RPIF allows the amounts dedicated to these two funds to exceed \$2.5 million each, although as a concession to the Independent Budget Analyst (IBA), the proponents agreed to a three-year imposition of the \$2.5 million cap on the regional park improvement fund. The elimination of the cap represents the major policy change regarding the allocation of excess revenue funds to the RPIF (the percentage of Park revenues in excess of \$20 million remains the same), while the MBPIF experiences not only an elimination of the \$2.5 million maximum, but a substantial increase in the percentage of Park revenue above \$20 million dedicated to this source. As *Table 1* shows, with the fiscal ramifications of this proposal in effect, the MBPIF and RPIF would receive additional revenues that otherwise would have been allocated to the City's General Fund. The forecasted fiscal impacts to both Improvement Funds and the corresponding loss to the General Fund from FY 2009 – FY 2016 are provided below.

<b>FY</b>	<b>Estimated Lease Revenue</b>	<b>General Fund</b>	<b>Mission Bay</b>	<b>Regional Parks</b>	<b>Annual Loss to General Fund</b>
2009	\$29,867,208	\$24,933,604	\$2,466,802	\$2,466,802	
			<b>75% of Excess</b>	<b>25% of Excess</b>	
2010	\$30,763,224	\$23,000,000	\$5,263,224	\$2,500,000	\$2,763,224
2011	\$31,686,121	\$23,000,000	\$6,186,121	\$2,500,000	\$3,686,121
2012	\$32,636,705	\$23,000,000	\$7,136,705	\$2,500,000	\$4,636,705
2013	\$33,615,806	\$23,000,000	\$7,961,854	\$2,653,951	\$5,615,806
2014	\$34,624,280	\$23,000,000	\$8,718,210	\$2,906,070	\$6,624,280
2015	\$35,663,008	\$20,000,000	\$11,747,256	\$3,915,752	\$10,663,008
2016	\$36,732,899	\$20,000,000	\$12,549,674	\$4,183,225	\$11,732,899

Source: IBA Report 08-85. July 25, 2008

## Theoretical Foundation

The rationale given by the proponents of the charter amendment for requiring an additional allocation of MBP revenues towards capital upkeep/restoration of the Park as well as other regional parks centers on the historically insufficient investment in capital upkeep for the park itself, given the annual revenues generated from Mission Bay Park. Table 2 below displays funding under the current ordinance from FY 2005 – FY 2008.

Table 2: Mission Bay Lease Revenue Allocations: 2005 - 2008				
		25% > \$20M	25% > \$20M	
FY	Lease Revenue	Mission Bay	Regional Parks	Net to General Fund
2005	\$23,177,612	Ordinance	Ordinance	\$23,177,612
2006	\$27,020,561	Suspended	Suspended	\$27,020,561
2007	\$27,383,052	\$1,940,200	\$1,940,200	\$23,502,652
2008	\$27,800,000	\$1,950,000	\$1,950,000	\$23,900,000

While the expenditure on capital improvements represents a valid and important category of expenditure, this proposal decidedly grants priority to the capital improvements in MBP over all other General Fund expenditures. For the sake of discussion of this measure, consider only three alternative City expenditures, (funds allocated towards reducing other maintenance-deferred assets owned by the City of San Diego, another unidentified General Fund need and a future emergency need) and the use of funds in excess of \$23 million for FY 2010 – FY 2014 and in excess of \$20 million in any following year.

Furthermore, suppose that the benefits derived from the different spending options are such that funding these options produces benefits in the following fashion:

$B = \text{Total Benefit} = f(E)$ ; where  $E = \text{General Fund Expenditure}$ ,

And the various funding options produce benefits such that:

Mission Bay Park:  $B_{MBP} = E^{1/3}$

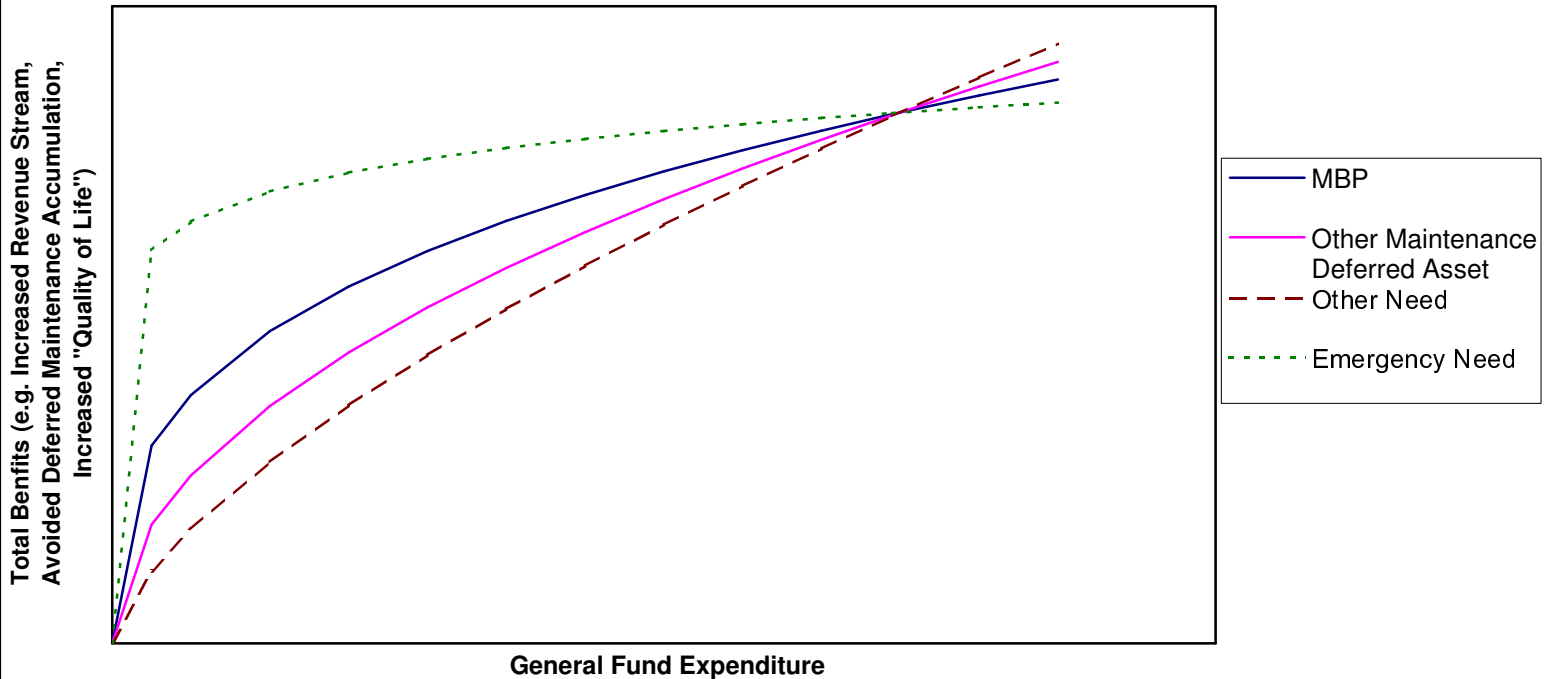
Other Deferred Maintenance Asset:  $B_{other} = E^{1/2}$

Other Unidentified Need:  $B_{NEED} = E^{2/3}$

Emergency Need:  $B_{EMERGENCY} = E^{1/10}$

The above scenarios illustrate the theoretical benefits associated with levels of funding for the four categories of City assets in this framework. Provided that the benefits associated with funding MBP ( $B_{MBP}$ ) with the excess lease revenue funds are greater than the benefits associated with expenditure options, this proposal passes a cost-benefit test. However, as the graphical presentation of the fictitious functional forms shows, if a need requiring general fund dollars arises with greater immediate marginal benefits, this proposed Charter Amendment locks in these excess funds, forcing the City to spend the dollars inefficiently. This concept is displayed prominently in the graph below by the “Emergency Need” at all x-axis points  $\leq 1$ , and less prominently by the varying rates of growth in benefits depending on the x-axis point of the function(s) in question (explained in greater detail in Footnote 1 on page 4).

**Theoretical Foundation of Proposal: Impact of Capital Upkeep or Other General Fund Expenditure on MBP vs. Other City Assets or Needs**



The proponents of the measure assert that Mission Bay Park produces benefits (directly through lease revenues and indirectly by providing an additional attraction to visitors, in turn creating additional economic gains for the City) in a fashion that other City assets do not. In other words, they assert that the benefits of maintaining Mission Bay Park in comparison to other uses of the excess funds provide the highest relative marginal benefit. The proposal passes a cost-benefit test until a scenario in which a greater marginal benefit exists, as displayed above by the “Emergency Need” scenario. Additionally, after a certain amount of funding for any purpose, diminishing returns reduce the additional benefits provided by funding that particular need relative to all others. In the case of such a scenario, prohibiting the ability of City officials to spend funds in a more beneficial manner results in inefficiency, rendering this proposal flawed.<sup>1</sup>

<sup>1</sup> As the theoretical foundation is presented here, taking the first derivative of each function and plugging in the current level of General Fund Expenditure ( $E$ ) reveals the expenditure option providing the greatest relative marginal benefit. For example: compare the *marginal* benefits with theoretical values for  $E$  for Mission Bay Park and for another General Need:

$$\frac{\partial B_{MBP}}{\partial E} = (1/3) E^{-2/3}$$

$$\frac{\partial B_{NEED}}{\partial E} = (2/3) E^{-1/3}$$

Setting these two partial derivatives equal provides a solution of  $E \approx .63$

Therefore, when  $0 \leq E \leq .63$ ,  $\frac{\partial B_{MBP}}{\partial E} > \frac{\partial B_{NEED}}{\partial E}$ ; when  $.63 \leq E$ ,  $\frac{\partial B_{MBP}}{\partial E} < \frac{\partial B_{NEED}}{\partial E}$ ; \*Note that the key to the solution is not the value of .63, but the fact that such a value exists! (Cont'd on next page).

The theoretical analysis presented above clearly articulates the rationale behind the IBA's expressed concerns regarding "actions to reduce both General Fund revenues and budgetary flexibility by dedicating general purpose revenues for specific purposes, especially in light of economic uncertainty and budgetary constraints, and the City's inability to suspend these allocations in the event of a fiscal emergency."<sup>2</sup>

### *Diminishing Marginal Returns*

The constraint applied by available lease revenues acts as a method of prohibiting expenditure on park maintenance so as to potentially mitigate the impact of diminishing returns. In other words, only earmarking funds above the lease revenue level of \$20 million somewhat prevents an exorbitant amount of expenditure on Capital Improvements in Mission Bay Park. However, the fact that this proposal disables the City from allocating funds away from park maintenance, even if alternative needs provide greater marginal benefit, again echoes the IBA's sentiment of concern that removing discretionary budgetary flexibility can be problematic. This potential situation is clearly shown in *Footnote 1* on pages 4 and 5. In this case, funds have been allocated to Mission Bay Park in an amount four times greater than those allocated to some other need. The marginal benefit of spending additional dollars on Mission Bay Park upkeep is dwarfed by the benefits of funding another need. While the functional forms and expenditure values are completely theoretical, they do express the main assumption set forth by the proponents, namely that the additional revenue generated by Mission Bay Park relative to other assets in need of funding justifies its prioritization. The proponents (likely) assert that the excess funds are not large enough to cause the onset of significant diminishing marginal returns, but the potential for the occurrence of other General Fund needs with greater marginal benefits (particularly an emergency) suggests the optimality of budgetary flexibility.

### **Prioritization of Capital Projects**

The following projects in Mission Bay Park, or Capital Improvements, are included in latest version of the ordinance (v 2.8) currently available to SDCTA:

- Restoration of navigable water, elimination of hazards, expansion of eelgrass beds through dredging
- Wetland expansion and water quality improvements identified in the Mission Bay Park Master Plan

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Cont'd from page 4: The general solution for a "Constrained Optimization" problem can be obtained by using the LaGrange Multiplier method to find optimal values of inputs (in this case expenditure values for any budgetary item). Due to the quantitative nature of this solution method and for brevity, staff has omitted a full analytic presentation. For the purposes of this staff report, consider that the solution showcases the optimality of budgetary flexibility.

<sup>2</sup> "Ballot Proposition Amending the City Charter to Designate the Use of Lease Revenues from Mission Bay Park." Office of the Independent Budget Analyst Report, 08-85. July 25, 2008.

- Restoration of shoreline treatments including restoration of beach sand and stabilization of erosion control features
- Expansion of endangered or threatened species preserves and upland habitats on North Fiesta Island
- Restoration or replacement of seawall bulkhead on Oceanfront Walk
- Completion of bicycle and pedestrian paths and bridges
- Repair, resurface and restripe parking lots.

Following the completion of these projects, improvements identified within the Mission Bay Park Master Plan can receive funding from excess revenue. However, these items maintain priority once they require further attention.

### **SDCTA Historical Precedent**

#### *Ballot Box Budgeting*

SDCTA's historical treatment of Ballot Box Budgeting is as follows:

“Any initiative or bond measure that is deemed to be ballot box budgeting would generally not be supported by the San Diego County Taxpayers Association.”

“Ballot Box Budgeting is defined as any measure voted on by the people, whether put on the ballot by the people or an elected governmental body, that would limit a government body or elected officials' ability to set budgeting priorities by tying their hands and permanently earmarking funds for a specific purpose.”

“This definition would not apply under the following conditions:

- 1) The measure was put on the ballot by an elected governmental body because of a legal obligation to do so or
- 2) The measure identifies a new revenue source to pay for itself.”

Table 3: Mission Bay Park Estimated Improvement Costs		
Cost Item	Cost Estimate in Millions (1992)	Adjusted for CPI Inflation: 1.5616 (1992 - 2008)
<b>Public Improvement Costs</b>		
North End		
Rose Creek Bridge	2	3.12
Wetland Expansion	12.5	19.52
De Anza Cove Channel	1.5	2.34
Nature Center	1.5	2.34
Pacific Beach Athletic Fields expansion	0.5	0.78
Fiesta Island & Bay		
West Shore Dredging	2	3.12
E.F.B. Island Dredging	1	1.56
Upland Habitat Preserve	0.75	1.17
Fiesta Island Channel	1.5	2.34
Regional Parkland	15	23.42
Playground Areas	1.5	2.34
Coastal Landscape	3	4.68
Sand Area Relocation	3	4.68
Entrance Causeway	2	3.12
PWC Launch & Service	0.75	1.17
South Beach Jetty	1	1.56
East & Tecolote Shores		
Westland Expansion South	0.5	0.78
Wetland Expansion at Tecolote Creek	1	1.56
Path Widening @ Creek	0.25	0.39
Shore Dredging	1	1.56
South Shores		
Regional Parkland	7.5	11.71
Waterfront Promenade	1.5	2.34
Playground Area	0.5	0.78
Coastal Landscape	3.2	5.00
Public Amphitheater	1	1.56
Ski-Club Relocation	1	1.56
Overflow Parking	6	9.37
Bike Overpass @ Sea World Entrance	1.2	1.87
Park-Wide Improvements		
General Landscape Rehabilitation	23.5	36.70
New Restrooms	7	10.93
Traffic & Transportation Improvements	15.5	24.20
General Signage & Information Displays	0.75	1.17
Bike & Pedestrian Pathways	12	18.74
Parking Lot Lighting	1.5	2.34
Art Program	2.5	3.90
<b>Sub-Total</b>	<b>136.9</b>	<b>213.78</b>
Design & Administration (25%)	34.22	53.44
<b>Total</b>	<b>171.12</b>	<b>267.22</b>
<b>General Rehabilitation</b>		
Landscape Retrofit	3.5	5.47



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Ingraham Street Landscaping	0.75	1.17
Ski Beach Pier	0.75	1.17
Sail Bay Landscaping	1.5	2.34
I-5 Buffer Landscape	1	1.56
Restroom Repairs	1.5	2.34
New Furnishings	0.5	0.78
Parking Improvements	1.5	2.34
Existing Path Widening & Lighting	2.5	3.90
Contingency	10	15.62
Total	23.5	36.70
<b>GRAND TOTAL</b>	<b>194.62</b>	<b>303.92</b>