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September 29, 2010

Overview of
Proposition 26

L E G I S L A T I V E A N A L Y S T ' S O
F F I C E

Presented to:
Senate Revenue and Taxation Committee
Hon. Lois Wolk, Chair
Assembly Revenue and Taxation Committee
Hon. Anthony Portantino, Chair

□
September 29, 2010

Proposition 26's Main Components

- Expands the Scope of what Is a State or Local Tax
- Raises the Approval Requirement for Some State Revenue Measures
- Voids Recently Passed, Inconsistent State

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Laws

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Existing Categories of Taxes, Fees, and Charges

- Taxes
 - Pay for broad general public services.
 - Examples: income, sales, and property taxes.
 - Uses: education, prisons, health and social services programs.
 - User Fees
 - User pays for the cost of a specific service or program.
 - Examples: state park entrance fees and garbage fees.
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Regulatory Fees

- Fees that pay for programs or services that place rules upon the activities of businesses or people to achieve a public goal.
- Fees that pay to offset public or environmental impacts of certain activities.
- Examples: fees on restaurants to pay for health inspectors and fees on the purchase of beverage containers to support recycling programs.

Property Charges

- Assessments that benefit the property owner.
- Examples: charges imposed on property developers to improve roads leading to new subdivision developments and assessments that pay for service and programs that benefit the property owner.

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Existing Tax and Fee Approval Requirements

Approval Requirements: State and Local Taxes, Fees, and Charges

State Local

Tax Two-thirds of each house of the Legislature for measures increasing state revenues.

- Two-thirds of local voters if the local government specifies how the funds will be used.

- Majority of local voters if the local government does not specify how the funds will be used.

Fee Majority of each house of the Legislature.

- Generally, a majority of the governing body.

Property Charges Majority of each house of the

Legislature.

- Generally, a majority of the governing body. Some also require approval by a majority of

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property owners or two-thirds of local voters.

- State or local governments usually can create or increase a fee or charge with a majority vote of the governing body.
- Creating or increasing a tax requires approval by two-thirds of each house of the state Legislature and the signature of the Governor (for state taxes) or a vote of the people (for local taxes).

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what Is a Regulatory Fee?

- Disagreements Regarding Regulatory Fees
- There is disagreement about regulatory fees and taxes—particularly when the money is raised to

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pay for a program
of broad public benefit.

- Sinclair Paint
- In 1991, the state began imposing a regulatory fee on paint companies and other businesses that make or previously made products containing lead. The state uses the money for lead poisoning programs.
- Sinclair Paint argued that the fee was a tax because (1) the program provides a broad public benefit, not a benefit to the regulated business, and (2) the companies that pay the fee have no duties regarding the lead poisoning program other than the payment of the fee.
- The California Supreme Court ruled in 1997 that the charge was a regulatory fee, not a tax, thus the Legislature could enact the fee by majority vote of each house.

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Major Provisions of Proposition 26

.Expands the Scope of what Is a State or Local Tax

- Classifies as taxes some fees and charges that government currently may impose with a majority vote.

- As a result, more state revenue proposals would require approval by two-thirds of each house of the Legislature and more local revenue proposals would require local voter approval.

.Raises the Approval Requirement for Some State Revenue Proposals

- Requires a two-thirds vote of each house of the Legislature to approve laws that increase taxes on any taxpayer, even if the law's overall fiscal effect does not increase state revenues.

.Repeals Recently Passed, Conflicting State Laws

- Repeals recent state laws that conflict with this measure, unless they are approved again by two-thirds

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of each house of the Legislature. Repeal
becomes effective in November 2011.

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Regulatory Fees That Benefit the Public Broadly

oil Recycling Fee

The state imposes a regulatory fee on oil manufacturers and uses the funds for:

- Public information and education programs.
- Payments to local used oil collection programs.
- Payment of recycling incentives.
- Research and demonstration projects.
- Inspections and enforcement of used-oil recycling facilities.

Hazardous Materials Fee

The state imposes a regulatory fee on businesses that treat, dispose of, or recycle

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hazardous waste and uses the funds for:

- Clean up of toxic waste sites.
- Promotion of pollution prevention.
- Evaluation of waste source reduction plans.
- Certification of new environmental technologies.

Fees on Alcohol Retailers

Some cities impose a fee on alcohol retailers and use the funds for:

- Code and law enforcement.
- Merchant education to reduce public nuisance problems associated with alcohol (such as violations of alcohol laws, violence, loitering, drug dealing, public drinking, and graffiti).

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Approval Requirements for
State Tax Measures

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- Current Law
 - Under the California Constitution, laws enacted to raise revenues must be approved by two-thirds of each house of the Legislature.
 - Under current practice, laws that increase the amount of taxes charged to some taxpayers but offer equal (or larger) reductions in taxes for other taxpayers have not been viewed as increasing revenues. Therefore, these laws may be approved by a majority vote of the Legislature.
 - Proposition 26 Expands Approval Requirement
 - Proposition 26 specifies that state laws that result in any taxpayer paying a higher tax must be approved by two-thirds of each house of the Legislature.
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Repeals Recent State Laws That Are Inconsistent with the Measure

- Repeal Requirement
 - Any state law enacted between January 1, 2010 and November 2, 2010 that is inconsistent with this measure would be repealed on November 2, 2011 unless it were re-enacted by the Legislature by a two-thirds vote.
 - Recent Fuel Tax Law Changes
 - The Gas Tax Swap. In the spring of 2010, the state increased taxes on gasoline suppliers, but decreased other fuel taxes paid by gasoline sellers. These tax changes do not raise overall revenues but give the state greater spending flexibility. Specifically, the tax changes allow the state to use fuel tax revenues—rather than general fund

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resources—to
pay about \$1 billion in annual debt
services costs for transportation
bonds.

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Fiscal Effects of Proposition 26

- Changes Approval Requirements
- The measure expands the scope of what is considered a tax. New laws to create—or extend—these types of revenue measures would be subject to the higher approval requirements for taxes. The fiscal effect would depend on future actions by the Legislature, local governing boards, and local voters.
- Over time, we estimate that the measure would reduce government revenues and spending statewide

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by up to billions of dollars annually compared with what otherwise would have occurred.

- Voids Inconsistent Laws
- Because some of the measure's provisions would be subject to future interpretation by the courts, we cannot estimate the full fiscal effect of the repeal provision.
- It is likely this measure would increase state General Fund costs by at least \$1 billion annually by reversing the recent fuel tax laws.
- These impacts could be avoided if the Legislature passed the laws again with a two-thirds vote of each house and the Governor signed them.

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