

UPDATE ON PROPERTY TAX SHIFT

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Prepared by Association of California Water Agencies

Impact on Many Enterprise Districts Higher Than Anticipated

ACWA has confirmed through conversations with the State Controller's Office that the property tax shift imposed on enterprise special districts by Governor Schwarzenegger and the Legislature as part of the local government budget package will be substantially larger for many districts than had been originally estimated. The package still includes a \$1.3 billion revenue shift in FY 2004-05 and FY 2005-06 from cities, counties, special districts and redevelopment agencies based on FY 2001-02 revenues, along with a constitutional amendment to protect local government revenues, now known as Proposition 1A, on the November 2 General Election ballot.

The original formula called for at least 40% of property tax revenues to be taken from enterprise special districts, as reported to the State Controller in FY 2001-02. In no event was the loss to be greater than 10% of total revenues from whatever source. New analyses from the State Controller's Office now show that while the 10% cap will not be exceeded, some districts will lose 100% of their property taxes for the next two years.

Over the last several weeks as the State Controller developed the actual calculations for the special districts' share of the shift, it has become clear that the contribution from non-enterprise districts would only result in \$50 million toward the total \$350 million. As a result, the share to be covered by enterprise districts is expected to rise from \$225 million to \$300 million. It was made clear from the beginning that special districts, along with cities and counties, would have to contribute \$350 million (both in FY 2004-05 and FY 2005-06) and that the hit on individual districts would be increased until that level was reached.

Some members have expressed fears that the Legislature will try to once again shift property tax revenues in FY 2006-07. With the passage of Prop. 1A, the state could only "borrow" tax revenues. However, the state must first pay off the VLF Gap Loan by that third year before pursuing any "loan" from local government. The state can only borrow those funds in two out of 10 years after a fiscal emergency is declared. Any loan would have to be paid back before property taxes could be borrowed again.

State Controller's Office to Submit Calculations Directly to Dept. of Finance

After multiple requests from ACWA to obtain a document with the final calculations for what enterprise districts will be required to shift, ACWA has been told that the State Controller's office will not release the numbers but plans to send them directly to the Department of Finance this week. As stated in the final budget trailer bill for the local government agreement, AB 2115, Chapter 610:

"The Controller shall determine the amount of the ad valorem property tax revenue reduction required for each enterprise special district in each county. The Controller shall then determine whether the total amount of ad valorem property tax revenue reductions is less than \$350 million. If, for either the 2004-05 or 2005-06 fiscal year, the total of the amount of these reductions is less than \$350 million, the total amount of ad valorem property tax revenue allocated to each enterprise special district, other than an

enterprise special district that is a transit district, shall be reduced by an additional amount equal to that district's proportionate share of the difference, provided that the total reduction under this section for a district shall not exceed 10 percent of that district's revenue from whatever source for the 2001-02 fiscal year, as reported in the 2001-02 edition of the State Controller's Special Districts Annual Report.

"If, as a result of this 10% limitation, any portion of the difference remains unapplied, that remaining portion shall, as many times as necessary, be applied in proportionate shares among those enterprise special districts, other than transit districts, for which a 10% limitation has not been reached, until a \$350 million reduction has been applied.

"The Controller shall, on or before October 25, 2004, notify the Director of Finance of the reduction amounts determined under this subdivision. The Director of Finance shall, on or before November 12, 2004, notify each county auditor of the allocation reductions required by this paragraph and Section 97.73."

Options and Actions

While the options for changing the terms of the budget deal are extremely limited, ACWA is pursuing several possibilities to reduce the short-term hit on our members, including personal briefings with key legislators to educate them on the true impact of the final budget deal on enterprise special districts.

Background

The late-July compromise reached between the Governor and legislative leaders was far different than earlier agreements reached between the Administration and local governments (California League of Cities, California State Association of Counties and California Special Districts Association). While earlier agreements had called for enterprise and non-enterprise special districts to more equally share the burden of the \$350 million special district property tax shift, the package enacted and reported to members in late July was as follows:

- Dependent districts were to be included as well as independent districts.
- The formula called for at least 40% of property taxes from enterprise districts or as much as necessary to meet the \$350 million requirement, as long as the hit did not exceed 10% of total revenues (from whatever source).
- Transit was to be hit at 3%.
- 10% of property taxes would come from non-enterprise districts.
- The hit on enterprise districts' share would increase but would still not exceed 10% of total revenues (from whatever source) if the total from dependent and independent districts fell short.
- Fire, police, hospital, library, veteran's memorial, mosquito and vector control were exempted from any property tax hit.

The addition of dependent special districts to the property tax shift was designed to offset the reduction in the non-enterprise special district share from 25% to 10%.

In the final days and hours of the budget negotiations, amendments were placed in the local government trailer bill that required only enterprise districts to pick up any property tax shortfall if the shift did not

result in generating the \$350 million. The rationale was that no district should lose more than 10% of their total revenues, but that enterprise districts have the ability to cover revenue losses through rate increases.

While neither ACWA nor anyone else foresaw the extent to which the late changes would impact our members, we were concerned enough to make the following statements in an advisory to members and to the press in late July:

“ACWA is concerned that the formula for allocating the \$2.6 billion shift from local governments over the next two years places a disproportionate burden on water and sewer districts, which are already struggling to meet the demands of a growing population and are facing rapidly escalating costs. Many California citizens will pay more for their water and sewer rates as a result of this agreement, which has the effect of protecting other interests at the expense of water and sewer rate payers.

“ACWA and its members will nevertheless continue to work cooperatively and collaboratively with other local governments, the administration and the Legislature to further improve the relationship between state and local governments, by protecting the revenue base of both.”

As a result of these concerns, the ACWA Board voted in July to stay neutral on the budget package, but in September did vote to support Prop. 1A.

From the beginning, ACWA has lobbied for equity and fairness and the basic agreement reached with the Governor and local government was fair. Subsequent actions exempting particular types of districts has now resulted in a disproportionate burden on enterprise districts as ACWA had feared.