February 22, 2002

Hon. Bill Lockyer
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Tricia Knight
Initiative Coordinator

Dear Attorney General Lockyer:

Pursuant to Elections Code 9005, we have reviewed the proposed initiative entitled "Community Public Health and Safety Protection Act—Option 3" (file number SA2002RF0004).

BACKGROUND

Under the California Constitution and statutes, state and local governments provide an array of services for California residents. For example:

- Cities, counties, and special districts (considered local governments in this measure) provide local public safety and local transportation, parks, recreation, and library programs. Counties also provide health and welfare services.
- State government (and school districts) provides educational programs, highways, public safety, and health and social services.

The Constitution and state law currently give the state considerable authority over local government finances. For example, subject to certain constitutional and statutory constraints, the state may modify the level of financial resources available for local government programs, alter the distribution of revenues among local governments, and/or adjust the manner in which the cost of programs is shared by state and local governments.

Over the last several decades, in response to changing economic conditions and program needs, the state has used this authority over local government finance to:

- Change the allocation of property taxes among local governments and school districts.

- Both create and repeal programs that subvene funds and tax revenues from the state to local governments.
- Modify the manner in which the state and local governments share the costs of health, social service, and criminal justice programs.
- Authorize new local taxes and modify existing taxes in a manner that changed the amount of revenues received by local governments.

In total, these actions have altered the allocations of billions of dollars annually. For instance, property tax allocation changes made in the early 1990s shift more than $4 billion dollars annually from local governments to schools. The realignment program enacted in 1991 shifts more than $3 billion annually in former state program costs to counties, while providing an equivalent amount of new revenues.

MAJOR PROVISIONS OF THE INITIATIVE

This measure amends the state Constitution to significantly reduce state authority over local government finance.

Provisions Relating to Funding Changes. This measure restricts the state from:

- Reducing the amount of revenues a local government received from any local tax—such as the property tax, local sales tax, or utility users tax. The state would be prohibited from lowering revenues to an amount less than the revenues received by a local government in the prior fiscal year, adjusted for the cost of living and population growth.
- Reducing the amount of resources received from state subventions, such as the vehicle license fee, the realignment program, and public safety programs. Allocation formulas in place in 2001-02 could not be altered by the state.
- Increasing a local government's statutory share of cost for a program that is financed jointly by state and local governments.

Provisions Requiring Local Government Reporting. Under current law and practice, most local governments adopt annual budgets and undergo financial audits. Many local governments also produce documents describing local performance goals and service levels. This measure specifies that all local governments must produce a written description of local service goals and priorities. In addition, at the end of the year, every local government must (1) issue a report evaluating the extent to which local expenditures conformed to its local service goals and priorities and (2) undergo a financial audit.

FISCAL EFFECT

Provisions Relating to Funding Changes

This measure would significantly constrain future state authority over local finances. As a result, if this measure were in place, the state could not enact in the future some of the fiscal changes that were permissible in the past. Instead, the state would need to implement *different* actions to respond to changes in economic conditions or program objectives.

While it not possible to estimate with precision the fiscal effect of actions the state may implement in the future in response to this measure, we estimate that over time these actions would result in the following impacts.

Impact on Local Government Resources. Total local government resources would be higher than they otherwise would have been. This is because the state would have limited ability to decrease subventions or local tax revenues. For example, the state would be unable to eliminate or reduce funding for an existing subvention, or change the allocations among individual local governments. Furthermore, the state's ability to shift property tax revenues from local governments to schools or to implement future tax exemptions (such as in the sales tax or property tax) would be constrained. As a result of these factors, local resources would be significantly higher than they otherwise would have been—potentially by several billions of dollars annually. This would allow local governments to have higher levels of service—or lower local taxes and fees—than they would have had.

Impact on the State. The constraints on the state's ability to lower local resources would have a commensurate impact on the state. In response, the state would have two basic choices: (1) decrease spending on all other state programs (that is, non-local government subventions) and/or (2) raise state taxes.

Provisions Requiring Local Government Reporting

Some local governments would experience increased costs to comply with the performance review and audit requirements specified in the measure. Statewide, these costs could exceed several million dollars annually.

Summary

The initiative would have the following major fiscal effects:

- Significant restrictions on state authority over local government finances.
- Higher local resources than otherwise would have been the case—potentially several billions of dollars annually. Commensurate fiscal impact on the state,

in the form of reduced spending on non-local government programs and/or higher state taxes.

Sincerely,

Elizabeth G. Hill
Legislative Analyst

B. Timothy Gage
Director of Finance