



CALIFORNIA BUDGET PROJECT

August 12, 2010

A Preliminary Review of Proposition 22

Proposition 22, which will appear on the November 2, 2010 ballot, would amend the state Constitution to eliminate the state's ability to borrow or shift local revenues and certain state revenues that historically have funded transportation programs to help address a state budget shortfall. The following table provides a preliminary review of Proposition 22. The California Budget Project will release a comprehensive analysis of Proposition 22 in the near future. Proposition 22 was placed on the ballot by initiative and is supported by the League of California Cities and the California Redevelopment Association.

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Key Provisions of Proposition 22 Compared to Current Law

Property Taxes: Redevelopment Agencies

	Current Law	Proposition 22
Allocation	<p>State law allows cities and counties to establish redevelopment agencies to help eliminate “blight” in a designated area.</p> <p>Redevelopment agencies receive most of the growth in property tax revenues attributable to property value increases (the “tax increment”) in the project area.</p> <p>A portion of tax increment revenues must be shared with other local agencies, including counties and school districts, and at least 20 percent must be used to preserve, improve, or expand the supply of affordable housing.</p> <p>The state periodically requires redevelopment agencies to shift additional tax increment revenues to school districts. Such a shift allows the state to reduce General Fund spending to help close a budget shortfall.</p> <p>The July 2009 budget agreement required redevelopment agencies to make two such transfers totaling \$2.1 billion – \$1.7 billion in 2009-10 and \$350 million in 2010-11. Redevelopment agencies sued to block these transfers. On May 4, 2010, a Sacramento County Superior Court judge ruled that the transfers do not violate the state Constitution. Redevelopment agencies filed an appeal on August 30, 2010, and this appeal was still pending at the time of publication.</p>	<p>Prohibits the Legislature from shifting redevelopment agency revenues to school districts or other agencies, except to make payments required as of January 1, 2008 or to increase, improve, or preserve the supply of affordable housing.</p> <p>Declares that “the Legislature has been illegally circumventing Section 16 of Article XVI [of the state Constitution] in recent years by requiring redevelopment agencies to transfer a portion of [their share of property] taxes for purposes other than the financing of redevelopment projects.” This language is intended to retroactively declare the \$2.1 billion fund shift – which is subject to litigation initiated by redevelopment agencies – to be invalid.</p> <p>It is unclear how these provisions would affect the \$2.1 billion fund shift. Proposition 22’s declaration that such shifts are illegal “could affect the outcome of the pending litigation regarding these payments,” according to the Legislative Analyst’s Office (LAO).</p>

Key Provisions of Proposition 22 Compared to Current Law

Property Taxes: Cities, Counties, and Special Districts

	Current Law	Proposition 22
Allocation	<p>Prior to Proposition 13 of 1978, cities, counties, school districts, and other local agencies had the authority to impose property tax rates. Property owners paid a total rate equal to the sum of the rates of each jurisdiction in which the property was located.</p> <p>Proposition 13 amended the state Constitution to cap the countywide property tax rate at 1 percent and gave the Legislature responsibility for allocating the proceeds of the property tax among local agencies in the county in which a property is located.</p> <p>Proposition 1A of 2004 amended the state Constitution to restrict the state's ability to reallocate property tax revenues in a county. For example, the measure requires a two-thirds vote of each house of the Legislature to reallocate property taxes <i>among</i> local governments – cities, the county government, and special districts – within a county.</p> <p>Proposition 1A also strictly limits the state's ability to reallocate property taxes <i>between</i> local governments and educational agencies – school districts, community colleges, and county offices of education – in a county and requires the state to repay, with interest, any amounts shifted. Reallocating property taxes in this manner allows the state to reduce General Fund spending to help close a budget shortfall.</p> <p>Specifically, the state may temporarily reallocate property taxes from local governments to educational agencies if the Governor proclaims a severe state fiscal hardship and the Legislature approves the shift by a two-thirds vote of each house. Property tax revenues shifted from local governments must be repaid – with interest – within three years, and such a shift may occur no more than twice in a 10-year period.</p> <p>In 2009, the Legislature borrowed 8 percent of each local government's property taxes – the maximum allowed by Proposition 1A – for a total statewide shift of \$1.9 billion in 2009-10.</p>	<p>Eliminates the state's ability to temporarily reallocate property taxes from local governments to educational agencies. Consequently, the state could no longer borrow local property tax revenues to help close a budget gap.</p>

Key Provisions of Proposition 22 Compared to Current Law

State Excise Tax on Gasoline and Diesel Fuel		
	Current Law	Proposition 22
Rate	<p>The Legislature imposes a per-gallon excise tax rate on gasoline and diesel fuel.</p> <p>The Legislature increased the excise tax rate on gasoline from \$0.180 per gallon to \$0.353 per gallon effective July 1, 2010 and exempted gasoline from the General Fund portion of the state sales tax (see below). The additional excise tax rate on gasoline – \$0.173 per gallon in 2010-11 – will be adjusted annually starting in 2011-12 so that revenues raised will equal the revenues that would have been raised by the General Fund portion of the state sales tax on gasoline.</p> <p>The excise tax rate on diesel fuel is currently \$0.180 per gallon. The Legislature decreased this rate to \$0.136 per gallon and increased the state’s sales tax rate on diesel fuel by 1.75 percentage points effective July 1, 2011 (see below). The excise tax rate on diesel fuel will be adjusted annually starting in 2012-13 so that the revenue loss will equal the revenue gain attributable to the increased state sales tax on diesel fuel.</p> <p>These changes were enacted in March 2010 as part of a complex “fuel tax swap.”</p>	No Change

Key Provisions of Proposition 22 Compared to Current Law

State Excise Tax on Gasoline and Diesel Fuel

	Current Law	Proposition 22
Allocation	<p>All revenues are deposited into the Highway Users Tax Account (HUTA).</p> <p>Revenues from the first \$0.18 per gallon of the excise tax on gasoline and <i>all</i> revenues from the excise tax on diesel fuel are allocated as follows: Two-thirds for state highway maintenance and repairs and one-third to cities and counties for local streets and roads.</p> <p>The portion of the excise tax on gasoline added by the fuel tax swap – \$0.173 per gallon in 2010-11 – is also deposited into the HUTA, but is distributed using a different formula. This portion of the excise tax on gasoline provides ongoing funding for:</p> <ul style="list-style-type: none"> • All annual debt-service payments related to Proposition 192 of 1996 bonds and three-quarters of annual debt-service payments related to Proposition 1B of 2006 bonds; • The State Highway Operation and Protection Program (SHOPP) and the State Transportation Improvement Program (STIP); and • Cities and counties for local streets and roads. <p>The Legislature may amend HUTA allocations by a majority vote of each house.</p> <p>The Legislature may authorize the state, cities, and counties to use up to 25 percent of their share of HUTA funds to pay debt service on voter-approved transportation bonds.</p> <p>The state Constitution allows the state to borrow HUTA funds for cash-flow purposes. In addition, the state may borrow these funds for a longer period if the Governor declares a fiscal emergency or if General Fund revenues are projected to decline after adjusting for inflation and population growth. The state must repay borrowed funds within three years, but does not have to pay interest.</p>	<p>Prohibits revenues deposited into the HUTA from being permanently or temporarily loaned to the state's General Fund or any other state fund, including for cash-flow purposes.</p> <p>Prohibits the Legislature from modifying HUTA allocation formulas in effect as of June 30, 2009 unless the California Transportation Commission (CTC) holds public hearings and the Legislature approves the change by a two-thirds vote of each house in a stand-alone bill.</p> <p>Imposes new restrictions on the state's use of HUTA funds. The state could use its share of HUTA funds to pay debt service on voter-approved transportation bonds only if the bonds were issued by the state "on and after" November 2, 2010 and if voters approved using HUTA funds for such a purpose.</p> <p>Allows a city or county to use up to 25 percent of its share of HUTA funds to pay debt service on voter-approved transportation bonds issued by that jurisdiction without seeking subsequent voter approval and regardless of when the bonds were issued.</p> <p>Declares that if the Legislature reduces or repeals excise taxes on motor vehicle fuels and "adopts an alternative source of revenue to replace the moneys derived from those taxes," the replacement revenue must be deposited into the HUTA and allocated to cities, counties, and the state according to the statutory formula in effect as of June 30, 2009.</p>

Key Provisions of Proposition 22 Compared to Current Law

State Sales Tax on Diesel Fuel		
	Current Law	Proposition 22
Rate	The Legislature imposes and sets a tax on the sale and use of goods, including diesel fuel. The Legislature established an additional sales tax rate of 1.75 percent on diesel fuel effective July 1, 2011 as part of the fuel tax swap.	No change
Allocation	<p>State law requires most of the revenues raised by the state sales tax on diesel fuel – including the 1.75 percentage point increase effective July 1, 2011 – to be deposited quarterly into the Public Transportation Account (PTA).</p> <p>State law requires PTA funds to be used for “transportation planning and mass transportation purposes, as specified by the Legislature.”</p> <p>Historically, local transit agencies received 50 percent of PTA funds and the state received the remaining 50 percent for intercity rail and other state and regional public transportation projects. However, the Legislature changed the statutory allocation formula as part of the fuel tax swap. Beginning in 2011-12, local transit agencies will receive 75 percent of PTA funds and the state will receive 25 percent.</p> <p>The Legislature may amend PTA allocations by a majority vote of each house, subject to certain court-imposed limitations.</p> <p>The Legislature may use PTA funds to pay debt service on voter-approved rail- and transit-related bonds, subject to certain court-imposed limitations.</p> <p>The state Constitution allows the state to borrow PTA funds for cash-flow purposes. In addition, the state may borrow these funds for a longer period if the Governor declares a fiscal emergency or if state revenues are projected to decline. The state must repay these funds within three years, but does not have to pay interest.</p>	<p>Amends the state Constitution to reflect the current statutory requirement that most diesel fuel sales tax revenues be deposited quarterly into the PTA. However, the measure does not specifically address revenues raised by the additional 1.75 percent sales tax rate on diesel fuel scheduled to take effect on July 1, 2011.</p> <p>Prohibits PTA revenues from being permanently or temporarily loaned to the state’s General Fund or any other state fund, including for cash-flow purposes.</p> <p>Specifies in the state Constitution that PTA funds must be used for “transportation planning and mass transportation purposes,” and defines those terms.</p> <p>Maintains the historical allocation of PTA funds by amending the state Constitution to require 50 percent of PTA funds to go to local transit agencies and 50 percent to the state. This change would reverse the new allocation established as part of the fuel tax swap. Moreover, the allocation required by Proposition 22 could not be changed without voter approval.</p> <p>Prohibits the state from using PTA funds to pay debt service on voter-approved bonds.</p>

Key Provisions of Proposition 22 Compared to Current Law

State Sales Tax on Gasoline		
	Current Law	Proposition 22
Rate	The Legislature exempted gasoline from the General Fund portion of the state sales tax effective July 1, 2010 as part of the fuel tax swap.	No change
Allocation – Proposition 42 of 2002	<p>Historically, most revenues raised by the state sales tax on gasoline were deposited into the state General Fund. These revenues funded a range of programs, including education, with only a small share used for transportation purposes. Proposition 42 of 2002 amended the state Constitution to dedicate the portion of gasoline sales tax revenues deposited into the General Fund to transportation purposes. These revenues ceased to exist when the Legislature exempted gasoline from the General Fund portion of the state sales tax.</p> <p>Proposition 42 required gasoline sales tax revenues to be transferred from the General Fund to the Transportation Investment Fund (TIF) and allocated as follows: 40 percent to the STIP, 40 percent to cities and counties for local streets and roads, and 20 percent to the PTA for public transportation. The Legislature could amend these allocations by a two-thirds vote of each house in a stand-alone bill.</p> <p>The state could suspend the transfer to the TIF only if the Governor declared a severe state fiscal hardship and the Legislature approved the suspension by a two-thirds vote of each house in a stand-alone bill.</p> <p>Proposition 1A of 2006 further restricted the state’s ability to suspend the transfer. The measure required the state to repay the full amount suspended – with interest – within three years and prohibited the state from suspending the transfer more than twice in a 10-year period.</p> <p>Proposition 42 revenues were counted as General Fund revenues for the purpose of calculating the Proposition 98 guarantee for K-14 education. These revenues increased the state’s Proposition 98 obligation despite the fact that they were required to be used to fund transportation programs and could not be used to support schools.</p>	<p>Requires Proposition 42 revenues to be deposited directly into the TIF, rather than first being deposited into the state General Fund. This provision would become operative if the General Fund portion of the state sales tax on gasoline were reinstated or if a court determined that the Legislature had adopted an alternative source of revenues to replace the revenues formerly raised by the General Fund portion of the state sales tax on gasoline (see below). It is unclear whether depositing Proposition 42 revenues directly into the TIF would affect calculations of the Proposition 98 funding guarantee for K-14 education.</p> <p>Prohibits the state from permanently or temporarily borrowing or redirecting – including for cash-flow purposes – any revenues that would otherwise be deposited into the TIF.</p> <p>Prohibits the Legislature from modifying the TIF allocation formula unless the CTC holds public hearings and the Legislature approves the change by a two-thirds vote of each house in a stand-alone bill.</p> <p>Declares that if the Legislature reduces or repeals the state sales tax on gasoline and “adopts an alternative source of revenue to replace the moneys derived from those taxes,” the replacement revenue must be deposited into the TIF and allocated as required by the state Constitution.</p>

Key Provisions of Proposition 22 Compared to Current Law

State Sales Tax on Gasoline		
	Current Law	Proposition 22
Allocation – Proposition 111 of 1990	<p>The state sales tax on gasoline was applied to the entire purchase price, including the base price and the per-gallon state excise tax. Proposition 111 of 1990 doubled the state excise tax from \$0.09 per gallon to \$0.18 per gallon, thereby increasing the sales tax revenues raised from each gallon of gasoline sold. State law – but not the state Constitution – requires these additional sales tax revenues to be deposited quarterly into the PTA.</p> <p>These revenues ceased to exist when the Legislature exempted gasoline from the General Fund portion of the state sales tax.</p>	<p>Amends the state Constitution to reflect the current statutory requirement that Proposition 111 revenues be deposited quarterly into the PTA. This provision would become operative if the General Fund portion of the state sales tax on gasoline were reinstated.</p>
Allocation – “Spillover”	<p>State law – but not the state Constitution – requires a certain portion of revenues from the state sales tax on gasoline, when available, to be deposited quarterly into the PTA. This portion – known as “spillover” – reflects “net revenue from [a] 4.75 percent sales tax on gasoline in excess of [a] 0.25 percent sales tax on all other goods,” according to the LAO.</p> <p>These revenues ceased to exist when the Legislature exempted gasoline from the General Fund portion of the state sales tax.</p>	<p>Amends the state Constitution to reflect the current statutory requirement that spillover revenues be deposited quarterly into the PTA. This provision would become operative if the General Fund portion of the state sales tax on gasoline were reinstated.</p>

Key Provisions of Proposition 22 Compared to Current Law

Vehicle License Fee		
	Current Law	Proposition 22
Rate	The Legislature sets the Vehicle License Fee (VLF) rate, which is applied to the depreciated value of cars and trucks. The VLF rate includes a 0.65 percent base rate and a temporary rate of 0.5 percent that expires on June 30, 2011.	No change.
Allocation	<p>The state Constitution requires VLF revenues raised by the 0.65 percent rate to be distributed to cities and counties. The Legislature may reallocate these revenues to reimburse a local government – counties, for example – for the cost of providing a new program or a higher level of service mandated by the state.</p> <p>Approximately one-third of the temporary 0.5 percent VLF rate is allocated to local public safety programs, with the remainder deposited into the state’s General Fund.</p>	Eliminates the state’s ability to reallocate revenues raised by the 0.65 percent rate to reimburse local governments for a new program or a higher level of service mandated by the state.
Other Local Revenues		
	Current Law	Proposition 22
Local Taxes	Local governments – including counties, “general law” cities, and special districts – may only impose a tax if the Legislature authorizes them to do so. Only “charter” cities may impose taxes without legislative authorization under the state Constitution’s “municipal affairs” doctrine. Local governments impose a range of taxes, including the local portion of the sales tax, business license taxes, and utility user taxes.	Prohibits the Legislature from reallocating, transferring, borrowing, appropriating, restricting the use of, or otherwise using “the proceeds of any tax imposed or levied by a local government solely for the local government’s purposes.”