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February 19, 1998

Hon. Daniel E. Lungren
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Connie Lemus
Initiative Coordinator

Dear Attorney General Lungren:

Pursuant to Elections Code 9005, we have reviewed the proposed constitutional initiative entitled "Tax Limitation Act of 1998" (File No. SA 98 RF 0001). The measure would impose stricter voting requirements for the imposition of, or increase in, certain taxes and fees.

BACKGROUND

Requirements for Increasing State Taxes. Under current law, the California Constitution provides that changes in state taxes enacted by the Legislature for the purpose of increasing revenues require a two-thirds vote in each house of the Legislature. In the case of initiative tax-increase measures put before the voters, a majority vote of the electorate is required for approval.

In practice, the two-thirds vote requirement for legislative tax changes noted above is currently interpreted as applying to a measure's aggregate net impact on state tax liabilities. Thus, for example, a single measure which both increases one type of tax and decreases another would require a two-thirds vote, if the net revenue impact of the two

changes combined was positive. Alternatively, only a majority vote would apply if there was no net increase in aggregate taxes. It also should be noted that a tax-law change which increases taxes for some individual taxpayers but reduces them for others in an equal amount (and thus does not raise taxes in the aggregate), does not require a two-thirds vote.

Requirements for Increasing State and Local Regulatory Fees. The state and local governments impose many different fees, including fees for property-related services, user fees (such as park entrance fees), and "regulatory" fees. State and local governments typically impose regulatory fees to offset the costs of programs to promote the health, safety, or well-being of residents. For example, local governments impose building inspection, plan check, and rent control fees. In addition, the state and certain local governments impose pollution abatement fees and other environmental regulatory fees. In some cases, the amount of a regulatory fee is closely linked to the cost of regulating the fee payer's operations. In other cases, particularly in the case of pollution abatement fees, the fee structure is designed to reflect the burdens on, or benefits from, the regulatory activity. Current law authorizes the state to impose regulatory fees upon a majority vote of the Legislature or a majority vote of the electorate approving an initiative. Current law does not require voter approval of regulatory fees imposed by local governments.

PROPOSAL

This measure provides for restrictions on establishing new taxes and regulatory fees and on increasing existing ones.

State Taxes. The measure provides that any increases in state taxes made by the Legislature (whether by increased rates or changes in methods of computation, any other increase in an existing tax, or any new tax) require a two-thirds vote in both houses of the Legislature. Regarding any such tax increases due to legislative measures or initiatives placed before the voters, a two-thirds vote of the electorate also would be required.

State and Local Regulatory Fees. The measure changes the approval requirement for (1) fees imposed on a manufacturer or seller of a product to mitigate past, present, or future adverse impacts of products, and (2) regulatory fees that exceed the reasonable cost of regulating the fee payer's operation. Specifically, local governments must subject these fees to a two-thirds vote of their electorate. In addition, the measure requires state fees to be approved by either a two-thirds vote of the Legislature or the statewide electorate, as applicable.

FISCAL EFFECTS

The fiscal impact of this measure would depend in part on how the measure is interpreted. Generally, however, because the measure places restrictions on increasing taxes and fees, it could result in some state tax increases not being adopted and some state and local regulatory fee increases not occurring. Thus, it would reduce future state and local revenues by unknown amounts.

State Tax Effects. Again, the measure raises the vote requirement for certain state tax increases—those that are “packaged” with tax decreases. Under this measure, these increases require a higher vote requirement. Consequently, fewer may pass, resulting in reduced revenues. This could occur, for example, if a revenue-decreasing provision (such as a federal conformity provision) is enacted without an accompanying revenue-increase provision that was initially planned, because of the latter’s inability to muster a two-thirds vote.

In addition, it would be more difficult to modify the distribution of the tax burden by changing the mix of revenues from different taxes, to the extent that a two-thirds vote would be required if any individual taxes were being increased. This, in turn, could affect the relative distribution of taxes paid among different individuals and businesses.

State and Local Regulatory Fee Effects. Several fee provisions of the measure are not clear, and their interpretation could significantly alter the measure’s fiscal effects relating to fee increases. In this analysis, we have assumed that the measure applies only to new and increased fees, and that the measure does not apply to fees other than regulatory fees.

Assuming the above, we estimate that passage of this measure would have the following fiscal effects:

- *Future Revenues From Regulatory Fees.* Given the two-thirds vote approval requirement for some regulatory fees under the proposal, state and local governments themselves may choose not to impose some fees in the future, or to reduce the amount of the fees they adopt to avoid the vote-approval requirement. In other cases, new fee proposals may be placed before the voters but rejected, due to the two-thirds vote requirement. To the extent that any of these outcomes occur, state and local governments would realize lower regulatory fee revenues than they would have absent this measure. Because many environmental programs are funded by regulatory fees, this measure could significantly decrease

these programs' revenues. The extent of the decrease to environmental or other programs' future revenues is unknown.

- *Election and Administrative Costs Would Increase.* Local governments would incur increased election costs to place some new or increased regulatory fees before the voters. In addition, state and local governments would incur increased administrative costs to evaluate future regulatory fees to determine whether the fees exceeded government's cost to regulate the fee payer's operation. The total amount of these increased costs is unknown.

Summary of Fiscal Effects. We estimate that this initiative would have the following fiscal effects:

- Unknown, but probably not significant, reductions to state tax revenues.
- Unknown, but potentially significant, reductions in state and local regulatory fee revenues.

Sincerely,

Elizabeth G. Hill
Legislative Analyst

Craig L. Brown
Director of Finance