

Investigation of the Financing of Local Government Services

Introduction

Engage a local government official in conversation about government finances long enough and sooner or later you will hear something like: “Well, what we really need to do is fix California’s local government financing system. But, we can’t do that on the local level!” Well, neither can the Grand Jury.¹

However, what the Grand Jury can do is understand the system and do what we can to serve the interests of the citizens of this county within that system. This year’s Grand Jury chose to dedicate its efforts to investigating this financing system by examining three main areas related to local government finance:

- The impact of land use decisions on local government finances
- The role of Redevelopment Agencies in financing local government
- The procedure for determining fees and assigning cost of local government services through inter-departmental and inter-government charges and the raising of revenue through fees charged to the public.

Legislative Background

In 1978 the citizens of this state passed Proposition 13, the seminal event in state and local government financing. Prior to Proposition 13 the state and local financing system was relatively simple: State taxes financed state responsibilities and local revenues paid for local responsibilities. If local government needed more revenue, they could simply increase property taxes to meet that need.

Most people know that Proposition 13 restricted the ability of state and local government to increase property taxes.² What may be less clear is what happened in response to that restriction.

¹ Currently, there are efforts to begin a reform of this system on the state level. For example, AB 1221 would reduce local government’s share of sales tax by ½% and swap in an equal percentage of property tax revenue. The swap would give local government a greater property tax base and make housing and job-creating uses relatively more attractive. Because property tax revenue tends to be more stable and grow faster than sales tax receipts, the swap is overwhelmingly good for cities. Analysis shows that more than 80% of cities come out ahead in the swap, with particularly good results for built-out cities and cities pursuing balanced commercial/residential growth.

² Between 1975 and 1978 the assessed value of owner occupied homes in California increased a staggering 111% and tax levies rose by 92%.with no perceptible improvement in local government services. Homeowners revolted and passed Proposition 13. Proposition 13 set the property tax rate at 1 % of assessed value, rolled assessments back to their 1975 values, and limited increases in assessed value to 2 % until a property was sold. When a property was sold or newly built, it was assessed at full market value and then rose by up to 2% yearly. Proposition 13 also required a 2/3 vote of the people for local special taxes. (Those with a designated purpose.) but, allowed a majority vote of the people or the local governing body to pass taxes for general (undesigned) purposes. In 1986

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Local government didn't go out of business. They didn't necessarily cut services. They did gradually lose a substantial proportion of their property tax revenue as the state appropriated a greater proportion of those taxes for public K-12 education.

Local governments soon looked for other sources of revenue such as fees, assessments, and utility and sales taxes to make up for the loss of property tax revenue. Voters responded in 1996 with Proposition 218 which limited assessments, fees, and charges on property to the cost of the special benefits or services provided to the property owner and required approval of property owners. Assessments, charges, or fees which exceed the benefit or service provided are taxes requiring voter approval under Proposition 13.

The end result was that local governments lost some of their financial independence, shifted to new sources of revenue, and became less and less interested in residential and industrial development that did not also generate some other form of revenue.

Proposition 86 changed the law to require a two-thirds vote of the public for general purpose taxes as well. Finally, Proposition 13 gave state lawmakers responsibility for allocating property tax revenues among local jurisdictions.