

**California Commission on Tax Policy  
in the New Economy**

Sacramento  
February 24, 2003

Proceedings

## **FEBRUARY 24, 2003: SACRAMENTO**

√Commissioner's Notes

A Framework for Fiscal Responsibility

Honorable Dick Ackerman - California State Senator

√Factors to Consider for the April Interim Report Talking Points

Nick Bollman - President, California Center for Regional Leadership

√Government Reform Studies

Roger Dunstan – Assistant Director, California Research Bureau

√Fiscal Reform: Equity, Stability, Harmony

Chris Norby - Orange County Board of Supervisors

Testimony

Commissioner Scott Peters

Honorable John Campbell - California State Assembly Member

Scott Farris - Governor's Office of Planning and Research

Jon Coupal - President, Howard Jarvis Taxpayers Association

Honorable Jim Brulte - Minority Leader, California State Senate

Assemblyman Dave Cox - Assembly Minority Leader

## **CALIFORNIA COMMISSION ON TAX POLICY IN THE NEW ECONOMY**

California State Capitol Building, Senate Room 112  
Sacramento, CA 95814  
February 24, 2003  
FINAL AGENDA

- 8:20 AM Chairman Rosendahl  
Meeting called to order  
Roll Call and Introductions
- 8:30 AM Senator Dick Ackerman, Vice Chair, Senate Budget and Fiscal Review  
Committee
- 8:45 AM Assemblyman Dave Cox, Assembly Minority Leader
- 9:00 AM Commissioner Scott Peters, Property Tax / Revenue Sharing
- 9:50 AM Chris Norby, Orange County Board of Supervisors
- 10:00 AM Assemblyman John Campbell, Vice Chair, Assembly Budget Committee
- 10:15 AM Commission Business  
Approval of meeting dates and locations for March and April 2003  
Working group organization
- 10:30 AM Nick Bollman, California Center for Regional Leadership
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- 12:30 PM Chairman Rosendahl  
Public Commentary  
Concluding Remarks  
Adjournment

Agendas for public bodies supported by the California Technology, Trade and Commerce Agency, are available at <http://commerce.ca.gov>. For additional information regarding this notice, please contact Marshall Graves, California Technology, Trade and Commerce Agency, 1102 Q Street, Suite 6000, Sacramento, CA, 95814, (916) 445-7654, [mgraves@commerce.ca.gov](mailto:mgraves@commerce.ca.gov)

Angie's Minutes

### **Assemblyman John Campbell**

AB Limit the growth in spending. Rain day reserve. An amount could be invaded in where revenue drops below. Spending limits. Constitution reform is the most important,

Previously both houses have always spent all funds available. Constitution restriction so that the legislation does the right thing. On the revenue side. Simplify tax laws.

Revenue Side:

Delete the entire state income tax. Saving to the stat would be substantial if we did away with state taxes.

General off with consumption taxes or sales tax.

California needs to take in to consideration of the federal level. If you have a spending cap you can balance the validity.

Third area of restructure: Incentives in place in government. The are re not there. Responding to incentives in front of them by spending it all. Giving service at a lower cost will be punished.

4th How does local government finance and what incentives does that have.

Local government should not be incentivised by state government. Distortion at the local level. State government is a high state of government. More that can be done to separate the streams of revenue.

5<sup>th</sup> The process in which the way is approved and signed by the governor. Of the 22 or the 23 past budget have been late to be signed. The 10<sup>th</sup> of May is based on the tax filing due date so the governor has the numbers. There is only about 5 to 10 days to negotiate the numbers so we can have more budget approved in a timely manner. The majority vote is not his preferred

Spending side is the most important area needed to be restructured. The chances would be less

If you see the

History of the spending limit as the economy is growing spending should be below. It was discovered that spending limit should allow spending based on growth. CalTAX acknowledge the failing of the spending limit. There is a two-year cycle that does not allow us to work outside of that. I don't see how

Fundamental to

Respectfully disagree. Government cannot artificial [in productivity growth if the government has population growth. The limit would force the government to make decisions based on priority. This cap should put somewhat of a limit on what it spends on Productivity of the private sector and public section. California is a high cost environment. Data processor and programmer are at a much lower cost and makes a higher demand on education and technology. No dividend in growth. Local government has a spending cap. What if in a unit of local government.

Brewer: The agreement in the past has been if we conformed, we would lose more than we would gain. No needing the use of FTB. Based on zero based budget and two years budget would require money being borrowed from one year to the next. Should be looked at and discussed.

Zero based budget falls into the

Structural reform.

Bill Weintraub: FTB would still be needed for collection of business taxes and enforcement, residency,

Are there specific

Residency can be resolved

Being debated since 1941. Could FTB be merged with?

Apply a rate to federal tax rate and brackets would need to be adjusted to

What would remain in place is the

Bill Weintraub: Can this be done legislatively.

Assembly; Yes, it can be done legislatively. A year such as this one could

Bill Weintraub - Income tax vs. consumption tax. It costs CA more to have state tax. What effects does consumption tax. I don't have a

Local government - legal concern or practical concern.

If they get a certain amount of tax,

Could put a percentage  
It's more of a practical issue than a legal issue.

Approval dates of meeting dates

Rossmann and Brewer

Scott Farris is coordinator from the Governor's office. 445-6139

His role Planning Office of research. Director of special projects. Idempotent commission that doesn't have indecent staff. Help in coordinating

Erica - Economy background

Mica - Communications

Wyoming

We certainly are dealing with how do we balance the budget. WE appreciate your access to the Governor. Welcome to year two as we prepare to finalize the.

Roger and Martha from Research Bureau has helped tremendously in putting together the interim report.

Appreciate Joan and Jesse.

Daniel Zingali suggested the Chairman meet Nick Bowman. Chairman will be asking for donation from the foundations. Nick will also be assisting with fund raising.

Framing comments about the ending. 1977 New York Task force - Technically it never went bankrupt.

Avoiding Bankruptcy

Successful because it forced many Commissions to come to the table in a different way 2<sup>nd</sup> there was an agreement between the unions / municipal.

10% of the budget and long-term proposal.

Last = independent control board = City was bound by budget controls. Policy reforms

How do you get to end games? Going out to the public is very important and will be controversial. Having public hearing allows to engage the public.

There has already been enormous amount of work done. . Being aware of the policy Implications would be

Looking at growth in California

Looking at screens

There is no single solution

But if you can find a package in line with each other.

Trade offs will have to be made and not every one will get to.

1. Mythology for budget control – make sure it's a real budget that doesn't foreclose
2. Operate with a reserved fund. – Protect the reserve funds.
  3. Boarding the tax base.
  4. Realignment moving – in powering local government to raise its own revenue
  5. Budget reforms - Longer term impacts and essential
  6. Lowering the voc threshold – Decreasing the pressure on the budget
  7. Way in which we can Tax sharing / protected the local revenue base

Small group to start looking at the end game as you are putting together your recommendations

Regional civic leaders – work with a network of 20 organization strong with three Es  
Social and economic benefits. Local, business, private.

Steve leaving

Recommendation should be made as a group.

March 12<sup>th</sup> =

March 24<sup>th</sup>

April 14<sup>th</sup>

April 21<sup>st</sup> Noon to late afternoon

Comm

Sean is going to propose a fifth committee to addresses structural reform.

Chairman, we will discuss this when we break down to groups.

Betty's staff

Howe do you see

Any suggestions on process. How we take our adhoc groups. Negotiation will happen in other sessions.

The opportunity is being allowed by having meeting in the north and south.

Get as direct involvement from the key stakeholders.

Brewer: Severity of the problem. In order to get where we are going we need to talk about it.

Near bankruptcy – it's expensive – we complicate it if we don't address issues.

Mark to provide some feedback on what they might be thinking

Doing it without scaring the public or stock exchange.

Home 24<sup>th</sup>. Helpful to hear from the Bluecoats people who have been through the process.

Stake holders

Commission will have presentations of ideas

Goldberg wants to put it out on the table to get the by participant support.

Chairman asks commissioners to work closely with coordinator to reflect California and want them to be part of this process.

Next public hearing will be key.

Chairman thanks them for

John Coupal, President of Howard Jarvis

Structural form should happened on the spending side and not from the revenue

Just as every California family lives within a budget so must the government. Spending must be appropriate and not at the expense of the economy.

Long-term tax bourdon should allow businesses to

Freed man  
George Shultz

Raising

Are there things from the revenue side – should not be an excused to raise taxes.

Volatility of our revenue source.

Adjustments made to even out that volatility.

Property tax has been the most stable in California. As property change hands

Forbes magazine – property tax revenue are going up.

Prop 13 is coming up on its 25<sup>th</sup> Anniversary. We do not oppose or support either

We are looking forward to California families

Weintraub - Prop 13 affecting individual homeowners. Position on sales tax

Not familiar with what sales tax issues have been discussed.

For example, Candy is not taxed yet Aspirin is taxed.

Your positions – on income taxes

We are looking at all those proposals

The most productive individuals are being driven out of California

Will have Fiscalization of commercial revenues.

Growth Structural reform

Lenny:

World-class explosion, that a greater part tax share. In LA the residential were 39%

Multi family 14 percent

Single increased substantially

Coupal: Business would reap a great windfall did not pan out to be true.

Increase in the

Brewer: Severity of the property tax – tax bill didn't increase 2% or more Pool Case:  
Prop 13 base does not allow for more than a 2% increase. Language says in prop 13 2%  
year to year. If the court of appeals upholds

Senator Bernardi Leader

Scott Peters Tax issues from a local government perspective.

Non-partisan – by partisan

January 29<sup>th</sup> of last year. - Structural issues, fairness issues

- Define the problem correctly
- Some say it's spending / some say it's restraint
- Budget grew by 37%
- Money came from capital gains - 9.3 percent
- Year 2000 \$85 billion came from 7 high tech corporations.
- Returning to the mean
- Where we are today – we are in the high \$60 billion
- Spending Gap.
- General fund can grow no more than
- Don't want any tax increases - When the economy is strained, you don't want to increase tax

WE believe we have to do what the governor details in his budget. Tight enough that Governor can overspend.

Prop 98 -

Voters has the right to tell us what to do. Maintained the integrity of prop 98

Lenny: 1997 tax package what good. \$8 Billion worth

What would you get rid of right now? What would you cut back?

Over the last two years the Governor has also increased tax increases.

Chairman: Golden opportunity for the Golden State – we are not looking into pointing fingers. Is there any structure reform? We need to correct and make sure that this never happens again.

High tech company are moving out of California. Additional reduction in the year. Structural reform that we need is a “spending cap” to make sure it general fund doesn't grow as

Burton: Rainy day fund, any though on this issue.

Spending caps can have component parts to them, requiring bigger reserve, requiring money to go into infrastructure.

Weintraub: What would you do to keep businesses in California

It's not just competition, locally, nationally and world wide.

Repelling the worker's comp. \$4.7 dollar expenditures to employers.

Job growth took off after the

Tom Hannigan

Medical – Medicaid

Social safety

Assembly Jim Brutle

\$30 billion - yes we are a donor state to the federal government.

We have this problem because we overspend ourselves.

Brewer:

Couldn't we just cut by 37% spending?

Assembly member: No we couldn't, we have had increase in education and in healthcare.

1999-2000 \$8 billion dollar surplus

55 majority

split roles

STTP Role

If you believe we have a revenue problem then the above would work

Becky Yee: Define our spending. A large percentage of the 37% achieving

We should do it when we have a surplus not when we have a revenue shortage.

Incentive: means to incent. We have to incentives for businesses to come to California.

What this legislature doesn't understand is that there is a directly correlation Capital is a moral it grows where there is a capital gain. Job growth in 1990s began after the huge Silicon Valley job growth

Need to make business inexpensive.

Chris Nor

I'd like to get your thought on Chris's Norby's presentation

Sales taxes go to local government.

We need to find a way to

There is no incentives for local government to create jobs. We need to, for example, give 5% of personal tax to local government.

March 14<sup>th</sup>

Monday, March 24<sup>th</sup> – James Irvine Foundation 10am – 4pm

Mar

Burton Motion to approve

Brewer seconded

All approved.

Burton: Consistency and uniformity

Structural reform should include “spending issues”

The governor has a different meaning for structural reform than the Commission does.

Focusing largely on the structural reform.

Sales and Tax

March 12<sup>th</sup> meeting will include some structural strategy. State Board of Equalization is included.

Telecom Tax: Will presentation be ready

What is contained in the sales tax?

Controller’s office will work with Betty

Board of Equalization is always looking into enforcing the use tax

Sales tax laws having loopholes and addressing them  
After the interim report is completed, what is our role?

A final report which we are mandated to complete the by end of the year.

If Commission feels they should go forward it should be reported to the Governor

It's too early to say at this point.

Burton: MADE MOTION TO GO FORWARD WITH THE 5 SUB COMMITTEES.

Bill Daunbrowki: SECOND MOTION

12<sup>TH</sup>

MINUTES WILL BE READY

Larry: Mr. Bowman has laid out a good start.

Motion to adjourn Brewer

Weintraub.

CALIFORNIA COMMISSION  
ON TAX POLICY IN THE NEW ECONOMY

**State Capitol Building**

**Senate Room 112**

**February 24, 2003**

**Commissioners' Notes**

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No speaker presentations are available

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California Commission on Tax Policy in the New Economy  
**Proposed Meeting Dates and Locations**

**For March and April 2003**

Wednesday, March 12	State Capitol Building Sacramento
Monday, March 24	James Irvine Foundation Offices San Francisco
Monday, April 14	Southern California Association of Governments Los Angeles
Monday, April 21	State Capitol Building Sacramento

Tax Commission Working Groups

Proposed for Discussion on 2/24/03

Commissioner	Sales & Use Taxes ----- Internet Transactions Streamlined Sales Tax Project (SSTP) Value Added Taxes	Property Tax Revenue Sharing	Telcom Tax	Income Tax ----- Corporate Individual Capital Gains
Brewer	Member	Member		
Burton	Member		Member	
Carr	Member	Member		
Dombrowski	Member	Member		Member
Goldberg	Member	Member		Chair
Peters		Chair	Member	
Rossman			Chair	Member
Weintraub	Chair		Member	Member
Updated: 2/19/03				

Slide 1

SENATE  
Republican Caucus

## A Framework for Fiscal Responsibility

January 2003

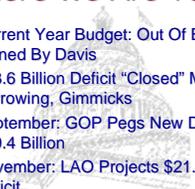


Slide 2

SENATE  
Republican Caucus

## Where We Are Today

- Current Year Budget: Out Of Balance When Signed By Davis
- \$23.6 Billion Deficit "Closed" Mainly By Borrowing, Gimmicks
- September: GOP Pegs New Deficit At \$19.4 Billion
- November: LAO Projects \$21.1 Billion Deficit
- January: Davis Says Deficit Is \$34.6 Billion



Slide 3

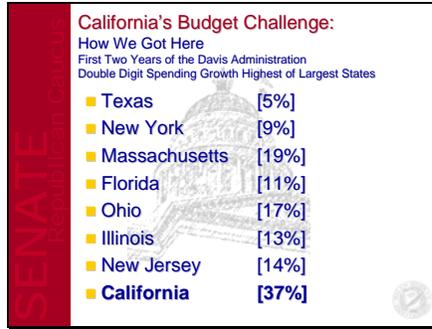
SENATE  
Republican Caucus

## How We Got Here

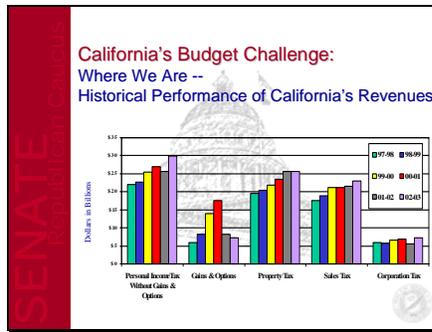
- Dramatic State Spending Growth: 37% in First Three Years
- Failure To Heed Signs of California Recession
- One-Time Funds Spent On Ongoing Programs
- Result: Multi-Year Structural Budget Deficit



Slide 4



Slide 5



Slide 6

**Where We Are**

**LAO** legislative analyst's office  
44 YEARS OF SERVICE

"The Recovery Has Not Been Of Sufficient Magnitude To Create New Jobs..."

Slide 7

**Where We Are**

**FORECAST**  
THE LEADING INDEPENDENT FORECAST PROVIDING INSIGHT TO  
DECISION MAKERS IN BUSINESS, ACADEMIA AND GOVERNMENT

Consumer Spending, Not  
Business Investment, Has  
Driven Recovery So Far

Slide 8

**Factors Compounding  
California's Economic  
Problems**

- High Commercial & Industrial  
Electricity Rates
- High Business Insurance Rates
- High Workers Compensation Costs

Slide 9

**A Framework For  
Fiscal Responsibility**

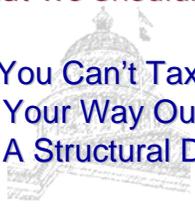
- Moratorium On Bills Punishing California  
Business
- Roll Back Bills Punishing California Job  
Creators
- Hard Freeze On State Spending
- Put Spending Cap Initiative Before  
Voters
- Multi-Year Deficit Elimination

Slide 10

SENATE  
REPUBLICAN CAUCUS

## What We Shouldn't Do

# You Can't Tax Your Way Out Of A Structural Deficit



Slide 11

SENATE  
REPUBLICAN CAUCUS

## What We Shouldn't Do

 CAIO  
INSTITUTE

Raising Taxes vs. Cutting  
Spending :

- Unemployment Rate:
  - ◆ 3.6% In Tax-Cutting States
  - ◆ 4.2% In Tax-Raising States



Slide 12

SENATE  
REPUBLICAN CAUCUS

## What We Shouldn't Do

 CAIO  
INSTITUTE

- Employment Growth:
  - ◆ 25% In Tax-Cutting States
  - ◆ 9% In Tax-Raising States
- Personal Income Growth:
  - ◆ 75% In Tax-Cutting States
  - ◆ 57% In Tax-Raising States



DRAFT

California Commission on Tax Policy in the New Economy

Factors to Consider for the April Interim Report  
Talking Points for Nick Bollman  
February 24,2003

- Methodology for spending control
  1. indexing
  2. trigger mechanisms
  
- “Rainy day” reserve fund
  1. discretionary limits
  2. changes in mandated programs
  
- Broadening the tax base
  1. volatility issues
  2. services
  3. exemptions
  
- 1) Structural reform
  1. multi year budgeting
  2. relaxing of earmarked funds
  3. changing fiscal year designation
  
- 2) Increasing local control
  1. more pay as you go
  2. revenue sharing
  3. TCRP – traffic congestion relief plan

Chris Norby, Supervisory Orange County 4<sup>th</sup> District  
10 Civic Center Plaza  
Santa Ana, CA 92701  
Phone: 714-834-440  
Fax: 714-834-2045

## **FISCAL REFORM: EQUITY, STABILITY, HARMONY**

### *Restructuring Local Government Finance in California*

California's fiscal crisis provides us a historic opportunity to structurally reform how local government is financed.

Our current system has evolved into a Byzantine maze of diversions, subventions, pass through, subsidies and chronic finger pointing among cities, counties, school districts and the state for who deserves more money. We endlessly blame each other for taking away "our" money.

I was a public school teacher for 20 years, a member of the Fullerton City council for 18 years, and now an Orange County Supervisor for two months. As a teacher, I saw cities take away school money through redevelopment diversions. As a city official, I saw the schools taking away money through ERAF diversions, and neighboring cities raiding our sales tax base by stealing our auto dealerships. And we all blamed the state, especially now that I am a county supervisor.

The time to blame each other is over. The state is us. All local governments are created and empowered by the state, and it is the legislature that now must and can fix our broken system of financing local government.

How do we fix it? Two steps:

- 1) Change the property tax allocations to guarantee all cities and counties a greater and more equitable share of their property taxes.
- 2) In exchange, send the local share of the sales tax to the state general fund to help pay for public education.

Free city and county governments from their reliance on sales taxes by assuring them the property tax revenues they need. Pool state sales tax revenues to assure adequate funding for public education.

By weaning local government away from sales taxes, we end the fiscalization of land use and the subsidization and over-building of commercial development. We end the shameless shakedown of cities by big box retailers, auto dealers, and NFL team owners for even-greater public handouts. In Orange County alone, over \$30 million in public

dollars have been given to Costco for building new stores and an estimated \$300 million has been handed to Costco statewide. Ending reliance on sales tax will break the cycle of wasteful commercial subsidies and restore these public funds to serving the public.

Costco's, Wal-Mart's, auto dealers, hotels, and even pro sports franchises will continue to do business in California without these massive giveaways. As a state California is too rich a market to ignore. With sales taxes going into a statewide pool, there will be no motive for local governments to continue the wasteful bidding wars over the next big box or car dealer. With more property taxes assured, cities and counties will welcome housing, as quality residential will pay for itself with increased property tax revenues.

In 1999, the Public Policy Institute of California issued its report "California and the Local Sales Tax." It conducted a poll of 330 city managers statewide as to their land use preferences for their cities. Their overwhelming choice was for new retail. At the bottom of the list was industrial. Second to last was residential. Cities want consumption, not production. Cities want people to buy things, not make things. Cities value people as consumers, not homeowners. But, we can change this by altering the fiscal incentives that have created these distorted priorities

Let our fiscal system reflect our values: Quality neighborhoods. Fair treatment for all businesses, not subsidizing the large at the expense of the small. And a proper jobs housing balance that allows people to work close to where they live and live close to where they work.

With greater reliance on property taxes, cities and counties will encourage housing, neighborhood maintenance and quality of life. With less reliance on sales taxes, we will stop subsidizing commercial development and leave business decisions up to the free market, where they belong.

A key component of this formula is to allow cities and counties to pool their redevelopment funds into their general funds. Allow redevelopment revenues to be used for operations and maintenance that benefit all. End the artificial distinction between redevelopment funds and general funds. End the wasteful shell game by which cities use redevelopment monies to subsidize retail to get sales tax.

Redevelopment agencies now divert \$2.1 billion annually, or 10% of all property taxes statewide, most of it to subsidize corporate retailers, hotels, auto malls, multiplexes and even gambling casinos. It's no surprise that Governor Davis now proposes to tap these funds for public education. Public money should build classrooms, not Costcos. A better solution however, is to restore the \$2.1 billion to city and county general funds in exchange schools getting more sales tax revenues.

With that additional \$2.1 billion in redevelopment funds flowing to their general funds, local governments will have more money for infrastructure and services. With sales taxes flowing to the state, there would be no incentives to subsidize retail. This would not simply re-slice the pie. IT would increase the size of the pie. Ending sales tax and

property tax giveaways to private businesses will free more money to serve the public. I claim no personal credit for proposing this property-sales tax shift today. It has been long discussed by academics and policymakers. It was specifically recommended by the Wilson/Hertzberg Commission and Speaker Villaraigosa's Commission on State and Local Government Reform. That was in 1999. 2003 brings us a new sense of urgency, an urgency to bring rationality and equity into a broken system, and to free money once serving private interests to now serve the public interest.

Now is the time. We are the leaders. This is the vision. Lets make it happen.

**California Research Bureau  
California State Library**

**To:** William J. Rosendahl, Chair  
Commission on Tax Policy in the New Economy

**From:** Roger Dunstan  
Assistant Director

**Date:** February 10, 2003

**Subject:** Government Reform Studies

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Growing concern over the problems of state and local government have led to the formation of a variety of commissions and groups over the last decade. These entities have issued a variety of studies and recommendations. In this memo, I summarize those conclusions that most directly relate to the jurisdiction of the Commission on Tax Policy in the New Economy.

These entities can be divided into two groups. The first group is concerned with state government and local government and their recommendations cover both levels of government. The objective of these groups was governmental structural reform. The second, and larger, group focused mainly on local government, although their recommendations would affect state government.

These other reform proposals and studies do not address all of the public finance issues that the commission must address. Because of the emphasis on local government, there are many recommendations on sales and property tax. Other issues such as electronic commerce and telecommunications taxes are not considered.

**1. California Governance Consensus Project.** <http://www.csus.edu/calst/cgcp/>

This project was a broad-based collaborative efforts focused on reforming California government. Thirty-four statewide organizations representing business, government, labor, education, public safety, health, environmental, human services, and taxpayer interests were involved with the project. The project focused on two fundamental questions:<sup>i</sup>

- How to secure sufficient and stable revenues for essential government operations while appropriately constraining governmental authority to tax and spend.
- What the division of responsibilities should be between the state and local governments.

Although the consensus project did not come to a consensus, they did produce a conceptual plan that was, well, close to a consensus. The project identified major elements that they described as “definitely included in the Project’s current proposal.” Among those that relate to the commission’s jurisdiction are:<sup>ii</sup>

- Require majority voter approval for special taxes, except property taxes, which would remain capped as provided for under Proposition 13.
- Require the state budget be approved on time, be balanced when enacted and include an adequate reserve.
- Require a review of all state taxes, including all tax expenditures, every four years.
- Change the Legislative vote for tax expenditures (i.e., tax exemptions, credits, deductions and the like) from the current majority to a two-thirds vote. Maintain the majority vote requirement for tax changes that are neutral with regard to amount and incidence.
- Dedicate a ¼ cent increase the sales and use tax for purposes the public will support.
- Require any future initiative containing a super-majority vote requirement to be approved by an equal super-majority vote.

Other measures were identified as possibilities for inclusion. These are:

- Dedicate all business real property taxes to the general support of local governments within each county to equalize and stimulate local business development beyond present incentives for retail sales tax generators.
- Transfer specified portions of residential real property taxes on a county-by-county basis to the support of local governments to stabilize local government financing and to increase incentives for residential development.
- Change the current, two-thirds Legislative vote requirement for approval of the state budget to a majority vote.
- Require the state to adopt a balanced and timely budget with forfeiture of pay, per diem or other allowances for the period of delay by the Governor and Legislators when the budget is approved after the Constitutional deadlines for the Legislature and the Governor
- Designate a minimum reserve contribution requirement for non-recessionary years and provide a maximum level of reserves for all years. Allow the Legislature to expend reserves by a two-thirds majority vote during recessionary years or during emergencies.

## **2. California Constitution Revision Commission**

<http://www.library.ca.gov/CCRC/pdfs/execsum.pdf>

In 1994, the Governor and Legislature appointed the 23 members of the California Constitution Revision Commission. The Commission had a broad charge and looked at the structure of state government, the state local relationship, and the state budgetary processes.

Most of the recommendations the Commission made focused on government structure, however, the following relate to state fiscal policy:

- Enact measure to keep the state budget in balance. These include provide a mechanism for balancing the budget during the fiscal year and prohibiting the enactment of any legislation that threatens to imbalance the budget.
- Lengthen the fiscal year from one to two years.
- Require a three percent general fund reserve.
- Prohibit borrowing to finance a deficit.

Many of these recommendations also appeared later in a report by the California Citizens Budget Commission, *A 21<sup>st</sup> Century Budget Process for California*.

Within the last decade there have been six major reform proposals that focused on local government, but their recommendations would affect state taxation. These were driven by the desire to overhaul the relationship between state and local governments. As such their recommendations do not address all of the issues that the commission is charged with examining.

The state-local relationship has been examined frequently and changed throughout California's statehood. However, the scrutiny intensified in the wake Proposition 13's passage. This measure reduced the property tax, which was the core of local government finance. Over the last 25 years, there have been more statutory and constitutional changes, which have further affected state and local finance. The result of these efforts has left many observers concerned about a situation where the state significantly controls local government revenue sources and local governments depend on revenues, such as sales tax, that result in less than optimal land use decisions. Observers are concerned that local governments rely too heavily on the sales tax, with a result that they fight bitterly over auto dealers and big box retail development. Conversely, local governments have almost no incentive to allow industrial land because of how little property tax they receive. Residential development almost always costs local governments more for the services than they receive back in taxes.

Following is a summary of the major reform reports. I listed only those of most direct relevance to the commission's responsibilities.<sup>iii</sup>

### **1. Speaker's Commission on State and Local Government Finance**

<http://speaker.metroforum.org/report/report.pdf>

This commission was created by then Assembly Speaker Antonio Villaraigosa. The membership of the commission was composed of 35 community leaders from around the state.

Their main recommendations were to:

- Direct a portion of the one percent locally-levied sales tax to the state. In turn, local governments would receive an equivalent portion of the property tax that

now goes to K-12 schools. This would reduce the fiscal incentives that local governments have for permitting retail development and increase the return for approving housing and industrial development. The commission was also concerned that increasing electronic commerce eventually would erode the sales tax and have a negative fiscal impact on local governments.

- Over a prolonged period, shift the Education Revenue Augmentation Fund (ERAF) monies back to counties, cities, and special districts. Local governments previously received these property tax funds but during the fiscal crisis of the early 1990s, the funds were shifted to K-12. By increasing the amount of property tax they receive, local governments would have more discretionary funds and also increased incentives for permitting housing and industrial development.
- Place the existing vehicle license fee subvention in the state constitution. This action would ensure that local governments would continue receiving these funds. The commission was concerned that local governments continue receiving these funds, which are a major source of discretionary funds. The commission also recommended placing in the constitution that the state must replace the revenue lost by any reduction in the vehicle license fee.

The commission also made recommendations designed to strengthen the relationship between citizens and governments and improve the relationship between the state and. The commission detailed a variety of recommendations to implement this objective.

## **2. The State Controller's State Municipal Advisory Reform Team (SMART)**

<http://www.sco.ca.gov/eo/genint/taxforce2000/index.shtml>

Former Controller Kathleen Connell released this report in 1999. The reform team was composed of elected officials and representatives of business, labor and academia. Their main recommendations were:

- Distribute locally-levied sales tax to all jurisdictions on the basis of population. This recommendation would end the current distribution, which is done on a geographic basis determined by the location of the point of sale. This would reduce the incentives that local governments face in attempting to attract retail and also equalize distribution of those sales tax funds.
- The ERAF shift would have been capped and subsequent growth in the revenues would go to local governments. The state would have to make up the difference and transfer that amount to local schools.
- This entity also made recommendations on state local government relations.

## **3. Commission on Local Governance for the 21<sup>st</sup> Century**

Assembly Member Robert Hertzberg authored AB 1484 (Chapter 943, Statutes of 1997) which created this commission. The Governor and the Senate and Assembly Rules Committees appointed the 15-member commission. The commission completed its report and made the following recommendations:

- Reduce local reliance on the sales tax.
- Realign state and local responsibilities and resources.

#### **4. League of California Cities**

<http://www.cacities.org/>

The League created a task force to develop a fiscal reform plan. The conclusions of the task force are:

- Increase the property tax allocation to local governments.
- Swap future sales tax to the state for additional property tax.

#### **5. California State Association of Counties**

[http://www.csac.counties.org/legislation/fiscal\\_reform/](http://www.csac.counties.org/legislation/fiscal_reform/)

The California State Association of Counties (CSAC) develop a reform proposal that recommended the following:

- Allocate the locally-levied sales tax by dividing the funds into three pools. One pool would be a continuation of the point of sale allocation. There would also be a per capita pool and an equity pool for poor jurisdictions.
- Exchange vehicle license fee money for a portion of the personal income tax.
- Return the ERAF property tax.
- Make a variety of changes in the state-local government relationship.

#### **6. Legislative Analyst's Office**

[http://www.lao.ca.gov/020300\\_ab8/020300\\_ab8.pdf](http://www.lao.ca.gov/020300_ab8/020300_ab8.pdf)

In 1999, the Legislative Analyst's Office (LAO) released a report that contained five options for allocating the property tax. These alternatives are:

- Set a statewide rate for property tax. Each local government would receive a set share of the property tax based on the services they provide.
- Provide local control over ERAF.
- Set property taxes for local government services and schools.
- Reduce the state and local sales tax. Local governments would also give up a portion of the VLF revenues for a larger share of the property tax. Local governments would have more freedom to raise property tax and nonresidential property would be assessed at market value.
- Realign state and local programs and finance.

If you have any questions, please call me at 653-9254.

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<sup>1</sup> California Governance Consensus Project, Executive Summary [www.csus.edu/calst/cgcp/page1.htm](http://www.csus.edu/calst/cgcp/page1.htm)

<sup>1</sup> California Governance Consensus Project. "Conceptual Plan as Modified at the March 2, 1999 Plenary Meeting. <http://www.csus.edu/calst/cgcp/page2a.htm>

<sup>1</sup> This discussion relies heavily on J. Fred Silva and Paul G. Lewis, *Changing the Order of Things: Six Proposals for Local Finance Reform*. Prepared for the Conference on Local Finance Reform, Davis California.

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<sup>i</sup> California Governance Consensus Project, Executive Summary [www.csus.edu/calst/cgcp/page1.htm](http://www.csus.edu/calst/cgcp/page1.htm)

<sup>ii</sup> California Governance Consensus Project. "Conceptual Plan as Modified at the March 2, 1999 Plenary Meeting. <http://www.csus.edu/calst/cgcp/page2a.htm>

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