PROPOSITION

1A PROTECTION OF LOCAL GOVERNMENT REVENUES

OFFICIAL TITLE AND SUMMARY

Prepared by the Attorney General

Protection of Local Government Revenues

- Protects local funding for public safety, health, libraries, parks, and other locally delivered services.
- Prohibits the State from reducing local governments' property tax proceeds.
- Allows the provisions to be suspended only if the Governor declares a fiscal necessity and two-thirds of the Legislature approve the suspension. Suspended funds must be repaid within three years.
- Also requires local sales tax revenues to remain with local government and be spent for local purposes.
- Requires the State to fund legislative mandates on local governments or suspend their operation.

Summary of Legislative Analyst's Estimate of Net State and Local Government Fiscal Impact:

- Significant changes to state authority over local finances. Higher local government revenues than otherwise would have been the case, possibly in the billions of dollars annually over time. Any such local revenue impacts would result in decreased resources to the state of similar amounts.

Final Votes Cast by the Legislature on SCA 4 (Proposition 1A)

Assembly:	Ayes 64	Noes 13
Senate:	Ayes 34	Noes 5

ANALYSIS BY THE LEGISLATIVE ANALYST

BACKGROUND

Local Government Funding

California cities, counties, and special districts provide services such as fire and police protection, water, libraries, and parks and recreation programs. Local governments pay for these programs and services with money from local taxes, fees, and user charges; state and federal aid; and other sources. Three taxes play a major role in local finance because they raise significant sums of general-purpose revenues that local governments may use to pay for a variety of programs and services. These three taxes are the property tax, the uniform local sales tax, and the vehicle license fee (VLF). Many local governments also impose optional local sales taxes and use these revenues to support specific programs, such as transportation. Figure 1 provides information on these major revenue sources.

State Authority Over Local Finance

The State Constitution and existing statutes give the Legislature authority over the taxes described in Figure 1. For example, the Legislature has some authority to change tax rates; items subject to taxation; and the distribution of tax revenues among local governments, schools, and community college districts. The state has used this authority for many purposes, including increasing funding for local services, reducing state costs, reducing taxation, addressing concerns regarding funding for particular local governments, and restructuring local finance. Figure 2 describes some of these past actions the Legislature has taken.

Requirement to Reimburse for State Mandates

The State Constitution generally requires the state to reimburse local governments, schools, and community college districts when the state

ANALYSIS BY THE LEGISLATIVE ANALYST

FIGURE 1

LOCAL GOVERNMENT TAXES

Property Tax

- Local governments receive general-purpose revenues from a 1 percent property tax levied on real property.
- During the 2003-04 fiscal year, local governments received approximately $15 billion in property tax revenues. (An additional $16 billion in property taxes went to schools and community colleges.)
- There is wide variation in the share of property taxes received by individual local governments. This variation largely reflects differences among local agency property tax rates during the mid-1970s, the period on which the state's property tax allocation laws are based.

Vehicle License Fee (VLF)

- The VLF is a tax levied annually on the value of vehicles registered in the state.
- For about a half century, the VLF rate was 2 percent of vehicle value. In 1999, the Legislature began reducing the rate charged to vehicle owners, with the state "backfilling" the resulting city and county revenue losses.
- During 2003-04, the VLF (set at a rate of 0.65 percent of vehicle value) and the VLF backfill would have provided about $5.9 billion to cities and counties. The state, however, deferred payment of part of the backfill to 2006.
- Under current law, most VLF revenues are allocated to counties for health and social services programs. Some VLF revenues are allocated to cities for general purposes.

Local Sales Tax (Uniform)

- Cities and counties receive revenues from a uniform local sales tax levied on the purchase price of most goods—such as clothing, automobiles, and restaurant meals. This tax is sometimes called the "Bradley-Burns" sales tax.
- During 2003-04, this tax was levied at a rate of 1.25 percent and generated about $5.9 billion.
- Under current law, 80 percent of sales tax revenues is distributed to local governments based on where sales occur—to a city if the sale occurs within its boundaries, or to a county if the sale occurs in an unincorporated area. The remaining 20 percent of local sales tax revenues is allocated to counties for transportation purposes.
- Beginning in 2004-05, local governments will receive additional property taxes to replace some local sales tax revenues that are pledged to pay debt service on state deficit-related bonds, approved by voters in March 2004.

Local Sales Tax (Optional)

- Cities and counties can impose certain additional sales taxes for local purposes.
- During 2003-04, 40 jurisdictions levied these optional sales taxes and generated about $3.1 billion.
- Most revenues are used for transportation purposes.

"mandates" a new local program or higher level of service. For example, the state requires local agencies to post agendas for their hearings. As a mandate, the state must pay local governments, schools, and community college districts for their costs to post these agendas. Because of the state's budget difficulties, the state has not provided in recent years reimbursements for many mandated costs. Currently, the state owes these local agencies about $2 billion for the prior-year costs of state-mandated programs. In other cases, the state has "suspended" state mandates, eliminating both local government responsibility for complying with the mandate and the need for state reimbursements.

PROPOSAL

Limitations on Legislature's Authority to Change Local Revenues

This measure amends the State Constitution to significantly reduce the state's authority over

FIGURE 2

MAJOR STATE ACTIONS AFFECTING LOCAL FINANCE

Increasing Funding for Local Services. In 1979, the state shifted an ongoing share of the property tax from schools and community colleges to local governments (cities, counties, and special districts). This shift limited local government program reductions after the revenue losses resulting from the passage of Proposition 13, but increased state costs to backfill schools' and community colleges' property tax losses.

Reducing State Costs. In 1992 and 1993, the state shifted an ongoing share of property taxes from local governments to schools and community colleges. In 2004, the state enacted a similar two-year shift of property taxes ($1.3 billion annually) from local governments to schools and community colleges. These shifts had the effect of reducing local government resources and reducing state costs. The state also reduced its costs by deferring payments to local governments for state mandate reimbursements (most notably in 2002, 2003, and 2004) and for a portion of the vehicle license fee (VLF) "backfill" (2003), described below.

Reducing Taxation. Beginning in 1999, the state reduced the VLF rate to provide tax relief. The state backfilled the resulting city and county revenue losses.

Addressing Concerns Regarding Funding for Specific Local Governments. In the past, the state has at various times adjusted the annual allocation of property taxes and VLF revenues to assist cities that received very low shares of the local property tax.

Restructuring Local Finance. In 2004, the state replaced city and county VLF backfill revenues with property taxes shifted from schools and community colleges.

For text of Proposition 1A see page 16.

PROTECTION OF LOCAL GOVERNMENT REVENUES

ANALYSIS BY THE LEGISLATIVE ANALYST (CONT.)

major local government revenue sources. Under the measure the state could not:

- *Reduce Local Sales Tax Rates or Alter the Method of Allocation.* The measure prohibits the state from: reducing any local sales tax rate, limiting existing local government authority to levy a sales tax rate, or changing the allocation of local sales tax revenues. For example, the state could not reduce a city's uniform or optional sales tax rate, or enact laws that shift sales taxes from a city to the county in which it is located.
- *Shift Property Taxes From Local Governments to Schools or Community Colleges.* The measure generally prohibits the state from shifting to schools or community colleges any share of property tax revenues allocated to local governments for any fiscal year under the laws in effect as of November 3, 2004. The measure also specifies that any change in how property tax revenues are shared among local governments within a county must be approved by two-thirds of both houses of the Legislature (instead of by majority votes). For example, state actions that shifted a share of property tax revenues from one local special district to another, or from a city to the county, would require approval by two-thirds of both houses of the Legislature. Finally, the measure prohibits the state from reducing the property tax revenues provided to cities and counties as replacement for the local sales tax revenues redirected to the state and pledged to pay debt service on state deficit-related bonds approved by voters in March 2004.
- *Decrease VLF Revenues Without Providing Replacement Funding.* If the state reduces the VLF rate below its current level, the measure requires the state to provide local governments with equal replacement revenues. The measure also requires the state to allocate VLF revenues to county health and social services programs and local governments.

The measure provides two significant exceptions to the above restrictions regarding sales and property taxes. First, beginning in 2008–09, the state may shift to schools and community colleges a limited amount of local government property tax revenues if: the Governor proclaims that the shift is needed due to a severe state financial hardship, the Legislature approves the shift with a two-thirds vote of both houses, and certain other conditions are met. The state must repay local governments for their property tax losses, with interest, within three years. Second, the measure allows the state to approve voluntary exchanges of local sales tax and property tax revenues among local governments within a county.

State Mandates

The measure amends the State Constitution to require the state to suspend certain state laws creating mandates in any year that the state does not fully reimburse local governments for their costs to comply with the mandates. Specifically, beginning July 1, 2005, the measure requires the state to either fully fund each mandate affecting cities, counties, and special districts or suspend the mandate's requirements for the fiscal year. This provision does not apply to mandates relating to schools or community colleges, or to those mandates relating to employee rights.

The measure also appears to expand the circumstances under which the state would be responsible for reimbursing cities, counties, and special districts for carrying out new state requirements. Specifically, the measure defines as a mandate state actions that transfer to local governments financial responsibility for a required program for which the state previously had complete or partial financial responsibility. Under current law, some such transfers of financial responsibilities may not be considered a state mandate.

Related Provisions in Proposition 65

Proposition 65 on this ballot contains similar provisions affecting local government finance and mandates. (The nearby box provides information on the major similarities and differences between these measures.) Proposition 1A specifically states that if it and Proposition 65 are approved and Proposition 1A receives more yes votes, none of the provisions of Proposition 65 will go into effect.

FISCAL EFFECTS

Proposition 1A would reduce state authority over local finances. Over time, it could have significant fiscal impacts on state and local governments, as described below.

Long-Term Effect on Local and State Finance

Higher and More Stable Local Government Revenues. Given the number and magnitude of past state actions affecting local taxes, this measure's restrictions on state authority to enact such measures in the future would have potentially major fiscal effects on local governments. For example, the state could not enact measures that permanently shift property taxes from local governments to schools in order to reduce state costs for education programs. In these cases, this measure

ANALYSIS BY THE LEGISLATIVE ANALYST (CONT.)

PROPOSITIONS 1A AND 65

Propositions 1A and 65 both amend the State Constitution to achieve three general objectives regarding state and local government finance. The similarities and differences between the two measures are highlighted below.

Limits State Authority to Reduce Major Local Tax Revenues

Effect on 2004–05 State Budget.

- *Proposition 65's* restrictions apply to state actions taken over the last year, and thus would prevent a major component of the 2004–05 budget plan (a $1.3 billion property tax shift in 2004–05 and again in 2005–06) from taking effect unless approved by the state's voters at the subsequent statewide election.
- *Proposition 1A's* restrictions apply to future state actions only, and would allow the planned $1.3 billion property tax shift to occur in both years.

Effect on Future State Budgets.

- *Proposition 65* allows the state to modify major local tax revenues for the fiscal benefit of the state, but only with the approval of the state's voters.
- *Proposition 1A* prohibits such state changes, except for limited, short-term shifting of local property taxes. The state must repay local governments for these property tax losses within three years.

Reduces State Authority to Reallocate Tax Revenues Among Local Governments

Effect on Revenue Allocation.

- *Proposition 65* generally requires state voter approval before the state can reduce any individual local government's revenues from the property tax, uniform local sales tax, or vehicle license fee (VLF).
- *Proposition 1A* prohibits the state from reducing any local government's revenues from local sales taxes, but maintains some state authority to alter the allocation of property tax revenues, VLF revenues, and other taxes. Proposition 1A does not include a state voter approval requirement.

Local Governments Affected.

- *Proposition 65's* restrictions apply to cities, counties, special districts, and redevelopment agencies.
- *Proposition 1A's* restrictions do not apply to redevelopment agencies.

Restricts State Authority to Impose Mandates on Local Governments Without Reimbursement

- *Proposition 65* authorizes local governments, schools, and community college districts to decide whether or not to comply with a state requirement if the state does not fully reimburse local costs.
- *Proposition 1A's* mandate provisions do not apply to schools and community colleges. If the state does not fund a mandate in any year, the state must eliminate local government's duty to implement it for that same time period.

would result in local government revenues being more stable—and higher—than otherwise would be the case. The magnitude of increased local revenues is unknown and would depend on future actions by the state. Given past actions by the state, however, this increase in local government revenues could be in the billions of dollars annually. These increased local revenues could result in higher spending on local programs or decreased local fees or taxes.

Lower Resources for State Programs. In general, the measure's effect on state finances would be the *opposite* of its effect on local finances. That is, this measure could result in decreased resources being available for state programs than otherwise would be the case. This reduction, in turn, would affect state spending and/or taxes. For example, because the state could not use local government property taxes permanently as part of the state's budget solution, the Legislature would need to take *alternative* actions to resolve the state's budget difficulties—such as increasing state taxes or decreasing spending on other state programs. As with the local impact, the total fiscal effect also could be in the billions of dollars annually.

Less Change to the Revenue of Individual Local Governments. Proposition 1A restricts the state's authority to reallocate local tax revenues to address concerns regarding funding for specific local governments or to restructure local government finance. For example, the state could not enact measures that changed how local sales tax revenues are allocated to cities and counties. In addition, measures that reallocated property taxes among local governments in a county would require approval by two-thirds of the Members of each house of the Legislature (rather than majority votes). As a result, this measure would result in fewer changes to local government revenues than otherwise would have been the case.

Effect on Local Programs and State Reimbursements

Because the measure appears to expand the circumstances under which the state is required to reimburse local agencies, the measure may increase future state costs or alter future state actions regarding local or jointly funded state-local programs. While it is not possible to determine the cost to reimburse local agencies for potential future state actions, our review of state measures enacted in the past suggests that, over time, increased state reimbursement costs may exceed a hundred million dollars annually.

For text of Proposition 1A see page 16.

PROP 1A PROTECTION OF LOCAL GOVERNMENT REVENUES

ARGUMENT in Favor of Proposition 1A

PROPOSITION 1A—A HISTORIC AGREEMENT TO PROTECT LOCAL TAXPAYERS AND VITAL LOCAL GOVERNMENT SERVICES.

Proposition 1A is a historic bipartisan agreement among local governments, public safety leaders, the State Legislature, Republican Governor Arnold Schwarzenegger, and is authored by Democratic State Senator Tom Torlakson.

Proposition 1A prevents the State from taking and using funding that local governments need to provide services like fire and paramedic response, law enforcement, health care, parks, and libraries.

These individuals and groups urge a YES vote:

- Governor Schwarzenegger
- State Controller Steve Westly
- California Professional Firefighters
- California Fire Chiefs Association
- California Police Chiefs Association
- California State Sheriffs' Association
- California Association of Public Hospitals and Health Systems
- League of California Cities
- California Special Districts Association
- California State Association of Counties

PROPOSITION 1A IS NEEDED TO STOP THE STATE FROM TAKING LOCAL GOVERNMENT FUNDING.

For more than a dozen years, the State has been taking local tax dollars that local governments use to provide essential services—more than $40 billion in the last 12 years. Even in years with state budget surpluses, the State has taken billions of local tax dollars.

These State raids result in fewer firefighters, fewer law enforcement officers, longer waits in emergency rooms—or higher local taxes and fees.

PROPOSITION 1A PROTECTS PUBLIC SAFETY, EMERGENCY HEALTH CARE, AND OTHER LOCAL SERVICES.

Local governments spend a vast majority of their budgets providing critical services, including:

- Fire protection
- Paramedic response
- Law enforcement
- Emergency medical
- Health care
- Parks and libraries

Cities and counties also revitalize downtowns and create jobs and affordable housing using redevelopment agency funding. Redevelopment agency tax increment revenues are already protected by the State Constitution and do not need to be further protected by Proposition 1A.

PROPOSITION 1A PROTECTS LOCAL TAXPAYERS AND WON'T RAISE TAXES.

Proposition 1A will *not* raise taxes. It simply ensures that *existing* local tax dollars continue to be dedicated to local services. It also helps *ensure local governments aren't forced to raise taxes or fees to make up for revenue raided by the State.*

PROPOSITION 1A PROVIDES FLEXIBILITY IN A STATE BUDGET EMERGENCY—AND WON'T TAKE FUNDING FROM SCHOOLS OR OTHER STATE PROGRAMS.

Proposition 1A protects only *existing* levels of local funding. It does not reduce funding for schools or other state programs. And, 1A was carefully written to allow flexibility. It allows the State to *borrow* local government revenues—only in the event of a fiscal emergency—if funds are needed to support schools or other state programs.

PROPOSITION 1A IS A BETTER APPROACH THAT REPLACES THE NEED FOR PROPOSITION 65.

Proposition 65 was put on the ballot earlier this year before this historic agreement was reached. Proposition 1A is a better, more flexible approach to protect local services and tax dollars. That's why ALL of the official proponents of 65 are now ENDORSING PROPOSITION 1A AND OPPOSING PROPOSITION 65.

Join Governor Schwarzenegger, Senator Torlakson, firefighters, police officers, sheriffs, paramedics, health care leaders, taxpayers, business and labor leaders.

PROTECT LOCAL TAXPAYERS AND PUBLIC SAFETY. Vote YES on PROPOSITION 1A. Vote NO on PROPOSITION 65.

GOVERNOR ARNOLD SCHWARZENEGGER

CHIEF MICHAEL WARREN, *President*
California Fire Chiefs Association

SHERIFF ROBERT T. DOYLE, *President*
California State Sheriffs' Association

REBUTTAL to Argument in Favor of Proposition 1A

Proposition 1A was cooked up at the last minute as part of a bad budget deal.

There were no public hearings.

Proposition 1A protects local governments, but it hurts education by allowing the State to raid your property taxes that fund your local schools. And it puts that into the State Constitution!

Proposition 1A prevents the Legislature from lowering taxes by locking in the local sales tax rate. That goes into the State Constitution too!

Proposition 1A jeopardizes critical programs. As California's fiscal challenges continue, the State budget ax will fall even harder on funding for K–12 education, higher education, children's health care, programs for seniors, and public safety.

Proposition 1A gives local politicians a blank check without any scrutiny over how the money is spent.

We can do better. We deserve better.

Vote NO on Proposition 1A.

CAROLE MIGDEN, *Chairwoman*
State Board of Equalization

PROTECTION OF LOCAL GOVERNMENT REVENUES

PROP 1A

ARGUMENT Against Proposition 1A

We should protect local taxpayers, not irresponsible spending by local governments. Vote NO on Proposition 1A.

As Chairwoman of the State Board of Equalization, I know that too many branches of government waste too much money.

Proposition 1A gives local governments a spending guarantee without any fiscal accountability or oversight. It's a blank check for spending and turns a blind eye to waste.

Did you know that the City of Stockton is emptying its cash reserves to build a downtown arena, but at the same time they're trying to raise taxes to pay for police officers and firefighters? They've got their priorities backwards.

Did you know that the City of Los Angeles raised their water rates, but at the same time they're being audited for wasting millions on unnecessary public relations contracts?

California has a responsibility to help and support local governments. We are all in this together. But NO one should be exempt from fiscal oversight and accountability. Checks and balances are essential.

Public schools in California are funded by Proposition 98. But in 1988, California's teachers included specific language to hold school districts accountable for the money they spend.

There is NO fiscal accountability provision in Proposition 1A.

Every new school bond we've placed on the ballot contains specific accountability provisions to guarantee that the money is spent the way the voters intend.

There is NO fiscal accountability provision in Proposition 1A.

Every one of California's Water, Parks, and Wildlife bonds had strict accountability provisions.

There is NO fiscal accountability provision in Proposition 1A.

California is facing serious budget challenges. There have been great sacrifices made to meet those challenges... cuts in children's health care, nursing home care, and college admissions.

Why should local politicians get a blank check? I say NO they shouldn't. Why should local politicians get a guarantee that sick children don't get? I say NO they shouldn't.

This NO fiscal accountability Proposition deserves a NO vote!

Please join me in voting NO on Proposition 1A.

CAROLE MIGDEN, *Chairwoman*
State Board of Equalization

REBUTTAL to Argument Against Proposition 1A

Contrary to misleading claims made by the opponent of 1A, THIS MEASURE INCREASES FISCAL ACCOUNTABILITY.

Prop. 1A increases local budget accountability by keeping tax dollars close to home, where voters have more control.

Prop. 1A will also make the State more accountable by preventing it from taking and using local government funds—except in a fiscal emergency.

FOR YEARS, *THE STATE* HAS HAD A BLANK CHECK to take your local tax dollars. PROP. 1A TEARS UP THAT BLANK CHECK and requires the State to live within its means.

The opponent would have you believe the State is in a better position to manage your local tax dollars than your city or county leaders. In fact, over the past decade, cities and counties have tightened their belts, increased accountability, and prioritized spending for essential local services.

Prop. 1A does NOT increase local government funding and does not take one dime from schools, state health care services, or any other state program or service.

Prop. 1A does NOT increase taxes. The measure PROTECTS *EXISTING* LOCAL TAX DOLLARS—WHICH ARE USED TO PROVIDE FIREFIGHTING, LAW ENFORCEMENT, EMERGENCY ROOM CARE, PARAMEDIC RESPONSE, and other essential local services.

Prop. 1A supporters know it's time to end business as usual in Sacramento and stop the State from taking and using local government funds.

Join Governor Schwarzenegger, firefighters, law enforcement officers, paramedics, and taxpayer groups.

PROTECT LOCAL TAXPAYERS AND PUBLIC SAFETY SERVICES. VOTE YES on 1A.

SENATOR TOM TORLAKSON, *Chair*
Senate Committee on Local Government

LOU PAULSON, *President*
California Professional Firefighters

CAM SANCHEZ, *President*
California Police Chiefs Association