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Fifth District

March 28, 2008

To: Supervisor Yvonne B. Burke, Chair
Supervisor Gloria Molina
Supervisor Zev Yaroslavsky
Supervisor Don Knabe
Supervisor Michael D. Antonovich

From: William T Fujioka
Chief Executive Officer

SACRAMENTO UPDATE

Budget Hearings

State-Local Fiscal Relationships. On Thursday, March 27, the Senate Committee on Budget and Fiscal Review held an overview hearing to have the Legislative Analyst's Office (LAO) provide the Committee with a history of the main events in the evolution of the fiscal relationship between the State and its counties, cities and special districts. Attending the hearing were the Committee Chair Senator Ducheny and Senators Ackerman, Alquist, Cogdill, Kehoe, Lowenthal, Machado, Margett, Padilla, Romero, Scott and Steinberg.

The primary focus of the LAO presentation was on the period from 1972 to the present, but highlights of the key changes in the State-local relationship during California's first 120 years were also provided to the Committee. Chief among these was a Senate Constitutional Amendment approved by the voters in 1910 as the Separation of Sources Act. This is the measure that gave counties, schools and other local entities exclusive control over the property tax which was not changed until the enactment of Proposition 13 in 1978 gave control of property tax allocation to the Legislature.

The year 1972 was chosen as the starting point for the period of more intensive examination because that was the year when the first State mandated cost reimbursement provisions were enacted into law. These mandate reimbursement provisions were only one part of the Property Tax Relief Act of 1972 which was enacted

in SB 90 (Leroy Greene, Chapter 1406, Statutes of 1972). The overall purpose of the Act was to limit the ability of schools, counties and other local agencies to levy taxes. Consequently, the language requiring the State to reimburse counties, schools and other local entities for State-mandated costs was added to mitigate the limitation of local taxing authority.

The attached LAO document, Major Milestones and Supplement to Major Milestones, essentially provides an outline of the LAO's comments to the Committee. Even though the two LAO documents provide a statutory tour through the major State-Local fiscal events that have occurred in the last 35 years, the complexity, impact and sheer number of events affecting counties and other local governments is daunting.

At the end of the two and a half hour hearing, the Chair and Members of the Committee seemed to agree that the fiscal relationship between the State and its counties, cities and special districts was extremely tangled and not conducive to understanding by, or accountability to, the people of California. There also seemed to be agreement that the fiscal relationship, which Senator Cogdill called the "ultimate Gordian knot", indicated a major need to realign programs, revenues and responsibilities.

The Senate Budget Committee will have a hearing next Thursday at 9:30 a.m., or upon adjournment of the Senate, to allow counties, cities and special districts to present their perspective on today's hearing, current fiscal conditions, and the State Budget.

Public Assistance Automation Efforts. On March 24, 2008, Assembly Budget Subcommittee #1 held a hearing to consider several automation issues that included the Governor's 2008-09 budget proposals for the Statewide Automated Welfare System (SAWS) and the LAO's alternative budget proposal to reduce the number of SAWS consortia from four to two systems.

Representatives from the State Health and Human Service Agency's Office of System Information (OSI) provided background on their collaboration with the California Welfare Director's Association's (CWDA) consortia strategy for a statewide welfare automation system. The County's LEADER system is one of the four approved consortia for public assistance automation. LEADER's 2007 estimated caseload is 346,958 cases representing 34 percent of all cases statewide. OSI proposes that funding for LEADER be decreased in the current year by \$11,460, and by \$597,360 in FY 2008-09 as a result of a 13-month extension to the planning phase of the project. These amounts support the County efforts to maintain the LEADER procurement process.

The LAO recommends enactment of legislation establishing a goal of standardizing and limiting the State's SAWs system to no more than two automated systems, but did not provide specific language for this proposal. The LAO advised that this would reduce costs and increase efficiency. In addition, the LAO urged increasing legislative oversight of information technology consortia contracts that support these systems.

CWDA testified in support of the Governor's Budget Proposal to maintain the four consortia reminding the subcommittee members that in 1995 the legislature enacted legislation to establish no more than four consortia, to be managed locally after the State recognized one statewide automation system was not feasible.

Assembly Member Jim Beall expressed concerns about supporting the Governor's proposals to fund the four consortia while cutting CalWORKs grants for families. He suggested the Subcommittee consider a proposal that reduces costs by possibly consolidating systems. Overall, there was consensus among the subcommittee members to continue discussions.

The subcommittee took no action on these items.

Status of County-Sponsored Legislation

County-sponsored SB 579 (Wiggins), as amended on March 24, 2008, would allow the Board to permit the reinstatement of firefighters over 60 years of age who retired after April 1, 2007 and repeal a provision requiring the County Fire Chief to retire by April 1, 2009. SB 579 is an urgency measure that would be effective immediately, upon approval of the Governor. A hearing has been set for April 9, 2008 in the Assembly Committee on Public Employees, Retirement and Social Security. There is no support or opposition on file.

County-sponsored SB 1184 (Kuehl), which would require full CD4 AIDS test reporting, and would result in the reporting of additional HIV/AIDS cases to the State, passed the Senate Health Committee on March 26, 2008 by a vote of 9 to 0, and now proceeds to the Senate Appropriations Committee. A representative from the County's Department of Public Health testified that full CD4 reporting will bring in additional Federal Ryan White Care Act Funds, and that the bill is an effective public health measure to better track HIV/AIDS cases.

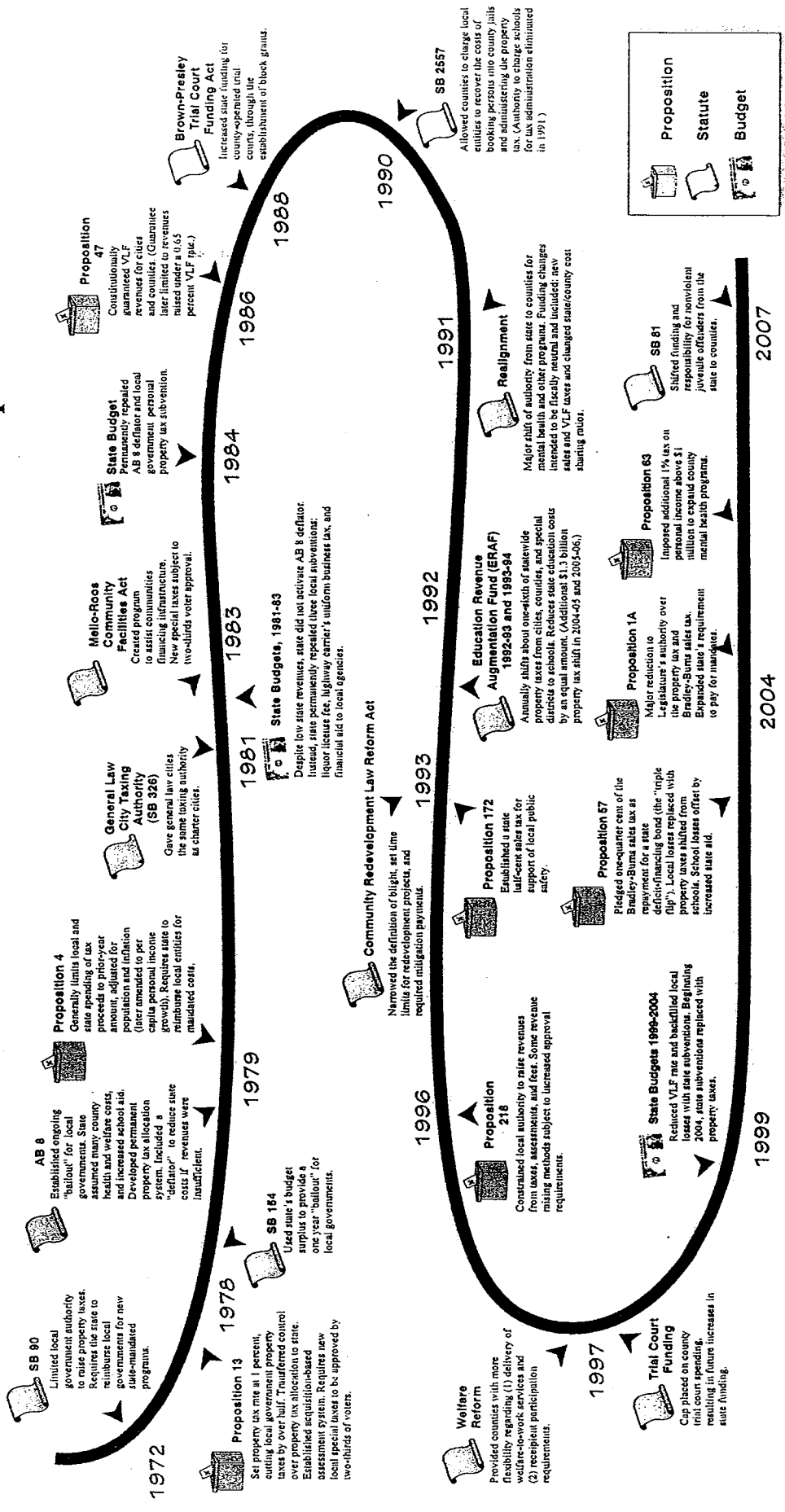
We will continue to keep you advised.

WTF:GK:MAL
DW:IGR:hg

Attachment

c: All Department Heads
Legislative Strategist
Local 660
Coalition of County Unions
California Contract Cities Association
Independent Cities Association
League of California Cities

Major Milestones: 35 Years of the State-Local Fiscal Relationship



Proposition
Statute
Budget

Contact-Marianne O'Malley-(916) 319-8315

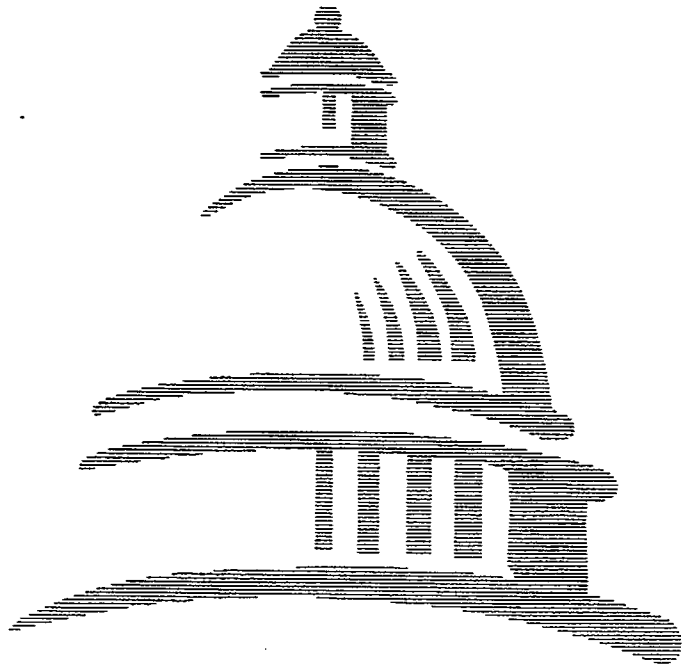
March 27, 2008

March 27, 2008

Supplement to Major Milestones: 35 Years of the State-Local Fiscal Relationship

LEGISLATIVE ANALYST'S OFFICE

Presented to:
Senate Budget and Fiscal Review Committee
Hon. Denise Moreno Ducheny, Chair





Themes in State-Local Fiscal Relations



Throughout the Nation

- When multiple governments serve the same people, tensions inevitably arise over which level of government makes the rules for public services and which level of government pays the bills.
- A strong state role in local finance makes sense if the state's objective is to maximize equity in the allocation of public resources—for example, school equalization. A strong local role makes sense if the state's goal is to foster experimentation, innovation, or responsiveness to local preferences—for example, local parks and public safety.
- The government that raises the revenue generally sets the rules as to how funds are spent.
- If local government does not reduce program costs to reflect state funding limitations, interest in replacement revenues inevitably emerges.
- To promote the best program outcomes and reflect current public preferences, state and local program responsibilities should be reevaluated and resorted periodically.



Particularly Notable in California

- Given the size and diversity of California, it is difficult for the state to gauge each local government's needs and preferences. As a result, state funding formulas often default to sealing in place revenue distributions made years—or decades—earlier.
- County shares of program costs and school property taxes have played a role as a state-local fiscal balancer.
- The lines between state and local resources—and state and local responsibilities—have blurred, making it difficult for Californians to know which level of government to hold accountable and causing inter-governmental tension.



Proposition 13 of 1978 (Including Subsequent Amendments)



Provisions

- **Property Tax Limit.** The maximum property tax rate is 1 percent of the "full cash value" of the property. Any property tax rate approved by two-thirds of local voters for debt is in addition to the 1 percent rate.
- **Assessment Limit.** Full cash value is determined when a property changes hands, or 1975-76, whichever is later. Increases in assessed value are limited to 2 percent annually, or the consumer price index, whichever is less.
- **Allocation of Property Tax.** Property tax revenues are to be collected by the counties and apportioned "according to law."
- **New or Increased Taxes.** New or increased state taxes must be approved by two-thirds of the Legislature. Local governments may impose "special taxes" if they are approved by two-thirds of the local voters.



Legislature's Post Proposition 13 Implementation Decisions

- Whether and how to help local governments respond to this reduction in revenues.
- Whether any state relief would be temporary or permanent.
- How property taxes would be allocated among several thousand local governments.



LAO, Cal Facts, December 4, 2006

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STATE-LOCAL FINANCES

Paying for County, City, and Special District Services

2003-04

	Counties	Cities	Special Districts ^a
Total Revenues <i>(In Billions)</i>	\$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.

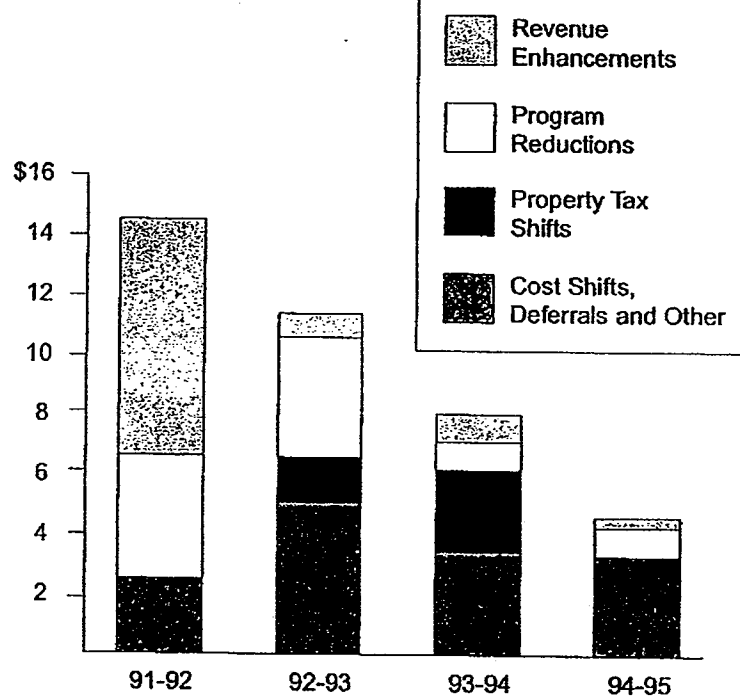


LAO, *Reversing the Property Tax Shifts,* April 2, 1996

Figure 1

Strategies to Address Budget Gaps 1991-92 Through 1994-95

(In Billions)

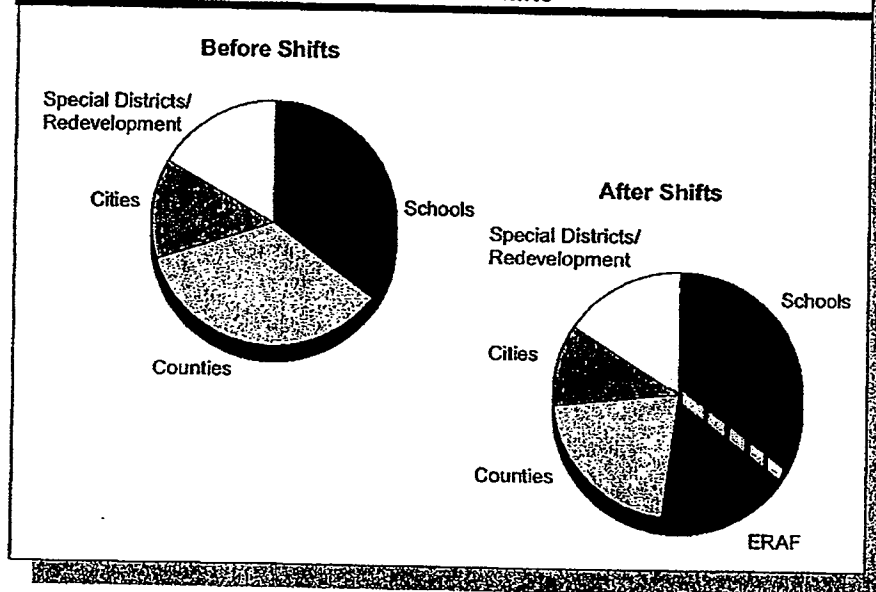




LAO, *Reversing the Property Tax Shifts,* April 2, 1996

Figure 2

Reallocating the Property Tax Pie The Impact of the 1992-93 and 1993-94 Shifts





LAO, *Shifting Gears: Rethinking Property Tax Shift Relief*, February 2, 1999

Figure 2

Relief Measures Associated With Property Tax Shifts

Measures Closely Linked to the Tax Shift

- Proposition 172.** Provides one-half cent in sales tax revenues annually to counties and cities. These funds (\$1.9 billion in 1998-99) must be spent on public safety purposes. The funds do, however, indirectly "free up" local general purpose revenues for other purposes.
- Trial Court Funding Relief.** State assumed growth in trial courts costs, absorbed all trial cost in small counties, and reduced costs to other counties. Relief "frees-up" about \$472 million of local government general purpose revenues in the budget year.
- The Citizens Option for Public Safety (COPS) Program.** \$100 million statewide to cities and counties to augment front line law enforcement. Annually appropriated in the budget.
- General Assistance.** State granted counties authority to reduce grant levels through the "fiscal distress" (SB 1033) process; to "count" the in-kind value of medical, housing, and other assistance; and to place a time limit on employable people receiving aid. County savings are unknown, potentially \$100 million or more annually.
- Fines and Forfeiture Funds.** Cities and counties receive a greater share of revenues from tickets issued for moving traffic violations. Funds may be used for general purposes. Relief probably exceeds \$62 million annually.
- Property Tax Administration Loan Program.** Provides annual forgivable loans to counties for property tax administration. Counties benefit from increased property tax yields. Program authorized for several years at \$60 million.
- Teeter.** Authorized a one-time mitigation of the property tax shift (totaling \$292 million) from counties which elected to make certain changes to the distribution of delinquent property taxes.

Measures Influenced by the Tax Shift

- California Work Opportunity and Responsibility to Kids (CalWORKs).** Program changes and hundreds of million of dollars in new fiscal incentives, a portion of which may be available in the future for other county programs.
- Disproportionate Share Hospital Program.** State implemented new program to provide federal funds to county and private hospitals. Program typically provides hundreds of millions of dollars to counties annually.
- County Juvenile Probation Services.** State funds (approximately \$200 million) for operations. Annually appropriated in the budget.
- Public Library Foundation Program.** State funds (\$39 million) for public libraries. Annually appropriated in the budget.
- Adult Protection Program.** State provided \$20 million in current year for an expanded county program.



LAO, Cal Facts, December 4, 2006

STATE-LOCAL FINANCES

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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.



LAO, Cal Facts, December 6, 2004

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STATE-LOCAL FINANCES

Approval Requirements for State and Local Revenues

State Level	Legislative Approval	Voter Approval
Taxes	2/3	None
General obligation bonds	2/3	Majority
Other debt ^a	Majority	None
Fees	Majority	None

Local Level	Governing Body Approval	Voter Approval
City or county "general" taxes (revenues used for unrestricted purposes)	2/3 (Majority for charter cities)	Majority
City or county "special" taxes (revenues used for specific purposes)	Majority	2/3
All school or special district taxes	Majority	2/3
City, county, and special district general obligation bonds	Majority	2/3
K-14 district general obligation bonds	2/3	55 percent ^b
Other debt ^a	Majority	None
Property assessments	Majority	Majority of property owners. Votes weighted by assessment liability
Property-related fees	Majority	2/3 of voters or majority of property owners ^c
Fees—all other	Majority	None

^a Includes revenue and lease-revenue bonds and certificates of participation.

^b Exceptions: The State Constitution (1) requires approval by two-thirds of voters if the district does not meet certain requirements, and (2) specifies that a majority of voters can approve bonds used for repairing or replacing unsafe public school buildings.

^c No vote required for gas, electric, water, sewer, refuse, or developer fees.



LAO, Cal Facts, December 4, 2006

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STATE-LOCAL FINANCES

California's Property Tax Has Changed Significantly

Dollars in Billions

Years ^a	Revenue	Tax Distribution			
		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.



Proposition 1A's Changes to Legislative Authority Over Local Finance



Property Tax

- The Legislature may not permanently shift property tax revenues from noneducation local governments to schools.
- The Legislature may shift property tax revenues *temporarily* from noneducation local government to schools under the following circumstances:
 - The Governor declares a “severe state fiscal hardship.”
 - Two-thirds of the Legislature votes to suspend Proposition 1A.
 - The amount of property taxes shifted in each county is limited to 8 percent of prior-year noneducation agency property taxes.
 - The Legislature enacts a statute to provide repayment within three years.
- The Legislature may not change any city, county, or special district’s share of the property tax without a two-thirds vote of both houses of the Legislature.
- The Legislature may not use property taxes to reimburse noneducation agencies for mandated programs.



Proposition 1A's Changes to Legislative Authority Over Local Finance

(Continued)



Sales Tax

- With minor exceptions, 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.
- 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 state deficit-related bonds.



Vehicle License Fee (VLF)

- The Legislature may 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 Legislature's use of these additional revenues.



Proposition 1A's Changes to Legislature's Mandate Reimbursement Requirements

- Proposition 4 (1979) generally requires the state to reimburse local governments for mandated new programs or higher levels of service.

- Proposition 4 did not:
 - Set a time line for the state to make reimbursement payments.
 - Specify whether a state action to change a local government's share of a cost for a program constituted a reimbursable mandate.

- Proposition 1A (2004) requires the state to pay mandate bills in the annual budget, or suspend or repeal the mandate.
 - Does not apply to education or employee relations mandates.
 - Allows mandate bills from before 2004 to be paid over time.

- Proposition 1A (2004) expands the definition of a mandate to include transfers of financial responsibility from the state to local government. Specifically, Proposition 1A says transfers may be reimbursable mandates if:
 - the program shift is by the Legislature to cities, counties, and special districts.
 - The program is required, not optional.
 - The state previously had financial responsibility for it.



Major LAO Publications on the State-Local Fiscal Relationship

LAO Publication	Date
<i>Parole Realignment: LAO Alternative Budget Package</i>	March 10, 2008
<i>Realignment Revisited: An Evaluation of the 1991 Experiment in State-County Relations</i>	February 6, 2001
<i>Reconsidering AB 8: Exploring Alternative Ways to Allocate Property Taxes</i>	February 3, 2000
<i>Shifting Gears: Rethinking Property Tax Shift Relief</i>	February 2, 1999
<i>A Primer on the Vehicle License Fee</i>	June 17, 1998
<i>Why County Revenues Vary: State Laws and Local Conditions Affecting County Finance</i>	May 7, 1998
<i>A Perspective on the Vehicle License Fee</i>	February 18, 1998
<i>ERAF and the 1997-98 State Budget</i>	June 18, 1997
<i>Property Tax Shift</i>	February 19, 1997
<i>A Perspective on County Fiscal Restraints, P&I (p. 115-124)</i>	February 1996
<i>Understanding Proposition 218</i>	December 1996
<i>Property Taxes—Why Some Local Governments Get More Than Others</i>	August 21, 1996
<i>Reversing the Property Tax Shifts</i>	April 2, 1996
<i>Redevelopment After Reform: A Preliminary Look</i>	December 29, 1994
<i>Making Government Make Sense: Developing a Reform Proposal</i>	July 21, 1994
<i>The 1991-92 State and Local Program Realignment, P&I (p. 103-136)</i>	February 1992
<i>The County-State Partnership, P&I (p. 159-188)</i>	February 1991



Other LAO Publications on the State-Local Fiscal Relationship

LAO Publication	Date
<i>Improving the Mandate Process</i>	February 21, 2007
<i>Allocating Local Sales Taxes: Issues and Options</i>	January 24, 2007
<i>What is a Mandate: Learning Through Examples</i>	January 16, 2007
<i>What Is a Mandate: An Overview</i>	January 16, 2007
<i>State Oversight of Redevelopment</i>	November 18, 2005
<i>An Assessment: Governor's Local Government Proposal</i>	May 24, 2004
<i>Vehicle License Fee Issues</i>	February 18, 2004
<i>Booking Fees</i>	February 18, 2004
<i>Mandates: Mounting Liabilities and Need for Reform</i>	February 18, 2004
<i>Another Property Tax Shift?</i>	February 18, 2004
<i>Mandates: Overview of Process and Issues</i>	May 28, 2003
<i>Water Special Districts: A Look at Governance and Public Participation</i>	March 15, 2002
<i>Peace Officer Procedural Bill of Rights (POBOR) mandate</i>	February 20, 2002
<i>The Vehicle License Fee and the 2002-03 Budget</i>	February 20, 2002
<i>Property Tax Administration Funding Not Ideal Approach</i>	February 17, 2000
<i>California Counties: A Look at Program Performance</i>	May 21, 1998
<i>Proposition 172—How Did It Affect Spending for Public Safety?</i>	June 9, 1994
<i>Common Cents—Background Material on State and Local Government Finances</i>	October 1993
<i>Enterprise Special Districts, P&I (p. 88-93)</i>	February 1992
<i>Accommodating California's Growth, P&I (p. 97-110)</i>	February 1989
<i>Trial Court Funding and County Finances, P&I (p. 337-349)</i>	February 1989
<i>The Governor's 1995-96 State-County Realignment Proposal, P&I (p. 133-151)</i>	February 1995
<i>Restructuring the State-Local Relationship, P&I (p. 109-136)</i>	February 1994
<i>Making Government Make Sense: Applying the Concept in 1993-94</i>	May 1993
<i>Making Government Make Sense: A More Rational Structure for State and Local Government, P&I (p. 111-132)</i>	February 1993
<i>Restructuring Government in California, P&I (p. 101-109)</i>	February 1993