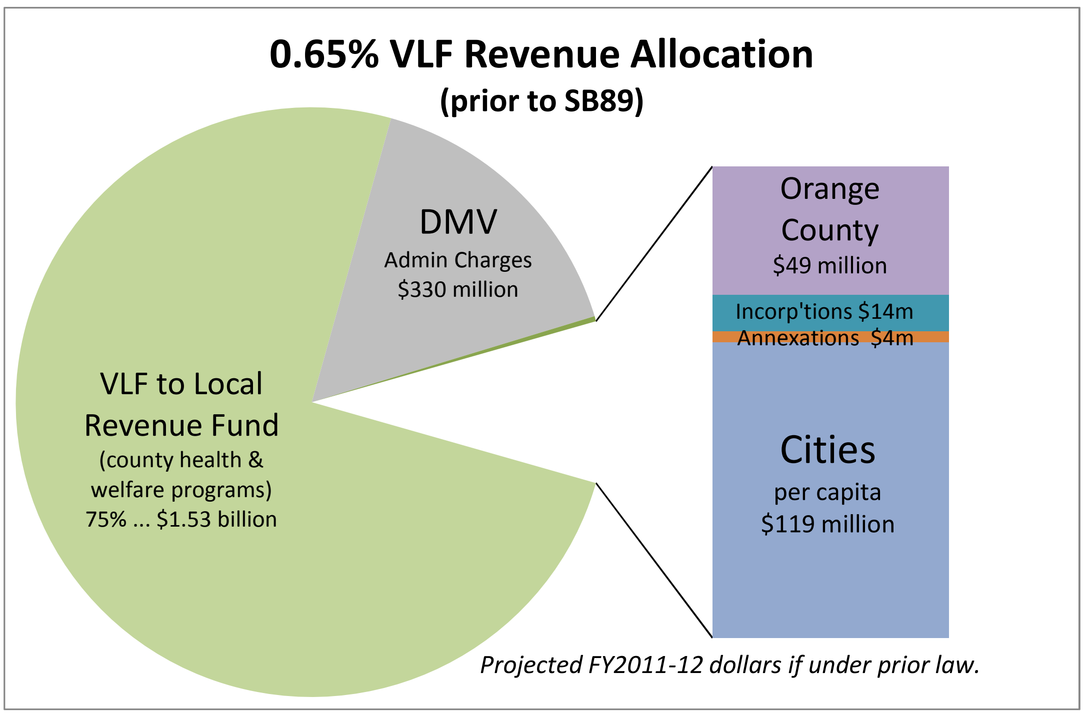
The Vehicle License Fee (Motor Vehicle In-Lieu Tax): Background

Californians have paid the vehicle license fee (VLF), also called the "motor vehicle in-lieu tax," with their vehicle registrations since 1935. The California Constitution requires the proceeds of the 0.65% VLF to go to cities and counties only and prohibits the Legislature from directing that the funds be used to pay for new state mandates on local government after 2010.

Seventy-five percent of revenues from the 0.65% VLF are transferred to the state's Local Revenue Fund to pay counties for various health and welfare services. Under the law through FY2010-11, the state Department of Motor Vehicles takes about 65% (over $325 million) of the remaining funds for administrative charges, leaving just over $180 million for cities and counties. Through FY2010-11, the funds were allocated as follows:

- $49 million to Orange County. When VLF allocations were restructured in 2004, the County continued to receive these revenues from VLF rather than receiving this amount in the form of additional property tax share. The payments are first dedicated to the repayment of bankruptcy debt and then as a general county revenue.
- Special allocations to newly incorporated cities (would have been $14 million in FY2011-12). These special allocations compensate cities that have incorporated since 2004 due to an inequity resulting from the VLF-Property Tax Swap of 2004.
- Special allocations to inhabited annexations (would have been $4 million in 2011-12). These special allocations balance the fiscal disincentive of cities annexing inhabited areas as a result of the VLF – Property Tax Swap of 2004 due to an inequity resulting from the VLF-Property Tax Swap of 2004.
- Remainder on a per capita basis to city general funds (about $119 million in FY2011-12).



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Supplemental Law Enforcement Funding (SLESF) and other State Law Enforcement Grants: Background

As a part of the 2009 state budget agreement, a number of law enforcement grant programs heretofore funded by the state general fund were instead funded in FY2009-10 and FY2010-11by a 0.15% state VLF increase. This temporary tax ended on June 30, 2011. The 0.15 VLF rate was intended to generate around $500 million, the approximate level of total funding of the grant programs in prior years. But the tax garnered just $414 million in FY2009-10 and $442 million in FY2010-11.

Most of the funding for these programs goes to county sheriffs, but two are of particular importance to cities:

- Citizens Option for Public Safety Frontline Law Enforcement grants
- Jail Detention Facility Grants to Sheriffs which, if funded, preempt county booking fee charges to cities and other local agencies.

The following table shows the law enforcement grant programs and allocations over the last two years.

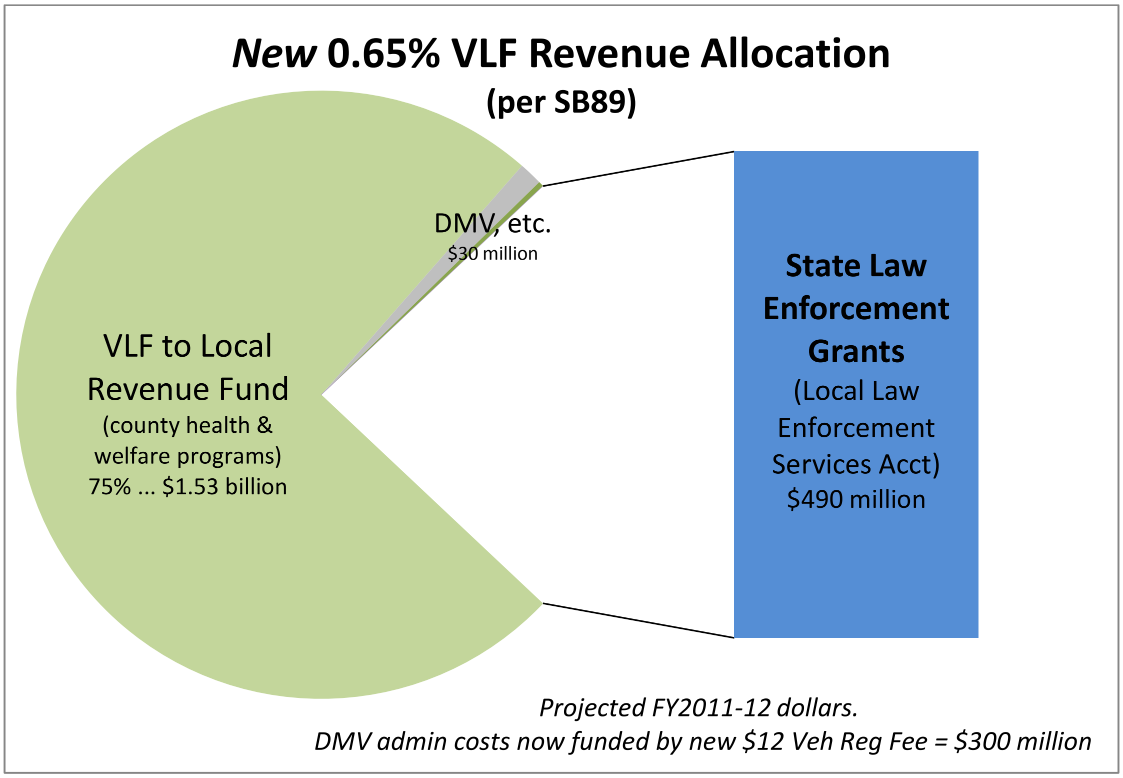
0.15% Law Enforcement VLF				
Local Safety and Public Protection Account in the Transportation Tax Fund				
Effective through June 30, 2011. Cal Rev&Tax Code §10752.2				
	Actual 2009-10	Estm. 2010-11		
Total Revenues from 0.15% VLF:	414,560,614	442,000,000	Apportionment	
				Of Rate
Jail Detention Facility Grants	25,951,494	27,669,200		6.26%
SLESF: jail constr/ops	9,095,045	9,697,038	5.15%	42.60%
SLESF: Distr Atty	9,095,045	9,697,038	5.15%	^^
SLESF: COPs Frontline Law Enf	70,111,320	74,751,924	39.70%	^^
Juvenile Justice Crime Prevention	88,301,411	94,146,000	50.00%	^^
Small Rural Sheriffs	15,255,831	16,265,600		3.68%
Juvenile Probation	125,155,849	133,439,800		30.19%
Juvenile Camps & Ranches	24,251,796	25,857,000		5.85%
Cal Emergency Mngmt Agency*	47,342,822	50,476,400		11.42%
	414,560,614	442,000,000		100.00%

*Includes Cal-MMET, Vertical Prosecution Block Grants, Evidentiary Medical Training, Public Prosecutors and Public Defenders, Calif Gang Violence Suppression, CALGANG, MultiAgency Gang Enforcement Consortium, Rural Crime Prevention, Sexual Assault Felony Enforcement, High Tech Theft Apprehension & Prosecution.

SB89 City Motor Vehicle License Fees Shifted to Fund State Law Enforcement Grants

As the 2011-12 Fiscal Year approached, the Governor signed SB89. Provisions in SB89, made public just hours before the legislative floor votes, shift hundreds of millions of Vehicle License Fee revenues to fund the state law enforcement grants beginning FY2011-12. The scheme works as follows:

- The "Vehicle License Registration Fee" is increased by $12 to produce approximately $300 million in FY2011-12. This is a true fee[1] that funds state DMV vehicle license registration operations. This new funding source "frees up" $300 million of Motor Vehicle License Fee (MVLF) revenue that had been used to fund DMV operations.[2] This money is transferred to a new Local Law Enforcement Services Account (LLESA) to fund the law enforcement grants. This portion of the scheme was included in the early June budget that was vetoed by Governor Brown.
- In addition, beginning July 1, 2011, SB89 transfers the remaining MVLF revenue (about $190 million after the Local Revenue Fund allocation for county health and welfare programs) previously allocated to cities and the County of Orange to the LLESA.



Impacts of SB89

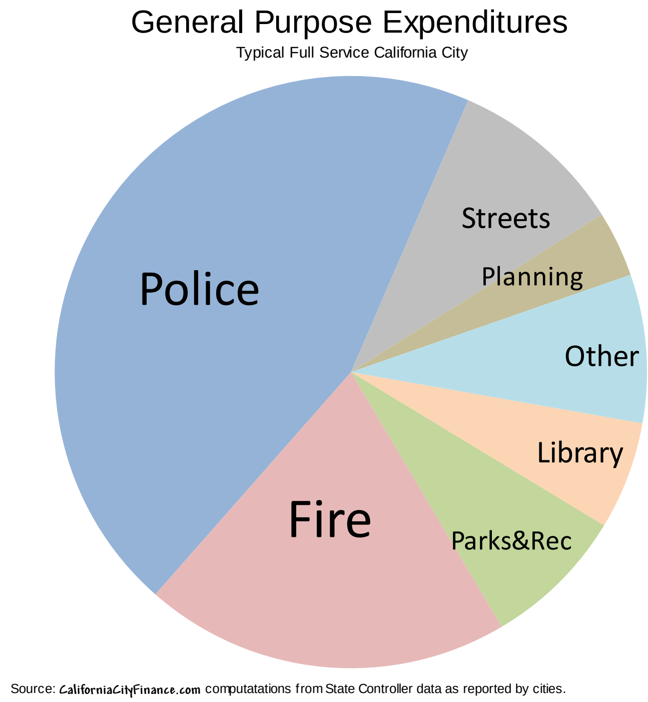
1. The SB89 VLF Shift Impacts Public Safety Services

MVLF revenues go to city general funds. An average of over 60% - and often 2/3 or more—of city general fund revenues are spent on police and fire services. The recent economic downturn has forced most cities to make significant budget reductions. Having already made substantial reductions in non-safety programs (parks, libraries, streets), cities throughout California are now cutting police and fire staffing and service levels.

[1] The legal distinction is important. A fee increase may be approved by majority vote. A tax increase requires two-thirds approval of each house of the Legislature.

[2] DMV/FTB administrative charges to the 0.65% VLF would have been over $330 million in FY2011-12, over 15% of total VLF revenues. These excessive charges most likely violate the provisions in Section 15 of Cal Constitution Article XI requiring VLF revenues to go to cities or counties, less *reasonable* administrative charges.

SB89 takes $130 million of city general revenue (VLF) and shifts it to save state law enforcement grant programs. Less than $100 million of these grant funds will come back to cities, earmarked for police services. But these funds will be entirely offset by the loss of city VLF.



2. SB89 Makes New City Incorporations Fiscally Unviable and Severely Imperils Four Recently Incorporated Cities.

Following the VLF Swap in 2004, special legislation was enacted to remedy a fiscal disincentive for new incorporations created by the swap. The law did not provide a property tax in lieu of VLF share for cities incorporating after 2004. A special allocation from city VLF funds was established to compensate for this. Newly incorporated cities ALSO receive an artificially inflated population factor in the VLF allocation during their first five years for start-up costs. Consequently, VLF is an especially critical revenue source for these new cities.

The elimination of discretionary MVLF revenue for cities and these special allocations has the effect of making these new cities fiscally unviable.

3. SB89 Makes Annexations of Inhabited Areas Fiscally Unviable

Prior to the VLF swap, the additional population added to a city as a result of the annexation of an inhabited area provided the city with greater per capita VLF revenue. This is critical funding for the municipal services that must be provided to the area (police, fire, parks, library, planning, streets, etc.). A provision of the 2004 VLF Swap law denies cities the growth in property tax revenue[3] attributable to the development pre-existing in an annexation. Special legislation was enacted after the 2004 swap to remedy this disincentive to annex inhabited areas with a special ongoing additional allocation of revenues for annexations.

4. SB89 Unfairly Costs Orange County $50 million per year.

In the 2004 VLF - Property Tax Swap, the state's backfill to local governments for the VLF tax cut was eliminated and instead counties and cities received additional property tax share. Counties gave up all of their discretionary per capita VLF for property tax share, except Orange County. Because a portion of their VLF revenue allocation was pledged to bonded debt related to the county's bankruptcy proceedings, Orange County did NOT receive $54 million per year in property tax revenue, but instead continued to receive these funds from the VLF. (Under the law, the $54 million amount is adjusted for the change in VLF revenue collections, which have declined since 2004.)

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[3] Specifically the property tax in lieu of VLF amount.