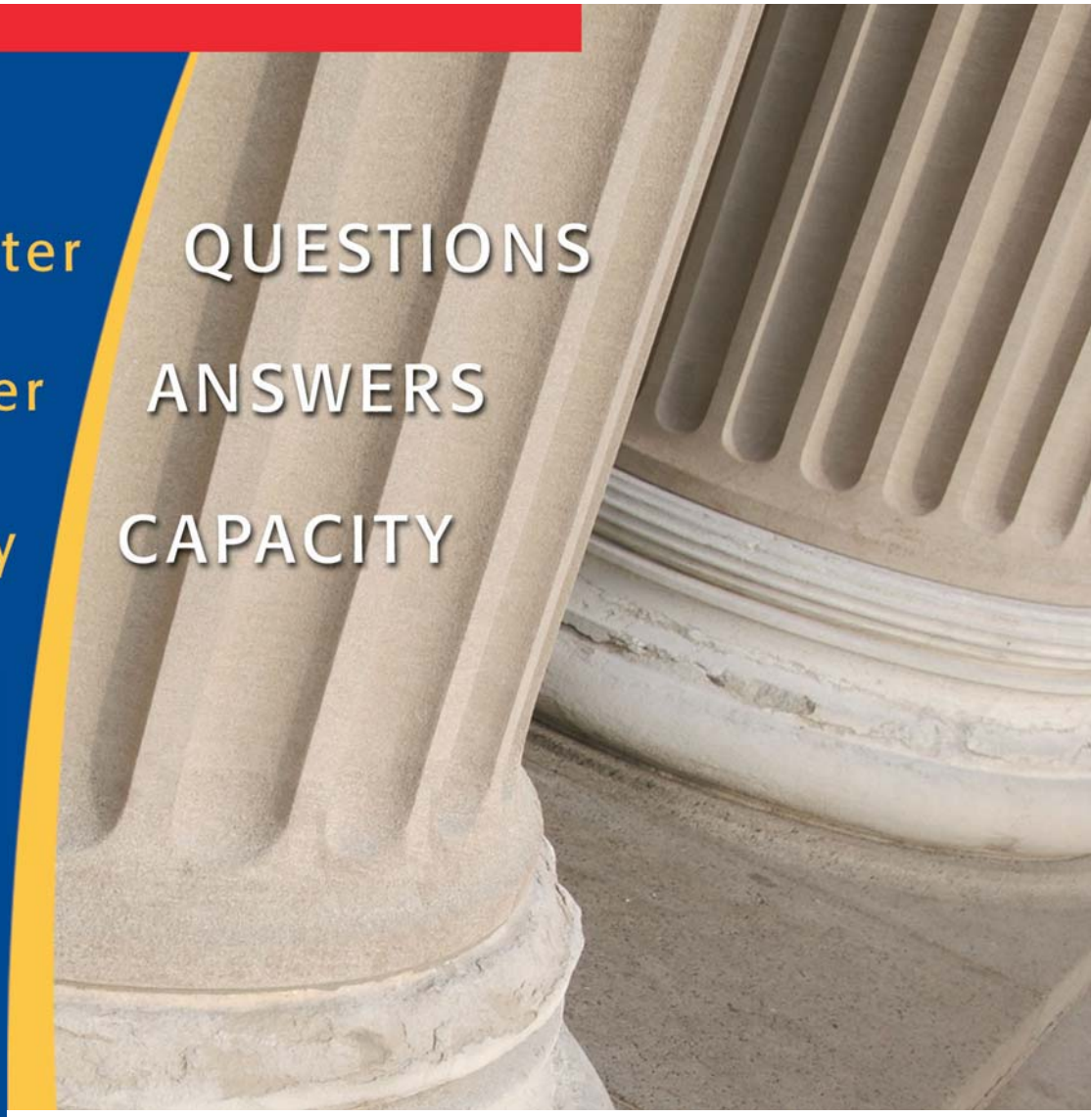
Ask Better QUESTIONS

Give Better ANSWERS

Expand County CAPACITY



COURSE MATERIALS

Financing California Counties

Diane Cummins

CI 151

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151: Financing California Counties

Faculty Biography

CSAC INSTITUTE FOR EXCELLENCE IN COUNTY GOVERNMENT

DIANE M. CUMMINS

Diane Cummins currently serves as the Special Advisor to the Governor on State and Local Realignment. She officially retired in late 2008 after a distinguished 31-year career in California government, but has been brought back to advise the Governor in an area of her particular expertise.

Ms. Cummins was appointed Chief Fiscal Policy Advisor to the President pro tem of the State Senate in January, 1999. In that capacity, Ms. Cummins served as the primary staff for the Senate on fiscal matters related to the State Budget, major initiatives and legislation. She was the primary staff person representing the pro tem in budget negotiations with the Governor's Office and the Assembly. Ms. Cummins also advised the President pro tem on issues related to revenue and taxation policy and issues in the Human Services program area.

Prior to her appointment in the Senate, Ms. Cummins served as the Chief Deputy Director, Budgets in the Department of Finance where she acted as a key advisor to the Governor and was the Governor's primary contact with the Legislature in budget matters.

Before serving in that capacity, Ms. Cummins served as the Deputy Director for legislation, the Program Budget manager for Health and Human Services, and a variety of other positions in the Department of Finance. During her 21-year tenure in the Department of Finance, Ms. Cummins was a key staff person on several major policy initiatives, including 1991 Realignment, the 1997 state assumption of trial court funding, the 1997 state welfare reform effort which resulted in the state CalWORKs program and Foster Care Reform.

Ms. Cummins is widely respected for her knowledge of the State Budget as well as her expertise in state-local funding issues and court financing. She is a frequent guest lecturer on various and policy issues.

Ms. Cummins was a 2008 recipient of the California State Association of Counties Distinguished Service Award and the 2006 Western Center on Law and Poverty Advocacy Award.

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FINANCING CALIFORNIA COUNTIES

State-Local Finances Through the State Budget

Why Is History Important?

- Interesting
- Context to the fiscal condition of counties – Counties receive over half their funding from intergovernmental aid
- State budget includes issues affecting counties
- Learn from the past and avoid mistakes

Why Is History Important?

- Understand the consequences and unintended consequences
- Reform discussions – What is the local government perspective
- What's the biggest problem in the state-local relationship and how you would fix it?

Who Is Local Government?

- K – 12 school districts (about 1,000)
- Community College Districts (72)
- Courts (58) (quasi)
- Special Districts (about 3,300)
- Cities (482)
- Counties (58)
  - Municipal Services in unincorporated area
  - County-wide services
  - Administer programs for the State

Property Taxes – Pre Prop 13

- Each local agency: city, county, special district and school set its own property tax rate to meet its needs (majority vote of the governing body)
- The average aggregate tax rate by 1978 was about 2.5 to 2.7 percent of market value
- The local assessor assessed the value of each property, usually on a 2 to 3-year cycle

Property Taxes – Pre Prop 13

- As a homeowner, you could see the rate each local entity assessed on your property tax bill
- Local officials were setting the tax rate and making decisions about how to spend local tax money
- Local Accountability

The Decade of the 1970's

Tax Turmoil and Stress

Legislative Inaction
Proposition 13 – June, 1978

What Did Proposition 13 Do?

- Limit the property tax rate to 1%, except for pre-existing debt
- Assessed value of all property rolled back to 1975-76 value
- Assessed value increase by inflation annually, ≤ 2%
- Property assessed at fair market value upon change in ownership or completion of construction

What Did Proposition 13 Do?

- Allocation of property tax subject to state law
- Required a 2/3 vote for state tax increases and a 2/3 vote for local special taxes
- Immediate fiscal effect – loss of 55 to 57% of property tax revenue, about $6.88 billion

Unintended Consequences of Proposition 13

- Concentrated power of money at the state level
- Made locals more dependent on sales tax
- Led to emergence of redevelopment as an economic tool which had some good and some "less good" features
- Led to a greater reliance on fees – e.g. developer fees, assessment districts as well as other financing methods – e.g. Mello Roos Districts – as locals made up for lost funding

Unintended Consequences of Proposition 13

- Disproportionately affected local jurisdictions without much revenue raising authority – libraries, park and recreation districts
- Increased the state's role in delivering and financing of local services

State's Response

- 1978-79 one-year bailout
- 1979-80 long term fiscal relief
- AB 8 – transfer of property tax from schools (K-12 and community colleges) to cities, counties and special districts
- State assumption of programs or shares of programs in health and human services
- State used this as an opportunity to comply with the Serrano school equalization requirement
- AB 8 included a "deflator" in case the state could not afford the bail out on a long-term basis

Consequences of AB 8

- Relative share of property tax received by each local agency varied considerably, as had their tax rates
- Counties varied in the level of services provided; the share of the area incorporated; the population in the unincorporated area and wealth. Service demands could outstrip revenue

Consequences of AB 8

- Proportionate share of state's buyout of health and human services programs varied considerably by county
- Counties provide services on a county-wide basis but had limited authority to raise revenue – not taken into account in AB 8
- All of these factors, funding inequities, varying service levels, were locked in place by AB 8

Proposition 4 (1979)

- Added Article XIIIB to the Constitution. Limits growth of certain tax proceeds for state and local governments
- Section 6 specifies local mandate reimbursement requirements for new program or higher level of service unless: local request; defines a new crime or changes definition of a crime; or imposed prior to 1975

The Decade of the 80's

- The Deflator activated but in-lieued
- VLF reductions
- Medically Indigent Adults transferred from State Medi-Cal to counties
- Supplemental property tax roll – linked to school reforms
- New Partnership Task Force Report on state-local relationship – recommendations included realignment

The Decade of the 80's

- 1984 repeal of Deflator
- 1986 Proposition 47 constitutionally guaranteed VLF to cities and counties
- 1986 Proposition 62 – 2/3 vote of governing body and majority of taxpayers for new general taxes
- Constitutional amendment to allow property tax as a guarantee for GO bonds with a 2/3 vote of the electorate

The Decade of the 80's

- Federal Immigration Reform and Control Act (IRCA) – California receives over $2 billion for a 5-year period
- 1987 statute allowed small counties to increase their sales tax by ½ % with a 2/3 vote of Supervisors and a majority vote of the electorate

The Decade of the 80's

- 1988 Brown-Presley Trial Court Funding Act – block grants to counties
- Proposition 99 – surtax on cigarettes and tobacco products, revenue dedicated to health education and health care along with a few resource programs
- Proposition 98 – Constitutional funding guarantee for K-14 schools

The Decade of the 90's

- State budget cuts in 1990 with backfill of SLIAG funds ($175 million from indigent healthcare)
- County revenue raising authority to provide relief to counties
- Lawsuits filed over the 1982 transfer of the MIA program
- 1991-92 Realignment

Realignment

- $7 billion budget problem
- Community Mental Health, Medically Indigent Adult and AB 8 Health Block Grant would have been eliminated
- Needed revenue to make it work. Increase in alcohol beverage tax to national average and VLF depreciation schedule for $942 million (plus 1/2 cent for local crime prevention)

Realignment

- As budget problem grew so did Realignment
- $2.2 billion – VLF depreciation and ½ cent sales tax
- Included changing sharing ratios in Health and Human Services programs
- 3 primary accounts
- Base and growth
- Equity
- Mandates
- What are poison pills?

The Decade of the 90's

- 1992-93 and 1993-94 property tax shifts (ERAF) – Counties lost $525 Million in 92-93 and $1.998 billion in 93-94
- 1993-94 local government relief: Proposition 172 and mandate relief
- 1997-98 State assumes costs above county MOE for trial courts
- 1997-98 CalWORKs reform with significant county flexibility and performance incentives
- 1997-98 CYA Sliding Scale

VLF Tax Cuts, VLF Loans, The Triple Flip and Prop. 1A

- 1998 VLF tax cut required a hold harmless back-fill to cities and counties
- Proposition 42 – guaranteed transportation funding but could the state afford (2002)
- 2003-04 cities and counties – a "fair share" of the cuts through $1.3 billion VLF gap loan.
- First economic recovery bond assumed as part of the budget

VLF Tax Cuts, VLF Loans, The Triple Flip and Proposition 1A

- Governor Davis recalled in October 2003. Arnold Schwarzenegger elected
- Governor's first action was to reduce the VLF; used Section 27 of the Budget to pay locals
- The VLF backfill became property tax taken from the schools and allocated to cities and counties. First year, same share of VLF; after that, grows according to property tax in each county

VLF Tax Cuts, VLF Loans, The Triple Flip and Proposition 1A

- Propositions 57 – the Economic Recovery Bonds (ERBs) ($15 billion)
- Proposition 58 – requires a balanced budget and increasing reserves
- Both passed in the March 2004 election

VLF Tax Cuts, VLF Loans, The Triple Flip and Proposition 1A

- ERBs paid for with "the Triple Flip"
  - Local sales tax rate reduced by one-quarter percent
  - State sales tax increased by one-quarter percent for bond costs
  - Value of the quarter cent in each jurisdiction is transferred from school property tax to cities and counties (hold harmless)
- Triple Flip will be undone when the ERBs are paid off (June 2016)

Proposition 1A

- SCA 4 approved by the voters in November, 2004
- Point was to "level the playing field" – state could no longer move property tax from cities, counties and special districts to the schools on a permanent basis
- Governor declare an emergency; 2/3 vote of the Legislature
- Could borrow a specified amount of property tax but the Constitution required it to be paid back within 3 years with interest

Proposition 1A

- Could be borrowed twice in 10 years; had to be paid back before borrowing again
- Defined an increased share of program costs as a reimbursable mandate
- For the 2004-05 and 2005-06 budgets, cities, counties and special districts each gave up $350 million of property tax as "their share" of budget reductions
- 2009-10 budget, state borrowed $1.9 billion
- 2009 – SB 678 Felony Probation

Mandates

- SB 90 (1972)
  - State limited property tax so provided "relief" to locals
  - File a claim with the Board of Control if a bill or regulation had new requirements
- Proposition 4 (1979)
  - Added Article XIIIB to the Constitution – limited growth in appropriations of certain tax proceeds
  - Section 6 specifies local mandate reimbursement requirements

Mandates – A Side Note

- Mandate Relief of the 90's
- Proposition 1A (2004)
  - Requires state to pay claims in the budget or suspend or repeal mandate
  - Authorized claims prior to 2005-06 to be paid over time
  - State cannot use property tax to pay for a mandate
  - Expands definition to include transfer of financial responsibility from state to local governments

More Limits

- Proposition 22 (November 2010) – reduces the state's authority to use or redirect state fuel tax revenue and local property tax revenues
- Proposition 26 (November 2010) – broadens the definition of "taxes" to include payments previously considered to be state and local fees and charges

2011-12 Governor's Budget

- Realignment 2011
- $5.9 billion program transfer of public safety programs
- $5.9 billion in revenue from 5 year extension of 0.50% VLF rate and 1 cent sales tax
- Constitutional guarantee of on-going funding
- Mandate protection for the state
- Pay-as-you legislation for realigned programs
- Federal law changes and lawsuits paid 50/50

Policy Rationale

- Government services closer to the people
- Protect essential public services
- Focus on core services
- Clarity of roles between state and locals
- Reduce state operations
- Program and fiscal responsibility at one level
- Maximum flexibility in providing services
- 3-Judge Panel on prison overcrowding

Final 2011-12 Budget

- 1.0625 cents of state General Fund sales tax reduced
- 1.062 cents state special fund sales tax increased
- $5.1 billion in sales tax revenue
- $453.4 million VLF for local public safety programs
- Funds dedicated to Local Revenue 2011
- Allocations for 1 year

Programs Realigned

- Court Security
- Local Public Safety Programs
- Lower Level Offenders/Parole Violators/Parole
- Existing Juvenile Justice Realigned Programs
- Mental Health – EPSDT and Managed Care
- Substance Use Disorder Programs
- Foster Care/Child Welfare Services
- Adult Protective Services

	2012-13	2012-13 Growth	2013-14	2013-14 Growth	2014-15	2014-15 Growth
Law Enforcement Services	**$1,942.6**		**$2,121.7**		**$2,079.6**	
Trial Court Security Subaccount	496.4	10.3	506.7	12.0	518.7	22.6
Enhancing Law Enforcement Activities Subaccount[1]	489.9	-	489.9	-	489.9	-
Community Corrections Subaccount[2]	842.9	77.3	998.9	89.7	934.1	169.1
District Attorney and Public Defender Subaccount[2]	14.6	5.2	17.1	6.0	15.8	11.3
Juvenile Justice Subaccount	98.8	10.3	109.1	12.0	121.1	22.6
Youthful Offender Block Grant Special Account	*(93.4)*	*(9.7)*	*(103.1)*	*(11.3)*	*(114.4)*	*(21.4)*
Juvenile Reentry Grant Special Account	*(5.4)*	*(0.6)*	*(6.0)*	*(0.7)*	*(6.7)*	*(1.2)*
Growth, Law Enforcement Services	**103.1**	**103.1**	**119.7**	**119.7**	**225.6**	**225.6**
Mental Health[3]	**1,120.6**	9.6	**1,120.6**	11.1	**1,120.6**	21.0
Support Services	**2,604.9**		**2,807.2**		**3,033.7**	
Protective Services Subaccount[4]	1,640.4	157.1	1,817.9	137.4	1,970.6	197.9
Behavioral Health Subaccount[5]	964.5	24.8	989.3	73.8	1,063.1	200.1
Women and Children's Residential Treatment Services	*(5.1)*	-	*(5.1)*	-	*(5.1)*	-
Growth, Support Services	**191.5**	**191.5**	**222.3**	**222.3**	**419.0**	**419.0**
Account Total and Growth	**$5,962.7**		**$6,391.5**		**$6,878.5**	
Revenue						
1.0625% Sales Tax	5,508.1		5,924.2		6,404.4	
Motor Vehicle License Fee	454.6		467.3		474.1	
Revenue Total	**$5,962.7**		**$6,391.5**		**$6,878.5**	

This chart reflects estimates of the 2011 Realignment subaccount and growth allocations based on current revenue forecasts and in accordance with the formulas outlined in Chapter 40, Statutes of 2012 (SB 1020).

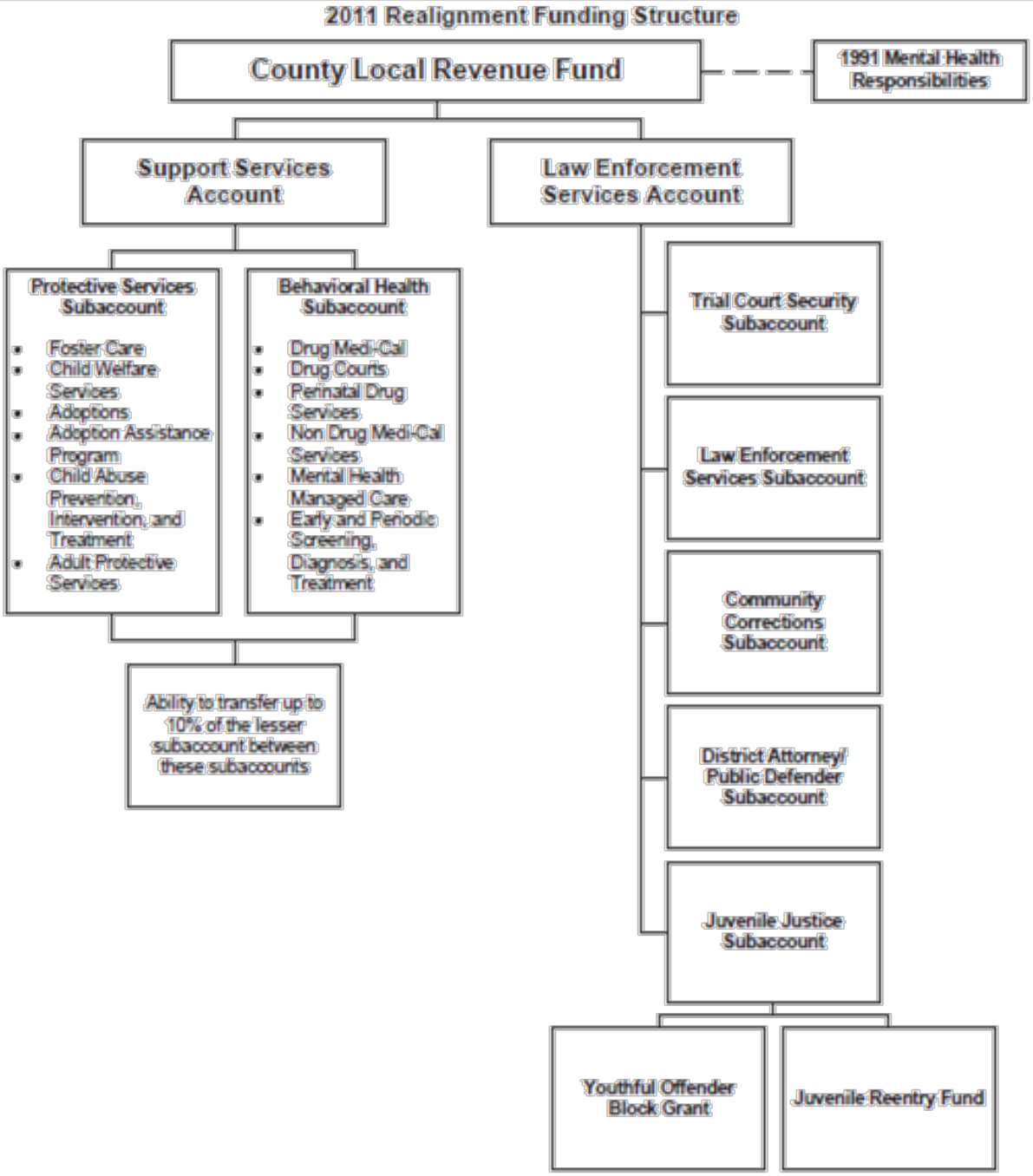
[1] Allocation is capped at $489.9 million.

[2] 2012-13 and 2013-14 growth is not added to subsequent fiscal year's subaccount base allocations.

[3] Growth does not add to base.

[4] Rolling base includes a $200 million Child Welfare Services Restoration and incremental funding for Chapter 559, Statutes of 2010 (AB 12). AB 12 funding increments consist of: $18.2m in 2012-13, $20.4m in 2013-14, and $15.3m in 2014-15.

[5] The Early and Periodic Screening, Diagnosis, and Treatment and Drug Medi-Cal programs within the Behavioral Health Subaccount do not yet have a permanent base.


2011 Realignment Funding Structure
County Local Revenue Fund
1991 Mental Health Responsibilities
Support Services Account
Law Enforcement Services Account
Protective Services Subaccount
Foster Care
Child Welfare Services
Adoptions
Adoption Assistance Program
Child Abuse Prevention, Intervention, and Treatment
Adult Protective Services
Behavioral Health Subaccount
Drug Medi-Cal
Drug Courts
Perinatal Drug Services
Non Drug Medi-Cal Services
Mental Health Managed Care
Early and Periodic Screening, Diagnosis, and Treatment
Ability to transfer up to 10% of the lesser subaccount between these subaccounts
Trial Court Security Subaccount
Law Enforcement Services Subaccount
Community Corrections Subaccount
District Attorney/ Public Defender Subaccount
Juvenile Justice Subaccount
Youthful Offender Block Grant
Juvenile Reentry Fund

Other Local Government Proposals

2011- 12

Eliminate redevelopment agencies

2012-13

MOE for In-Home Supportive Services

The Rest of the Story

- November, 2012 Proposition 30 guaranteed funding for 2011 Public Safety Realignment
- Mandate Protections for the State
- 50/50 funding for federal changes or court decisions
- Pay-as-you go legislation or regulations

What's Next?

- Health Care Reform
- Phase 2 Realignment?
- What haven't we thought of?

California's Governments Rely on a Variety of Taxes

State Taxes	Current Rate	Comments/Description
Personal Income	Marginal rates of 1% to 9.3% Additional 1% surcharge on high incomes (7% AMT[a])	Married couples with gross incomes of $27,426 or less need not file. The top rate applies to married couples' taxable income in excess of $86,934. The surcharge is placed on taxable incomes of $1 million or more.
Sales and Use	6.25%[b]	Applies to final purchase price of tangible items, except for food and certain other items.
Corporation		
General Corporations	8.84%[c] (6.65% AMT)	Applies to net income earned by corporations doing business in California.
Financial Corporations	10.84% (6.65% AMT plus adjustment)	For financial corporations, a portion of the tax is in lieu of certain local taxes.
Vehicle Fuel	18¢/gallon of gasoline or diesel fuel	Tax is collected from fuel distributors or wholesalers with equivalent taxes levied on other types of vehicle fuels.
Alcohol and Cigarette		Tax is collected from manufacturers or distributors. Equivalent taxes are collected on sale of other tobacco products.
Wine and beer	20¢/gallon	
Sparkling wine	30¢/gallon	
Spirits	$3.30/gallon	
Cigarettes	87¢/pack	
Horse Racing License Fees	0.4% to 2%	Fees/taxes are levied on amounts wagered. Rate is dependent on type of racing and bet, and where the wager is placed.
Insurance	2.35%	Insurers are subject to the gross premiums tax in lieu of all other taxes except property taxes and vehicle license fees.

Continued

California's Governments Rely on a Variety of Taxes (*Continued*)

Local Taxes	Current Rate	Comments/Description
Property	1% (plus any rate necessary to cover voter-approved debt)	Tax is levied on assessed value (usually based on purchase price plus the value of improvements and a maximum annual inflation factor of 2%) of most real estate and various personal and business property.
Local Sales and Use	1% to 2.5%[d]	Collected with state sales and use tax. Revenues go to cities, counties, and special districts.
Vehicle License Fee	0.65%[e]	Tax is applied to depreciated purchase price. It is collected by the state and distributed to cities and counties.
Other Local	Varies by jurisdiction	Types of taxes and rates vary by jurisdiction. Includes utility users tax, business license tax, and transient occupancy taxes.

[a] Alternative minimum tax.

[b] Includes rates levied for state-local program realignment and local public safety, and repayment of deficit-financing bonds.

[c] A 1.5 percent rate is levied on net income of Subchapter S corporations.

[d] A portion of sales and use tax revenues formerly received by local governments (0.25 percent) is used for debt service on the state's deficit-financing bonds. Local governments are compensated through additional property taxes.

[e] The state shifted additional property tax revenues to cities and counties beginning in 2004-05 to compensate for the vehicle license fee rate reduction from 2 percent.

Initiative Measures Have Had Major State-Local Fiscal Implications

Measure/Election	Major Provisions
Proposition 13/ June 1978	• Limits general property tax rates to 1 percent, limits increases in assessed value after a property is bought or constructed. • Makes Legislature responsible for dividing property tax among local entities. • Requires two-thirds vote for Legislature to increase taxes, and two-thirds voter approval of new local special taxes.
Proposition 4/ November 1979	• Generally limits spending by the state and local entities to prior-year amount, adjusted for population growth and inflation (now per capita personal income growth). • Requires state to reimburse locals for mandated costs.
Proposition 6/ June 1982	• Prohibits state gift and inheritance taxes.
Proposition 7/ June 1982	• Requires indexing of state personal income tax brackets for inflation.
Proposition 37/ November 1984	• Creates state lottery and allots revenue to education. • Places prohibition of casino gambling in State Constitution.
Proposition 62/ November 1986	• Requires approval of new local general taxes by two-thirds of the governing body and a majority of local voters (excludes charter cities).
Proposition 98/ November 1988	• Establishes minimum state funding guarantee for K-12 schools and community colleges.
Proposition 99/ November 1988	• Imposes a 25 cent per pack surtax on cigarettes and a comparable surtax on other tobacco products, and limits use of surtax revenue, primarily to augment health-related programs.
Proposition 162/ November 1992	• Limits the Legislature's authority over PERS and other public retirement systems, including their administrative costs and actuarial assumptions.
Proposition 163/ November 1992	• Repealed "snack tax" and prohibits future sales tax on food items, including candy, snacks, and bottled water.

Continued

Initiative Measures Have Had Major State-Local Fiscal Implications

Measure/Election	Major Provisions
Proposition 172/ November 1993	• Imposes half-cent sales tax and dedicates the revenue to local public safety programs.
Proposition 218/ November 1996	• Limits authority of local governments to impose taxes and property-related assessments, fees, and charges. • Requires majority of voters to approve increases in all general taxes, and reiterates that two-thirds must approve special taxes.
Proposition 10/ November 1998	• Imposes a 50 cent per pack surtax on cigarettes, and higher surtax on other tobacco products. • Limits use of revenues, primarily to augment early childhood development programs.
Proposition 39/ November 2000	• Allows 55 percent of voters to approve local general obligation bonds for school facilities.
Proposition 42/ March 2002	• Permanently directs to transportation purposes sales taxes on gasoline previously deposited in the General Fund. • Authorizes state to retain gasoline sales taxes in General Fund when state faces fiscal difficulties.
Proposition 49/ November 2002	• Requires that the state fund after-school programs at a specified funding level.
Proposition 57/ March 2004	• Authorizes $15 billion in bonds to fund budgetary obligations and retire the state's 2002-03 deficit.
Proposition 58/ March 2004	• Requires a balanced budget, restricts borrowing, and mandates creation of a reserve fund.
Proposition 1A/ November 2004	• Restricts state's ability to reduce local government revenues from the property tax, sales tax, and vehicle license fee.
Proposition 63/ November 2004	• Imposes an additional 1 percent tax on incomes of $1 million and over to fund mental health services.
Proposition 1A/ November 2006	• Limits state's ability to retain gasoline sales taxes in General Fund and constitutionally requires repayment of past-year loans to transportation.

Votes Required to Increase Taxes, Fees, Assessments, or Debt

Measure	Approval Requirement: Governing Body	Approval Requirement: Voters
State		
Tax	2/3	None
Fee or assessment	Majority	None
General obligation bond	2/3	Majority
Other debt	Majority	None
Initiative proposing new revenue or debt	None	Majority
Local		
Tax		
Funds used for general purposes	2/3[a]	Majority
Funds used for specified purposes	2/3[a]	2/3
Property assessment	Majority	Majority[b]
Fee	Majority	None
General obligation bond		
K-14 districts	2/3	55%
Cities, counties, and special districts	2/3	2/3
Other debt	Majority	None

[a] For most local agencies.

[b] Only affected property owners vote. Votes weighted by assessment liability.

- At the local level, most types of revenue increases require approval of both the governing body and the voters.

Paying for County, City, and Special District Services

2003-04

	Counties	Cities	Special Districts[a]
Total Revenues (*In Billions*)	**$46.3**	**$42.8**	**$8.6**
Sources of Revenues			
Property taxes	13%	7%	24%
Sales and other taxes	7	28	—
User charges, permits, assessments, fines	20	43	53
Intergovernmental aid	52	8	12
Other revenues	9	13	11

[a] Nonenterprise special districts only.

- Counties receive roughly half of their revenues from the state and federal government and must spend these funds on specific health and social services programs. About one-fifth of county revenues come from local taxes. Counties use tax revenues to pay for public protection and other local programs, as well as paying the required "match" for state and federal programs.
- Cities receive over 40 percent of their revenues from various user charges. Cities use these funds to pay for electric, water, and other municipal services. Over one-third of city revenues come from local taxes, the largest of which is the sales tax. Cities spend about one-fourth of their revenues on public safety programs, such as police and fire.
- Special district financing varies significantly based on the type of service the district provides.

Major Local Programs—2006-07

Program	Policy Control	Funding[a]
Education (K-14)	School Districts/State	
CalWORKs	State/Federal	
Child Welfare Services	State/Federal	
General Assistance	Counties/State	
Mental Health	Counties/State/Federal	
Substance Abuse Treatment	Counties/State/Federal	
Jails	Counties/State	
Probation	Counties/State	
Police/Sheriff	Local/State	
Trial Courts	State	
Parks and Recreation	Local	
Streets and Roads	Cities/Counties	

Federal State Local

[a]All funding distributions are LAO estimates.

Property Taxes

Property Taxes are a primary source of revenue for local governments. They are collected and distributed within individual counties and cannot cross county lines. Per the Constitution and state law, the revenue is allocated to cities, counties, schools (K-12 and community colleges), and special districts.

Unlike cities, counties, schools and special districts, which are funded through property taxes directly, redevelopment agencies are funded through property tax *increment*. When a local government forms a redevelopment agency, the existing property tax value of the redevelopment area becomes the base value. As property values increase over time, the portion that exceeds the base – known as the tax increment – goes to the redevelopment agencies to fund their activities.

Property Taxes Prior to 1978

Before Proposition 13 passed in June, 1978, the local assessor valued property periodically (generally on a 2-year cycle). Property values and tax bills could vary greatly from year-to-year.

The governing boards of cities, counties, schools, and special districts could control their revenues by increasing or decreasing property tax rates within their jurisdictions (within some limits) as they saw fit.

Before 1978, the average statewide combined tax rate was 2.67 percent.

Proposition 13 – What Did It Do?

Limited the property tax rate to 1 percent, except for preexisting indebtedness.

The assessed value of all property was rolled back to its 1975-76 value.

Assessed value can increase by inflation, not to exceed 2% annually. When there is a change in ownership or completion of construction, the property is assessed at its fair market value (usually the purchase price).

No other property, sales or transaction tax can be levied on real property.

The allocation of the property tax was now subject to state statute – the Constitution was amended to read "apportioned according to law". Previously, each taxing entity received the revenue from the rate it imposed.

The fiscal effect was a loss of about 55 to 57 percent of property tax or almost $7 billion.

For counties, property taxes declined as a revenue source from 34% to 22%.

Prop 13 severely limited future growth from property tax revenue.

Prop 13 also established a two-thirds vote requirement for raising taxes at the state level and a two-thirds vote for special taxes at the local level.

What are some of the unintended consequences of Prop 13?

Concentrated fiscal power at the state level; counties administer programs for the state but have limited authority to raise money for their share of cost or to raise money for those county-wide local programs.

Made locals more dependent on the sales tax.

Led to a greater reliance on fees – developer fees, assessment district fees as well as the use of other financing methods – e.g. Mello-Roos districts.

Increased the State's role in the delivery and financing of local services.

The State's Response to Prop 13

1978 – a one-year bailout plan; essentially an allocation of property taxes from schools to other local entities to back-fill about 94% of the loss in property tax revenue. For counties, the bailout was $424 million in state aid plus a buy-out of the county share of cost for Medi-Cal, SSI/SSP and Food Stamp Administration plus an increased state share of AFDC and Foster Care. Total value of the county bail out was about $1.5 billion.

1979 – AB 8 Long Term Fiscal Relief for Local Government

The value of the fiscal relief was about $4.8 billion.

A portion of the property tax base was shifted from schools to cities, counties and special districts; the state assumed a greater share of the costs for schools.

For counties, their property tax base was increased by the block grant amount provided in 1978-79, adjusted by changes in state funding of certain health and human services programs. These included permanent buy out of the county share of cost for Medi-Cal, SSI/SSP and the Adoptions program and assumption of the total "AB 8" public health subvention. There were also changes in the state sharing ration of other health and human services programs.

There was a "deflator" included in AB 8. In recognition of the fact that the state might not be able to sustain funding the bailout, AB 8 contained a "trigger", designed to reduce the bailout to local governments and schools, on a permanent basis if state revenues fell short of a particular rate.

Points to Consider Regarding AB 8

The relative share of property tax received by each local agency varied considerably by county because their tax rates varied considerably prior to Proposition 13.

Counties varied in the level of service they provided; the proportion of areas incorporated; the population in unincorporated areas and wealth. Therefore, service demands could quite easily outpace available revenue.

Counties provide a number of services on a countywide basis (assessor, DA, General Assistance, indigent health, county jails, probation) but under Proposition 13 had limited mechanisms to raise revenue to meet those needs. AB 8 did not take that into account.

The proportion of the state's buyout of health and human services programs varied considerable by county.

All of these factors, funding of a particular service level plus all the potential inequities, were locked into place by the AB 8 formula.

Has the question been asked, does a 1 percent rate, allocated among several local jurisdictions, leave enough resources for the county to fund what are considered "local" services? The question has been asked and the demonstrated answer is "no".

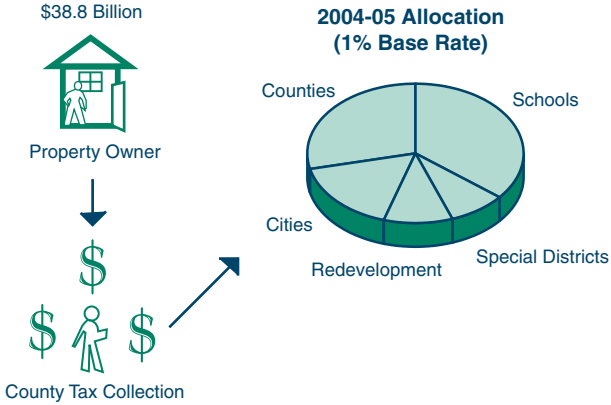
Property Taxes

TABLE 15—2006-07 GENERAL PROPERTY TAX DOLLAR[a], BY COUNTY

County	Property tax dollars[b]				
	City	County[c]	School[c]	Other districts	Total
1	2	3	4	5	6
Alameda	$.20	$.14	$.43	$.23	$1.00
Alpine	--	.62	.26	.12	1.00
Amador	.04	.32	.62	.02	1.00
Butte	.05	.11	.62	.22	1.00
Calaveras	.01	.18	.68	.13	1.00
Colusa	.06	.26	.59	.09	1.00
Contra Costa	.08	.12	.50	.30	1.00
Del Norte	.01	.18	.64	.17	1.00
El Dorado	.02	.22	.49	.27	1.00
Fresno	.12	.13	.63	.12	1.00
Glenn	.06	.20	.69	.05	1.00
Humboldt	.03	.19	.64	.14	1.00
Imperial	.08	.13	.61	.18	1.00
Inyo	.01	.28	.61	.10	1.00
Kern	.05	.25	.59	.11	1.00
Kings	.07	.22	.54	.17	1.00
Lake	.02	.22	.55	.21	1.00
Lassen	.04	.20	.71	.05	1.00
Los Angeles	.15	.21	.45	.19	1.00
Madera	.03	.14	.72	.11	1.00
Marin	.11	.17	.59	.13	1.00
Mariposa	--	.26	.69	.05	1.00
Mendocino	.01	.27	.60	.12	1.00
Merced	.07	.22	.62	.09	1.00
Modoc	.03	.27	.64	.06	1.00
Mono	.04	.30	.42	.24	1.00
Monterey	.06	.16	.63	.15	1.00
Napa	.10	.19	.66	.05	1.00
Nevada	.07	.14	.58	.21	1.00
Orange	.10	.07	.62	.21	1.00
Placer	.07	.17	.64	.12	1.00
Plumas	.01	.21	.67	.11	1.00
Riverside	.06	.11	.49	.34	1.00
Sacramento	.10	.17	.52	.21	1.00
San Benito	.02	.12	.59	.27	1.00
San Bernardino	.06	.10	.43	.41	1.00
San Diego	.12	.13	.62	.13	1.00
San Francisco	--	.61	.31	.08	1.00
San Joaquin	.10	.19	.57	.14	1.00
San Luis Obispo	.08	.24	.61	.07	1.00
San Mateo	.10	.14	.61	.15	1.00
Santa Barbara	.05	.19	.60	.16	1.00
Santa Clara	.09	.14	.62	.15	1.00
Santa Cruz	.06	.12	.57	.25	1.00
Shasta	.06	.13	.65	.16	1.00
Sierra	.01	.52	.33	.14	1.00
Siskiyou	.06	.21	.69	.04	1.00
Solano	.13	.16	.46	.25	1.00
Sonoma	.06	.20	.60	.14	1.00
Stanislaus	.06	.11	.73	.10	1.00
Sutter	.09	.16	.64	.11	1.00
Tehama	.04	.25	.68	.03	1.00
Trinity	--	.29	.66	.05	1.00
Tulare	.05	.20	.60	.15	1.00
Tuolumne	.01	.29	.63	.07	1.00
Ventura	.08	.16	.52	.24	1.00
Yolo	.18	.09	.56	.17	1.00
Yuba	.03	.21	.68	.08	1.00
Totals	$.11	$.17	$.53	$.19	$1.00

a. Includes ad valorem levies for debt service on land and/or improvements only, but excludes special assessments levied on other than an ad valorem basis (e.g., per parcel).
b. These proportions are based on the initial allocations as shown in Table 14 without any adjustment for the subsequent allocation of ERAF funds to either the Sales and Use Tax Compensation Fund or to cities and counties due to the Vehicle License Fee swap.
c. County levies for school purposes such as junior college tuition and countywide school levies are included with school levies.

Property Taxes Are Distributed to Many Entities Within a County



- Property taxes are collected by each county government. The revenues are then distributed to a variety of governments, including the county, cities, school districts, redevelopment agencies, and special districts.
- The property tax rate is limited to 1 percent by the Constitution, plus any additional rate necessary to pay for voter-approved debt. The average tax rate across the state in 2004-05 was 1.09 percent.
- Property tax revenues collected in a county can be distributed only to a local entity within that county.
- Until the state's deficit-financing bonds are completely paid off, about one-tenth of the schools' share of property taxes is redirected to cities and counties. The state backfills the school losses.

California's Property Tax Has Changed Significantly

Dollars in Billions

		Tax Distribution			
Years[a]	Revenue	Schools	Counties	Cities	Other[b]
1977	$10.3	53%	30%	10%	7%
1979	5.7	39	32	13	16
1994	19.3	52	19	11	18
2005	35.4	34	28	19	19

[a] Information for 1977 includes debt levies. Data for 2005 is estimated.

[b] Redevelopment agencies and special districts.

- 1977—Before 1978, local agencies determined the property tax rate and its distribution of revenues.

- 1979—Proposition 13 (1978) set a maximum tax rate of 1 percent and shifted control over the distribution of property taxes to the state. The state basically prorated these revenues among local agencies except that it gave a smaller share to schools and backfilled the schools' losses with state aid.

- 1994—Facing fiscal pressure in the early 1990s, the state modified the distribution of property taxes to give a greater share to schools (thereby reducing state school spending).

- 2005—The state shifted a greater share of property taxes to cities and counties to offset their losses due to the (1) reduction in the vehicle license fee rate and (2) use of local sales taxes to pay the state's deficit-financing bonds.

Extensive Use of Redevelopment by Local Agencies in Some Counties

	Percent of 2004-05 Countywide:	
	Property Value Under Redevelopment	Property Taxes to Redevelopment
Top Four Counties		
Butte	38%	26%
Riverside	33	24
San Bernardino	35	25
Santa Cruz	26	16
Statewide Average	15	10
Selected Other Counties		
Los Angeles	16%	10%
Sacramento	7	5
San Francisco	7	7

- If a city or county creates a redevelopment project area to address urban blight, its redevelopment agency receives the future growth in property taxes from the area. (Absent redevelopment, schools and other local agencies receive these tax revenues.)
- Redevelopment projects range from 2 acres to over 46,000 acres. Local agencies in four counties have placed so much property under redevelopment that more than one-quarter of their countywide assessed property value is under redevelopment.
- Statewide, redevelopment agencies receive 10 percent of property taxes paid by property owners, but this percentage varies significantly at the local level. The City of Fontana's redevelopment agency receives more than 77 percent of property taxes paid in the city.

Realignment – 1991

As part of a strategy to balance the 1991-92 budget (with a shortfall of $14.3 billion), a realignment of programs between the state and the counties with a tax increase (an alcohol tax and a VLF depreciation schedule change) was proposed in Governor Wilson's first Budget (January, 1991)

Ultimately the sales tax was increased by one-half cent and the VLF depreciation schedule was adjusted to increase revenue to match the "cost" of the programs being realigned – about $2.2 billion. Because of the recession, the first year of revenue was actually about $1.9 billion. Currently, Realignment revenues exceed $3 billion.

Chapters 87, 89, and 91, Statutes of 1991, established the State-Local Realignment Program by changing counties' responsibilities with regard to a variety of health, mental health, and social services programs. The legislation also provided that the increased revenue be deposited into the Local Revenue Fund to provide funding for these programs. It also contained formulas for distributing funds into a variety of accounts and subaccounts and instructions to the State Controller for disbursement of funds to the counties. Originally sales tax revenues were directed to all three Realignment accounts while VLF was largely directed to the Health account.

Chapter 100, Statutes of 1993, specified the process for distribution of growth in realignment revenues above the base amount available in the prior year. It provided that revenue in excess of that required to fund the base, be used to fund the Caseload Subaccount, the County Medical Services Subaccount, the five "equity" subaccounts (Special Equity, Indigent Health Equity, Community Health Equity, Mental Health Equity, and State Hospital Mental Health Equity) and the General Growth Subaccount.

All Realignment sales tax growth revenue is first directed to cover growth costs of the realigned Social Services programs. Once caseload growth costs have been funded in the Social Services Account, the Health and Mental Health accounts receive a portion of remaining growth money.

Transfers Between Accounts

Counties are allowed to transfer funds among the Health, Mental Health and Social Services accounts. Each county is allowed to transfer up to 10% of any account's revenue to the other two accounts. In order to do so, the county must document at a public meeting that the decision is being made to ensure the most cost-effective provision of services.

An additional 10% may be transferred from a county's Health Account to the Social Services Account under specified circumstances. Most counties have used this flexibility to support the Social Services entitlement programs.

The Caseload Subaccount: Under Realignment, counties' share-of-cost for some programs increased (e.g. Foster Care), while their share-of-cost for other programs decreased (e.g. AFDC, now CalWORKs). If shares were increased, county costs increased and decreased shares resulted in savings. Because the increased costs could exceed the savings, mandate claims for these increased county costs are avoided through the Caseload Subaccount. Due to the potential for unfunded mandates, the Caseload Subaccount is the first subaccount funded with sales tax revenue above the prior year's base amount. The calculation results in a "net" cost to the counties depending on caseload growth and some policy changes in the programs with the changed sharing ratios.

Requirements: In order to receive allocations from the Realignment accounts, each county is required to establish and maintain a local health and welfare trust fund comprised of three subaccounts (health, social services, and mental health). Since VLF moneys are constitutionally defined as local revenues, their use cannot be specified in State law. However, because the purpose of providing the dedicated revenue source to counties was to fund the realigned programs, the statute requires counties to deposit county general fund monies into the health and welfare trust fund in an amount equal to the VLF being deposited in order to receive an allocation from the sales tax. Realignment statute also requires that sufficient county general fund to meet maintenance-of-effort requirements in various health and mental health programs.

Poison Pills: At the time Realignment was enacted, there was some uncertainty about potential legal and constitutional challenges. To address the uncertainty, a series of "poison pills" were attached to various provisions. These poison pills provide that components of Realignment would become inoperative if certain conditions occur. Only one of the poison pills, the VLF, has been "pulled" so far and it has subsequently been repealed.

VLF Poison Pill

The VLF trigger provided that the depreciation schedule would become inoperative upon a final judicial determination by the California Supreme Court or California Court of Appeal that either 1) the allocation of funds from the VLF Growth Account of the Local Revenue Fund is in violation of the constitutional requirement that all revenues from the VLF shall be allocated to cities and counties according to statute (Art. XI, Sec 15) or 2) the State is obligated to reimburse counties for costs of providing medical services to medically indigent adults pursuant to Chapters 328 and 1594 of the Statures of 1982.

The VLF poison pill was triggered March 1, 2004 as a result of the second condition being met by a final court determination in the case of *County of San Diego v. Commission on Mandates* (2003). The impact of the poison pill was avoided by the adoption of emergency regulations by DMV maintaining the existing depreciation schedule and the VLF poison pill provisions were repealed by Chapter 211, Statutes of 2004.

Sales and Excise Tax Poison Pill

The poison pill for the sales and excise taxes provides that the increases authorized by Section 6051.2 (sales tax) and Section 6201.2 (excise tax) shall become inoperative after a determination by the California Supreme Court or California Court of Appeal that the revenues collected and deposited into the Local Revenue Fund are either 1) General Fund proceeds of taxes appropriated pursuant to Article XIIIB of the California Constitution or 2) "allocated local proceeds of taxes" as used in Subdivision (b) of Section 8 of Article XVI of the California Constitution (Proposition 98).

Program Shift and Cost Sharing Poison Pill

The third and final poison pill, if triggered, would render inoperative all of the provisions of Realignment if there is a determination by the Commission on State Mandates which is not appealed by the Department of Finance, or a determination by the California Supreme Court or California Court of Appeal that any provision of those acts is a state mandated local program requiring State reimbursement. This poison pill would be triggered only if the estimated statewide cost of reimbursement exceeds $1.0 million on an annual basis.

It is unclear exactly what would occur if the Realignment legislation, or a significant portion of it, becomes inoperative. If counties were required to continue to fund these programs at the Realignment level, it would seem that they would have a strong case for a mandate claim. However, undoing Realignment statutes might shift these costs back to the State.

Components of 1991-92 State-Local Realignment

Transferred Programs			Cost Shift to Counties (1991-92 in millions)
Mental Health			$750
Community			452
State Hosp for County Patients			210
IMDs			88
Public Health			$506
AB 8 CHS)_			503
Local HS			3
Indigent Health			$435
MISP			348
CMSP			87
Local Block Grants			$52
Stabilization			15
Juvenile Justice			37
County Cost-Sharing Ratio Changes	State/County of Nonfederal Costs prior law	State/County of Nonfederal Costs Realignment	1991-92 costs shifted
Health			$30
CCS	75/25	50/50	30
Social Services			$441
AFDC-FC	95/5	40/60	363
CWS	76/24	70/30	42
IHSS	97/3	65/35	235
CSBG	84/16	70/30	13
Adoptions	100/0	75/25	12
GAIN	100/0	70/30	26
AFDC – FG + U	89/11	95/5	-155
County Admin (AFDC-FC, FG, U Foodstamps	50/50	70/30	-95
Additional County Exp.			$2,212

from the Department of Motor Vehicles to the Franchise Tax Board (FTB) in order to increase the effectiveness of delinquent collections. The first $14 million collected annually by the FTB is allocated to counties' mental health accounts as part of realignment. The distribution schedule is developed by the State Department of Mental Health in consultation with the California Mental Health Directors Association.

Jurisdictions Affected

All counties are affected by realignment and receive funding from the two revenue sources. In addition, a few cities also receive realignment funding due to their historical responsibility for some of the realigned programs. Berkeley receives funding for both mental health and health programs. Long Beach and Pasadena receive funding for health programs. The Tri-City area (Claremont, LaVerne, and Pomona) receives funding for mental health programs.

Allocation of Revenues

The original allocations to each jurisdiction were based on their level of funding in these program areas just prior to realignment. These allocations, as of 1991, were in many cases rooted in historical formulas and spending patterns. For instance, funding for the AB 8 county health programs was based on county spending in the 1970s for such programs. As such, realignment did not represent an overhaul of the historical allocation formulas in these program areas. Instead, the realignment formulas emphasized maintaining the county funding levels in existence at the time of its enactment.

The realignment legislation established a revenue allocation system in which the total amount of revenues received in one year becomes the base level of funding for the following year for each jurisdiction (excluding the VLF delinquent collections allocation). For instance, a county's total realignment allocation in 1997-98 became its base level of revenues for 1998-99. Growth in revenues between the two years was then allocated based on a series of statutory formulas. Thus, a county's base revenues in 1998-99 plus any growth revenues received in that year becomes the base for 1999-00.

Figure 2 (see page 8) illustrates how these revenues are allocated. The allocation of growth revenues is described in more detail below.

Growth Revenues. Any amount by which the sales tax and VLF realignment revenues have grown is deposited into a series of state subaccounts, each associated with one of the mental health, social services, or health accounts of each county. Sales tax growth funds are first committed to the:

- ***Caseload Subaccount.*** The caseload subaccount (part of the social services account) provides funds to repay counties for the changes in cost-sharing ratios for specified social services programs (and CCS, a health program) implemented as part of realignment. The payments from the caseload subaccount are calculated based on annual changes in caseload costs and made a year in arrears. The

payments to each county are the *net* of all changes in caseload costs when compared to their costs under pre-realignment cost-sharing ratios. In other words, the county payments are adjusted to reflect both cost increases and savings due to caseload changes.

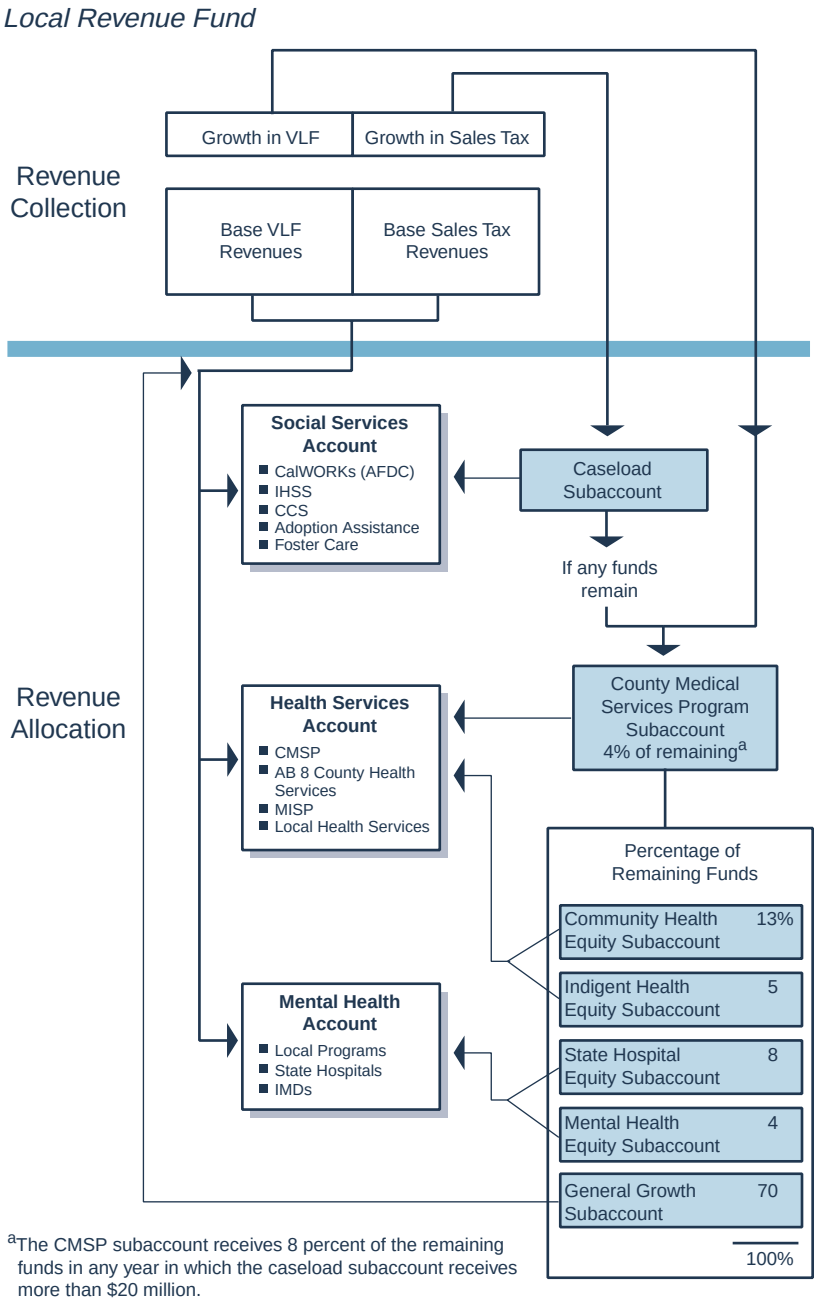
Any remaining sales tax growth funds and *all* VLF growth funds are allocated to the following subaccounts (which then flow back into one of the three main accounts, as noted in parentheses).

- ***County Medical Services Program Subaccount.*** The CMSP subaccount (health account) provides funding for health programs to those counties which participate in CMSP.

- ***General Growth Subaccount.*** The general growth subaccount (all three accounts) makes its allocations to counties in proportion to their share of state funding for the non-social services caseload realigned programs.

Figure 2

Allocation of Realignment Revenues



[a]The CMSP subaccount receives 8 percent of the remaining funds in any year in which the caseload subaccount receives more than $20 million.

- ***Equity Subaccounts.*** There are four active subaccounts designed to provide payments to those counties below the statewide average in various components of health and mental health funding. The statewide average for equity is defined in statute by a formula based on population and poverty. These equity subaccounts will cease operating within several years when their total lifetime allocations reach $207.9 million. The four subaccounts are the *Community Health Equity Subaccount* (health account), *Indigent Health Equity Subaccount* (health account), *State Hospital Equity Subaccount* (mental health account), and *Mental Health Equity Subaccount* (mental health account).

Figure 3 summarizes the specific distributions of revenues in 1998-99, when realignment revenues totaled $2.9 billion. In that year, the total amount owed the caseload subaccount exceeded the total growth in sales-tax revenues. Consequently, no other subaccount received funding from the sales tax growth in 1998-99, and the remaining 1998-99 caseload obligation is allocated from the 1999-00 sales tax growth. In those years where caseload allocations account for the entire amount of sales tax growth, VLF growth funds are allocated to the subaccounts in the same proportion as the 1996-97 allocations.

Figure 3

Distribution of Realignment Revenues

1998-99
(In Millions)

	Account			
	Mental Health	Social Services	Health	Total
Base Revenues (from 1997-98)	$888	$691	$1,144	**$2,723**
Growth Subaccounts				
Caseload		$96		**$96**
CMSP	—	—	$9	**9**
Community Health Equity	—	—	11	**11**
Indigent Health Equity	—	—	5	**5**
State Hospital Equity	$6	—	—	**6**
Mental Health Equity	4	—	—	**4**
General Growth	25	5	29	**59**
Totals	**$923**	**$792**	**$1,197**	**$2,912**
VLF Collections	$14	—	—	**$14**
Total Revenues	**$937**	**$792**	**$1,197**	**$2,926**

Note: Totals may not add due to rounding.

Transfer Provisions

Although funds are deposited into the three separate accounts in each county, the realignment statute allows for transfers of dollars among these accounts in certain circumstances. These transfers allow counties to adjust program allocations to best meet their service obligations.

Each county is allowed to transfer up to 10 percent of any account's annual allocation to the other two

accounts. In order to take advantage of this provision, the county must document at a public meeting that the decision is being made to ensure the most cost-effective provision of services. Each county may transfer an additional 10 percent *from* the health account *to* the social services account under specified conditions. Each county may also transfer an additional 10 percent *from* the social services account *to* the mental health or health accounts under specified conditions. All transfers apply for only the year in which they are made, with future allocations based on the pre-transfer amounts.

"Poison Pill" Provisions

At the time of the enactment of the realignment statutes, it was unclear whether the legality or constitutionality of any of the components would be challenged. Therefore, a series of "poison pill" provisions were put into place that would make components of realignment inoperative under specified circumstances. These provisions are still active and fall into three types.

Reimbursable Mandate Claims. If, as a result of the realignment provisions, (1) the Commission on State Mandates adopts a statewide cost estimate of more than $1 million or (2) an appellate court makes a final determination that upholds a reimbursable mandate, the general provisions regarding realignment would become inoperative.

Constitutional Issues. Although local entities receive their realignment VLF allocations as general purpose revenues, the realignment statute requires that each entity must then deposit an equal amount of revenues into their health and mental health accounts. Section 15 of Article XI of the State Constitution requires VLF revenues to be subvened to cities and counties. If a final appellate court decision finds that the realignment provisions related to VLF deposits violate the Constitution, the VLF tax increase from 1991 would be repealed.

Similarly, if a final appellate court decision finds that revenues from the half-cent realignment sales tax are subject to Proposition 98's education funding guarantee, this portion of the sales tax would be repealed.

Court Cases Related to Medically Indigent Adults. If a final appellate court decision finds that the 1982 legislation that transferred responsibility from the state to counties for providing services to medically indigent adults constitutes a reimbursable state mandate, the VLF increase would be repealed.

If any of these poison pill provisions were to take effect, the affected statute would become inoperative within three months, with the precise timing dependent on the particular provision.

Proposition 1A – Changes to Local Finance

In November, 2004, the voters approved Proposition 1A (SCA 4) which restricts the state's ability to reduce local government from the property tax, sales tax, and vehicle license fee. (Article XIII, Sec 25.5)

Specifically, in terms of the **property tax**, 1A states:

The Legislature may not permanently shift property tax revenues from other local governments to schools.

The Legislature may shift property tax revenues temporarily from other local government to schools under certain circumstances (this provision may only be used twice every 10 years and may not be used unless the first amount borrowed is repaid):

- The Governor declares a "severe state fiscal hardship".
- Two-thirds of the Legislature votes to suspend Prop 1A.
- The amount of property tax revenue shifted in each county is limited to 8 percent of prior-year noneducation agency property taxes.
- The Legislature enacts a statute, at the same time, to provide repayment within three years.

The Legislature can only change a city's, county's or special district's share of the property tax with a two-thirds vote of both Houses.

The Legislature may not use property tax revenue to reimburse locals for mandated programs.

In terms of the **sales tax**, 1A states:

With limited exception, the Legislature may not reduce any local sales tax rate, limit existing local authority to levy a sales tax, or change the allocation of local sales tax revenues.

The Legislature may not extend the "triple flip" or reduce the property taxes provided to cities and counties as replacement for the local sales taxes pledged to pay debt service on the state's Economic Recovery Bonds (ERBs).

In terms of **Vehicle License Fees (VLF)**, 1A states:

The Legislature can not reduce the VLF rate below 0.65 percent, unless it provides replacement funding to cities and counties.

If, the Legislature increases the VLF rate above 0.65 percent, there are no restrictions on the use of the additional revenue.

State Mandated Local Programs

SB 90

Chapter 1406, Statutes of 1972 (SB 90), also known as the "Property Tax Relief Act of 1972", among other things began to place some limitations on the ability of local governments to increase local property tax rates to support their operations. In view of the limitation, the legislation also provided that if the State mandated either a new program or a higher level of service in an existing program, either through legislation or administrative regulation, the State would provide additional funding to carry out the program so locals wouldn't have to reprioritize local programs to pay for the new mandate. Of course, since these provisions were statutory, it was possible for the Legislature to waive or "disclaim" the reimbursement requirement in any legislation that imposed a new mandate.

The first administrative body the Legislature empowered to hear mandate claims was the Board of Control.

Proposition 4

In 1979, the voters passed Proposition 4 (the Gann Initiative) which added Article XIIIB to the Constitution limiting the growth in the appropriation of certain tax proceeds for the State and local governments, including schools.

Section 6 of Article XIIIB further specified local mandate reimbursement requirements:

"Sec 6 (a) Whenever the Legislature or any state agency mandates a new program or higher level of service on any local government, the State shall provide a subvention of funds to reimburse that local government for the costs of the program or increased level of service, except that the Legislature may, but need not, provide a subvention of funds for the following mandates:

(1) Legislative mandates requested by the local agency affected.
(2) Legislation defining a new crime or changing an existing definition of a crime.

(3) Legislative mandates enacted prior to January 1, 1975, or executive orders or regulations initially implementing legislation enacted prior to January 1, 1975."

What are the flaws in Section 6 from a local government perspective?

Over time, there was dissatisfaction with the Board of Control's work on mandate reimbursement. Chapter 1459, Statutes of 1984, added sections 17500 et seq. to the Government Code which created the Commission on State Mandates as a quasi-judicial body with the exclusive authority to interpret and implement Article XIIIB, Section 6.

Some statutory guidelines were included in he legislation but in reality, relatively little was understood about mandates were to be interpreted. Because of this, the courts have had to interpret many of the key terms and concepts and few have been codified. For example, in *County of Los Angeles et al. v. State of California, 43 Cal. App. 3d, 46* (1987), the court found that the term "higher level of service"….must be read in conjunction with the predecessor phrase "new program" to give it meaning. But the term "program" is not defined.

Mandate Relief

During the fiscal crisis of the 1990's, hundreds of hours were spent on trying to come to agreement on "mandate relief" to help mitigate the property tax shifts. It was extremely difficult for all parties to agree that a particular mandate should be "suspended", and thus, not funded though some relief was provided.

Over time, it became more or less routine to defer payments to local government for mandates as a mechanism to help balance the State budget.

Proposition 1A

Because of concerns over the State's untimely payment of mandate claims, locals included mandate provisions in Proposition 1A.

Specifically, Proposition 1A requires the state to pay mandate bills in the annual budget, or suspend or repeal the mandate. This provision does not apply to education or employee relations mandates.

Proposition 1A also authorizes payable claims from prior to 2004 and that had not been paid by 2005-06, to be paid over time as prescribed by law.

Property tax revenue cannot be used to reimburse local government for the costs of a new program or higher level of service.

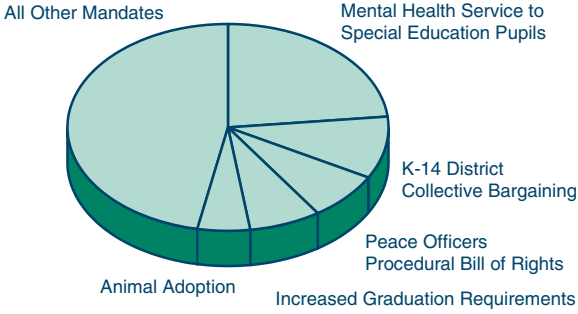
Proposition 1A also expands the definition of a mandate to include transfers of financial responsibility from the state to local government. Specifically, transfers may be reimbursable mandates if:

- The Legislature shifts complete or partial financial responsibility to cities, counties or special districts
- The program is required (not optional)
- The State previously had complete or partial financial responsibility for the program

This provision was added to make certain the state, as part of balancing its budget, could not shift programs to the locals without reimbursement.

Five State Mandates Account for Half of the State's Payments

$440 Million
(Estimated 2006-07 Costs)



- If the state mandates that a local government provide a new program or higher level of service, the Constitution generally requires the state to provide reimbursement.

- School districts, counties, and other local governments currently implement over 80 state reimbursable mandates. Five mandates account for about half of the state's annual mandate payments.

- The state has accumulated a large backlog of unpaid mandate bills, which it is beginning to pay. In 2006-07, these mandate bills totaled more than $1 billion.

- The Legislature may "suspend" a mandate in the budget act. Suspending a mandate makes local agency implemention of the mandate optional for one year. In 2006-07, the state budget suspended more than 30 mandates. Some of these mandates have been suspended annually for over a decade.

Realignment

The finances of the state and local governments have been closely linked since the passage of Proposition 13 in 1978. Counties have been heavily dependent on state budget decisions regarding programs in which they share the cost and programs they administer for the state.

Government is most effective at the local level, where locally elected officials can tailor programs to local needs and priorities. In a state as diverse as California, it is difficult to establish programs that are equally effective and make sense in both large urban and small rural areas.

Over the past three decades, there have been attempts to clarify and simplify which level of government pays for what services. These efforts include the 1991 Realignment program, in which counties assumed responsibility for community mental health and indigent health funding, and the 1997 state assumption of trial court funding designed to bolster equal access to justice for citizens across the state.

2011 Public Safety Realignment

The 2011 Budget includes a major realignment of public safety programs from the state to local governments. The realignment moves program and fiscal responsibility to the level of government that can best provide the service, eliminating duplication of effort, generating savings, and increasing flexibility. The implementation of the Community

Corrections Grant Program authorized by AB 109 will end the costly revolving door of lower-level offenders and parole violators through the state's prisons.

The goals of realignment are to:

- Protect California's essential public services.
- Create a government structure that meets public needs in the most effective and efficient manner.
- Have government focus on core functions.
- Assign program and fiscal responsibility to the level of government that can best provide the service.
- Have interconnected services provided at a single level of government.
- Provide dedicated revenues to fund these programs.
- Provide as much flexibility as possible to the level of government providing the service.
- Reduce duplication and minimize overhead costs.
- Focus the state's role on appropriate oversight, technical assistance, and monitoring of outcomes.

With resources and program responsibility at the local level, each county Board of Supervisors can integrate programs across the spectrum of health and human services and law enforcement to best meet the needs of its citizens, limit program cost increases, and achieve better outcomes.

Constitutional Protection

The Governor is sponsoring an initiative to provide Constitutional protection for the revenue dedicated to 2011 Realignment. This initiative will also protect local government against future costs imposed upon them, as well as provide mandate protection for the state.

Realigned Programs

2011 Realignment gives counties the funding responsibility for:

- Substance Abuse Treatment programs

- Adult Protective Services
- Foster Care
- Child Welfare Services
- Adoptions and Adoption Assistance
- Child Abuse Prevention
- Mental Health Managed Care
- Early Periodic Screening, Diagnosis, and Treatment (EPSDT) Program
- Court Security
- Local Law Enforcement Programs (which include allocations for cities)
- Community Corrections Programs (Lower-Level Offenders, Parole, and Parole Violators)
- Juvenile Justice Programs

In addition, community mental health programs previously funded in 1991 Realignment are now funded by revenue dedicated for 2011 Realignment. The 1991 Realignment funding previously dedicated to mental health programs is allocated to a new Maintenance of Effort Subaccount in 1991 Realignment to cover costs of cash assistance grants to low-income families.

Funding Model for Lower-Level Offenders, Parole, and Parole Violators

As part of the implementation of AB 109, the Department of Finance developed a funding model based on assumptions about costs of activities for these offenders at the local level. For each category (parole violators, parolees, and local jurisdiction for lower-level offenders), an Average Daily Population was determined along with assumptions about average length of jail stays, program and treatment costs, and probation monitoring costs, as well as administrative costs. The California Department of Corrections and Rehabilitation developed month-by-month projections of persons on post-release community supervision and numbers of lower-level offenders in order to assist counties in planning for program needs.

The 2011-12 county funding allocation for this program was developed by the California State Association of Counties, working with county executive officers, using three factors —the estimates of the number of offenders who would be under the jurisdiction of each county, each county's population between the ages of 18 to 64, and a county's success under the felony probation program initiated under Chapter 608, Statutes of 2009 (SB 678).

The allocation for the community corrections programs was for 2011-12 only in order to gain more program experience before determination of a permanent allocation.

Local Implementation of Community Corrections Programs

Each county is required to have a Community Corrections Partnership, which is charged with developing an implementation plan to deal with the population serving their sentence at the local level. Most counties have completed their plans and offer a wide range of intermediate sanctions, supervision, and treatment options in addition to appropriate jail time. For example, counties can utilize Pre-Trial Release Programs with enhanced supervision, Day Reporting Centers, and flash incarceration in addition to providing behavioral health assessments and treatment, housing, and employment services. These intermediate sanctions and treatment services can help prevent the revolving door of the corrections system.

With only three months of information available, it is difficult to gauge exactly how numbers to date are tracking to 2011 Budget Act estimates on a county-by-county basis. The Administration will continue to work closely with counties to monitor and analyze the information to see if adjustments are necessary. This information will be useful in developing future allocations.

2011 Realignment Funding

The 2011 Realignment is funded through two sources – a state special fund sales tax of 1.0625 percent totaling $5.1 billion and $462.1 million in Vehicle License Fees (VLF).

Figure REA-01 identifies the programs and funding for 2011 Realignment.

At the time of the final Budget, the estimate for 2011-12 sales tax was $5,105.7 million. This estimate has been revised to $5,107 million. The 2011-12 VLF estimate at the time of budget enactment was $453.4 million. This estimate has been revised upward to $462.1 million. Pursuant to Chapter 40, Statutes of 2011, these funds are deposited into

Figure REA-01

2011 Realignment Funding

(Dollars in Millions)

Program	2011-12	2012-13	2013-14	2014-15
Court Security	$496.4	$496.4	$496.4	$496.4
Local Public Safety Programs	489.9	489.9	489.9	489.9
Local Jurisdiction for Lower-level Offenders and Parole Violators				
Local Costs	239.9	581.1	759.0	762.2
Reimbursement of State Costs	957.0	-	-	-
Realign Adult Parole				
Local Costs	127.1	276.4	257.0	187.7
Reimbursement of State Costs	262.6	-	-	-
Mental Health Services				
Early and Periodic Screening Diagnosis and Treatment	-	544.0	544.0	544.0
Mental Health Managed Care	-	188.8	188.8	188.8
Existing Community Mental Health Programs	1,104.8	1,164.4	1,164.4	1,164.4
Substance Abuse Treatment	179.7	179.7	179.7	179.7
Foster Care and Child Welfare Services	1,562.1	1,562.1	1,562.1	1,562.1
Adult Protective Services	54.6	54.6	54.6	54.6
Existing Juvenile Justice Realignment	95.0	98.8	100.4	101.3
Program Cost Growth	-	180.1	443.6	988.8
Total	**$5,569.1**	**$5,816.3**	**$6,239.9**	**$6,719.9**
Vehicle License Fee Funds	462.1	496.3	491.9	491.9
1.0625% Sales Tax	5,107.0	5,320.0	5,748.0	6,228.0
Total Revenues	**$5,569.1**	**$5,816.3**	**$6,239.9**	**$6,719.9**

the Local Revenue Fund 2011 on an ongoing basis for allocation to the counties and are available only for the purposes of 2011 Realignment.

Funding Structure for 2011 Realignment

Although the revenue stream for 2011 Realignment is ongoing, the program allocations were for the 2011-12 fiscal year only.

Following discussions with the California State Association of Counties, the Administration is proposing a permanent funding structure for 2011 Realignment

for both base and growth funding. Figure REA-02 displays the proposed County Local Revenue Fund structure.

The funding structure is designed to provide local entities with a known, reliable, and stable funding source for these programs. Within each Subaccount, counties will have the flexibility to meet their highest priorities. Counties will be able to use their funds to draw down the maximum amount of federal funding for these programs. In those programs in which there are federal requirements, such as federal eligibility and statewideness, counties will be responsible for meeting those requirements and will be responsible for penalties if they fail to achieve them. The state is committed to assisting counties as appropriate if they need federal state plan amendments, waivers, or other flexibilities.

The following concepts were important in determining the components of the funding framework:

Base Funding – Providing Stable Funding

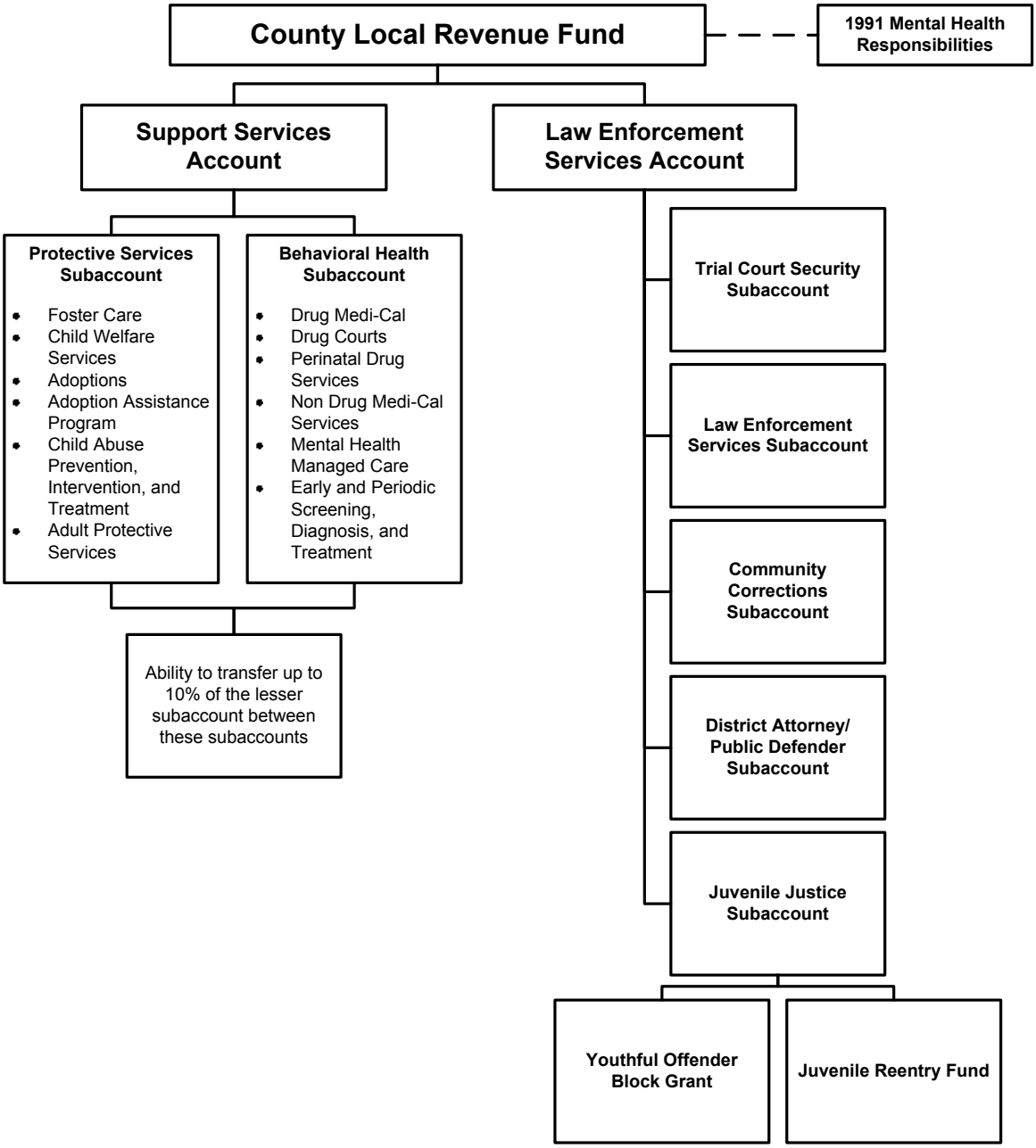
- The base in each Subaccount should not experience a year-over-year decrease. A statutory mechanism should be in place to deal with the possibility of a year's base being short due to significantly reduced revenues.
- The timing of the program's inclusion in 2011 Realignment and the implementation schedule should affect base funding for each program.
- The base should be a rolling base for each Subaccount; i.e., the base plus growth equals the subsequent year's base.
- The 1991 Mental Health program should continue to receive revenue based on its 1991 formula.

Growth Funding

- Funding for program growth should be distributed on a roughly proportional basis, first among Accounts, and then by Subaccounts.
- Within each Subaccount, federally required programs should receive priority for funding if warranted by caseload and costs.

Figure REA-02

2011 Realignment Funding Structure



- Growth funding for the Child Welfare Services (CWS) program is a priority once base programs have been established. Over time, CWS should receive an additional $200 million.

Transferability

- To provide flexibility, counties should have the ability to transfer a maximum of 10 percent of the lesser subaccount between the Subaccounts within the Support Services Account.
- Beginning in 2015-16, there should be a local option to transfer a portion of the growth among Subaccounts within the Law Enforcement Services Account.
- Transfers should be for one year only and not increase the base of any program.

Reserve Account

To provide some cushion for fluctuations in future revenue, a Reserve Account should be established when Sales and Use Tax revenues exceed a specified threshold.

Continuing the Work of Moving Government Closer to the People

Ongoing Implementation of 2011 Realignment

The Administration is committed to a continued partnership with county officials for the successful implementation of 2011 Realignment. These efforts include:

Refocus State Efforts. The Administration is committed to a 25-percent reduction in the state operations of program areas that have been realigned. Both the Departments of Alcohol and Drug Programs and Mental Health reduced their program components by that amount before transferring functions to the Department of Health Care Services (DHCS). The new Division of Mental Health and Substance Use Disorder Services within the DHCS will provide appropriate state oversight and assistance for programs realigned to the counties.

The Department of Social Services will develop its 25-percent reduction plan upon county decisions regarding workload within realigned programs and based on federal requirements.

County Flexibility. The Administration continues to support efforts to increase the flexibility of counties in administering programs.

Ongoing Training for AB 109. The Budget proposes $8.9 million for a second year of training efforts related to the implementation of AB 109 programs. Of this amount, $1 million is for statewide training efforts. The remainder is for allocation to each Community Corrections Partnership so the Partnerships have sufficient resources to review and amend plans based on the first year of program experience.

Other 2011 Realignment Efforts. As issues arise that appear to be systemic in implementation, the Administration will work with county officials to address them. For example, the Administration will work with counties to develop improved treatment and housing options for offenders who are incarcerated and suffer from mental illness, as necessary.

Increased Local Flexibility for Schools

Increasing local flexibility and local decision-making is not just associated with counties. Over the past 30 years, the state also has made more and more decisions for local schools. The Budget proposes a weighted pupil funding formula to be phased in over the next five years. This will reduce the complexity and administrative costs for school districts and provides significant additional flexibility to local districts by consolidating funding for the vast majority of categorical programs and revenue limits into a single source. Current accountability measures will be used, along with locally developed measures, as the basis for evaluating and rewarding school performance under this new finance model.

Juvenile Justice Reform

One of the more successful efforts over the past 15 years has been the change in jurisdiction of juvenile offenders from the state to counties. Over the last decade, the number of wards in state juvenile facilities has decreased from over 10,000 to approximately 1,100.

The Administration wants to build on this success and eventually have the counties manage all youthful offenders. This effort must be done thoughtfully and carefully to provide the best placement and treatment options for these youth. The Budget proposes to stop the intake of new juvenile offenders to the Division of Juvenile Justice (DJJ) effective January 1, 2013. The DJJ's population will gradually diminish through attrition.

The state is committed to providing the necessary resources and assistance to local governments for a successful transition. Recognizing that counties will need resources and support to secure appropriate placements and treatment options for additional offenders, many of whom need mental health and substance abuse treatment, the Budget proposes $10 million General Fund in 2011-12 for counties to begin planning for this population. To help with the transition and prevent the disinvestment of funds in juvenile justice at the local level, the state will delay collection of recently imposed additional fees for those wards housed in the DJJ.

Phase 2 Realignment

The implementation of Phase 2 of Realignment is linked to the ongoing discussion of how California will implement federal health care reform.

Under health care reform, counties will have a significant role in Medi-Cal eligibility determinations. The focus of the Phase 2 Realignment discussion with counties and others in the coming months will revolve around the appropriate relationships between the state and counties in the funding and delivery of health care as about two million additional people will shift from county indigent programs to the Medi-Cal caseload. Additional data are needed to inform decisions about implementation.

The discussion also will involve what additional programs the counties should be responsible for when the state assumes the majority of costs of healthcare.

Notes

Topic _____

Date _____ Page _____

ABOUT THE CSAC INSTITUTE

*The **California State Association of Counties** (CSAC) is the voice of California's 58 counties at the state and federal level. The Association's long-term objective is to significantly improve the fiscal health of all California counties – from Alpine County with a little more than 1,200 people to Los Angeles County with more than 10 million – so they can adequately meet the demand for vital public programs and services. CSAC also places a strong emphasis on educating the public about the value and need for county programs and services.*

*The **CSAC Institute for Excellence in County Government** is a professional, practical continuing education program for county officials. The experience is designed to expand the capacity and capability of county elected officials and senior executives to provide extraordinary services to their communities. The Institute is a program of CSAC and was established in 2008 with the first courses offered in early 2009.*

*For more information please visit **www.csacinstitute.org**.*