



COUNTY OF SAN MATEO
Inter-Departmental Correspondence

Board of Supervisors

DATE: August 20, 2004

BOARD MEETING DATE: August 31, 2004

TO: Honorable Board of Supervisors
FROM: Richard Gordon, 3rd District Supervisor *RGM*
SUBJECT: Proposition 1A, Protection of Local Government Revenues

RECOMMENDATION:

Approve the resolution in support of Proposition 1A, Protection of Local Government Revenues on the November 2, 2004 statewide ballot.

BACKGROUND:

Over the past 12 years the state has shifted \$44 billion in local property taxes to meet its school funding requirements. The County of San Mateo has lost \$818 million during this period.

When the Governor announced his proposed budget for fiscal year 2004-05, he projected additional transfers of local property tax to schools.

A coalition of local governments (California State Association of Counties, the California League of Cities and the California Special District Association) said that enough was enough and sought to remedy this problem by collecting signatures for a statewide ballot initiative to protect local government funding. This effort resulted in Proposition 65 on the November 2004 ballot.

The coalition of local governments also sought to meet with the Governor to discuss his current proposal and the ballot initiative. The Governor initially entered into negotiations with local government regarding specifics for this year's budget. Those negotiations were later expanded to include the State Legislature. Leadership of the California State Association of Counties was actively involved in these negotiations and as a member of the CSAC Executive Committee I was provided with daily updates of the progress of these negotiations. These negotiations concluded with the adoption of the 2004-05 State Budget. As part of the 2004-05 State Budget agreement, the Governor and Legislative leaders passed Senate Constitutional

Amendment 4 (Torlakson), which appears as Proposition 1A on the November 2, 2004 statewide ballot.

In short, Proposition 1A would provide enhanced protection to local government revenues. As part of the agreement counties, cities, redevelopment agencies and special districts are required to shift a total of \$1.3 billion in each of the next two fiscal years.

The budget agreement is contained in Senate Constitutional Amendment 4 (Torlakson) Senate Bill 1096 (Budget and Fiscal Review Committee). Attachment A breaks down the elements of the agreement as it impacts Vehicle License Fees (VLF), property and sales tax, as well as mandate relief.

In 1978, the \$25 billion state budget included a whopping \$5 billion surplus. That same year California voters overwhelmingly passed Proposition 13 to permanently reduce and cap the local property tax to one percent. The single rate replaced the multiple property tax rates imposed by local governments. The revenue from the one percent rate is shared in each county by the cities, special districts, schools and the county. Generally, each jurisdiction's property tax allocation is based on their historic share of the property tax in effect prior to Proposition 13. Proposition 13 also shifted the authority to allocate property taxes to the state.

DISCUSSION:

Proposition 1A will stop the annual raid on local property taxes by allowing no more than two *loans* within a 10-year period, subject to special conditions being met. Specifically, Proposition 1A would prevent the Legislature from reducing the combined property tax share of cities, special districts and counties except to borrow the funds on a temporary basis during a "severe state fiscal hardship." Restriction to this exception include:

- The 2003 VLF loan must be repaid before borrowing occurs;
- Loans can only occur twice within a 10-year period;
- The loan -- the total amount of revenue loss -- must be repaid with interest within 3 years and prior loans must be repaid before borrowing can occur a second time within that 10-years;
- The loan amount is limited to no more than eight percent of the total amount of property tax allocated to cities, counties and special districts in the previous fiscal year (current fiscal year eight percent is equal to roughly \$1.3 billion); and
- The reduction can only occur upon a 2/3^{rds} vote of the Legislature.

Proposition 1A prevents the state from borrowing or taking local sales and use taxes. Last year, the Legislature suspended one-quarter cent of the basic one percent sales tax until the state's fiscal recovery bonds are repaid. This ballot measure also prevents the state from extending the period during which the one-quarter cent is suspended; from failing to pay the property tax backfill during the period of suspension; and from failing to restore the full sales tax rate when the deficit reduction bonds are repaid.

The State Constitution guarantees all of the VLF revenue to cities and counties. However, no specific rate is set or amount guaranteed. The current VLF rate is two percent. During the dot-com boom, flush with revenue the Legislature provided tax relief by reducing local revenues cutting the VLF rate by 67 percent and promising to backfill the revenue loss to cities and counties. However, cities and counties have not received a backfill. Under Proposition 1A, cities and counties will receive the promised backfill in the form of increased allocation of property taxes beginning in 2006. The County's share of the VLF gap payment is estimated to be \$14 million.

This provision represents a significant change, because the current constitutional provision does not guarantee a specific rate to cities and counties.

Beginning in 2005-06, Proposition 1A, requires the Legislature each fiscal year's budget, to either appropriate sufficient funds to reimburse local governments for their costs of complying with a mandate or suspend the operation of the mandate for that fiscal year with two specific exceptions:

- For employee organization related mandates; and
- Costs incurred prior to the 2004-05 fiscal year that have not been paid prior to the 2005-06 fiscal year. The statute provides that these costs may be paid over a five-year period beginning in 2005-06. Mandate is defined as a transfer of responsibility for a state program or service.

Finally, Proposition 1A obfuscates the need for Proposition 65, the local initiative that requires a 2/3rds vote of the Legislature and voter approval for any reduction in local government financing. Proposition 1A is a comprehensive alternative to Proposition 65 that is intended to supersede it in its entirety.

VISION ALIGNMENT:

Support for Proposition 1A respects the *Shared Vision 2010* commitment for responsive, effective and collaborative government and keeps goal #20; that government decisions are based on careful consideration of future impact, rather than temporary relief or immediate gain.

FISCAL IMPACT:

The 2004-05 State Budget impact on the County of San Mateo is estimated to be a loss of upwards of \$10 million; with a similar loss in 2005-06. The enactment of Proposition 1A would restore predictability of local revenues in future years. Proposition 1A does not raise taxes; nor does it reduce funding for schools or any other state program; and it does not preclude the state from taking local government revenues in a fiscal emergency.