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November 23, 1999

Hon. Bill Lockyer
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Diane Calkins
Initiative Coordinator

Dear Attorney General Lockyer:

Pursuant to Elections Code Section 9005, we have reviewed the proposed initiative constitutional amendment (File No. SA1999RF0049). The measure:

- Increases the state's sales tax by 1.5 percentage points.
- Eliminates all resident-student fees for public higher education.
- Requires the Superintendent of Public Instruction to enhance K-12 public-education and social service programs.
- Requires state and local governments to adopt affirmative action programs and give preferential treatment in public education and public contracting to persons or groups that have faced racism or sexism.

As Section 9005 directs, our review addresses the potential effects of the measure on state and local government costs and revenues.

Raising State Sales Tax

Proposal. The state sales tax rate is currently 6 percent, of which 5 percent is allocated to the state's General Fund, 0.5 percent is allocated to the local public safety fund, and 0.5 percent is allocated to the local revenue fund. A uniform local tax rate of 1.25 percent is levied in all counties, and local governments are authorized to levy an optional additional tax of not to exceed 1.5 percent. Currently, total sales tax rates range from 7.25 percent to 8.5 percent. This measure would add an additional statewide rate of 1.5 percent to the sales tax. The measure would not result in a similar increase in the companion *use* tax rate. Revenues generated by the tax increase would be deposited in the Student Higher Education Trust Fund, created by the measure.

Increased State Revenue. Assuming the measure goes into effect in December 2000, we estimate that it would result in approximately \$3.2 billion in additional sales tax revenue for 2000-01 (partial-year effect), and approximately \$6.0 billion in 2001-02 (full-year effect). The increase in the sales tax rate could result in a slight percentage reduction in state General Fund and local sales tax revenues due to reduced consumer demand caused by higher prices.

Revenue generated by the increased sales tax would be deposited in the Student Higher Education Trust Funds, created by the measure. As discussed below, up to half of these funds would be used to offset the impact of eliminating fees at public colleges and universities and the remaining funds would be appropriated to the Superintendent of Public Instruction for various education and social services programs.

State Appropriations Limit Consideration. Article XIII B of the California Constitution limits the amount of certain funds that the Legislature may appropriate in any year. The Constitution adjusts this "state appropriations limit" each year for changes in the cost-of-living and population. Currently, the state is significantly below the appropriations limit. By increasing sales tax revenues, this measure could cause revenues to exceed the limit. In such cases, the Constitution requires the state to return 50 percent of any excess to taxpayers and to allocate 50 percent of any excess to public schools. As a result of this allocation to schools, the Proposition 98 guarantee would be raised by the amount of the allocation to schools, thereby increasing mandatory state spending for education in future years.

Eliminating Resident-Student Fees

Proposal. The Legislature establishes student-fee levels in statute for the California Community Colleges (CCC) and California State University (CSU). The University of California (UC) Board of Regents sets student fees for the university. Current fees for the three segments are shown in Figure 1:

Figure 1			
Annual Fee for California Residents for Full-Time Students			
	Undergraduate	Graduate	Professional
California Community Colleges	\$330	—	—
California State University	\$1,795	\$1,873	\$1,873
University of California	\$3,857	\$4,448	up to \$10,824

This measure eliminates all student fees for California residents that attend any of California’s public colleges or universities.

Reduced Fee Revenue. The measure would reduce annual student-fee revenues to the community colleges, CSU, and UC by roughly \$2 billion. The measure would replace these revenues with funds from the increased state sales tax revenue.

Costs of Changing Enrollments. By eliminating student fees, higher education enrollments would increase, and there would be a significant shift of students from private to public colleges. Students would also shift from community colleges to the more costly CSU and UC systems, and from the CSU to the more costly UC system. Annual state costs for higher education would increase significantly, perhaps in the range of \$500 million to \$1 billion. These General Fund costs would be roughly offset by reduced financial aid costs due to the elimination of student fees. Increases in public higher education enrollments would also increase state capital costs of constructing higher education facilities by a significant amount.

Expanding K-12 and Social Services Programs

Proposal. Public K-12 education is provided to about 5.8 million students—ranging from infants to adults—through over 1,000 locally governed school districts and county offices of education. The Superintendent of Public Instruction (SPI) heads the State Department of Education (SDE). The SPI administers the allocation of state funds, and

some federal funds, to local school agencies and provides general oversight of K-12 programs throughout the state. The SDE directly operates some programs, including two State Schools for the Deaf and the State School for the Blind. This measure appropriates funds to the SPI for various educational and social services programs that the SPI “. . .deems fit to enhance the Quality of Life of the People of California and protect and serve the needs of poor children. . .”

Fiscal Effect. The measure would appropriate the balance of funds in the Higher Education Trust Fund (roughly \$4 billion) each year to the Superintendent of Public Instruction for various education and social services programs.

Requiring Affirmative Action

Proposal. Proposition 209, which the voters approved in 1996, prohibits the state and local governments from giving preferential treatment in public education, public contracting, and public hiring to anyone based on their race, sex, color, ethnicity, or national origin. This proposed initiative repeals the provisions of Proposition 209 and in its place requires state and local governments to create affirmative action programs and give preferential treatment in public education and public contracting to persons or groups that have been victims of racism and sexism.

Increased State and Local Costs. The measure could potentially increase costs of state and local agencies by perhaps tens of millions of dollars annually by requiring that they administer preferential contracting programs.

Summary of Fiscal Effect

This measure would have the following major fiscal impacts:

- Annual increase in state sales taxes of about \$6 billion, with the revenues used to replace public college resident fees (roughly \$2 billion) and fees for various education and social services programs (roughly \$4 billion).
- Significant increase in state capital costs for constructing public higher education facilities.

- Increase in state and local costs of potentially tens of millions of dollars per year to implement preferential contracting programs.

Sincerely,

Elizabeth G. Hill
Legislative Analyst

B. Timothy Gage
Director of Finance