

December 16, 2011

Hon. Kamala D. Harris
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Dawn McFarland
Initiative Coordinator

Dear Attorney General Harris:

Pursuant to Elections Code Section 9005, we have reviewed the proposed constitutional amendment related to the 2011 realignment of state programs and revenues (A.G. File No. 11-0061 #1S).

BACKGROUND

State and Local Governments Operate and Fund Different Programs

The state and local governments operate various programs in California. Most of these services are delivered by local governments—counties, cities, special districts, schools, and redevelopment agencies. Programs operated by state and local governments are funded through a variety of sources, including federal funds, taxes, and fees.

Criminal Justice System. In California, the state funds and operates prisons and supervises parolees released from prisons. The state also funds the court system through a combination of state General Fund resources and various fine and fee revenues. Counties operate jails and supervise probationers, as well as provide prosecutors and public defenders for the court system. Cities provide police services. The state provides some funding—such as grants—to local governments for criminal justice activities, but most local law enforcement activities are funded from local revenues.

Health and Human Services Programs. The state and local governments—primarily counties—operate and fund a variety of health and human services programs, including mental health services, substance abuse treatment, foster care and child welfare services, and adult protective services. These programs are funded through a combination of state, federal, and local funds, with the specific share of costs assigned to the state and local governments varying by program.

Proposition 98 Minimum Annual Funding Guarantee. In 1988, voters approved Proposition 98. Including later amendments, Proposition 98 establishes a guaranteed minimum

annual amount of state and local funding for K-14 schools. Generally, Proposition 98 provides K-14 schools with revenues that grow each year with the economy and the number of students. The guaranteed funding is provided through a combination of state General Fund appropriations and local property tax revenues. Proposition 98 expenditures are the largest category of spending in the state's budget—totaling roughly 40 percent of state General Fund expenditures. With a two-thirds vote, the Legislature can suspend the Proposition 98 guarantee for one year and provide any level of K-14 schools funding it chooses.

State-Reimbursable Mandates. The California Constitution generally requires the state to reimburse local governments when it “mandates” a new local program or higher level of service. Over the years, the courts have interpreted this requirement in a way that has not required state reimbursement for many state measures that have the effect of increasing local costs.

2011 Realignment Legislation

As part of the 2011-12 budget plan, the Legislature enacted a major shift—or “realignment”—of state program responsibilities and revenues to local governments. In total, the realignment plan provides \$6.3 billion to local governments (primarily counties) to fund various criminal justice, mental health, and social services programs in 2011-12, and ongoing funds for these programs annually thereafter.

Shift of State Program Responsibilities. The realignment package includes \$6.3 billion in 2011-12 for court security, adult offenders and parolees, public safety grants, mental health services, substance abuse treatment, child welfare programs, adult protective services, and other programs. Implementation of this package began in 2011.

Shift of Revenues to Cover Program Costs. To fund the realignment of these programs, the budget provides a total of \$6.3 billion in revenues from three sources to local governments to implement the realigned programs. Specifically, the state redirected 1.0625 cents of the state’s sales tax rate to counties. In addition, the realignment plan redirects an estimated \$453 million from the base 0.65 percent vehicle license fee (VLF) rate for local law enforcement programs. Under prior law, these VLF revenues were allocated to the Department of Motor Vehicles for administrative purposes and to cities and Orange County for general purposes. The budget also shifts \$763 million on a one-time basis in 2011-12 from the Mental Health Services Fund (established by Proposition 63 in November 2004) for support of the Early and Periodic Screening, Diagnosis, and Treatment Program and Mental Health Managed Care program.

Exclusion of Revenues From Proposition 98 Calculation. A budget-related law (Chapter 43, Statutes of 2011) excluded the redirected 1.0625 cent sales tax revenues from the Proposition 98 calculation, reducing the minimum guarantee by roughly \$2 billion. Chapter 43 excluded these revenues, however, contingent on the approval of a ballot measure by November 2012 that (1) reauthorizes the exclusion of the 1.0625 cent sales tax revenues from the Proposition 98 calculation and (2) provides funding for school districts and community colleges by an amount equal to the reduction in the minimum guarantee due to the exclusion. Absent a ballot measure with these specific provisions, Chapter 43 would increase the Proposition 98 minimum guarantee back to its original level.

PROPOSAL

The measure amends the Constitution to require the state to continue providing revenues to local governments to pay for the programs realigned in 2011, unless the state reduces these local program responsibilities.

Authorizes Some Changes to Realignment Programs and Revenues. The measure permits the state to reduce the amount of sales tax and VLF revenues provided to local governments for realignment as long as there is a commensurate reduction in local realignment program responsibilities. If the state reduced realignment revenues by an amount *greater than* the reduction in realignment program responsibilities, the measure requires the state to backfill the revenue difference to local governments. The measure also allows the state to substitute funding from other revenue sources as long as the alternative funding level is at least equal to the amount that would have been generated by the sales tax and VLF. Finally, the measure requires a four-fifths (80 percent) vote of each house of the Legislature to reduce, eliminate, reallocate funding for, or make other changes to, certain public safety grant programs realigned to local governments in 2011.

Constrains State's Ability to Impose Additional Requirements. Under the measure, a local government would not be required to fulfill a statutory or regulatory requirement approved after October 2011 related to the realigned programs unless the requirement (1) imposed no net additional costs to the local government or (2) the state provided additional funding sufficient to cover its costs.

Limits Local Governments From Seeking Additional Reimbursements. This measure specifies that the legislation creating 2011 realignment would not be considered a state-reimbursable mandate. Therefore, local governments would not be eligible to seek reimbursement from the state for any costs related to implementing the legislation (as enacted prior to October 2011). Similarly, the measure specifies that any state regulation, executive order, or administrative directive issued to implement the already enacted legislation would not be a state-reimbursable mandate.

State and Local Governments Could Share Some Unanticipated Costs. The measure specifies that certain unanticipated costs related to realignment would be shared between the state and local governments. Specifically, the state would be required to fund at least half of any new local costs resulting from certain changes in federal statutes or regulations. The state also would be required to pay at least half of any new local costs resulting from federal court decisions or settlements related to realigned programs if (1) the state is a party in the proceeding, and (2) the state determines that the decision or settlement is not related to the failure of local agencies to perform their duties or obligations.

FISCAL EFFECT

Impact on State and Local Governments. This measure would change the state's authority over the 2011 realignment. Under the measure, the state could not shift any realignment funds to other programs unless it reduced the scope and costs of the realignment programs. Similarly, the state could not take actions that increased realignment program costs unless it provided

additional funds for this purpose. As a result, local government's net fiscal position regarding realignment would be more stable than otherwise would be the case. Any impact would depend on how the state would have acted in the future absent the measure. By providing the constitutional protections to counties described above, the measure could have a significant impact.

With regard to the state, the measure would have the related impact of restricting the state's ability to make unilateral changes—either reducing local revenues or raising local costs—in the 2011 realignment.

Impact on Proposition 98 Minimum Guarantee. As noted earlier, absent a ballot measure raising additional revenues for schools, current statute requires that the realignment sales tax revenues be included in the calculation of the minimum guarantee. This initiative does not explicitly mention Proposition 98 or school funding. However, by dedicating realignment revenues for local governments, the measure has the effect of constitutionally excluding those revenues from the Proposition 98 calculation and safeguarding the monies for local governments. As a result, the Proposition 98 minimum guarantee is lowered. Despite the drop in the guarantee, school funding would not necessarily be reduced, as the Legislature has discretion to spend more than the Proposition 98 minimum guarantee, other resources permitting.

Summary of Fiscal Effect

This measure would have the following major fiscal impacts:

- Limitation on the state's ability to change 2011 realignment, resulting in a more stable net fiscal situation for local governments.
- Decrease in Proposition 98 school minimum funding guarantee. Actual impact on school spending would depend on state decisions in balancing its annual budget.

Sincerely,

Mac Taylor
Legislative Analyst