



CITY OF MONTCLAIR

Montclair Civic Center
5111 Benito Street
Montclair, CA 91763

January 17, 2013

TO: Honorable Mayor and City Council

FROM: Edward C. Starr, City Manager

SUBJECT: CITY MANAGER'S WEEKLY REPORT: January 11-17, 2013

➤ **CITY MANAGER/ADMINISTRATIVE SERVICES DEPARTMENTS**

- Earlier this month, President Obama signed House Resolution 8, the American Tax Relief Act of 2012, averting the tax component issues centered around what has been described as the "fiscal cliff." Resolving the nation's budget crisis is essential to future growth of the economy, the financial health of investment earnings, the fiscal integrity of state and local institutions, and the personal income profile for each citizen.

Background

The fiscal cliff was the combination of several unrelated fiscal policy events that were set to come into play on January 1, 2013.

1. *Taxes.* Numerous "Bush-era temporary tax cuts" were set to expire on December 31, 2012, raising projected federal tax revenue by an estimated \$494 billion in 2013—stemming primarily from upward adjustments to personal income tax brackets. The 10 percent income tax bracket would have been eliminated, establishing the 15 percent tax bracket as the lowest rate. Other tax brackets would have increased as follows: 25 percent to 28 percent; 28 percent to 31 percent; 33 percent to 36 percent; and 35 percent to 39.6 percent.

Dividends were to revert to being taxed as ordinary income (rather than taxed at the capital gains rate of 15 percent), which meant that in 2013, some individuals would have had dividend earnings taxed at nearly three times the amount they would have been taxed in 2012.

In the realm of estate and gift taxes, without Congressional action, the current \$5 million estate, gift, and generation-skipping transfer tax (GST) exemptions would have been reduced to \$1 million in 2013, exponentially increasing the number of American households subject to the estate tax. The Economic Growth and Tax Relief Reconciliation Act of 2001 would have phased-out the estate and GST taxes completely by 2010, while retaining the gift tax at a \$1 million exemption and 35 percent tax rate. However, Congress acted to reverse the phase-out of the estate tax by passing a bill in 2010 that raised the estate and gift tax exemption to \$5 million, with a 35 percent rate through December 31, 2012.

2. *Spending Cuts.* Mandatory federal spending cuts of \$1.2 trillion were to automatically go into effect January 3, 2013, by means of a Congressional process called "sequestration." Under sequestration, an amount of money equal to the difference between the cap set in the current Federal Budget Resolution and the amount actually appropriated for expenditures in all federal departments is "sequestered" by the Federal Treasury and not handed over to the agencies to which funds were originally appropriated by Congress. In theory, each federal agency would have the same percentage of appropriations withheld under sequestration.

Sequestration was first established as federal fiscal policy in the Gramm-Rudman-Hollings Deficit Reduction Act of 1985, with certain programs such as Social Security and certain parts of the Defense budget excluded from the process. However, the number of exempted programs expanded over past decades—which means that sequestration would significantly impact remaining programs in order to achieve the total required reductions—an action that would virtually cripple activities of nonexempt programs, including the Community Development Block Grant Program and its fiscal assistance to local governments.

Prior to adoption of the American Tax Relief Act of 2012, a large number of economists and government leaders expressed concern that the double-impact of increased taxes and spending cuts would seriously harm the nation's recovering economy.

What the American Tax Relief Act of 2012 Means

1. *Tax Rates.* The Act made the "Bush tax cuts" permanent for individuals whose income does not exceed the following thresholds:

\$400,000 for single filers, \$425,000 for heads of household, \$450,000 for those filing jointly, and \$225,000 for those who are married filing separately. This means 2012 income tax rates **will not** increase for taxpayers with annual earnings below the \$400,000/\$425,000/\$450,000/\$225,000 thresholds. Individual marginal tax rates of 10 percent, 15 percent, 25 percent, 28 percent, 33 percent, and 35 percent will remain.

For those taxpayers whose annual earnings exceed the \$400,000/\$425,000/\$450,000/\$225,000 thresholds, tax rates on income above the thresholds will permanently rise from a maximum rate of 35 percent to a new tax rate of 39.6 percent.

2. *Capital Gains.* The Act raises the top rate for capital gains and dividends to 20 percent, up from the Bush-era maximum rate of 15 percent. The top rate is applicable only to taxpayers whose income exceeds the \$400,000/\$425,000/\$450,000/\$225,000 thresholds. All other taxpayers will continue to enjoy a maximum capital gains and dividends tax rate of 15 percent.

A zero percent rate will continue to apply to capital gains and dividends to the extent income falls below top earnings within the 15 percent tax bracket.

Qualified dividends for all taxpayers continue to be taxed at capital gains rates, rather than ordinary income tax rates. Starting in 2013, higher income taxpayers must also start paying a 3.8 percent additional tax on net investment income under the Patient Protection and Affordable Care Act (colloquially referred to as Obama-Care).

3. *Alternative Minimum Tax (AMT).* The Act puts a patch on the AMT for 2012 and subsequent years by increasing the exemption amounts. The current rate, which is retroactive back to 2011, provides an exemption of \$50,600 for single taxpayers, \$78,750 for joint filers, and \$39,375 for married filing separately. In addition, the Act provides for an annual inflation adjustment to the exemption amounts for years beginning after 2012.
4. *Itemized Deductions.* The limitation on itemized deductions, which had been eliminated by the 2010 Tax Relief Act, now applies under the new law. The Act also revives the personal exemption phase-out rules, but with applicable income threshold levels that are higher than in the past.
5. *Estate Tax.* Under the Act, the estate, gift, and generation-skipping transfer tax rates are now unified and permanently rise to a maximum federal estate tax rate of 40 percent on estates of decedents dying

after December 31, 2012, and valued at over \$5 million, indexed to inflation (\$5.12 million in 2012). The Act also makes permanent the "portability" between spouses. Portability allows the estate of a decedent who is survived by a spouse to make a portability election to permit the surviving spouse to apply the decedent's unused exclusion to the surviving spouse's own transfers during life and at death.

6. *Roth IRA Transfers.* The Act lifts restrictions and now allows participants in 401(k) plans with in-plan Roth conversion features to make transfers to a Roth account anytime. Congress made this change to raise revenue because a conversion is a taxable event.
7. *Extension of Deductions/Credits.* The Act reinstated both the Pease limitation on itemized deductions and the Personal Exemption Phase-Out (PEP). These apply to those whose income reaches the following thresholds: \$300,000 for those who are married filing jointly, \$275,000 for heads of household, \$250,000 for single filers, and \$150,000 for married filing separately. The PEP reduces the allowable exemption for individuals in these categories by 2 percent for every \$2,500 over the threshold, and the Pease limitation reduces the allowed itemized deduction by 3 percent once an individual's income exceeds the thresholds.

Deductions and credits that were either extended temporarily or permanently by the Act include the following:

- ✓ State and local sales tax deduction
- ✓ Child tax credit of \$1,000 (5-year extension)
- ✓ Adoption credit/assistance
- ✓ Child and dependent care credit
- ✓ Employer-provided child care credit
- ✓ American Opportunity Tax Credit for qualified tuition and related expenses
- ✓ Deduction for qualified tuition and related expenses (5-year extension)
- ✓ Earned income tax credit (5-year extension)
- ✓ Student loan interest deduction
- ✓ Teachers' classroom expense deduction
- ✓ Mortgage insurance premiums treated as qualified residence interest
- ✓ IRA distributions to charity
- ✓ Exclusion from gross income of discharge of qualified principal residence indebtedness
- ✓ Parity for exclusion from income for employer-provided mass transit and parking benefits

- ✓ Special rule for contributions of capital gain real property made for conservation purposes
 - ✓ Tax-free distribution from individual retirement plans for charitable purposes
8. *Business Deductions.* Popular deductions related to businesses extended by the Act through 2013 include the following: \$500,000 limit on the expensing of machinery and equipment, with a \$2 million investment limit; and 50 percent bonus depreciation and Work Opportunity Tax Credit.
 9. *Unemployment.* The Act extends federal unemployment provisions through 2013.
 10. *Congressional Pay.* The Act retains a pay freeze on Members of Congress through 2013.
 11. *Farm Bill.* The Farm Bill is extended for 9 months.
 12. *Medicare Reductions.* The Act places a temporary hold on Medicare cuts for doctors through 2013.
 13. *Sequestration.* The automatic spending and budget cuts that come into effect once the debt ceiling has been reached is delayed for two months in order to give Congress more time to come to a decision on the debt ceiling issue.

While not a part of the American Tax Relief Act of 2012, there are three tax adjustments in 2013 that should be noted.

1. Congress chose not to extend the "Social Security payroll tax holiday" (FICA) that expired December 31, 2012; accordingly, **all income earners paying the Social Security tax** will now pay an additional 2 percent (for a total amount of 6.2 percent) in payroll taxes on the first \$113,700 of income.
2. The Affordable Care Act of 2010 instituted **two** new Medicare taxes: For taxpayers with incomes that cross the threshold of \$250,000 (married filing jointly), \$200,000 (single filers), or \$125,000 (married filing separately) a 0.9 percent Medicare Hospital Insurance tax will be assessed on any wages/small business income that exceeds the threshold; and for individuals in these same categories, a new 3.8 percent Medicare surtax on the lesser of certain types of investment income or adjusted gross income will also be assessed.

What Happens Next?

The Act temporarily averted the fiscal cliff but did nothing to deal with what is the next major political battle: debt ceiling negotiations.

The debt ceiling is the federal government's authorized borrowing limit. The current limit of \$16.4 trillion was reached on December 31, 2012—the Obama Administration has now implemented temporary and "extraordinary measures" to ensure the government does not default on its debts. However, Congressional republicans see the debt ceiling debate as an opportunity to demand cuts to entitlement programs. Conversely, Congressional democrats and the President demand a two-pronged approach to deficit reduction that includes both increasing revenue and decreasing spending, and that the debt ceiling limit itself is not negotiable.

The standoff over the debt limit will be compounded because of a confluence of events likely to occur if Congress does not reach agreement on the debt ceiling:

1. By the end of February 2013, the Treasury Department has announced it may be unable to pay the government's bills.
2. On March 1, 2013, across-the-board cuts in spending (sequestration) will begin.
3. On March 27, 2013, there exists the possibility of a government shutdown.

Understandably, many Americans are concerned with the looming debt ceiling fight, recalling the same debate in 2011 that caused Standard & Poor's to downgrade the United States' credit rating. Moreover, the debate is likely to fuel economic uncertainty, which could slow and possibly reduce hiring, personal and corporate earnings, a wide range of economic activity and financial investment, and improvement to an already fragile recovery. Some economists argue the United States could easily return to a recessionary cycle lasting several years.

Finally, there is concern final resolution to the debt ceiling issue may be bogged down by efforts to reform the tax structure and raise revenue. While it may be necessary to address each issue, they should be part of a larger debate and should not be used to prolong the nation's economic recovery.

➤ **COMMUNITY DEVELOPMENT DEPARTMENT**

- Yesterday, the City's Por La Vida Program hosted a *Power Up in 10* workshop, instructed by representatives from San Bernardino County's Department of Public Health. Approximately 30 participants from Por La Vida and other health education programs attended the "train the trainer"

workshop. Participants learned a series of ten easy stretches they can now teach to groups of all ages.

Check out Page 10 for a collage of photos from the workshop.

➤ ***POLICE DEPARTMENT***

- Reserve Officers conducted their first Traffic Enforcement Program of the new year on January 12. They issued 51 citations, cited an unlicensed driver and impounded the vehicle, and recovered an unoccupied stolen vehicle. They also assisted Officers by handling calls for service.

The next Traffic Enforcement Program is scheduled for February 9.

Our appreciation goes to Reserve Captain Ron Foss, Reserve Sergeant Scott Stephenson, and Reserve Officers Joe Kuskie and Nick Lopez.

➤ ***FIRE DEPARTMENT***

- Firefighters/Paramedics Nathan Brooks and Stan Boehm recently completed probationary Firefighter testing. Nathan successfully passed the first trimester of written and manipulative testing and will now be reassigned to Station 152 for the second trimester of training and testing. Stan successfully completed his one-year written and manipulative testing, which now completes his probationary period.

Through their hard work, studies, and assistance from their assigned Captains and crews, Nathan and Stan were well prepared for the testing process.

Congratulations, Nathan and Stan!

➤ ***PUBLIC WORKS/SUCCESSOR REDEVELOPMENT AGENCY***

- Construction began just after the first of the year on the Northwest Montclair Pavement Rehabilitation Project. The project limits include most residential streets north of San Bernardino Street and west of the San Antonio Channel to the City limits. Work includes removal and replacement of several trees that have damaged sidewalks and curbs, grinding pavement, overlaying pavement with new asphalt, and restriping.

Funding for this \$800,000 project is split between Proposition 1B, a state measure approved by California voters in 2006 intended for work on local streets and roads, and Measure I, approved by San Bernardino County voters in 2004, intended for transportation-related improvements and maintenance. Work will continue through the end of January and will be completed in February.

The picture below shows the grinding operation at the intersection of Pradera Avenue and Cambridge Street.



ECS:spa

*"Let no man pull you low enough to hate
him."*

~ Martin Luther King, Jr.

JANUARY 2013



17	Public Works Committee Meeting City Hall Conference Room	2:00 p.m.
21	Martin Luther King, Jr. Day – City Hall Closed	
22	Code Enforcement Committee Meeting	6:00 p.m.
22	City Council Meeting Council Chambers	7:00 p.m.
24	League of California Cities General Membership Inland Empire Division Dinner Meeting The Event Center at San Manuel Village, 27923 Highland Avenue, Highland	6:00 p.m. - 9:00 p.m.
28	Planning Commission Meeting Council Chambers	7:00 p.m.
29	City Manager's Staff Meeting City Hall Conference Room	9:00 a.m.

FEBRUARY 2013



04	City Council Meeting Council Chambers	7:00 p.m.
06	Community Action Committee Meeting Council Chambers	7:00 p.m.
11	Planning Commission Meeting Council Chambers	7:00 p.m.
12	City Manager's Staff Meeting City Hall Conference Room	9:00 a.m.
12	Midyear Budget Review Council Chambers	6:00 p.m.
13	Oversight Board Meeting Council Chambers	6:00 p.m.
18	Presidents' Day – City Hall Closed	
19	Code Enforcement Committee Meeting City Hall Conference Room	6:00 p.m.
19	City Council Meeting Council Chambers	7:00 p.m.
21	Safety Committee Meeting City Hall Conference Room	9:00 a.m.
21	Public Works Committee Meeting City Hall Conference Room	2:00 p.m.
25	Planning Commission Meeting Council Chambers	7:00 p.m.
26	City Manager's Staff Meeting City Hall Conference Room	9:00 a.m.

Power Up In 10



January 16, 2013

