Senate Budget and Fiscal Review— Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Richard Roth, Chair
Senator Tom Berryhill
Senator Norma Torres

Thursday, March 27, 2014
9:30 a.m. – Rose Ann Vuich Hearing Room 2040

Consultant: Mark Ibele

Local Government Finance

<u>Proposed Discussion and Vote Calendar</u>

Issues Proposed for Discussion / Vote

9210 Local Government Financing

Item Overview: The 9210 budget item includes several programs that make state subventions to local governments. In past years, the payments have included General Fund appropriations for constitutionally-required repayment of 2009-10 Proposition 1A borrowing from local governments; a small subvention related to former redevelopment agencies (RDAs) to help retire a portion of outstanding debt that was backed by the personal property tax; and a subvention of for counties and cities within those counties for insufficient Educational Revenue Augmentation Fund (ERAF) resources.

Budget Overview: The proposed budget for the 9210 item is $16.0 million General Fund. This is comprised of $8.5 million in subventions to the counties of Alpine, Amador, and San Mateo (and cities within those counties), and $7.5 million for the proposed State-County Assessors' Partnership Agreement Program. The subventions are related to the so-called 'Triple Flip' and 'Vehicle License Fee (VLF) Swap,' both of which are described below. The Department of Finance (DOF) indicates it will not know the final subvention amounts for each of these counties until the May Revision.

Issue 1: Subventions to Alpine, Amador, and San Mateo Counties (Governor's Budget Proposal)

Proposal: The Governor's budget proposes a General Fund subvention of $8.5 million to backfill Alpine, Amador, and San Mateo counties due to circumstances that reduced property tax directed to those county governments, and cities within those counties, in 2012-13. These circumstances also occurred in these counties in the prior year, and the state provided a subvention. The revenue losses will likely continue to some degree in the future, but the Administration indicates its current proposal is of a one-time nature.

Background and Detail: Legislation enacted early in the Schwarzenegger Administration shifted local property tax from schools to cities and counties to accommodate two state fiscal initiatives. Schools were then backfilled with state funds for each of these initiatives. Overall, the fiscal changes resulted in a large net revenue gain for cities and counties as the replacement revenue streams have grown faster than the relinquished revenue streams. However, unique circumstances reportedly reversed this outcome in 2010-11 for Amador County and in 2011-12 and 2012-13 for Alpine, Amador, and San Mateo counties, and it is possible this outcome could occur for a few additional counties in the future.

In the 2004 primary election, voters approved Proposition 58, which allowed the state to sell Economic Recovery Bonds (ERBs) to pay its accumulated budget deficit. The local sales tax for cities and counties was reduced by one-quarter cent and the state sales tax was increased by one-quarter cent to create a dedicated funding source to repay the ERBs. Property tax was redirected from schools to cities and counties, and the state backfilled schools via the Proposition 98 funding guarantee. This financing mechanism is sometimes called the Triple Flip, and the process was intended to hold local governments harmless. At the time the ERBs are repaid (in 2016-17, or earlier under the Governor's budget proposal), the local sales tax rate will be restored, and no flip—triple or otherwise—will be necessary.

Also in 2004, the Legislature enacted the VLF Swap. The measure was designed to provide a more reliable funding mechanism to backfill cities and counties for the local revenue decrease resulting from the action that the reduced the VLF tax on motor vehicle from 2.0 percent of a vehicle's value to 0.65 percent of a vehicle's value. Here again, the state redirected property tax from schools to cities and counties to make up for the VLF cut and backfilled schools for the property tax loses with state funds.

The backfill for the Triple Flip and the VLF Swap must originate from property taxes either shifted from the Education Revenue Augmentation Fund (ERAF) or from non-basic aid K-12 and community college districts (but not from so-called 'basic aid' schools). This funding mechanism stopped fully working for Amador County reportedly in 2010-11 due to all the schools in those counties becoming basic aid schools. Basic aid schools receive sufficient local property tax to fully fund the per-student amounts required by the Proposition 98 guarantee, and therefore, the state's funding is minimal. Due to this basic aid situation, current law will not provide backfill for such schools for any property tax shifted to cities and counties. County auditors have reportedly reduced or discontinued the shift of property tax from schools to those cities and counties.

Staff Comments: The financing shifts and educational financing provisions are complex, and perhaps not entirely relevant to making a determination on this budget request. Some issues for consideration are the following:

- The funding shifts included revenue growth uncertainty and risk, as the relative growth of various revenue streams over many years was unknown. On a statewide basis, data suggests most counties have received a net benefit from the shifts.

- There was no backfill guaranteed in the original legislation, although the Alpine, Amador and San Mateo outcomes were also not anticipated. The enacting legislation did not include provisions for the state to backfill locals with new subventions if the baseline funding mechanism proved to be insufficient.

- At the time of the legislation, stakeholders were likely aware of the risk of variable levels of growth for different revenue streams, but may not have anticipated that outcome of all schools within the county becoming basic aid.

The overall approach to this issue has generally been ad hoc in nature, and a response to facts and circumstances. This would be of significant concern if the magnitude of the General Fund relief were to continue indefinitely or increase in magnitude. However, the DOF indicates that the unwinding of the Triple Flip should result in a general decrease in existing relief to counties and lessen the chances that the problem will extend to additional counties.

LAO Perspective: LAO has suggested in the past that the state could reimburse cities and counties for all Triple Flip and VLF Swap funding shortfalls, as proposed in the Governor's budget or, in recognition of the significant fiscal benefits cities and counties receive under the VLF Swap, reimburse cities and counties only where necessary to replace actual sales tax and VLF revenue losses (what they would have received had they retained these revenue streams). Either level of reimbursement could be accomplished through the budget or through a shift in property taxes. The former approach would provide more revenue certainty for local governments while the latter would be more reflective as to the actual costs.

Staff Recommendation: Staff recommends holding the item open, pending May Revision request.

Vote:

Issue 2: State-County Assessor's Partnership Agreement Program (Governor's Budget Proposal and Trailer Bill Language)

Proposal: The Governor's budget proposes $7.5 million and trailer bill language (TBL) to enact a state-county program to improve assessments for property tax purposes throughout California. The budget proposal establishes a State - County Assessors' Partnership Agreement Program (SCAPAP) to enhance local property assessment efforts. The SCAPAP would begin on a three-year pilot basis, funded at $7.5 million per year, and administered by the DOF.

The SCAPAP will be limited to nine county assessors' offices competitively selected from a mix of urban, suburban, and rural counties. To participate in the SCAPAP, the county must submit an application to DOF demonstrating work to be performed. The county must also agree to provide its Assessor's office with a specified amount of matching county funds each fiscal year to generate additional property tax revenues for local agencies by doing the following:

- Enroll newly-constructed property and incorporate property ownership changes.
- Reassess property to reflect current market values.
- Enroll property modifications that change the property's taxable value.
- Respond to assessed valuation appeals.

Under the proposal, DOF will review the applications and select participants on the strength of each County's proposal. As the three-year program term nears its expiration date, the DOF proposes to evaluate the results and issue findings to the Legislature. The Administration and the Legislature would then determine whether to continue the program in its current form, expand the program to more counties, or allow it to expire.

Each year, participating counties would have to report to the Administration the number and taxable value of properties added to the local property tax roll as a result of activities undertaken with grant funds. In addition to new or updated assessments, each county would report the total amount of property taxes preserved when staff successfully defended a property owner's appeal to reduce their property's taxable value. The Administration would determine whether each county's pilot was successful, based on whether a county pilot resulted in additional property tax revenues being allocated to schools that are at least three times larger than the amount of the state grant in that county. (Additional revenue from the program includes revenue accelerated, increased, or preserved by staff hired using state grants and county matching funds). The Administration's calculation would not vary by county based on the schools' share of countywide property taxes in that county. The Director of Finance would have authority to terminate the grant program in any county that does not meet this level of return. The Administration's grant program is a three-year pilot program, after which the Administration would use its findings to make a recommendation as to whether the Program should be continued in its current form, expanded to include additional county assessors' offices, or terminated in 2017-18.

Background: County assessors are responsible for assessing real and qualifying personal property for property tax purposes, and for maintaining and updating property tax rolls. Beginning in 1995, the state provided annual General Fund loans to county assessors' offices to enable them to more quickly enroll newly-constructed property and account for property ownership changes. The additional property tax revenue received by schools through these efforts reduced the state's Proposition 98 General Fund costs, and the loans to the assessors were thereafter forgiven. The loan program was reconstituted in 2002 as a grant program, known as the Property Tax Administration Grant Program. This program operated until 2005‑06, when it was eliminated as a savings measure.

The underlying rationale for property tax assistance programs is that the counties may not be receiving proper 'price signals' (net of return). That is, because the property tax revenues that go to the state may not be incorporated in the counties' staffing calculus, a less than optimal amount of resources may be devoted to assessment activities. While most local governments that receive property taxes reimburse the county for their proportionate share of administrative costs, schools and community colleges ("schools") are not required to pay these costs. Instead, counties pay the schools' share of costs as well as their own. Statewide, counties pay about two-thirds of the cost to administer the tax while receiving less than one-third of the revenues they collect. As a result of this imbalance, there have been long-standing concerns that—without an additional incentive—counties might not fund property tax administration at an efficient level. If property tax administration were not funded appropriately, this could have a fiscal effect on the state because local property taxes that go to schools generally offset required state spending on education.

LAO Perspective: LAO has provided a thorough review and analysis of the Administration's proposal, and further developed some of the aspects of the pilot project in a constructive manner. Overall, it views the proposal favorably, but indicates that there are some specific changes that could improve the program. LAO recommends:

- Altering the proposed dollar-for-dollar county match to reflect each county's share of benefits from additional spending on property tax activities. This would address the likelihood that (under a one-to-one match) counties that receive a greater share of property taxes would have a greater incentive to participate in the program.

- Providing for a guaranteed state grant for three years, without early termination. Under the Administration's proposal, counties that failed to meet the 3/1 benefit/cost threshold would be terminated from the program. While the current proposal could result in greater state revenue, it may also result in failure to gain full knowledge of the characteristics of a successful program and terminate programs that are only more successful over a somewhat longer term.

- Allocating the state grant in proportion to the total property value in that county. Under the Administration's proposal, each county would receive the same amount—thus some counties would receive larger grants, relative to their size—than other counties. This alternative approach is an attempt to control for that potential asymmetry.

- Selecting county participation based on random selection, when possible. This would help ensure that the design of a final program (if any) would be informed by the participation of counties with varying characteristics, rather than having a pilot which might be biased in favor of characteristics that benefit the state.

Staff Comments: The Administration's proposal to reinitiate assistance to counties to improve the Administration of the local property tax is an appropriate one. The benefits derived from property tax revenues benefit the state—and taxpayers statewide—as well as local governments. To explore potential benefits of additional support through a pilot program is reasonable, although it carries with it some tensions. Fundamentally, the overarching goals of the program seem to be both to generate additional revenues and also to determine what type of program works. While these twin goals may be largely compatible, they could also be at odds with each other. For example, the Governor's budget indicates that programs will be selected 'competitively' on the 'strength' of each county's proposal. It is likely that a program that may not be 'competitive' in terms of revenue generation could be quite informative with respect to important design features in a program. Staff recommends additional discussions to allow for further refinement of and improvements to the Governor's proposal.

Staff Recommendation: Hold open.

Vote:

Issue Proposed for Discussion / Vote

Local Government Revenues

This issue relates to local government revenues and proposed changes in statute that could affect the allocation and distribution of such resources.

Issue 1: Stranded Supplemental Property Taxes (Governor's Budget Trailer Bill)

Proposal: Under current law, certain property taxes, collected pursuant to the supplemental role, cannot legally be distributed to local governments if all a county's school districts are basic aid. The Administration proposes trailer bill language (TBL) that would address this technical issue and allow for the distribution of these "stranded" property taxes. When all of a county's K-12 schools are basic aid, the legislation proposed by the Administration would take the property tax that currently cannot be distributed to the county's K-12 schools and redistribute that sum to the county, County Office of Education, Community Colleges, cities, and special districts. The distribution would be proportionate to each affected taxing entity's share of the 'AB 8 base.' (AB 8 [Greene], Chapter 282, Statutes of 1979, was the initial legislation establishing the local property tax allocation system.)

Background: Revenue and Taxation Code Section 75.70 contains a formula for distributing supplemental roll property tax revenues. Each affected taxing entity receives a specified share, based primarily on its share of the AB 8 base property tax revenues. After the county, cities, special districts, Community Colleges, and the County Office of Education have been filled to their statutory caps pursuant to the formula, the remaining supplemental roll revenue is distributed to non-basic aid K-12 schools. Specifically, the statutes state the remainder shall be distributed to each K-12 school based on its average daily attendance (ADA), as certified by the Department of Education.

Since basic aid schools have a certified ADA of 'zero', they receive no supplemental roll revenue. When the supplemental roll was created in the 1980s, it was the intent of policymakers that the revenues only go to those K-12 schools with the greatest funding need. Since basic aid schools are filled to their revenue limits solely with property tax revenues, their need for supplemental roll revenue is less than that of the non-basic aid districts that receive significantly less property tax revenue.

At least one county (Plumas) has a unique situation in that: (1) each affected tax entity has been filled to its statutory supplemental roll cap, and (2) there are no non-basic aid K-12 schools in the County to absorb the remaining supplemental roll revenues. Consequently, for at least three years, the previous county auditor-controller was holding the excess monies in an impound account. The accumulated balance is estimated to be $2.6 million.

Staff Comment: The proposal from the Administration is a largely technical change allowing for the appropriate distribution of property taxes to local governments.

Staff Recommendation: Adopt the TBL proposed by the Administration.

Vote:

Issues Proposed for Discussion

Issue 2: Vehicle License Fee Adjustment Amount (Informational Issue)

Issue: As a result of reductions in the vehicle license fee (VLF) and shifts of revenue sources pursuant to realignment (and previous legislation), some newly-incorporated cities—as well as cities with newly-annexed areas—do not receive revenue that they would otherwise have received under prior law. Specifically, cities used to receive a VLF ‘bump’ under prior law. The reduction in financial resources has resulted in significant fiscal challenges for these cities, with potential impacts on their financial stability.

Background: In lieu of a property tax on motor vehicles, the state collects the annual VLF and allocates the revenues, minus administrative costs, to cities and counties. In 1998, the Legislature began cutting the VLF rate from 2 percent to 0.65 percent of a vehicle's value. The General Fund backfilled the lost VLF revenues to cities and counties. As part of the 2004-05 budget agreement, the Legislature enacted the ‘VLF Swap’ which replaced the backfill to local governments from the General Fund, with property tax revenues that otherwise would have gone to schools through the Educational Revenue Augmentation Fund (ERAF). This replacement property tax funding is known as the "VLF adjustment amount." The General Fund backfills schools for their lost ERAF money.

Before 2004, for the first seven years after incorporation, new cities received VLF funds under a formula that calculated their population as three times the number of the city's registered voters. This formula deliberately overstated a new city's population, resulting in a higher share of VLF funds. This so-called VLF bump gave a new city more money during its start-up period. The VLF Swap did not reallocate extra property tax revenues to cities that were not in existence when the state was compensating cities for the difference between the 2% and 0.65% VLF rates. As a result, new cities received less VLF funding than they would have if they had incorporated before the VLF Swap. Similarly, a city that annexed an inhabited area received less VLF revenue than it would have before the VLF-property tax swap. Because the amount of the per capita VLF allocations went down when the Legislature cut the VLF rate, the amount of additional VLF revenue coming to a city as the result of annexing an inhabited area was also sharply reduced. The VLF Swap did not compensate cities for this reduction. Cities only receive additional property tax revenues in lieu of lost VLF based on the future growth of assessed valuation in the annexed area.

Cities asked the Legislature to reallocate a portion of existing cities' remaining VLF funds to new cities and to cities that annex inhabited areas to help make new city incorporations and city annexations financially feasible. In response, the Legislature passed AB 1602 (Laird), Chapter 556, Statues of 2006, which changed the allocation of VLF funds to restore the reduced VLF revenues for city incorporations and annexations that were lost under the VLF Swap. Subsequently, the 2011 Realignment Proposal shifted several state programs and commensurate revenues to local governments. The Legislature passed Senate Bill 89 (Committee on Budget and Fiscal Review), Chapter 35, Statutes of 2011, which recalculated the Department of Motor Vehicle's administration fund to $25 million and increased vehicle license registration by $12 per vehicle to offset DMV's budget reduction. SB 89 also eliminated the $153 million in VLF revenues allocated to cities and shifted those revenues to fund public safety realignment. The passage of Proposition 30 in 2012 amended the Constitution to permanently dedicate a portion of the sales tax and VLF to local governments to pay for the programs realigned in 2011-12. It also temporarily increased the sales tax for four years and state personal income taxes for seven years.

Staff Comment: Cities argue that SB 89's elimination of VLF allocations jeopardizes the financial viability of recently incorporated cities and cities that annexed inhabited areas. Local officials want the Legislature to recalculate the VLF adjustment amount to give additional resources to four recently incorporated cities and to cities that annexed inhabited areas after 2004.

Staff Recommendation: Informational issue.

8885 Commission on State Mandates

Item Overview: The Commission on State Mandates (Commission) is a quasi-judicial body created for the purpose of determining state mandated costs. The objective of the Commission is to impartially hear and determine if local agencies and school districts are entitled to reimbursement for increased costs mandated by the state consistent with Article XIII B, Section 6 of the California Constitution. The Commission consists of the Director of Finance, the State Controller, the State Treasurer, the Director of the Office of Planning and Research, and a public member and two local government representatives appointed by the Governor and approved by the Senate.

Budget Overview: For 2013-14, the Commission was budgeted at $1.9 million and 13 positions for state operations. This administrative support level was increased slightly from the prior year‘s funding of $1.6 million. For 2014-15, the administrative support resources will remain flat. Costs associated with funding mandates proposed in the Governor's budget for 2014-15 are approximately $36.2 million (all funds) and $33.6 (General Fund).

Background: The Commission is responsible for determining whether a new statute, executive order, or regulation contains a reimbursable state mandate on local governments, and for establishing the appropriate reimbursement to local governments from a mandate claim. The Constitution generally requires the state to reimburse local governments when it mandates that they provide a new program or higher level of service. Activities or services required by the Constitution are not considered reimbursable mandates. The Constitution, as amended by Proposition 1A of 2004, requires that the Legislature either fund or suspend local mandates. Payments for mandate costs incurred prior to 2004 are one exception noted in the Constitution—such pre-2004 mandate costs can be repaid over time. Another exception in the Constitution is for mandates related to labor relations. In these cases, the state can defer payment of the mandates and still retain the mandates' requirements. In most cases, if the Legislature fails to fund a mandate, or if the Governor vetoes funding, the legal requirements are considered suspended pursuant to the Constitution.

Mandate reimbursement claims are filed with the Commission for the prior fiscal year—after that fiscal year is completed and actual costs are known. The state pays the mandate claims in the following fiscal year. For example, local costs incurred in 2012-13 are reported and claimed in 2013-14, and the state will reimburse locals for these costs as part of the 2014-15 budget. Suspending a mandate does not relieve the state of the obligation of reimbursing valid claims from prior-years, but it does allow the state to defer payment. For example, several elections-related mandates were suspended for the first time in the 2011-12 budget. This means the activities for locals were optional in 2011-12 and locals cannot claim reimbursement for any new costs incurred in 2011-12. However, the mandate claims for these costs in 2009-10 and 2010-11 are still due—either over time or all at once in the year when the mandate suspension is lifted. The state owes local governments approximately $1.8 billion in non-education mandate payments. Of this, about $900 million is associated with pre-2004 mandate claims. The Governor proposes to pay-off the pre-2004 mandate costs in 2015-16 and 2016-17 as part of the elimination of the 'wall of debt'.

Issues Proposed for Discussion

Issue 1: Mandate Process (Informational Issue)

Determining whether a particular state requirement is a state-mandated local program and the process by which the reimbursable cost is determined is an extensive, time-consuming, and multi-stage undertaking. State and local officials have expressed significant concerns in the past about the mandate determination process, especially its length and the complexity of reimbursement claiming methodologies.

A lengthy period of review and determination presents several difficulties that affect both the state and local governments. Among the most important are flip sides of the same coin, specifically:

- Local governments must carry out the mandated requirements without reimbursement for a period of some years, plus any additional time associated with development of the mandate test claim, appropriation of reimbursement funds, and the issuance of checks.

- State mandate liabilities accumulate during the determination period and make the amount of state costs reported to the Legislature higher than they would be with an expedited process. Policy review of mandates is hindered because the Legislature receives cost information years after the debate regarding their imposition.

Last year the Commission was appropriated resources for additional staff, with the requested positions directed to increasing the capacity of the Commission in order to comply with statutory time frames and accelerate the reduction in the backlogs associated with various Commission activities. These activities include addressing test claims, establishing and amending parameters and guidelines, developing statewide cost estimates, and addressing incorrect reductions claims.

Staff Comment: Commission staff indicates that progress has been made regarding reducing the administrative backlog associated with the mandate process. That is, the additional resources budgeted for the Commission during the current year have had a beneficial impact. Clearly, this is only the administrative component of a larger local mandate issue, but it nevertheless is a positive sign. The resources appear to have resulted in reducing the delays that have been endemic to the current system. The committee may ask the Commission to discuss its current activities and recent reported improvements.

In addition, last year, the Administration indicated that it would pursue policies to improve the mandate process, including deferring decisions to local government decision-makers and allowing for maximum flexibility. The committee could request that the Administration discuss the direction that it has taken (or will be taking) with respect to these reforms.

Questions:

1. *Commission: Can you provide us additional detail on the backlog and how this has been addressed over the last year after the receipt of the budget augmentation?*

2. <u>LAO and Commission:</u> *What is the overall time period for the full mandate process at this point? Short of a full-blown overhaul of the process, are their additional steps that the Legislature could take to address the mandate process?*

Staff Recommendation: Informational issue.

Issues Proposed for Discussion / Vote

Issue 2: Mandate Funding (Governor's Budget Proposal)

The Governor's mandate proposal is a continuation of the status quo in terms of funded mandates**.** The Governor's budget proposes expenditures of $33.6 million (General Fund) related to 13 non-education mandates. These 13 mandates are identical to those funded and kept in force during the current year, the payments on which constitute the bulk of the General Fund cost for this item. These mandates all relate to public safety or property taxes and are listed in the following table:

Mandate Funding in Governor's Budget
General Fund
(Dollars in Thousands)

Funded Mandate Title	Amount
Allocation of Property Tax Revenue	$520
Crime Victim's Domestic Violence Incident Reports	175
Custody of Minors-Child Abduction and Recovery	11,977
Domestic Violence Arrests and Victim's Assistance	1,438
Domestic Violence Arrest Policies	7,334
Domestic Violence Treatment Services	2,041
Health Benefits for Survivors of Public Safety Officers	1,780
Medical Beneficiary Death Notices	10
Peace Officer Personnel Records	690
Rape Victim Counseling	344
Sexually Violent Predators	7,000
Threats Against Police Officers	3
Unitary Countywide Tax Rates	255
Total Funded	**$33,567**

Staff Comment: At the time the agenda was finalized, no concerns had been raised with this budget request. The mandates selected for funding continue the policy adopted in previous years by the Legislature.

Staff Recommendation: Approve the budget request for continued funding of selected local government mandates.

Vote:

Issue 3: Mandate Suspensions (Governor's Budget Proposal)

The Governor's budget proposes the suspension of numerous mandates in order to achieve budgetary savings. Almost all of these mandates have been suspended for several years, typically as part of the budget process. In general, mandate suspension has not been subject to thorough policy review that would evaluate the costs and benefits of the mandate, but rather have been suspended solely for the purpose of budgetary savings. The policy decision to establish the mandate in the first place has not generally been a major part of the discussion.

Mandates proposed for suspension include mandates suspended in prior years plus two new mandates with statewide cost estimates. The two new mandates with statewide cost estimates are Local Agency Ethics and Tuberculosis Control, which are in **boldface** in the table presented below.

Mandates Suspended in Governor's Budget
General Fund Savings 2014-15
(Dollars in Thousands)

Suspended Mandate Title	Savings
Adult Felony Restitution	$0
Absentee Ballots	49,422
Absentee Ballots-Tabulation by Precinct	68
AIDS/Search Warrant	1,596
Airport Land Use Commission/Plans	1,263
Animal Adoption	36,305
Brendon Maguire Act	0
Conservatorship: Developmentally Disabled Adults	349
Coroners' Costs	222
Crime Statistics Reports for the Dept. of Justice and as Amended	158,627
Crime Victims' Domestic Violence Incident Reports II	2,007
Deaf Teletype Equipment	0
Developmentally Disabled Attorneys' Services	1,201
DNA Database & Amendments to Postmortem Exams: Non-ID Bodies	310
Domestic Violence Background Checks	19,222
Domestic Violence Information	0
Elder Abuse, Law Enforcement Training	0
Extended Commitment, Youth Authority	0
False Reports of Police Misconduct	10
Fifteen-Day Close of Voter Registration	0
Firearm Hearings for Discharged Inpatients	157
Grand Jury Proceedings	0
Handicapped Voter Access Information	0
Identity Theft	83,470
In-Home Supportive Services II	443
Inmate AIDS Testing	0

Judiciary Proceedings for Mentally Retarded Persons	274
Law Enforcement Sexual Harassment Training	0
Local Agency Ethics	***29***
Local Coastal Plans	0
Mandate Reimbursement Process I	6,910
Mandate Reimbursement Process II (consolidation of MRPI and MRPII)	0
Mentally Disordered Offenders' Treatment as a Condition of Parole	4,910
Mentally Disordered Offenders' Extended Commitments Proceedings	7,222
Mentally Disordered Sex Offenders' Recommitments	340
Mentally Retarded Defendants Representation	36
Missing Person Report III	0
Modified Primary Election	1,738
Not Guilty by Reason of Insanity	5,214
Open Meetings Act/Brown Act Reform	111,606
Pacific Beach Safety: Water Quality and Closures	344
Perinatal Services	2,338
Permanent Absentee Voter II	6,560
Personal Safety Alarm Devices	0
Photographic Record of Evidence	-78
Pocket Masks (CPR)	0
Post Conviction: DNA Court Proceedings	410
Postmortem Examinations: Unidentified Bodies, Human Remains	-466
Prisoner Parental Rights	0
Senior Citizens Property Tax Postponement	481
Sex Crime Confidentiality	0
Sex Offenders: Disclosure by Law Enforcement Officers	0
SIDS Autopsies	0
SIDS Contacts by Local Health Officers	0
SIDS Training for Firefighters	0
Stolen Vehicle Notification	1,117
Structural and Wildland Firefighter Safety	0
Tuberculosis Control	***133***
Very High Fire Hazard Severity Zones	0
Victims' Statements-Minors	0
Voter Identification Procedures	7,553
Voter Registration Procedures	2,481
Total Suspended	**$513,824**

LAO Perspective: In prior years, the Legislative Analyst's Office (LAO) has raised questions regarding a number of the mandates proposed for suspension. Depending on the particular mandate, the recommendations have included funding, repealing, or changing the underlying statute to reflect a best practices approach.

- **Elections Mandates.** The LAO has in the past recommended that the mandates relating to elections in the table above (in *italics*) not be suspended but rather funded in the budget, along with the direction that the Administration work with counties to explore alternative funding mechanisms. If these mandates were not suspended, the budgetary impact of funding these mandates would be about $100.0 million on a one-time basis, and a substantially lesser amount of $30.5 million annually thereafter.

Despite the suspension, to-date, it appears that no counties have deviated from providing services required pursuant to the previously mandated activities. Given that the state owes more than $114.0 million to counties for conducting past elections and counties are not required to comply with suspended statutes, there may be a moderate risk that one or more counties may opt not to comply during future elections. According to the LAO, "The longer the state suspends these mandates and the more elections mandates the state chooses to suspend, the greater the risk that at least one county will decide not to perform the previously mandated activities."

- **Newly Suspended Mandates.** Two mandates with newly-determined statewide costs estimates—Local Agency Ethics and Tuberculosis Control—are also proposed for suspension. (In order to 'stop the meter' on these mandates, the Administration proposed to suspend these last year, but this proposal was not adopted.) The LAO suggested the Legislature consider alternatives to the Tuberculosis Control mandate based on alternative funding for the activity. The state and local effort required to structure this alternative has not occurred.

  Regarding the Local Agency Ethics mandate, the Commission determined that state law established a mandate for some activities of certain local governments (largely general law cities, and certain special districts, that are required to pay compensation) related to adopting policies regarding the reimbursement of expenses and providing ethics training for officials who receive compensation. The LAO noted inconsistency of imposing the mandate on some local governments (that are required to pay compensation) and not on others. LAO recommends changes in law that would make compensation optional for all local governments (thus removing the mandate) or exclude from the requirement those local governments that are obligated to pay compensation.

Staff Comment: Other than the issues discussed above, no major concerns have been raised regarding the continued suspension of these mandates. Staff notes that suspending the election mandates would not preclude the Administration from working with counties to explore alternative funding mechanisms, as suggested by LAO. With the exception of the two mandates with recent statewide cost estimates noted above, the selected mandates in the figure have been suspended in prior years. Last year, the Legislature rejected the proposal to suspend the Tuberculosis Control mandate based on public health concerns. It initially adopted statutory revisions that would have 'unmandated' the Local Agency Ethics activities, but subsequently reversed this.

Staff Recommendation: Hold open the proposed suspension of the election mandates. Suspend the Local Agency Ethics mandate and adopt LAO recommendation to revise the applicability of the underlying statute and adopt placeholder TBL. Do not approve the suspension of the Tuberculosis Control mandate, which will be considered in Subcommittee 3, and conform to the action of that Subcommittee for this mandate. Approve the suspension of all the remaining mandates included in the Governor's budget.

Vote:

Issue for Discussion / Vote

Local Economic Development

This item includes topics that address local governments' ability to engage in local economic development efforts, including the Governor's proposal for a revised infrastructure financing district policy and the process of dissolving redevelopment agencies.

Issue 1: Reforming Infrastructure Financing Districts (Governor's Budget Trailer Bill Language)

Proposal: As a means of addressing concerns related to local economic development tools, the Governor proposes expanding the tax increment financing tool utilized by infrastructure financing districts (IFDs) to include a broader array of uses than those currently authorized. The Administration proposes legislation that is designed to ease the formation of IFDs and broaden the application of this financing alternative. Specifically, the proposal would:

- Expand the types of projects that IFDs can fund to include military base reuse, urban infill, transit priority projects, affordable housing, and associated necessary consumer services. The goal is to maintain the IFD focus on projects which have tangible quality-of-life benefits for the residents of the IFD project area.

- Allow cities or counties that meet specified benchmarks to create these new IFDs and issue related debt, subject to receiving 55 percent voter approval, instead of the current two-thirds vote requirement.

- Allow new IFD project areas to overlap with the project areas of former redevelopment agencies (RDAs), while strictly limiting the available funding in those areas to dollars available after payment on all of the former RDA's approved obligations.

- Expand the time in which IFDs can receive property tax increment from 30 years to 45 years, and allow the participating tax entities to issue loans to the IFDs to facilitate their establishment.

- Maintain the current IFD prohibition on the diversion of property tax revenues from K-14 schools, and require entities that seek to establish an IFD to gain the approval of the county, cities, and special districts that contribute their revenue, to the IFD.

The proposal notes that the expansion of the use of IFDs should not come at the expense of the continuing RDA dissolution process. If the establishing city or county formerly operated an RDA, the expanded IFD tool would be available to them only when they meet the following benchmarks:

- Receipt of a Finding of Completion from the DOF, demonstrating that the city or county has remitted all unencumbered cash assets of its former RDA to the affected taxing entities.

- Compliance with all RDA audit findings of the State Controller's Office.

- Resolution of any outstanding legal issues between the successor agency, the city or county that created the RDA, and the state.

Background: Under current law, IFDs are empowered to use tax increment financing to finance tax allocation bonds and use the proceeds for local development. IFDs may also exercise eminent domain powers while they are in existence. IFDs are less flexible than RDAs in the types of projects that they may fund, with financed projects generally limited to highways and transit projects; water, flood control, sewer, and solid waste projects; child care facilities; and libraries and parks. Furthermore, unlike RDAs, affected cities, counties, and special districts have the option to participate in the IFDs while schools cannot, resulting in no Proposition 98 impacts for IFDs. IFDs require a two-thirds vote by the affected electorate to be created.

The end of RDAs has prompted interest in the Legislature in developing a replacement program and a discussion of important elements that such a program might contain. In addition to IFDs, there are other existing programs—business improvement districts (BIDs), joint powers authorities (JPAs), property tax debt overrides, Mello-Roos financings, assessment levies, or other parcel taxes. However, none of these current local financing tools have all of the elements that made redevelopment so attractive and valuable to California cities and counties. Specifically, RDAs provided the sponsoring government with considerable resources and did so without requiring the approval of local voters or business owners; directly imposing increased costs on local residents or business owners; or requiring additional voter approval prior to issuing debt. However, they also caused a substantial diversion of property taxes from local schools and increased pressure on the General Fund.

There have been alternative proposals that allow local discretion in community development efforts and provide accompanying fiscal tools, but eliminate the fiscal exposure to the state. In 2012, two such measures—SB 1156 (Steinberg) and AB 2144 (Pérez, et al)—were adopted by the Legislature but vetoed by the Governor on the basis that the time was not right, given the continuing RDA dissolution process. In 2013, SB 1 (Steinberg) took a related approach with the proposed establishment of investment authorities that would be allowed to receive a non-school property tax increment if agreed to by the local government that would otherwise have received the property tax revenue. This measure was not ultimately adopted by the Legislature.

LAO Perspective: In the LAO's analysis of the Administration's IFD proposal, they recommend adopting most of the components of the proposal; however, they also make several suggestions regarding changes. Specifically, LAO recommends:

- Eliminating the ability of IFDs to fund retail facilities—unless they are oriented towards fulfilling sustainable communities' goals—because the collective benefit to local governments is limited.

- Rejecting the new audit ability for DOF's, recommending that IFDs be treated like other local governments, with required reporting to the SCO.

- Reworking the approval and creation process by (1) allowing all affected residents (not just those in the proposed IFD) to vote for its approval, and (2) clarifying that IFDs are a distinct local entity (like JPAs).

- Rejecting the proposal to require cities and counties to meet certain conditions—such as the resolution of legal disputes—as a requirement of establishing an IFD.

Staff Comments and Questions: Although recent policy changes with respect to redevelopment and enterprise zones have been successful in focusing revenues on essential state services, some suggest that they have also left local governments without the necessary tools to address issues related to economic development. The argument that the state's resources need to be concentrated for statewide services is a reasonable one. Just as reasonable is the position that additional tools need to be made available to local governments to address local concerns. While the focus and the operations of RDAs and EZ tax incentives were very different, they both provided support for local economic development and are now no longer long-term options.

The Administration's proposal is an attempt to address the current lacuna in local governments' economic development tool kit. The new tools made available last year under the tax incentive reformulation will provide some additional resources for local government. Specifically, the New Hiring Tax Credit will provide incentives for employers to locate within certain areas that were former enterprise zones, and the pilot projects associated with this program will serve additional areas in need of development. However, these programs will be more difficult for employers to qualify for and be much more curtailed in terms of the level of state support in foregone revenues. The California Competes Tax Credits may be a useful statewide tool in particular circumstances with particular firms, but they will not necessarily address specific areas of the state most in need of development assistance.

The Governor's proposal is an attempt to address some of the local economic development needs. By expanding the nature of the types of projects that IFDs can finance, the flexibility and usefulness of this tool is improved. However, it is not intuitively apparent why certain other public improvements could not be included as well, and leave more decision-making to local discretion in terms of projects to fund. In contrast, others have suggested that although the proposal allows for investment in housing, it does not require it, thus providing a poor substitute for the affordable housing requirement for RDAs. Lowering the voting threshold to 55 percent approval will make the IFD tool more accessible; however, other legislative proposals—such as SB 214 (Wolk)—would have eliminated the voter requirement for a city or county to create an IFD. Interestingly, the Governor's veto message for SB 214 indicated that expanding the scope of IFDs was premature, but expressed no concern regarding the vote elimination.

The Governor's proposal ties the expanded and reformed IFD to the status of RDA wind-down and the state budget, even though the actual linkage is indirect, at best. For example, the requirement on local governments to resolve legal disputes with the state in order to use the new tool could be interpreted as an enticement to abandoned perfectly reasonable legal actions regarding particular local projects. Given that many RDA dissolution issues are still winding their way through the court system, the revised IFD offered by the Governor is not likely to have widespread application in the near future. In addition, the proposed requirement that local governments comply with SCO audits, while reasonable on its face, may be a significant hurdle for local governments, since only 115 of approximately 400 audits have even been completed. Given this, the Legislature may want to consider adjusting these compliance requirements.

In addition, there may be some rationale for state support for local economic development. This must ultimately hinge on maintaining the state's budget on a strong fiscal track and be measured against other budgetary demands. Still, in some cases, an argument may be made for state support for projects of a regional or statewide benefit—such as transportation improvements, housing, or open space—or joint projects that benefit local schools in some manner. Such state support could be based on grants or loans, or possibly by using a pre-designated fixed amount of property tax increment, or an equivalent amount derived from state resources. Projects eligible for some degree of state support could be selected based on the degree to which they meet a certain level of state or regional impact—with greater support for those with a higher degree of regional or state impact.

Questions:

1. *LAO: Is it reasonable to tie the new IFD tools to the complete resolution of all legal actions against the state, regardless of the validity of such actions by local governments?*

2. *DOF: Since local governments can currently use their property tax increment for allowable public purposes, what is the advantage of the IFD proposal other than it may facilitate securitization?*

3. *LAO / DOF: Are there situations that would warrant state support for particular projects, for example, those with a regional or state-wide impact?*

4. *LAO: Is the scope of activities for local governments under the proposal reasonable? Specifically, given the loss of support for affordable housing with the dissolution of RDAs, should there be a requirement for housing?*

Staff Recommendation: Hold open.

Vote:

Issue for Discussion:

Issue 2: Dissolution of Redevelopment Agencies (Informational Issue)

Background: The process of winding down redevelopment agencies (RDAs) was not expected to be a straightforward process without uncertainty and controversy. Yet, the extreme complexity of dissolving the program has befuddled many, delaying the receipt of property taxes by school districts and resulting in a lack of clarity for local governments. In particular, allowing for the continuation of certain projects that meet pre-established criteria has been more complicated than most observers initially believed. As we noted last year, projects which are partially complete or require changes to existing agreements pose particular problems, and these problems have persisted through the past year. Local governments with various projects have raised questions regarding the application of the criteria, the consistency with which the criteria are applied, and what constitutes a reasonable level of state involvement with respect to local projects. Some local governments have expressed the view that the Administration has attempted to curtail projects in too aggressive a manner, given the intent of the enabling statutes, and sought to establish on-going state review of various projects.

AB 662 (Atkins) was one of the measures adopted by the Legislature to address some of these issues. For example, the bill would have clarified the flexibility of a successor to the RDA to enter into and alter contracts and agreements related to enforceable obligations, as long as additional tax increment is not committed to the project. The bill would also have allowed reasonable estimates and projections to be used to support payment amounts for enforceable obligations. The bill contained several other provisions that would have clarified the process for partially completed projects, provided flexibility to the RDA successors, and potentially paved the way for a less contentious process for the dissolution of RDAs. The bill was vetoed by the Governor, after the DOF indicated that unintended General Fund costs could occur. As confusion and conflict over the dissolution process continues, the Legislature may want to revisit these issues again, either in the budget or through policy committees, in order to assure that RDA dissolution continues on a fair and reasonable track, consistent with legislative intent.

Staff Comments and Questions: The RDA wind-down has been exceeding complex. Still outstanding are numerous legal issues, which have both impaired the timely flow of additional property taxes to local schools as well the ability of local governments to complete anticipated projects.

Questions:

1. *DOF: What are the major legal cases and issues still outstanding? What are the fiscal implications for the state and when will these be resolved?*

2. *DOF: What is the estimate for the amount of former RDA assets that can be additionally shifted to local schools?*

3. *DOF: What is the estimate for the total amount of property tax increment that is still subject to litigation?*

4. *<u>LAO:</u> Is there additional clarity that should be provided through legislation or regulations to govern the RDA dissolution process?*

Staff Recommendation: Informational issue.