The State-Local Fiscal Relationship: A Rough Road

- Prop 13 Property Taxes 1978
- Prop 14 Spending Limits 1979
- Prop 28 Taxes, Fees, Assessments etc 1996
- VLF “CarTax” cut & backfill 1999
- Prop 42 State Sales Tax to Transportation 2002
- Prop 57 “Triple Flip” 2004
- Prop 1A local $ protection 2004
- Prop 1A Redevelopment Property Tax Shifts 2008-2010
- Prop 1A VLF-Property Tax Swap 2008-2010
- Prop 22 Local $ Protection 2010
- Prop 25 Taxes, Regulatory Fee rules

In the Wake of Prop 13...
- Local gov’t fiscal innovation
- Fees, new taxes, JPA, consolidations, redevelopment
- State fiscal retrenchment
- Progeny of Proposition 13
  - 1986 Proposition 62
  - 1996 Proposition 218
- ERAF property tax shifts
  - from cities, counties, special districts beginning 1991-94

UCD CRD158: Community Governance
April 27, 2015
# The State of the State: Governor’s Proposed Budget 2014-15

![Image](image.png)

## 2014-15 Governor’s Budget General Fund Budget Summary

<table>
<thead>
<tr>
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<th>2013-14</th>
<th>2014-15</th>
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</thead>
<tbody>
<tr>
<td><strong>Resources</strong></td>
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<tr>
<td>Prior Year Balance</td>
<td>$2,528</td>
<td>$4,212</td>
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<tr>
<td>Revenues and Transfers</td>
<td>$100,147</td>
<td>$104,503</td>
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<tr>
<td><strong>Total Resources Available</strong></td>
<td>$102,675</td>
<td>$108,715</td>
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<tr>
<td><strong>Expenditures</strong></td>
<td></td>
<td></td>
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<tr>
<td>Non-Proposition 98 Expenditures</td>
<td>$57,515</td>
<td>$61,731</td>
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<tr>
<td>Proposition 98 Expenditures</td>
<td>$40,948</td>
<td>$45,062</td>
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<tr>
<td><strong>Total Expenditures</strong></td>
<td>$95,463</td>
<td>$106,793</td>
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<tr>
<td><strong>Fund Balance</strong></td>
<td>$4,212</td>
<td>$1,922</td>
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<tr>
<td><strong>Budget Stabilization Account / &quot;Rainy Day Fund&quot;</strong></td>
<td>$1,591</td>
<td></td>
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</tbody>
</table>
Governor’s Proposed Budget
State General Fund and Realignment Fund Revenue

- Personal Income Tax: $69,764, 59%
- Sales & Use Tax: $24,071, 20%
- Corporation Tax: $9,682, 8%
- Realignment Sales Tax: $9,569, 8%
- Insurance Tax: $2,297, 2%
- Other/Transfers: $1,281, 1%
- Vehicle License Fee: $2,071, 2%

State General Fund and Realignment Fund Expenditures

- Health& Human Svcs: $28,793, 24%
- K-12 Education: $45,251, 38%
- Higher Education: $12,377, 11%
- Corrections: $9,560, 8%
- Mental Health, Support Svces: $9,330, 8%
- Law Enforcement, Trial Court: $2,296, 2%

Local Revenue Fund

Business Services: $745, 1%
Legisl Judicial Exec: $2,844, 2%
ERB Payment: $1,591, 1%
General Govt: $3,191, 3%
Transportation: $212, 0%
Resources & Environment: $2,229, 2%

CaliforniaCityFinance.com
California State Budget Outlook

Voter Approved Revenues

- Personal Income Tax (Prop30)
- Sales and Use Tax (Prop30)
- Corporate Tax simplification (Prop39)

Risks

- Threat of Recession. It’s inevitable.
- Health Care Costs. Medi-Cal is budget’s 2nd largest program.
- Natural Disasters: draught, fires, flood, earthquake.
- Debts and Liabilities. In addition to budgetary debt:
  - $218 billion state retirement-related unfunded liabilities
  - $65 billion deferred maintenance
  - $9 billion unemployment insurance
- Capital Gains (10% of General Fund tax revenues) volatile, affected by stock market behavior.
### California’s Fiscal Outlook

#### LAO’s Hypothetical Recession

**Operating Deficits Return Under Hypothetical Recession Scenario**

| General Fund and Education Protection Account Combined (In Billions) |
|-------------------|-------------------|-------------------|-------------------|-------------------|
| Deferred payments to schools and community colleges | $10.4 | $6.4 | $6.1 | $0.0 | $0.0 |
| Economic Recovery Bonds | 7.1 | 5.2 | 3.9 | 0.0 | 0.0 |
| Loans from Special Funds | 5.1 | 4.9 | 3.9 | 2.9 | 0.0 |
| Unpaid mandated costs to local govs, schools, colleges | 4.3 | 4.9 | 5.4 | 5.4 | 0.0 |
| Underfunding of Proposition 98 | 3.0 | 2.4 | 2.4 | 1.8 | 0.0 |
| Borrowing from local governments (Proposition 1A) | 1.9 | 1.1 | 0.0 | 0.0 | 0.0 |
| Deferred Medi-Cal Costs | 1.2 | 2.0 | 1.8 | 1.7 | 0.0 |
| Deferral of state payroll costs from June to July | 0.8 | 0.7 | 0.8 | 0.8 | 0.0 |
| Deferred payments to CalPERS | 0.5 | 0.4 | 0.4 | 0.4 | 0.0 |
| Borrowing from transportation funds (Proposition 42) | 0.4 | 0.4 | 0.2 | 0.1 | 0.0 |
| **Total** | **$34.7** | **$28.2** | **$24.9** | **$13.1** | **$0.0** |

For FY2014-15, the Governor proposes to...

- Pay down remainder of school deferrals: $6.2 billion
- Pay off Economic Recovery Bonds early: $1.6 billion
- Repay special funds: $1.6 billion

---

### Eliminating the “Wall of Debt”

<table>
<thead>
<tr>
<th></th>
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<th></th>
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<tr>
<td>Deferred payments to schools and community colleges</td>
<td>$10.4</td>
<td>$6.4</td>
<td>$6.1</td>
<td>$0.0</td>
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<td>Economic Recovery Bonds</td>
<td>7.1</td>
<td>5.2</td>
<td>3.9</td>
<td>0.0</td>
<td>0.0</td>
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<td>Loans from Special Funds</td>
<td>5.1</td>
<td>4.9</td>
<td>3.9</td>
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<td>Unpaid mandated costs to local govs, schools, colleges</td>
<td>4.3</td>
<td>4.9</td>
<td>5.4</td>
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<tr>
<td>Underfunding of Proposition 98</td>
<td>3.0</td>
<td>2.4</td>
<td>2.4</td>
<td>1.8</td>
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<tr>
<td>Borrowing from local governments (Proposition 1A)</td>
<td>1.9</td>
<td>1.1</td>
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<td>0.0</td>
<td>0.0</td>
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<td>0.0</td>
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<tr>
<td>Deferred Medi-Cal Costs</td>
<td>1.2</td>
<td>2.0</td>
<td>1.8</td>
<td>1.7</td>
<td>0.0</td>
<td>0.0</td>
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<tr>
<td>Deferral of state payroll costs from June to July</td>
<td>0.8</td>
<td>0.7</td>
<td>0.8</td>
<td>0.8</td>
<td>0.0</td>
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<tr>
<td>Deferred payments to CalPERS</td>
<td>0.5</td>
<td>0.4</td>
<td>0.4</td>
<td>0.4</td>
<td>0.0</td>
<td>0.0</td>
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<td>0.4</td>
<td>0.2</td>
<td>0.1</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
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<tr>
<td><strong>Total</strong></td>
<td><strong>$34.7</strong></td>
<td><strong>$28.2</strong></td>
<td><strong>$24.9</strong></td>
<td><strong>$13.1</strong></td>
<td><strong>$0.0</strong></td>
<td><strong>$0.0</strong></td>
<td><strong>$0.0</strong></td>
</tr>
</tbody>
</table>
A Cautionary Tale: 
The Vehicle License Fee

1935 – State Vehicle License Fee (a tax) established
  - motor vehicles eliminated from the local property tax
  - revenue subvened to cities and counties

1981-84 – State budget trouble. Legislature diverts hundreds of millions of city & county VLF $

1986 – Prop47: VLF must go to cities and counties
  - but Legislature still decides the rate, the tax base and the allocation

1998 - Legislature & Gov Wilson pass VLF cut
  - with backfill for cities and counties

2003 – Gray Davis admin pulls trigger, raises VLF

2004 – Davis Recalled, Schwarzenegger elected
  - On his first day in office, Schwarzenegger cuts VLF - restoring backfill and punching a $4 billion ongoing hole in the state budget without any way to pay for it
A Little History... VLF Revenues and Allocations

VLF Backfill

VLF Revenue at 0.65% rate

Special Allocations

Counties Per Capita

Cities Per Capita

Admin Charges

H&W Realignment

Property Tax in-lieu of VLF (2004 on)

The VLF-Property Tax Swap of 2004

State General Fund

$4.4 b*

VLF Backfill

Cities & Counties

Property Tax in Lieu of VLF

Schools

$4.4 b

$4.4 b

* in FY2004-05
Vehicle Lic Fee $ Allocation

Prior to 2004

-$ VLF (including backfill)

$ VLF

Annexation

Existing City

New City

7yr “Bump”

$ VLF

Incorporating After 2004

$ VLF

Vehicle Lic Fee $ Allocation

With PropTax – VLF Swap of 2004

-$ PropTax in lieu of VLF

$ VLF

Annexation

Existing City

New City

Incorporating After 2004

$ VLF
Special Allocations for New Cities & Annexations

- **Vehicle Lic Fee $ Allocation**
- **VLF** $50+ per resident @time of annexation
- **$ PropTax in lieu of VLF**
- **5yr “Bump”**
  - **$ VLF**
- **New City Incorporating After 2004**

**AB1602 (Laird 2006)**

**SB89 Eliminated All City VLF (Diverted to Law Enforcement Grants)**

- **$ PropTax in lieu of VLF**
- **VLF** $50+ per resident @time of annexation
- **5yr “Bump”**
  - **$ VLF**
- **New City Incorporating After 2004**
The Lack of VLF Replacement Makes New Cities Fiscally Unviable

Cost and Revenue Impacts of New Development: The “Fiscalization of Land-Use”
Theoretical Comparison of Annual Costs and Revenues from Different Development Proposals - 5 acre parcel

City A  
Full Service - no UUT

<table>
<thead>
<tr>
<th>Property Size (acres)</th>
<th>Single-family Residential</th>
<th>Multi-family Residential</th>
<th>Industrial</th>
<th>Retail</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$5</td>
<td>$5</td>
<td>$5</td>
<td>$5</td>
</tr>
</tbody>
</table>

| Residential Units     | 95                        | 95                      | n/a        | n/a    |
|                       |                           |                         |            |        |
| Residential Cost per DU | 400,000                  | 180,000                 | n/a        | n/a    |
|                       |                           |                         |            |        |
| Retail Square footage per acre | n/a                  | n/a                    | 10,000     |        |
|                       |                           |                         |            |        |
| Property Value        | 8,000,000                 | 17,100,000              | 3,500,000  | 10,000,000 |
|                       |                           |                         |            |        |
| Property Tax AB8 share of 1% | 16.3%                 | 16.3%                   | 16.3%      | 16.3%  |

CITY REVENUES

<table>
<thead>
<tr>
<th>Property Tax Revenue</th>
<th>13,040</th>
<th>27,873</th>
<th>5,705</th>
<th>16,300</th>
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<tbody>
<tr>
<td>Property Tax Rev (InLieu of VLF)</td>
<td>3,600</td>
<td>7,695</td>
<td>1,575</td>
<td>4,500</td>
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<tr>
<td>Sales Tax Revenue</td>
<td>7,280</td>
<td>37,050</td>
<td></td>
<td>82,500</td>
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<td>Business License Tax</td>
<td>340</td>
<td>1,615</td>
<td>1,275</td>
<td>1,063</td>
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<tr>
<td>State Subventions &amp; other revs</td>
<td>2,268</td>
<td>23,877</td>
<td>128</td>
<td>367</td>
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<tr>
<td>TOTAL REVENUES</td>
<td>$ 26,528</td>
<td>$ 103,610</td>
<td>$ 14,183</td>
<td>$ 110,229</td>
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CITY EXPENDITURES

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<tr>
<th>Police Department</th>
<th>10,080</th>
<th>47,880</th>
<th>5,544</th>
<th>15,750</th>
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<tbody>
<tr>
<td>Fire Department</td>
<td>5,600</td>
<td>26,600</td>
<td>5,718</td>
<td>10,563</td>
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<tr>
<td>Public Works</td>
<td>7,700</td>
<td>7,600</td>
<td>1,870</td>
<td>5,313</td>
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<tr>
<td>Planning &amp; Community Devlpnt</td>
<td>1,900</td>
<td>4,750</td>
<td>1,100</td>
<td>5,125</td>
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<tr>
<td>Parks &amp; Community Services</td>
<td>2,240</td>
<td>10,640</td>
<td>370</td>
<td>1,050</td>
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<tr>
<td>Library</td>
<td>1,680</td>
<td>7,980</td>
<td>n/a</td>
<td>n/a</td>
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<tr>
<td>General Government</td>
<td>2,680</td>
<td>12,635</td>
<td>1,518</td>
<td>4,313</td>
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<tr>
<td>TOTAL EXPENDITURES</td>
<td>$ 24,980</td>
<td>$ 118,085</td>
<td>$ 14,120</td>
<td>$ 40,113</td>
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</tbody>
</table>

NET per unit $77 $ (152)

1. Enterprise services such as water, sewer, and garbage are not included. These services are funded by user fees, such that costs equate to revenues.
2. Property values assume $400,000 per single family home, $180,000 per multi-family unit, $200/sf for retail, $700,000 per acre for industrial.
3. City property tax share differs from city to city depending on (among other things) the service responsibility of the city and the pre-Prop13 property tax rate.
4. Retail assumes 10,000 sq ft retail per acre with taxable sales of $200 per sq ft, 75% is “new sales.” Residential assumes 4%/yr resale of sf, 2% for mf.

CaliforniaCityFinance.com
Circumstances & #'s Vary!

- Tax rates and shares vary
- Service responsibilities, levels, standards and impacts vary
- Projects vary