

Local Sales Taxes— What Role Can They Play in the 1993-94 State Budget?

Overview

The *May Revision of the 1993-94 Governor's Budget* continues to reflect the \$2.6 billion transfer of property tax revenues from local agencies to school districts that was originally proposed in January. The *May Revision*, however, provides some details about the allocation of this transfer among local agencies that were missing in the January proposal. Specifically, the Administration proposes to allocate \$2.1 billion of the shift to county governments, and allow them to offset some portion of this reduction through retention of property taxes that would otherwise be allocated to special districts. In addition, \$93 million of county property tax revenues would be recaptured as an offset to federal immigration funding in certain counties. City governments and redevelopment agencies would be required to transfer about \$288 million and \$65 million, respectively, to support schools.

The Governor proposes that property tax revenue losses in counties be accommodated in three ways. First, local county officials should ask voters to approve additional local sales taxes, revenue from which would support county programs. Second, the Legislature should pass legislation that eliminates all state mandates on county programs which are not related to public safety. Finally, the Administration would allow counties to retain some of the property tax funds that would otherwise be allocated to special districts.

To facilitate his call for local voters to decide what level of support to provide for county programs, the Governor has called for a statewide

special election to be held on November 2, 1993. While the justification for this special election has been framed in terms of allowing voters to make decisions on local sales tax increases, the state actually has no authority to place this question before the voters. Rather, current law requires that a statewide special election may only be called to decide a statewide initiative that has already qualified for the ballot. In effect, the special election merely provides county officials with the opportunity to consolidate a local election on the sales tax issue with a statewide election on other issues.

In this brief, we review the existing authority of counties to raise the local sales tax, and the viability of this proposed method for offsetting the county revenue losses associated with the proposed property tax shift. As we concluded in our May Revision analysis, the proposals to offset county property tax revenue losses fall short. The revenue likely to be generated from additional local sales taxes—if these taxes are put on the ballot, passed by the voters, and survive likely legal challenges—would offset less than 20 percent of counties' revenue loss, on average, in 1993-94.

Current Local Sales Tax Authority

Uniform Local Sales and Use Taxes. Since 1967, a standard 1.25 percent sales tax has been imposed in all counties under the authority provided by the Bradley-Burns Uniform Local Sales and Use Tax. The 1.25 percent tax applies on a countywide basis, but it actually amounts to 3 separate taxes.

First, each city levies a 1 percent tax based on the level of retail sales occurring within its boundaries. The county levies a 1 percent tax on sales occurring in the unincorporated area. The remaining 0.25 percent is levied countywide and is allocated to the county transportation fund for county mass transportation and highway programs.

The *state* sales tax rate is currently 6 percent. This consists of a basic rate of 5 percent, a 0.5 percent rate dedicated to local health and welfare programs (“realignment”), and a 0.5 percent temporary rate that is due to expire on July 1, 1993. The Bradley-Burns tax combined with the state sales tax rate results in a basic statewide tax rate of 7.25 percent.

Optional Transactions and Use Taxes. In addition to the uniform local sales taxes discussed above, current law provides additional authority for local sales tax levies under a variety of circumstances. At the present time, 20 of the state's 58 counties levy at least one of these optional taxes. (Figures 1, 2 and 3 show the current total sales tax rate in these counties, and lists the other counties which levy only the basic statewide rate of 7.25 percent.)

Most of the optional taxes are levied by a special purpose district under *specific* statutory authority. As Figures 1, 2, and 3 show, these optional taxes are being used overwhelmingly for

Figure 1**Counties Levying Optional Sales Taxes**

County	Optional Rates		Total Rate	County	Optional Rates		Total Rate
	Transportation Related	Other			Transportation Related	Other	
Alameda	1.00%	—	8.25%	San Benito	.50%	—	7.75%
Contra Costa	1.00	—	8.25	San Bernardino	.50	—	7.75
Fresno	.50	— ^a	7.75	San Diego	.50	—	7.75
Imperial	.50	— ^b	7.75	San Francisco	1.00	.25% ^d	8.50
Inyo	—	.50% ^c	7.75	San Joaquin	.50	—	7.75
Los Angeles	1.00	—	8.25	San Mateo	1.00	—	8.25
Madera	.50	—	7.75	Santa Barbara	.50	—	7.75
Orange	.50	—	7.75	Santa Clara	1.00	—	8.25
Riverside	.50	—	7.75	Santa Cruz	.50	.50	8.25
Sacramento	.50	—	7.75	Sonoma	—	.25	7.50

^a Rate increases by 0.1 percent in Fresno metropolitan area on July 1, 1993. Revenue from the tax will be used for cultural programs.

^b Rate is 8.25 percent in City of Calexico to provide funding for local hospital district.

^c Revenue used for general purposes.

^d Tax will expire on June 30, 1993

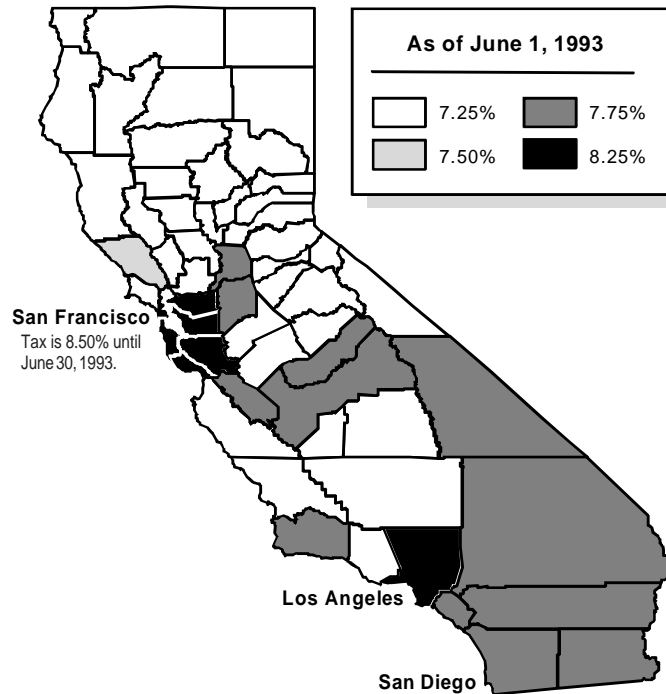
Figure 2**Counties Without Optional Sales Taxes**

Alpine	Kings	Napa	Sutter
Amador	Lake	Nevada	Tehama
Butte	Lassen	Placer	Trinity
Calaveras	Marin	Plumas	Tulare
Colusa	Mariposa	San Luis Obispo	Tuolumne
Del Norte ^a	Mendocino	Shasta	Ventura
El Dorado	Merced	Sierra	Yolo
Glenn	Modoc	Siskiyou	Yuba
Humboldt	Mono	Solano	
Kern	Monterey	Stanislaus	

^a Rate increases by 0.5 percent for general purposes on July 1, 1993.

Figure 3

County Sales Tax Rates



transportation purposes.

Current law, however, also provides three mechanisms for any *county* to levy additional sales taxes:

- **General Purpose Tax (Revenue and Taxation Code Section 7285).** A county board of supervisors can adopt an ordinance that establishes an additional sales tax. Revenues from the tax cannot be restricted as to the purposes for which it is imposed. The ordinance establishing the tax must be approved by a two-thirds vote of the board and by a simple majority of county voters. Only two counties, Del Norte

and Inyo, have adopted general purpose sales taxes. In addition, voters in the County of San Bernardino will vote on a sales tax proposal this summer.

- **Special Authority Tax (Section 7285.5).** The county board of supervisors may establish a special authority to levy a tax for specific purposes. The ordinance establishing this tax must contain a specific expenditure plan for the tax proceeds. Under these circumstances, state law requires that the ordinance establishing the tax must be approved by a two-thirds vote of the authority and by a simple majority vote of the

county's voters. Three counties—Madera, Monterey and Sonoma—have passed such a tax. The courts, however, invalidated Monterey's tax, ruling that the Constitution (Article XIII A) requires a two-thirds approval from voters.

■ **Local Public Finance Authority Tax (Section 7288).** Finally, a county or school district may establish a "local public finance authority" for the purpose of financing drug abuse prevention, crime prevention, health care programs, or public education. The board of directors of such an authority can adopt an ordinance that establishes a sales tax. The ordinance must be approved by two-thirds of the authority's board and a simple majority of county voters. To date, no such authority has been established. Furthermore, it is almost a certainty that two-thirds voter approval would also be needed to pass constitutional muster.

Limitations. Current law specifies three limitations that apply to the imposition of a new local sales tax. First, the sum of all local taxes, excluding the Bradley-Burns tax, may not exceed 1.5 percent. Given the current basic statewide sales tax of 7.25 percent, this limitation means that the total sales tax rate in any county cannot exceed 8.75 percent. As can be seen in Figure 1, only the City and County of San Francisco—at 8.5 percent—is approaching this limitation.

Second, the rate of an individual sales

tax established by any of the three mechanisms discussed above can be set only at 0.25 percent or 0.5 percent. Third, the sales tax cannot take effect until the first calendar quarter that occurs *at least* 110 days after the election if it is established by a board of supervisors, or at least 90 days after an election if established by a local public finance authority.

Legal Issues

Local Sales Taxes for General Purposes. As a result of recent court decisions, the constitutionality of the public vote requirement for a new sales tax levied for general purposes has come into question. In recent opinions, the Legislative Counsel argues that the voter approval requirements violate Article II, Section 9, of the State Constitution, which prohibits a public referendum on tax levies. Citing a ruling by the Fifth District Court of Appeals (*City of Woodlake v. Logan*), Counsel argues that the voter requirement for general purpose local sales taxes is an unconstitutional referendum on a local tax levy, and that the public vote requirement can be "severed" from the remainder of the statutory authorization for the tax. Under this logic, counties could levy a new sales tax by a two-thirds vote of the board of supervisors without a public vote and with no change in the existing statutes.

While the Board of Equalization (BOE) recognizes this uncertainty regarding general purpose sales taxes, it has ruled that it cannot administer a new countywide sales tax unless the tax has been approved by county voters. The BOE bases its ruling on Article III, Section 3.5 of the Constitution, which

requires it to abide by current law until a court rules that the law is unconstitutional. The Attorney General released an opinion on May 19, 1993, concurring with the BOE's ruling. Thus, as a practical matter, a new local sales tax must be approved by county voters before the BOE will collect revenue from the tax.

There is also a question as to whether current law allows a county to implement multiple additional general purpose sales taxes. That is, can counties use this authority more than once, as long as they remain below the 1.5 percent local sales tax cap? If the answer is "no," the two counties that have already adopted this type of sales tax would be forced to look to alternative mechanisms to offset property tax revenue losses proposed by the Governor.

Local Sales Taxes for Specific Purposes. In a recent decision (*Rider v. County of San Diego*), the Supreme Court ruled, in effect, that a new tax, in which revenues are earmarked for a specific governmental project or program, must be approved by two-thirds of county voters. As a result of this opinion, any tax approved by a special authority or local public finance authority established pursuant to current law must be approved by two-thirds of county voters, even though the statute requires only a majority public vote.

In some cases, a two-thirds voter approval may be argued to be necessary for new general purpose sales taxes as well. Specifically, if revenue from a new sales tax is dedicated by

a board to a specific county program (for example, law enforcement) normally funded by the county's general fund, it has been argued that the tax is actually a special tax requiring two-thirds voter approval.

Legal Challenges Likely. As a result of these uncertainties, counties are likely to face legal challenges for additional sales taxes on any one of the following legal grounds:

- General purpose taxes are, effectively, special taxes, thereby requiring an approval from two-thirds of county voters.
- Tax measures adopted by local public finance authorities require approval of two-thirds of county voters.
- General taxes cannot be subject to a vote of the people.

Fiscal Implications for Counties

As noted earlier, the Governor has proposed a special election in November to give county voters the opportunity to raise their local sales taxes to fund local programs. The Administration asserts that counties can accommodate their \$2.1 billion property tax losses by (1) retaining special district property tax revenues, (2) eliminating state mandates on local programs not related to public safety, and (3) obtaining voter approval for additional local sales taxes. Our review of the property tax proposal indicates that much of the special district property tax revenues are likely to be needed to main-

tain local fire protection and other critical activities. With regard to the elimination of mandates, the savings are not likely to be significant in the absence of immediate action to sponsor and advocate specific legislative changes on the part of the Administration.

This leaves the implementation of local sales taxes as the only alternative for substantial relief in 1993-94. However, even if all counties place measures on the November special election ballot and voters allow them to proceed with implementation of the tax, revenues would not be collected until April 1994. Under these circumstances, county revenues would increase by approximately \$360 million in 1993-94—about 17 percent of the amount of property taxes they would lose under the Governor's plan. This is because existing law requires a lengthy waiting period so that the BOE can get ready to administer the new tax. Specifically, a new sales tax cannot take effect until the first day of a calendar quarter *at least* 110 days after the election (90 days in the case of a local public finance authority). Although the Legislature could shorten this waiting period, thereby allowing counties to collect additional revenue, it is not certain whether the BOE, which administers all local sales taxes, would be able to implement new taxes much sooner.

Actually, counties do not need to wait until November to seek voter approval on local taxes. Special elections can be called in a county for the sole purpose of placing a sales tax ordi-

nance before the voters. Counties can call a special election no sooner than 88 days in advance of the election date. As a result, if counties act quickly, they could have a special election on a sales tax ordinance by the middle of September, which would allow counties to implement a new tax by January 1994. If all counties were to go this route, up to \$720 million could be raised in 1993-94, enough to offset about one-third of their losses.

In 1994-95, on a statewide basis, counties could receive approximately \$1.5 billion, still significantly short of replacing their property tax losses under the Governor's plan.

Conclusion

The uncertain legal status of existing county sales tax authority and the timing problems associated with putting local sales taxes in place lead us to conclude that they can play only a minor role, at best, in helping counties accommodate the large property tax revenue losses proposed by the Governor in 1993-94. Statutory changes may be needed to clarify this authority in some areas, so as to increase the certainty that these taxes can survive legal challenges in the short run. In the longer run, however, the use of local sales taxes should be tied to an overall restructuring of state and local functions so that local governments have the resources needed to meet program responsibilities and voter preferences.



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