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PROPOSITION 51: SHOULD CALIFORNIA EARMARK THE SALES TAX ON MOTOR VEHICLES?

The Planning and Conservation League (PCL) has qualified Proposition 51 for the November ballot, which would make changes to the way that the state funds transportation-related projects. Specifically, the measure would:

- transfer 30 percent of the state's share of sales tax revenues generated by automobile sales to a variety of transportation and environmental programs;
- allocate these funds to 17 specific spending categories;
- provide priority funding for specific projects; and
- make statutory changes to existing programs.

Proponents argue that the cost of meeting the state's transportation infrastructure needs is greater than the current level of resources dedicated to this purpose. They argue that Proposition 51 would provide additional resources to fund transportation systems that are less suseptible to gridlock. This paper examines the broader policy implications of this measure, without commenting on the merits or need for the programs that would receive funding if the measure passes.

WHAT WOULD PROPOSITION 51 DO?

Proposition 51 transfers 30 percent of the state's share of sales taxes paid on the sale and lease of new and used motor vehicles from the state's General Fund to a new Traffic Congestion Relief and Safe School Bus Trust Fund (Trust Fund), which would be established by the initiative. The Trust Fund would fund a variety of transportation and environmental programs. The Legislative Analyst's Office (LAO) estimates that approximately $460 million would be shifted from the state's General Fund to the Trust Fund in 2002-03, $950 million in 2003-04, and the transfer would increase annually thereafter.[1]

Proposition 51 creates 17 accounts dedicated to specific categories of spending within the Trust Fund and allocates a set percentage share of available funding to each account (Table 1). These shares would be fixed unless changed by a subsequent ballot measure. In addition to defining the precise percentage shares each spending category will receive, the measure includes a list of specific projects, totaling $215 million in 2003-04 (23 percent of the estimated $950 million allocated by the measure), which will have the first draw on resources in the Trust Fund.

While the PCL titled the initiative the Traffic Congestion Relief and Safe School Bus Act, only 8 percent ($76 million out of an anticipated $950 million) of the transferred revenues would be allocated to school buses. These funds can only be used to purchase or lease new, less polluting buses. No funds are allocated for operating or maintaining the school bus fleet. The remaining 92 percent of the funds would be used for other purposes.

Proposition 51 modifies existing programs, including increasing annual funding for the Environmental Enhancement and Mitigation Program Fund (EEMPF) from $10 million to $20 million. These moneys

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may be used for environmental enhancement or to mitigate the environmental impact of transportation projects. The measure makes permanent the Bicycle Transportation Account in the State Transportation Fund and the Safe Routes to School Program, and requires CalTrans to use recycled waste water when available and 50 percent organic compost, as well.

Table 1: Proposition 51 Creates Permanent Spending Categories For Trust Fund Resources

Account	Percentage Of Funds	Funding Level (In Millions)
Congestion Bottleneck Projects	16%	$152.0
Transit Capital (Facilities, Rolling Stock, Rights Of Way)	17%	$161.5
Transit-Oriented Development Incentives	3%	$28.5
Transit Service Expansion And Enhancements	16%	$152.0
Senior And Disabled Transportation	2%	$19.0
Rail/Street Grade Separations	4%	$38.0
Bicycle And Pedestrian Safety Law Enforcement	1%	$9.5
Pedestrian Utilization And Safety Projects	1%	$9.5
Bicycle Projects	2%	$19.0
Safe/Clean School Bus	8%	$76.0
Rural Public Transit	2%	$19.0
Traffic Safety Improvements	5%	$47.5
Passenger Rail Security	4%	$38.0
Improving Intercity Travel		
Intercity Rail Capital/Operations	4%	$38.0
Environmental Responsibility And Improvement		
Water Quality Transportation Enhancements	2%	$19.0
Air Quality Transportation Grants	3%	$28.5
Environmental Enhancements/Mitigation	10%	$95.0
Total:	**100%**	**$950.0**

Source: Planning and Conservation League and Legislative Analyst's Office. Calculations based on LAO estimate of funds controlled by the initiative for 2003-04.

In addition, Proposition 51 creates the Transportation Impacts Mitigation Trust Fund (TIMTF), which would permanently receive 10 percent of Trust Fund revenues. This fund would be allocated to projects similar to those funded by the EEMPF. After funding specific projects identified in the initiative, 20 percent of the remaining funds in the TIMTF would go to the nine Bay Area counties – Alameda, Contra Costa, Marin, Napa, San Francisco, San Mateo, Santa Clara, Solano, and Sonoma - that are members of the Metropolitan Transportation Commission (MTC). However, no other regional transportation entity is given a set share of TIMTF funds, and the measure does not provide a justification, in terms of state priorities for environmental mitigation efforts, for designating this share of funds to the MTC. The state's Resources Agency would administer these funds.

Is General Fund Revenue Growth A Reasonable Way To Judge Whether The State Can Afford The Transfer?

Proposition 51 contains provisions intended to limit the impact of the transfer on other General Fund priorities in years when the state experiences slow growth or declines in revenues. In years with:

- ***No or slow revenue growth:*** The transfer would be reduced if the Governor forecasts that current year General Fund revenues will fail to increase by an amount at least equal to the amount of the transfer.[2] Any reduction in the size of the transfer would be allocated proportionately among the various purposes funded by the measure.
- ***Revenue decline:*** The measure also allows for any balance in the fund to be transferred back to the General Fund if the May Revise forecast anticipates that revenues are expected to be lower than in the prior year.

While the measure reduces or suspends the transfer in years with slow growth or declines in revenues, suspension would not occur in many instances where the state faces a severe budget shortfall. This is because Proposition 51 does not take into account revenue growth needed to pay for increases in the cost of state services related to:

- ***Inflation***. By not taking into account the impact of inflation, this measure would result in an inflation-adjusted reduction in the funds available for state services in years where revenues barely exceeded the prior year's level;
- ***Population, enrollment, and caseload increases*** in programs such as higher education, Medi-Cal, or corrections;
- ***Reductions in federal aid*** that require an increase in state spending. For example, the state's share of Medi-Cal costs will increase in 2002-03 due to a change in the state-federal sharing ratio; this will increase the state's costs for Medi-Cal by approximately $174 million;[3] or
- ***Shifts in demand for state services related to economic or demographic shifts*** such as rising costs for public assistance during an economic downturn, or increased demand on higher education due to population growth trends.

While Proposition 51 includes a provision that "holds harmless" the level of the Proposition 98 guarantee, it would limit the resources available to fund the guarantee, thereby reducing revenues available for other programs and services, including health care, local government, public safety, and higher education. In recent years, the Legislature has "overfunded" the Proposition 98 guarantee, i.e., allocated more than the minimum amount required by the constitution. This was done largely because of recognition that the constitutional minimum guarantee was not providing districts with adequate resources to improve student achievement. By dedicating future General Fund revenues to the Trust Fund, Proposition 51 would limit the Legislature's ability to over fund the Proposition 98 guarantee, and what was established as a floor for school funding could become a ceiling.

Although Proposition 51 allows balances in the Trust Fund to be transferred to the General Fund in years when General Fund revenues decrease from the prior year, it provides for no flexibility to address a budget shortfall in years when revenues increase. Under current law, moneys in many special funds may be loaned to the General Fund in a budget crisis.[5] These loans can help to minimize funding cuts in critical state programs. In the current crisis, the Governor proposes to borrow $1.0 billion from the Traffic Congestion Relief Fund to help address the $23.6 billion budget gap. However, Proposition 51 does not permit loans of Trust Fund balances to the General Fund under any circumstances, thereby limiting the options available to the Legislature and the Governor to address future shortfalls.[6]

The state's current fiscal crisis illustrates the problems with Proposition 51's provisions designed to protect the state's General Fund. The Governor's May Revision projects that the state will face a $23.6 billion budget shortfall for the 2001-02 and 2002-03 fiscal years. However, the May Revision also includes projections that General Fund revenues will increase by $10.5 billion between 2001-02 and 2002-03.[4] If Proposition 51 were currently in effect, the provision designed to "safeguard" the General Fund would not apply in 2002-03, thereby increasing the magnitude of the state's fiscal problem by $460 million.

What Other Funds Are Available For Transportation?

The state Constitution already dedicates a number of specific revenue sources to transportation and the Legislature can appropriate General Fund moneys to any of the purposes specified in this measure. The state Constitution dedicates the proceeds of excise taxes on fuel (gas, diesel) to transportation. These taxes are anticipated to raise $3.2 billion for transportation in 2002-03. In addition, vehicle registration fees are earmarked for transportation-related public safety and regulatory activities. Vehicle registration fees will raise an estimated $2.1 billion in 2002-03.[7]

Proposition 111 of 1990 increased the revenues available for public transit by amending the state constitution to dedicate the sales taxes paid on the increase in the gas tax imposed by that measure to the Public Transportation Account. The Department of Finance estimates that $196 million in total revenues from the sales tax on fuel will be dedicated to the Public Transportation Account in 2002-03.[8] In addition, 18 counties, accounting for 82 percent of the state's population, have local-option sales tax rates that fund transportation programs.[9]

State law earmarks the proceeds of a ¼-cent sales tax rate for local transportation programs. This rate will provide an estimated $1.2 billion for local transportation programs in 2002-03.

Finally, Proposition 42, approved by voters in March 2002, permanently dedicates the sales tax paid on gasoline to transportation-related programs. Proposition 42 allocates approximately $1.3 billion annually to transportation beginning in 2003-04. Specifically, Proposition 42 allocates 20 percent of the funds toward public and mass transportation; 40 percent to transportation capital improvement projects; 20 percent to street and highway maintenance and repair conducted by cities; and 20 percent to street and highway maintenance and repair conducted by counties.

Table 2: Transportation Projects Currently Receive Funding From Various Sources

Transportation Funding Source	2002-03 (In Billions)
Excise Tax On Diesel And Gasoline Fuel	$3.2
Vehicle Registration Fees	$2.1
Sales Tax On Fuel Dedicated To Public Transit	$0.2
¼-Cent Local Sales Tax Rate	$1.2
Total:	**$6.7**
Sales Tax On Fuel Dedicated To Transportation Beginning In 2003-04	$1.3

Source: Department of Finance and Legislative Analyst's Office.

How Much Of The Budget Is Already Locked In?

Earmarking state resources for specific purposes reduces the state's ability to respond to changes in the state's fiscal circumstances and to adapt state spending to changing needs and priorities. In order to evaluate the impact of earmarking additional state General Fund resources, it is useful to examine how much flexibility the Legislature currently has over state spending. State revenues include those dedicated to special funds, which must be spent for specific purposes, and General Fund revenues that can be spent for any purpose.

One way to determine the level of legislative flexibility is to look how the state spends General Fund revenues. There is no precise definition of which state expenditures are mandatory and which expenditures are discretionary. At minimum, mandatory expenditures would include those required by or specified in the state Constitution (including revenues dedicated to specific purposes in the Constitution), expenditures mandated by voter-approved initiatives, and expenditures necessary to fulfill federal matching requirements. Even this definition is difficult to apply. For example, voters approved the "Three Strikes" initiative (Proposition 184 of 1994) imposing stiff prison terms on repeat offenders. While longer sentences increase state costs for corrections, there is no way to determine how much of the corrections budget goes for costs related to the "Three Strikes" initiative and how much goes for costs related to prisoners who committed crimes with sentences that could be modified by the Legislature.

Using a very minimal definition of mandatory spending, approximately two-thirds of state spending is mandatory and one-third (35 percent) is discretionary, i.e., expenditures over which the Legislature has control through the annual budget act.[10] However, this estimate treats all expenditures for programs as fundamental to the operation of the state, such as the court system, transportation (including the Department of Motor Vehicles), higher education (other than Community College expenditures covered by the Proposition 98 guarantee), and corrections, among others, as "discretionary." In reality, the

Legislature is much more constrained in its ability to reallocate General Fund spending.

A modestly expanded definition of "mandatory" spending that includes Legislative, Judicial, and Executive branch functions, tax collection, state air and water boards, forest fire protection, the Department of Motor Vehicles, corrections, and benefits paid to retired state employees, leaves 23 percent of state General Fund expenditures as discretionary. Even this expanded definition treats all state expenditures for the University of California and the California State University systems, housing, vehicle license fee reimbursements to local government, resources, and most state expenditures for environmental protection, among others, as discretionary.

What Does It Mean To Allocate Revenues At The Ballot Box?

Setting state budget priorities through the initiative process encourages the voters to consider spending for one area, such as transportation, in isolation from other state spending. While many voters may support spending for transportation and environmental mitigation projects, they might prefer to spend less than required by Proposition 51 if they knew that it could result in cuts to health, higher education, or non-transportation-related environmental protection programs or increases in taxes.

Proposition 51 sets priorities for state transportation-related spending by defining the percentage share of the Trust Fund's resources to be allocated to specific spending categories, such as transit capital and environmental mitigation. As it would take a subsequent ballot measure to reverse the transfer of funds or reallocate funds to different spending categories, the priorities outlined in Proposition 51 would be locked in, even if public priorities change in future years.

Priorities Or Pork: Can Ballot Box Budgeting Go Too Far?

Under current law, there is a public process involving local, regional, and state stakeholders to determine the state's transportation spending priorities. The product of this process is the State Transportation Improvement Program (STIP), which provides funding for projects for a period of five years following the approval date. The rationale behind this process is to maximize the efficient and effective use of limited state transportation resources to meet the state's needs for transportation infrastructure. The process for determining the STIP provides a forum for public input and regional and local priority setting, as well as the opportunity to amend the plan in future years if priorities change.

Proposition 51 gives specific projects first call on the Trust Fund's resources. Even though voters will be given the chance to approve or reject the projects through their vote on the initiative, they will be limited to a yea or nay on the entire list without an opportunity to discuss what should be on the list in the first place.

Although some of the spending categories under the Trust Fund include procedures to evaluate and prioritize projects that may be funded through the account, there is no evidence that the specific projects singled out for funding went through these procedures. In fact, it is unclear in some cases whether the projects should be funded either by the account under which they are listed or with state transportation-related funds at all. For example, Proposition 51 would provide $10 million over 10 years for the acquisition, construction, and equipping of the Oakland School for the Arts, a charter school. This project is funded through the Transit Capital Account, which was established to fund transit facilities and right-of-way purchases. Other projects funded by Proposition 51 that raise similar questions include:

- $40 million over four years for the City and County of San Francisco Golden Gate Park Concourse Authority to improve the Music Concourse area of Golden Gate Park.

- $50 million over five years for the City of Irvine to build a remote check-in facility for its airport.
- $7 million in 2003-04 for construction costs and $1 million per year in perpetuity for a nonprofit organization to build, maintain, and operate the state Railroad Technology Museum in Sacramento.

Questions To Consider

Proponents argue that the state's transportation infrastructure needs require a higher level of funding than under current law. However, if enacted by the voters in November, Proposition 51 would reduce the ability of the State to respond to changing fiscal conditions and needs, and establish spending priorities that could only be adjusted by a future ballot measure. Given the sheer volume of information that they will have to digest prior to the election, it is unlikely that most voters will be able to engage in the level of discussion regarding Proposition 51's impact on the state budget necessary to ensure the most effective and efficient use of limited state resources.

Proposition 51 raises several policy questions:

- Are current resources sufficient or inadequate for the purposes supported by this act?
- Should additional General Fund resources be earmarked for specific purposes, effectively isolating one area of spending from the rest of the state's budget?
- Should we establish future spending priorities based on current conditions?
- Should voters be asked to prioritize funding for specific projects without information on alternative projects or a realistic opportunity to deliberate these choices with other stakeholders?

Endnotes

[1] Secretary of State, *Initiative Update*, downloaded from http://www.ss.ca.gov/elections/elections_j.htm on May 9, 2002.
[2] The measure uses the May Revision forecast to determine whether the transfer would be reduced.
[3] Legislative Analyst's Office, *Analysis of the 2002-03 Budget Bill* (February 2002), p. C-15.
[4] Department of Finance, *California Governor's Budget May Revision, 2002-03* (May 14, 2002).
[5] Some transfers require the General Fund to make interest payments on the amounts transferred.
[6] Planning and Conservation League, *Traffic Congestion Relief and Safe School Bus Act Summary,* Section 2(e) downloaded from http://www.pcl.org/transportation/summary.html on April 30, 2002.
[7] Department of Finance, *Governor's Budget Summary 2002-03*, Schedule 8 (January 2002).
[8] Department of Finance May Revision estimate as cited by the Legislative Analyst's Office in email sent on May 21, 2002.
[9] State Board of Equalization, *2000-01 Annual Report* (May 2002), p. A-30, and Department of Finance, *Population Estimates with Annual Percent Change*, downloaded from http://www.dof.ca.gov/HTML/DEMOGRAP/E-1text.htm on May 28, 2002.
[10] Expenditures classified as mandatory include state contributions to employees' retirement plans; state funds used to match federal Medicaid (i.e., Medi-Cal); Foster Care; Child Welfare Services; Child Support; Temporary Assistance for Needy Families maintenance of effort dollars; Proposition 98 spending; Proposition 42 spending; debt service; and reimbursements to local governments for property taxes lost as a result of the homeowners' exemption and state mandates. Based on estimated General Fund expenditures from the *2002-03 Governor's Budget Summary* (January 2002).

Delaine McCullough and Jean Ross prepared this Brief. The California Budget Project (CBP) was founded in 1994 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The CBP is committed to improving public policies that influence the economic and social well-being of Californians and their communities. General operating support for the California Budget Project is provided by grants from the James Irvine, Ford, Charles Stewart Mott, Friedman Family, David and Lucile Packard, and California Wellness Foundations, the Penney Family Fund, and individual donations and subscriptions. Visit the CBP web site at www.cbp.org.
