California Budget & Policy Center

Constitutional Constraints on Moving Toward Universal Coverage in California

SCOTT GRAVES, DIRECTOR OF RESEARCH

CALIFORNIA STATE ASSEMBLY

SELECT COMMITTEE ON HEALTH CARE DELIVERY SYSTEMS AND UNIVERSAL COVERAGE

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California's Constitution Could Constrain Efforts to Achieve Universal Coverage

- Achieving universal health coverage in California could require tax increases to support additional, ongoing state spending. For example, a tax increase of over $100 billion would be needed to help finance a single-payer system.

- Key provisions of the state Constitution constrain the Legislature's ability to substantially raise taxes and dedicate the proceeds exclusively to universal health coverage. These provisions were added by:
  - **Proposition 98 of 1988**, as amended by Prop. 111 of 1990 (Article XVI, Section 8).
  - **Prop. 4 of 1979** (the "Gann limit"), as amended by both Prop. 98 and Prop. 111 (Article XIII B).

Proposition 98 (1988):

A Minimum Funding Guarantee for K-14 Education

Key issue related to universal health coverage:

Would K-14 education be required to receive a portion of new tax revenues raised to achieve universal coverage, even if the Legislature deposited these revenues into a *special fund*?

The Relationship Between Prop. 98 and "General Fund" Revenues: Varying Interpretations

In the context of Prop. 98, the state Constitution refers to **General Fund** revenues. It does not mention **special fund** revenues.

There are varying interpretations of what this means:

One view: Special fund revenues are distinct from General Fund revenues and therefore **would not be counted** in the Prop. 98 calculations.

Another view: The term "General Fund" encompasses a broader range of revenues. Special fund revenues **would be counted** in the Prop. 98 calculations.

Prop. 98 Refers to *General Fund* Revenues, Not *Special Fund* Revenues

- Prop. 98 (1988), as modified by Prop. 111 (1990), amended the state Constitution to guarantee a minimum funding level for K-12 schools and community colleges.

- In describing the calculations that determine each year's minimum funding guarantee, the state Constitution:

  - Refers to *General Fund* revenues and proceeds of taxes.
  - Does not mention *special fund* revenues as a factor in calculating the Prop. 98 guarantee.

- There are varying interpretations as to whether *special fund* revenues would factor into the Prop. 98 calculations.

One View: Special Fund Revenues *Would Not* Be Counted in Prop. 98 Calculations

- According to one school of thought, since *special fund* revenues are distinct from *General Fund* revenues – and are not mentioned in the context of Prop. 98 – they would not count in the Prop. 98 calculations.

- Based on this view, the Legislature could:
  - Increase taxes to achieve universal coverage, such as through a single-payer system; *and*
  - Deposit the new revenues into a special fund; *and then*
  - Permanently exclude these new revenues from the Prop. 98 calculations – in which case K-14 education would *not* benefit financially from the new revenues.

Another View: Special Fund Revenues *Would* Be Counted in Prop. 98 Calculations

- According to a second school of thought, the term "General Fund" – as used in the context of Prop. 98 – encompasses *a broader range of revenues* than those that are deposited into the state's General Fund.

- Based on this view, tax revenues that the Legislature deposits into a *special fund* to achieve universal coverage would be subject to the Prop. 98 calculations – even though they technically are not *General Fund* revenues. In other words, K-14 education would receive a significant portion of these new revenues.

Legislatively Excluding New Tax Revenues From Prop. 98 Could Prompt a Lawsuit

- Given these varying interpretations, the state could be vulnerable to legal challenges if the Legislature approved a major tax increase to fund universal health coverage and excluded the new revenues from the Prop. 98 calculations.

- Lawmakers could attempt to dissuade potential litigants by adding a "poison pill" to the bill that would trigger a severe consequence – such as automatically repealing the new taxes – if the state lost a Prop. 98-related lawsuit.

- Alternatively, the Legislature could ask the voters to both 1) approve new taxes to achieve universal coverage and 2) exclude the revenues from the requirements of Prop. 98.

Proposition 4 (1979):

A Limitation on Certain State and Local Spending

Key issue related to universal health coverage:

If the Legislature increased taxes to achieve universal coverage, would these new revenues cause the state to exceed its appropriations limit (or "Gann limit")?

How Does the State's Gann Limit Work?

1. Annually Calculate Limit

The state's Gann limit is based on spending in the 1978-79 fiscal year. The limit is annually adjusted for various factors, including changes in population and in the cost of living.

2. Determine Amount of Appropriations Subject to Limit

The limit applies only to *certain* appropriations from *tax proceeds*.

3. Determine If State Has "Excess" Revenues

If appropriations subject to the Gann limit reach that limit two years in a row, any remaining revenues over that period are considered to be "excess" revenues.

4. Allocate "Excess" Revenues

Any "excess" revenues must be divided equally between Prop. 98 spending and taxpayer rebates.*

* Excess revenues could be appropriated in whole or in part for purposes that are *exempt* from the Gann limit, in which case fewer (or no) dollars would be available for Prop. 98 and tax rebates.

Prop. 4 Created Spending Limits That Apply to State and Local Governments

- Prop. 4 (1979), as modified by both Prop. 98 (1988) and Prop. 111 (1990), amended the state Constitution to set limits on certain state and local spending (or "appropriations").
- These Gann limits are based on 1978-79 spending and are adjusted each year for changes in population and in the cost of living as well as for any transfers of responsibility.
- At the state level, if appropriations reach the limit over any two-year period, then any "excess" revenues must be divided equally between additional Prop. 98 spending and taxpayer rebates. (However, "excess" revenues may be reduced by appropriating them for purposes that are *exempt* from the Gann limit.)

The Gann Limit Applies to Appropriations From Tax Proceeds

- The Gann limit does not apply to *all* appropriations.
- Instead, it applies to appropriations from the "proceeds of taxes."
- At the state level, tax proceeds consist of:
  - Revenues from all general state taxes (for example, the personal income tax and the sales tax).
  - Proceeds from the investment of tax revenue.
  - Fee revenues that exceed the reasonable cost of providing a service or product.
  - Revenues carried forward from prior years.

Some Appropriations From Tax Proceeds Are Exempt From the Gann Limit

- Some state appropriations from the proceeds of taxes are exempt from the Gann limit.

- Exempt appropriations include the following categories:

  - State financial assistance to local governments.
  - Spending to comply with federal or court mandates.
  - Debt service.
  - Spending from certain gas tax revenues.
  - Certain capital outlay expenditures.
  - Spending from reserve funds.
  - Spending related to certain emergencies, such as a natural disaster.
  - Tax refunds.

Tax Increases to Achieve Universal Coverage Could Exceed the Gann Limit

- State tax revenues raised to pay for expanded health coverage would 1) be considered "proceeds of taxes" and 2) go toward services (health care) that would *not* be exempt from the state's Gann limit.

- An extremely large tax increase would cause the state to exceed the Gann limit over multiple years, triggering the "excess" revenue provision. (The state currently has about $12 billion of "room" under its limit.)

  - In order to avoid exceeding the Gann limit, the Legislature could ask the voters to revise the Gann limit provisions in the state Constitution.

Concluding Thoughts

Trying to Address Constitutional Constraints Without Voter Approval Would Be Risky

- Prop. 98 and the Gann limit constrain the Legislature's ability to substantially increase many types of appropriations, including those aimed at achieving universal coverage.

- Some advocates assert that these constraints could be addressed solely through the legislative process, without consulting the voters.

  - This is highly unlikely with respect to the Gann limit.
  - "Going around" Prop. 98 could trigger a lawsuit, putting at risk the taxes needed to fund universal coverage.

- Asking the voters to remove these constitutional constraints would provide a better path forward.

California Budget
& Policy Center

1107 9th Street, Suite 310

Sacramento, California 95814

916.444.0500

sgraves@calbudgetcenter.org

@CalBudgetCenter

@SHGraves29

calbudgetcenter.org